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Restructuring Bankruptcy & Insolvency Group Legal Alert

Government publishes amendments to the Pensions Regulator's "moral hazard" powers

Summary

In April 2008 the Government announced that it intended to extend the Pensions Regulator's "moral hazard" (anti-avoidance) powers. Drafting has now been introduced into the Pensions Bill which gives effect to these changes. Although the Pensions Bill is expected to become law at the end of the year, the Government has already confirmed that certain changes will be retrospective to 14 April 2008.

Background

The moral hazard powers enable the Regulator to impose a Financial Support Direction ("FSD") or a Contribution Notice ("CN") on a party which is connected with or an associate of a scheme's sponsoring employer(s) if it considers it reasonable to do so.

In detail

The Government's stated aim in introducing these changes was to adapt the Regulator's powers to meet an evolving market and to better secure members against the emergence of new alternatives to pensions buyouts, which it said could reduce the security provided by a scheme's sponsoring employer(s).

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The amendments to the Pensions Bill go further, however, than the mere question of buyouts.

The key changes from the existing legislation are:

- The introduction of a material detriment test for CNs, together with a code of practice (a draft of which has now been issued) setting out when the Regulator will use its power;
- A statutory defence to the imposition of CNs under the material detriment test;
- A requirement for the Regulator to have regard to the benefits a person has received from the employer in deciding whether it is reasonable to impose a CN (this already exists for FSDs);
- The removal of the requirement that acts must be committed in bad faith to be within the scope of a CN issued for preventing, compromising or settling a section 75 debt;
- Extension of the financial resources test (in the FSD regulation) for "insufficiently resourced" employers to include the resources of the group, rather than just a member of it; and
- Anti-avoidance measures relating to pension transfers.

The most significant change to the existing legislation is the introduction of the material detriment test (which will be retrospective to 14 April 2008) which shifts the focus from the motivation of the parties to the effect of their acts. The Regulator has also issued a draft code (which will have legal force once it takes effect) listing the circumstances in which it expects to issue a CN in the context of the new material detriment test. The specified circumstances include:

- Transfer of a scheme outside the UK;
- Transfer outside the UK of the sponsoring employer;
- The severing of employer support;
- Transfer to a less well funded scheme; and
- Business models which provide inappropriate financial benefits for the employer.

Comment

We now have more detail on the material detriment test. The new test is very wide and is certainly not expressly limited to transactions involving non-insured buyouts, which are the Government's intended target (although the code of practice goes some way to limiting the wide scope of the draft legislation). Although the statutory defence is welcome, it will, in practice, be hard to make out.

Given the breadth of the Government's amendments to the Pensions Bill, the provisions will need to be considered in any restructuring which involves a defined benefit pension scheme.

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