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The Pensions Regulator and moral hazard provisions

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Moral hazard – a busy area?

- Very few cases despite age of legislation – Pensions Act 2004
- Uncertainty as to ambit remains
- The view taken by tPR of the ambit of its powers may not be correct – *Bonas*
- Where is the actuary likely to become involved?



Moral hazard provisions – summary

- Section 38 – contribution notice – pay a specified sum
- Connected and associated
- Looking for act or series of acts – main purpose
 - To prevent the recovery of sums due or might become due section 75 PA95
 - Material detriment
- Reasonable test



Moral hazard provisions – summary

- Section 43 – financial support direction – 3 stages
 - FSD that target provide financial support – section 43
 - tPR to determine if the financial support set in place is reasonable – sec 45
 - If not, tPR can seek a section 47 contribution notice requiring the target to provide financial support in a specified sum
- Connected and associated
- Employer test - either service company or insufficiently resourced
- Reasonableness test
- Objective in approach



Common aspects

- Reserved regulatory powers – DP role then UT
- Trustees /PPF are almost undoubtedly directly affected parties – involved in proceedings
- Trustees will face large requests for documents by tPR in its investigation
- Trustees generally have taken an active role – obtain expert witness reports then relied upon by tPR, obtain witness statements



Cases

- No case to date gone for final full hearing before Upper Tribunal – first – Boxclever (2018)
- Sea Con, Lehman Brothers, Nortel Networks, Bonas, Carrington, Desmond settled or terminated after DP determination or before full UT hearing
- Others had warning notices issued and not reached the DP hearing settled or still live



Unresolved issues in moral hazard

- Sums sought under 38 and section 47 need to be reasonable
- Causation – how does it operate?
 - Is there liability for entire section 75 ‘debt’ or just a loss attributable to targets?
 - Is it possible to run a defence that liability must be confined to loss caused – ie – if the employer was in no position to discharge the section 75, then how can the target be liable?



Possible involvement of actuaries

- Acting as scheme actuary – section 75 estimate
- Expert evidence – examples
 - insufficiently resourced – look at a certain date in time – valuation of pension liabilities
 - Strength and otherwise of covenant by reason of acts (material detriment)
- Negotiations and potential settlement



Issues facing actuaries

- Decisions made, actions taken in the past can be under scrutiny – tPR can trawl through extensive history
 - Reasonableness test is not time restricted
 - Sec 38 CNs – 6 years from act
 - Section 43 – 2 years
- Can actuaries be pursued under section 38?



The future of moral hazard

- Since 2005, approximately 14 moral hazard cases with issued warning notice – no public listing !
- Since 2005, 29 regulated apportionment agreements approved by tPR
- Where is the future ?



Regulated apportionment agreements

- One of options for dealing with section 75 debt – Employer Debt Regulations
- RAAs - require approval of tPR and ‘no objection’ from PPF
- Trustees believe a reasonable likelihood of entering PPF assessment period in next 12 months (or in assessment)



Aspects of RAAs

- RAAs emerging as major restructuring tools
- Not restricted to cases where multi employers
- Subject to scheme rules, Newco created and becomes an employer
- Newco's participation enables original employer company to restructure without the section 75 liabilities



Role of tPR

- Regulator must consider arrangement reasonable
- tPR Statement 12/8/2010
- Treated like a clearance type application
- Not a reserved regulatory power



tPR Statement August 2010

- Relevant circumstances may include:-
- Whether insolvency of employer would otherwise be inevitable – other solutions?
- Whether scheme might receive more from an insolvency
- Whether a better outcome might otherwise be attained for the scheme by other means (including through the use of tPT's powers where relevant)
- Position of rest of employer group
- Outcome of proposals for other creditors



tPR Statement and subsequent reports

- *‘RAAs are extremely uncommon; the expectation when they were introduced into legislation was that they would be used rarely, which has proved to be the case ‘ (August 2010)*
- In 2009 – 4, 2010 – 5, 2013 – 7, 2014 – 5 and 2017 – 2
- Work and Pensions' Committee report (2017) viewed favourably RAAs – green paper



Assessment of moral hazard ‘better outcome’ in RAAs

- Very little assistance in how this has been assessed by tPR – no case law!
- Section 89 reports – parent company – ‘no legal obligation’ - *but this is always the case in any moral hazard case – it is the exact reason why moral hazard exists – to create a legal obligation where there is none*
- Length of investigation carried out – the ‘due diligence’ for RAAS – compare to time taken to date in assessment of moral hazard cases....



Role of actuaries in RAAs

- As with moral hazard cases
- More assistance needed within a shorter period of time ?
- Trustees will need expert assistance to assess the position of
 - The estimated deficiency
 - Assessment of potential moral hazard outcome
 - Position of other creditors
 - Viability of company to discharge pension obligations in future



The more active tPR

- tPR clearly keen to demonstrate that it is using its powers
- Section 231 warning notice issued
- Reserved regulatory power – will be a hearing before DP – need case to proceed to full hearing before DP and UT to enable it to provide assistance for future cases
- Expert evidence will be key



Potential issues on section 231

- Issues relating to methods and assumptions
- Issues relating to affordability – how do you deal with historic financial support provided by a parent with no legal obligation ?
- Duration of recovery plan?
- Sec5(10(cza))' ...to minimise any adverse impact on sustainable growth of an employer ‘



Raquel Agnello QC



Raquel is the leading Silk in the area of pensions and insolvency. She has led on many high profile cases on behalf of the Pensions Regulator (and won all of them), including on Nortel and Lehman in the Supreme Court. She has acted for trustees in cases involving the interpretation of the moral hazard provisions and whether the section 75 debt is assignable. Her wealth of experience in this area makes her a favourite to advise clients facing investigations and/or action by the Pensions Regulator against them, as well as advising on corporate restructurings.

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