

New Employer Debt Option

Amendments to the existing employer debt regulations will allow employers, in multi-employer defined benefit (DB) occupational pension schemes, to defer any requirement to pay an employer debt when they cease to employ their last active member (a deferred debt arrangement).

The Department for Work and Pensions has just issued its [response](#) to a consultation that took place in the spring of 2017. While a number of amendments have been made to the original proposals in the light of feedback from the industry, the government is to proceed with the underlying proposals.

Employers in multi-employer DB occupational pension schemes, who are ceasing to employ their last active member, or who have retained one or more active employees to avoid the consequences of the employer debt regulations, should consider whether a deferred debt arrangement now offers them a better route forward.

In this issue: [Background](#) | [Deferred Debt Arrangement](#) | [Periods of Grace](#) | [Comment](#)

Background

Where an employer (the deferred employer) in a multi-employer DB occupational pension scheme ceases to employ its last active member in the scheme, at a time when other employers still employ active members, then a debt known as a “section 75 debt” can be payable by the employer. The debt can be significant and arises in respect of benefits accrued whilst in the service of the deferred employer. It covers both current and former employees plus a proportion of any “orphan” members no longer allocated to a specific employer in the pension scheme.

There are already in existence a number of ways that the immediate payment of the debt can be delayed or passed on to another employer in the pension scheme. Each of these options has their restrictions and limitations.

Deferred Debt Arrangement

Amending regulations, coming into force on 6 April 2018, will allow deferred employers a new option to defer the requirement to pay an employer debt subject to them continuing to retain all their previous responsibilities under the pension scheme.

Thus deferred employers in a deferred debt arrangement will still be responsible for scheme funding and may be required to make deficit recovery payments where shortfalls are identified by regular actuarial valuations.

Entering a deferred debt arrangement

Either, an employer cessation event must have occurred before a deferred debt arrangement can be entered into, or one would have occurred but for a period of grace being entered into. (Periods of grace are covered below.)

Deferred employers wishing to use this option must first obtain the written consent of the trustees. In considering a request from an employer the trustees must act in the best interests of all members of the pension scheme and thus, even if the conditions below are met, consent will not be automatic.

Before giving their consent the trustees must be satisfied that the deferred employer's covenant to the scheme is not likely to weaken materially within the period of 12 months beginning with the date on which the trustees expect the deferred debt arrangement to take effect. Thus an assessment of the deferred employer's covenant will have to be undertaken as part of the process.

The pension scheme must not be in an assessment period with the Pension Protection Fund or being wound up. Trustees must also be satisfied the pension scheme is unlikely to enter an assessment period within the period of 12 months beginning with the date on which the trustees expect the deferred debt arrangement to take effect.

Other workarounds, such as a flexible apportionment arrangement, remain open to the deferred employer during the period of deferment.

Ending a deferred debt arrangement

The amending regulations provide that a deferred debt arrangement will continue until the first date on which one of a number of events has occurred. The table below (taken from a table in the DWP's response to the consultation) lists those events and the consequences of the event happening.

Events that will end the deferred debt arrangement	Consequences
The deferred employer employs a person who is an active member of the scheme.	The deferred employer will revert to being an employer in relation to the scheme. There will be no employment cessation event so no employer debt will be triggered.
The deferred employer and the trustees reach a mutual agreement to end the arrangement.	The date of the agreement will be the date of the employment cessation event. An employer debt may be triggered if the scheme is underfunded and will be calculated by reference to this date.
A relevant event occurs in relation to the deferred employer i.e. they become insolvent or are treated as being insolvent	This relevant event may trigger an employer debt if the scheme is underfunded on a section 75 basis at the time of the event and any employer debt due will be calculated by reference to this date.
All employers in the scheme have undergone a relevant event or become deferred employers.	At this date an employment cessation event will be deemed to take place for the deferred employer and any employer debt due may be calculated by reference to this date.

