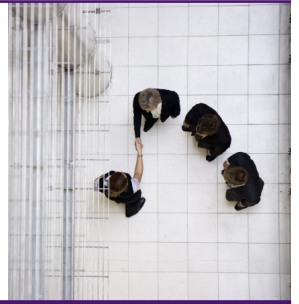


Review

Human Capital (Pensions)



Pensions & Employer Debt

THE LONG AWAITED DWP CONSULTATION

The DWP is consulting on proposals to amend the debt on employer regulations to make it easier for certain corporate restructures to take place without a debt being triggered in a defined benefit pension scheme. In broad terms a debt is currently triggered if a participating employer ceases to employ any active scheme members (but other participating employers continue to do so). The DWP has acknowledged that industry sees the debt regulations as a barrier to corporate restructuring and has, after lengthy informal consultation, now proposed two easements in the revised draft regulations: a general easement and a de minimis easement.

General easement

A debt would not be triggered if there were a transfer of assets and liabilities (including active pension scheme members) between two associated companies who participate in the same multi-employer pension scheme. The receiving employer must have its head office in the UK.

The requirements are set out in 8 steps, some of which are process driven. The key steps are 3, 5 and 7, summarised as follows:

Step 3 - The trustees of the scheme need to be satisfied that the receiving employer will be at least as likely as the exiting employer to meet the new liabilities that it is assuming (as well as its existing liabilities).

Step 5 - Both the exiting employer and the receiving employer should confirm that an insolvency event has not occurred to them and would be “unlikely” to occur to them within 12 months of the restructuring. The decision must be “reasonable”.

Step 7 - This is the actual corporate transaction itself, transferring assets, employees, pension scheme members and liabilities from the exiting employer to the receiving employer. The trustees must be satisfied that, immediately before completion of this step, there has been no change that would alter their decision in step 3. Step 7 must be completed within 12 weeks of the trustees notifying the exiting employer of the step 3 decision.

If it subsequently comes to light that steps 5 and 7 were not complied with, a debt is triggered and can be enforced by the trustees.

Our view

The proposed process is highly mechanistic. Although there is no requirement for a formal valuation to take place, there will inevitably still be advisory costs surrounding the covenant of the relevant employers. One wonders how the employers will come to a “reasonable” decision regarding the likelihood of insolvency under step 5. Also, the DWP has not allowed for the easement to apply in any more complicated transactions than a one-to-one transfer, so there may be bona fide restructurings that would not benefit from the general easement.

De minimis easement

The new de minimis easement is intended to apply for small scale “housekeeping” restructurings. Trustees must consider whether 4 factual conditions are met.

1. There must be no deficit in accordance with the last section 179 valuation¹.
2. No more than 2% of DB scheme members are employees of the exiting employer.
3. The relevant proportion of the s179 liabilities - calculated by multiplying the s179 liabilities of the scheme as a whole with the percentage identified in 2 above - must equal no more than £100,000.
4. In every rolling three year period no more than 5% of scheme members can be transferred under this easement.

The corporate restructuring must be completed within 12 weeks of the trustees' notification that the de minimis test is satisfied. The same insolvency considerations arise as mentioned under 'General easement'.

Our view

It is interesting to note that the draft regulations provide for a broad 'proxy' calculation of the exiting employer's interests in the scheme, by apportioning the s179 liabilities in accordance with member numbers. The transferring members may represent a higher proportion of the scheme liabilities than the average used in the de minimis test. It is difficult to assess how much the de minimis easement will be of use, especially in the current economic climate.

Hammonds will be working with the pensions industry to respond to the consultation which closes on 19 November 2009. If you would like to discuss any of these issues, please speak to your usual Hammonds' contact.

FURTHER INFORMATION

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¹ A section 179 valuation is carried out under the Pensions Act 2004 for assessing the risk based levy for PPF purposes.

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