

## **Church of England Pensions Board**

### **Church of England Funded Pensions Scheme (CEFPS)**

#### **Section 75 of the Pensions Act 1995**

##### **Introduction**

1. When an “employment cessation event” occurs in a multi-employer pension scheme, a debt arises under Section 75 of the Pensions Act 1995. Various changes to the provisions of this Section have been made over the years. Essentially, however, the departing employer becomes liable for a debt based on the cost of buying out that employer’s proportionate share of the total liabilities of the scheme with an insurance company. The debt is therefore usually significantly greater than any deficit arising on an ongoing funding basis.

##### **Section 75 Debt**

2. A Section 75 debt arises in three circumstances:
  - The employer concerned becomes insolvent; or
  - The scheme is wound up; or
  - The employer ceases to employ persons who are active members of the scheme at a time when at least one other person continues to do so.
3. In this context we have been advised that the reference to “employer” also includes a “Responsible Body” regardless of whether members are strictly employees.
4. As a result of amendments made by the Pensions Act 2004, an employer’s Section 75 debt is calculated as its proportionate share of the scheme deficit on a “buy out” basis (ie calculated by reference to the cost of securing benefits by purchase of an annuity from an insurance company). An employer’s proportionate share is:
  - Liabilities in respect of members who it has employed; and
  - A share of liabilities relating to members employed by employers no longer participating in the scheme (often known as “orphan” liabilities).
5. The calculation is complex and expensive and, like many schemes, we do not hold the data to carry it out wholly accurately.
6. The legislation means that you, as a Responsible Body, are liable for Section 75 debt if you cease to employ active members (although there are some limited circumstances where a debt would not arise). The sums involved are potentially substantial.

## **Why is this an issue for this scheme?**

7. We are advised that this legislation is of concern to many employers, both those of a commercial nature and otherwise. The issue is, however, of particular concern to the CEFPS. The scheme includes (broadly) two categories of Responsible Bodies. Firstly there are a number of Responsible Bodies which, in practice, participate in the scheme on a permanent basis. This category includes Diocesan Boards of Finance, the Church Commissioners, the Church Army, the Archbishops' Council, Westminster Abbey and St George's Chapel, Windsor. These Responsible Bodies cover the majority of members of the Scheme, currently 8147 out of a total active membership of 8380.
8. Secondly, there is a large number (in excess of 130) of much smaller Responsible Bodies, usually with fewer than 10 members, which include theological colleges, charities and other institutions such as hospices, university colleges and schools which have a chaplain. These Responsible Bodies generally have only a very small number of active members at any time (typically only one or two) and periodically will cease to have any active members (without there necessarily being any certainty as to whether they will re-commence employing active members in future).
9. The reason for allowing this second category of Responsible Bodies to participate in the scheme is to ensure that the clergy who move out of mainstream ministry for a period continue to benefit from scheme membership. However, the existence of the Section 75 debt means that the "price" for this continued scheme membership for the Responsible Body concerned is potentially high. There is therefore a real concern that, if no action were taken, these Responsible Bodies may be unable to continue to participate in the scheme, to the general detriment of the affected clergy and the Church as a whole. There is a further concern that smaller organisations which currently participate in the scheme could be severely affected financially to the extent that they become insolvent as a result of their last / only member leaving, retiring or dying.
10. For technical reasons, the Board has been advised that it cannot simply waive any Section 75 debt which falls due.
11. In light of these concerns, the Board sought advice from its professional advisers and, having obtained agreement from all current Responsible Bodies, amended the scheme rules in 2009 and again in 2012, with the consent of General Synod, to provide alternative arrangements as permitted by the legislation.

## **Current position**

12. The legislation allows schemes to adopt alternative approaches for handling Section 75 debts. One such alternative is by making use of what is called a “flexible apportionment arrangement” (FAA). This allows the amount of the debt to be modified so that it is less than the employer’s liability share, and for the remaining liabilities to be allocated to another employer or employers participating in the scheme. The Rules of the CEFPS have been amended to allow for FAAs or any other method to modify an amount that might otherwise be treated as a debt, subject compliance with relevant legislation.
13. In the CEFPS, participating employers (Responsible Bodies) have been designated as either “major” or “minor” bodies (the major bodies being those set out in para 7 above, ie mainly the dioceses and the Church Commissioners, while the minor bodies are the smaller participating organisations described in para 8 above). When a minor body ceases to have active members it is not required to pay a debt. Instead its liabilities are apportioned to the major bodies. This arrangement is a form of FAA and is set out in the Rules governing the CEFPS and operated in accordance with the Board’s policy set from time to time.
14. In general, the aim of the FAA is to apportion residual liabilities. This means that, in the case of the CEFPS, there is no need to calculate the actual amount of the debt for each departing employer. Carrying out a full calculation in each case would entail considerable cost in actuarial fees and mean that CEFPS would not be able to continue to accommodate the smaller Responsible Bodies.

## **All Responsible Bodies must agree**

15. The use of the FAA requires the specific agreement of each “Responsible Body” participating in the scheme to take on the relevant liabilities of the “minor” Responsible Bodies. All Responsible Bodies currently participating in the CEFPS have consented to this arrangement.
16. Therefore, as a condition of participating in the CEFPS new Responsible Bodies are required to consent by completing the participation agreement.
17. The mechanism for dealing with individual cases will be set out in a policy statement from the Board. The current policy is attached as an Appendix. This sets out how the apportionment arrangements will be applied in the majority of cases (involving Minor Responsible Bodies); other cases will be dealt with in the most appropriate manner depending on circumstances.

