

EXPLANATORY MEMORANDUM TO
THE OCCUPATIONAL PENSION SCHEMES (EMPLOYER DEBT AND
MISCELLANEOUS AMENDMENTS) REGULATIONS 2018

2018 No. 237

1. Introduction

- 1.1 This explanatory memorandum has been prepared by the Department for Work and Pensions and is laid before Parliament by Command of Her Majesty.
- 1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

- 2.1 Where an employer ceases to participate actively in a multi-employer defined benefit occupational pension scheme, that employer may be required to pay a sum of money into the scheme known as an “employer debt”. This instrument introduces a new procedure, the deferred debt arrangement, which enables such an employer to defer this requirement providing they meet certain conditions. The new deferred debt arrangement is intended to be of assistance to employers who cease to employ any active members of the scheme but want to continue their relationship as a statutory employer to it.
- 2.2 This instrument also makes some technical, clarificatory and consequential amendments.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

- 3.1 In the second report 2010-11 session at paragraph 6¹ the Joint Committee on Statutory Instruments commented on the way the existing definition of “receiving employer” in regulation 2(3A) (b) (ii) of the Occupational Pension Schemes (Employer Debt) Regulations 2005 (S.I. 2005/678)² (the “Employer Debt Regulations”) is drafted. This definition was inserted into the Employer Debt Regulations in April 2010 by the Occupational Pension Schemes (Employer Debt and Miscellaneous Amendments) Regulations 2010 (S.I. 2010/725)³ and is used in the restructuring provisions contained in regulations 6ZA and 6ZB of the Employer Debt Regulations.
- 3.2 Regulation 3(3) and (4) of this instrument amends the definition of receiving employer to provide for situations identified through consultation where the receiving employer is not associated with the exiting employer.

Other matters of interest to the House of Commons

- 3.3 As this instrument is subject to negative resolution procedure and has not been prayed against, consideration as to whether there are other matters of interest to the House of Commons does not arise at this stage.

¹ <http://www.publications.parliament.uk/pa/jt201011/jtselect/jtstatin/23/2303.htm>

² <https://www.legislation.gov.uk/ukxi/2005/678>

³ <http://www.legislation.gov.uk/ukxi/2005/725/contents/made>

4. Legislative Context

- 4.1 Employers in multi-employer occupational pension schemes are required under section 75 of the Pensions Act 1995 to pay their share of the scheme's liabilities on insolvency and winding-up and other prescribed circumstances. Section 75A of the Pensions Act 1995 provides powers to modify section 75 provisions in the case of multi-employer schemes.
- 4.2 The Occupational Pension Schemes (Employer Debt) Regulations 2005 (S.I. 2005/678)⁴ (the "Employer Debt Regulations") provide that in the case of multi-employer schemes a section 75 debt is also due when an employer ceases employing an active member of the scheme. This is known as "an employment cessation event."
- 4.3 The Employer Debt Regulations also prescribe the manner in which section 75 debts are calculated. A departing employer is liable for their share of the schemes' liabilities on a full buy-out basis.
- 4.4 The Employer Debt Regulations have been amended on a number of previous occasions to provide different mechanisms for employers to manage section 75 debts which serve to postpone, modify or re-assign the liability.
- 4.5 This instrument amends the Employer Debt Regulations to prescribe circumstances in which an employer debt may be deferred while the employer retains the responsibilities of a sponsoring employer for scheme funding and other purposes.

5. Extent and Territorial Application

- 5.1 This instrument extends to Great Britain.
- 5.2 The territorial application is Great Britain.
- 5.3 Northern Ireland will be making separate parallel provisions.

6. European Convention on Human Rights

- 6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation no statement is required.

7. Policy background

What is being done and why

- 7.1 Where an employer's relationship with an occupational pension scheme ends in what is known as an "employment cessation event" existing legislation sets out the requirements for what is commonly known as an "employer debt".
- 7.2 An "employer cessation" event occurs where an employer in a multi-employer pension scheme ceases to have any employees who are active members of the scheme at a time when at least one other participating employer continues to have employees who are active members. This could happen when for example when a large employer undergoes a corporate restructuring, or in the case of a smaller employer when their last member in the scheme retires.
- 7.3 The amount of the "employer debt" is calculated by reference to the cost of buying out members' benefits with an insurance company. This is called a "full buy out". If the scheme has sufficient funds to pay for all the members' benefits with an insurance

⁴ <https://www.legislation.gov.uk/uksi/2005/678>

company, no employer debt is payable. If the scheme does not have sufficient funds, an employer debt is payable. The rationale behind this requirement is to safeguard the funding of the pension scheme when the link to the employer has been broken.