Events that will end the deferred debt arrangement	Consequences
The scheme commences winding up.	The deferred debt arrangement will come to an end but there will be no employment cessation event. The calculation of the employer debt can be triggered at any time during the winding-up process.
The deferred employer restructures unless that restructuring follows the provision for a one-to-one restructuring in 6ZB or 6ZC of the Occupational Pension Schemes (Employer Debt) Regulations 2005 (as amended).	<p>The deferred debt arrangement will end on the date restructuring takes place (unless there is one-to-one restructuring and an employment cessation event will be deemed to have taken place. An employer debt may be triggered with reference to this date.</p> <p>In a one-to-one restructuring the deferred debt arrangement will come to an end where the receiving employer is a participating employer in the scheme. There will be no employment cessation event so no employer debt will be triggered.</p> <p>Where the deferred employer restructures in a way that its obligations to the scheme are the same the deferred debt arrangement will remain in place providing the employer's new structure continues to meet the conditions of the arrangement.</p>
A freezing event occurs.	The deferred debt arrangement will come to an end and the deferred employer will become a former employer. No employer debt will be triggered.
<p>The trustees of the scheme serve notice that the deferred debt arrangement has come to end on the basis that</p> <ul style="list-style-type: none"> • The deferred employer has failed to comply materially with its duties under the Scheme Funding Regulations • The deferred employer's covenant with the scheme is likely to weaken materially in the next twelve months; or • The deferred employer has failed to materially comply with its duties to disclose information under the 1996 Scheme Administration Regulations. 	The date of that notice will be treated as an employment cessation event in relation to the deferred employer. An employer debt may be triggered and will be calculated by reference to this date.

Periods of Grace

An employer can effectively defer the crystallisation of a section 75 debt by providing a period of grace notice to the trustees stating that it intends to employ an active member of the pension scheme in the next 36 months (if the trustees allow a period longer than 12 months). The amending regulations increase, from two months to three months, the time limit for an employer to serve a period of grace notice.

The deferred debt arrangement is available to employers who have entered a period of grace.

Comment

Since the introduction of the legislation dealing with employer debt under the Pensions Act 1995 there has been almost yearly tinkering with the legislation by successive governments. This latest revision to the regulations is a logical and sensible one balancing flexibility with the need to protect scheme funding. It will be of particular value to non-associated employers of a multi-employer DB occupational pension scheme. Non-associated employers have struggled to use the existing work arounds for deferring payment of an employer debt, with other employers reluctant to take on an apportioned debt or apportioned member liabilities.

Trustees will need to conduct a covenant assessment on the deferred employer before agreeing to a deferred debt arrangement, and will have to continually monitor the covenant throughout the life of the arrangement, as they are under a duty to terminate the arrangement if at any stage they conclude the deferred employer's covenant is likely to weaken materially in the following 12 month period.

The provision, allowing trustees to end a deferred debt arrangement based on a deteriorating employer covenant, may make deferred debt arrangements unattractive to employers. Employers may conclude they are effectively handing over control on when to trigger a section 75 debt to trustees, who may see it as a bargaining tool. It is also hard to see why an employer with no active scheme members should be treated differently to an employer with one active member (where the trustees would have no power to trigger a debt).

Authors

Gary Crockford, Head of the Knowledge Resource Centre
Nikki Williams, Senior Technical Consultant

Produced by the Knowledge Resource Centre

The Knowledge Resource Centre is responsible for national multi-practice compliance consulting, analysis and publications, government relations, research, surveys, training, and knowledge management. For more information, please contact your consultant or call us on 0800 066 5433.

This publication is for information only and does not constitute legal advice; consult with legal, tax and other advisors before applying this information to your specific situation.

Conduent HR Services is a trading name in the UK for Buck Consultants Limited (registered number 1615055), Buck Consultants (Administration & Investment) Limited (registered number 1034719), and Buck Consultants (Healthcare) Limited (registered number 172919), which are private limited liability companies registered in England and Wales. All have their registered office at 160 Queen Victoria Street, London EC4V 4AN. Buck Consultants (Administration & Investment) Limited and Buck Consultants (Healthcare) Limited are authorised and regulated by the Financial Conduct Authority.

©2018 Conduent Business Services, LLC. All rights reserved. Conduent, Conduent Agile Star, FYI® and For Your Information® are trademarks of Conduent Business Services, LLC in the United States and/or other countries.