### **What are the consequences if a Responsible Body withholds its agreement?**

18. If any major Responsible Body withholds its consent to these arrangements then it would mean that, on each and every “employer cessation event” a full actuarial assessment would need to be carried out to calculate the leaving employer’s Section 75 debt. That debt would need to be paid by the departing employer. The cost of carrying out such assessments would be prohibitive. Given the large number of minor Responsible Bodies, employer cessation events are a frequent occurrence. The likely result is that no new minor Responsible Bodies could be admitted to the scheme and existing minor Responsible Bodies may have to cease participation. The Board would be under a legal obligation to pursue any Responsible Body that ceased participation for the Section 75 debt. This could result in such bodies being forced into insolvency.

### **Conclusion**

19. The Board strongly believes that it is in the best interests of the clergy and the Church as a whole that the minor Responsible Bodies continue to be able to participate in the scheme so that clergy can benefit from continuity of pension provision. Without this arrangement this may not be possible.

20. The Board therefore requires all new Responsible Bodies to give their agreement to the arrangement in addition to the consents already obtain from current Responsible Bodies.

**May 2014**

## Policy Statement

### Section 75 Debts

This statement sets out the Policy of the Board to manage debts which may arise from Responsible Bodies under Section 75 or 75A of the Pensions Act 1995 (“**S75 Debts**”).

- 1** The Board has designated each existing Responsible Body as either a “Major Responsible Body” (“**Major RB**”) or a “Minor Responsible Body” (“**Minor RB**”). Any new entity admitted as a Responsible Body will be designated as a Major RB or a Minor RB on admission.
- 2** The Board’s policy is that Minor RBs should not be exposed to S75 Debts as this would be likely in practice to make their continued participation in the Scheme difficult.
- 3** If an event occurs which would otherwise give rise to a S75 Debt from a Minor RB, the Board intends the following:
  - (a) The Board will enter into an arrangement which is a “flexible apportionment arrangement” (“**FAA**”) in consequence of which all liabilities of the relevant Minor RB will be transferred to one or more Major RBs as described at (5) below.
  - (b) The Board does not expect to levy any charge on the relevant Minor RB in connection with the FAA but reserves the right to do so (ie to require the Minor RB to meet part or all of the S75 Debt) in exceptional circumstances.
  - (c) However, the Board can only enter into an FAA if certain conditions are met at the relevant time. In particular:
    - The relevant Minor RB stops employing (or being responsible for) active members of the Scheme and does not give the Trustees a “period of grace” notice under regulation 6A of the Occupational Pension Schemes (Employer Debt) Regulations 2005;
    - The Board must be satisfied at that time that the “funding test” set out in legislation will be met;
    - the Scheme is not in an assessment period (for the purposes of entry to the Pension Protection Fund) or being wound up at that time;
    - the Trustees are satisfied that an assessment period is unlikely to begin in relation to the Scheme within the next 12 months;
    - the consent of all Responsible Bodies affected by the FAA is obtained (see further section (7) below).

The Board will consider at any time when a S75 Debt would otherwise arise from a Minor RB whether these tests are met and, only if they are, will the Board enter into an FAA which has the effect described above. For the avoidance of doubt, if these conditions are not met at the relevant time, the S75 Debt due from the Minor RB will be calculated as its “liability share” in accordance with legislation.

- 4** Liabilities will be apportioned as follows:
  - 4.1** Where a Member leaves service with a Minor RB and immediately enters service with a Major RB, the liabilities in respect of that member will be apportioned to the relevant Major RBS.
  - 4.2** In all other case, the liabilities which would otherwise have been attributable to the Minor RB will be apportioned on a pro rata basis (by reference to their other liabilities to the Scheme) to all the major RBs. Any S75 Debt which becomes payable from a Major RB will be modified accordingly.
- 5** In the event that it is held by a competent Court or regulatory body that a S75 Debt arises from a person which is not a Responsible Body, paragraph 4.2 will be applied as if that person were a Minor RB.
- 6** It is a condition of an FAA that consent is obtained from both the entity whose debt is apportioned and the person to whom it is apportioned. In effect, this requires the consent of all Responsible Bodies. The Board will not implement the arrangements described in this Policy until such consent has been obtained.
- 7** The Board recognises that circumstances may arise where it is appropriate to enter into alternative arrangements for the management of S75 Debt. In particular, where two or more Responsible Bodies are merged, or where one Responsible Body takes over the business of another, it may be appropriate to enter into alternative arrangements so that the merged/ new/ replacement Responsible Body undertakes the liabilities of the outgoing Responsible Body (Bodies). The Board will consider proposals for such arrangements on a case by case basis. The Board will only enter into such arrangements if all applicable statutory conditions are met and must take account of the effect (if any) that such arrangements would have on other Responsible Bodies.
- 8** The Board will record the terms of each arrangement which it enters into for the purposes of managing S75 Debt (whether in line with Clauses 3 to 6 of this Policy or otherwise) in its minutes or in a formal agreement with the relevant Responsible Bodies.
- 9** The Board may vary its Policy at any time.