- 7.4 There are already a number of arrangements in which an employer need not pay an employer debt when an employment cessation event occurs. For example under the flexible apportionment arrangement, an employer's pension liabilities can be apportioned to another employer participating in the pension scheme. Such arrangements are more often used where employers are associated with each other. For example, they are in the same group of companies.
- 7.5 However a Call for Evidence in 2015⁵ found that where participating employers are from unconnected businesses or organisations, in what are known as "non-associated multi-employer schemes" pensions schemes, it is less likely that they are able to take advantage of existing arrangements. This could be because they have no other employer (associated employer) to transfer the debt to, so cannot use one of the apportionment arrangements. As they are often small employers in the charitable or voluntary sector they may risk insolvency if they cannot afford to pay an employer debt triggered by an employment cessation event.
- 7.6 This instrument is intended to ensure that all types of employers in multi-employer schemes are given feasible opportunities to manage their employer debt liabilities when they experience an employment cessation event. This will minimise the associated costs and economic distress to business, whilst keeping the interests of pension scheme members sufficiently protected.
- 7.7 The deferred debt arrangement will enable an employer in a multi-employer pension scheme to defer the requirement to pay an employer debt on ceasing to employ an active scheme member. The arrangement will need the consent of the trustees who must be satisfied that the employer can continue to meet its obligations to the scheme and that the arrangement will not be of detriment to the scheme as a whole.
- 7.8 Once in place the deferred debt arrangement can continue for an indefinite period and during this time the deferred employer will retain all their previous responsibilities to the scheme and be treated as if they were the employer in relation to that scheme.
- 7.9 The instrument set out the various circumstances in which the deferred debt arrangement will come to an end. For example if the scheme itself winds up or the employer becomes insolvent. If the employer's ability to support the scheme is getting weaker the trustees can end the arrangement. The instrument lists such events and sets out what will happen about the employer debt in each circumstance.
- 7.10 This instrument makes changes to enable an employer in a "period of grace" to enter a deferred debt arrangement. The "period of grace" arrangement is used by employers who temporarily cease to employ an active member of a pension scheme. The employer debt does not trigger for a period of up to 36 months, providing the employer employs another active member within that time. These changes will allow an employer in a period of grace to defer the requirement to pay an employer debt indefinitely providing they meet the conditions of the deferred debt arrangement. They also increase the notification period that employers have to write to trustees to seek permission to use the period of grace from two to three months.

⁵ Section 75 Employer Debt in Non-Associated Multi-Employer Defined Benefit Schemes

- 7.11 The instrument clarifies what is meant by a receiving employer in existing provisions for one to one restructuring arrangements that are not treated as employment cessations events. The policy intention remains the same that where an organisation is undergoing restructuring but merely changing its status, all other things remaining the same, the ‘receiving employer’ could be the new legal status of the exiting employer. The changes made capture situations, for example, where an organisation is changing from an unincorporated charity to incorporated company.
- 7.12 This instrument also makes some consequential changes to the Occupational Pension Schemes (Scheme Funding) Regulations 2005 S.I.2005/3377⁶ as a result of the introduction of the deferred debt arrangement. Some minor technical and clarificatory amendments have been made to the Employer Debt Regulations.

Consolidation

- 7.13 Informal consolidated text of instruments is available to the public free of charge via ‘the National Archives’ website

8. Consultation outcome

- 8.1 A consultation was undertaken from 21 April to 18 May 2017⁷. There were 46 responses from pension schemes, employers, adviser firms and representative bodies. Respondents in the main welcomed the introduction of the deferred debt arrangement saying it would be of particular help to employers in non-associated multi-employer schemes in managing an employer debt following an employment cessation event. The Government’s response to the consultation is published at: <https://www.gov.uk/government/consultations/the-draft-occupational-pension-schemes-employer-debt-amendment-regulations-2017>
- 8.2 A number of issues were raised about how the deferred debt arrangement would work in practice. Several changes have been made to these Regulations as a result. The main points and changes made are as follows.
- 8.3 The draft instrument issued for consultation included the requirement for the “funding test” to be satisfied as a condition of entry into the deferred debt arrangement. The “funding test” is used in some of the existing arrangement to manage employer debt where the responsibility passes to other employers. The test evaluates whether the remaining employers in the scheme will be able to satisfactorily fund the scheme after this has happened. The majority of respondents said that the funding test was not appropriate for the deferred debt arrangement as the employer who enters into a deferred debt arrangement remains responsible for the funding of the scheme. The requirement for the funding test has been removed in these Regulations.
- 8.4 Respondents acknowledged that trustee or scheme manager consent was necessary for an employer to enter into a deferred debt arrangement but felt in practice this might be difficult as the trustees or scheme managers have a duty to protect the members of the pension scheme. An amendment has been made to introduce a further condition for entry into the deferred debt arrangement. This requires that trustees or managers of the scheme are satisfied that an employer’s relationship to the scheme is not likely to

⁶ <http://www.legislation.gov.uk/ukxi/2005/3377/contents/made>

⁷ <https://www.gov.uk/government/consultations/the-draft-occupational-pension-schemes-employer-debt-amendment-regulations-2017>

weaken materially within the period of 12 months of entering the deferred debt arrangement.

- 8.5 Where an employer wishes to end a deferred debt arrangement some respondents questioned the need for trustee consent, whilst others did not think the employer should be able to choose the date to trigger the employer debt. An amendment has been made to permit the ending of the arrangement by mutual agreement of the trustee and employer. This will ensure that scheme member interests are protected.
- 8.6 Respondents noted that the deferred debt arrangement should end when the scheme winds up or is about to enter the Pension Protection Fund. Amendments have been made to facilitate both situations.
- 8.7 Some respondents questioned whether the deferred debt arrangement should end if the employer restructures as that does not necessarily weaken their relationship with the scheme. An amendment has been made so that the arrangement will not come to an end where one to one restructuring takes place. In a one to one restructuring the obligations toward the pension scheme of one participating employer (known as the exiting employer) are taken over by another participating employer in the scheme (known as the receiving employer). No employer debt is payable as no employment cessation event occurs as a result of them. This could happen for example when one employer merges with another associated employer, or an unincorporated employer incorporates.
- 8.8 Respondents did not think an employer debt should be triggered for an employer participating in a deferred debt arrangement if the scheme became a frozen scheme. “Frozen schemes” are pension schemes where all new accrual of rights to pensions has ceased. An amendment has been made so that the deferred debt arrangement will end when the scheme becomes frozen but no employer debt will be triggered
- 8.9 Respondents felt that the proposed clarification of a receiving employer whilst being more prescriptive than the current definition more clearly reflected the nature of the restructuring being undertaken. The main use identified was the situation where a charity changes its legal form to a Charitable Incorporated Organisation where the provision would be helpful in not triggering an employer debt.

9. Guidance

- 9.1 To assist employers, trustees and advisers in using the deferred debt arrangement the Pensions Regulator is updating its “Multi-employer schemes and employer departures” guidance. The Regulator’s guidance is available to the general public on its website. .

10. Impact

- 10.1 There will be benefits to businesses, charities or voluntary bodies. An employer choosing to enter a deferred debt arrangement will not have to pay the employer debt in full up-front, which may result in reduced financial pressure and prevent it from facing economic distress. The estimated impact to business that is scored through the Business Impact Target is a saving of £8.7 million per annum.
- 10.2 There is no impact on the public sector.
- 10.3 An Impact Assessment is submitted with this memorandum and will be published alongside the Explanatory Memorandum on the legislation.gov.uk website.

11. Regulating small business

11.1 The legislation applies to activities that are undertaken by small businesses.

12. Monitoring & review

12.1 The instrument contains a requirement for the Secretary of State for Work and Pensions a duty to review the provisions for the new deferred debt arrangement in new regulation 6F of the Employer Debt Regulations, and set out the conclusions of each review in a published report,

12.2 The first report must be published no later than five years after this instrument comes into force and subsequently at intervals of not more than five years.

13. Contact

13.1 Mary Collins at the Department for Work and Pensions Telephone:02074497409 or email: mary.collins@dpw.gsi.gov.uk can answer any queries regarding the instrument.