Baker McKenzie.

Pensions Update

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In This Issue

Pensions Disputes News

Regulator to prosecute Dominic Chappell

The Regulator has announced that it has brought prosecution proceedings against Dominic Chappell for failing to provide information and documents it requested under Section 72 of the Pensions Act 2004 during its investigation into the sale of BHS. The notices requiring information were issued to Mr Chappell on 26 April 2016, 13 May 2016 and 20 February 2017.

Mr Chappell was the director and majority shareholder of Retail Acquisitions Ltd at the time that the company purchased BHS.

The Regulator's press release can be found here.

Tata Steel: Regulated Apportionment Arrangement

On 11 August it was announced that Tata Steel UK had signed a Regulated Apportionment Arrangement ("RAA") with the Trustee of the British Steel Pension Scheme ("BSPS"). The effect will be to separate the BSPS and its potential statutory debt from the Tata Steel sponsoring companies. The Pension Protection Fund ("PPF") has confirmed that it has no objection to the RAA and the Regulator is expected to approve the RAA following the end of the relevant waiting period.

The terms of the RAA provide for Tata Steel UK to pay £550m into the BSPS (which the Regulator has commented is significantly more than would have been available on insolvency). The BSPS will also be provided with a 33% equity stake in Tata Steel UK.The BSPS will then enter a PPF assessment

period. A new scheme is to be established, sponsored by Tata Steel UK, into which BSPS members may transfer if certain qualifying conditions are met as to the new scheme's funding level and size. The new scheme would provide lower increases in payment for pensioners and revaluation for deferred members but has the potential to deliver benefits at higher than PPF levels.

The Regulator has commented that "*it is willing to work closely and constructively with employers who face real challenges in meeting their pension obligations due to difficult trading conditions*" and that "*its focus will always be on protecting members and the PPF*". This RAA will be the second that it has approved this year and the third in the last two years (following RAAs in respect of Hoover Ltd in June 2017 and Halcrow Group Limited in July 2016). It further develops the structure implemented by Baker McKenzie and approved by the Regulator in 2012 in respect of British Midland Airways.

Nevertheless the Regulator's willingness to consider such proposals can potentially offer a lifetime to distressed businesses and scheme members.

The Regulator has stressed that it does not agree to these types of arrangements lightly and that strict criteria must be met, including the condition that the employer is expected to become insolvent within the next 12 months.

New TPR definition of professional trustee

Following a consultation which ended in May, the Regulator has published a new policy setting out its definition of a "professional trustee", as well as a new monetary penalties policy. Whether a trustee is a "professional trustee" is a factor which the Regulator takes into account in determining any monetary penalties which it may impose under its statutory powers. As part of the scheme return, trustees are also require to tell the Regulator if any trustees are professional trustees.

The new policy document notes that the Regulator expects higher standards from "professional trustees" and so will normally apply higher penalties for those meeting the professional trustee description who fail to meet their duties. The Regulator considers a professional trustee to "*include any person, whether or not incorporated, who acts as a trustee of the scheme in the course of the business of being a trustee*". The Regulator would normally consider a person to be acting in the course of the business of being a trustee where the person "*represents or promotes themselves to the trustee or sponsors of one or more unrelated schemes… as having expertise in trustee matters generally (rather than just in certain areas), whether for remuneration or otherwise*".

The policy also sets out those types of trustee which the Regulator would not expect to meet the definition and notes that it will not automatically consider a trustee who is receiving remuneration for their trustee duties to be a professional trustee. It sets out a number of examples to illustrate where the definition may be met. The policy can be viewed here.

New DWP Guidance on implementing cap on early exit charge

New requirements will be introduced from 1 October 2017 to impose restrictions on early exit charges for scheme members aged 55 and over and who are eligible to access the pension freedoms.

The early exit charge restrictions apply when a member who has reached the normal minimum pension age takes, converts or transfers their pension benefits before their expected retirement age. Early exit charges are prohibited in respect of members who join a scheme after 1 October 2017 and are subject to a cap for members who joined before that date. The cap is the lower of 1% of the value of the member's benefits taken, converted or transferred and the amount provided under the scheme rules as at 1 October 2017. The relevant regulations provide that the value of the member's benefits are to be calculated in line with the statutory guidance. The DWP has now published that guidance.

The guidance confirms that market value adjustments (MVAs) or terminal bonuses (sometimes applied to "with profits" funds) are not prohibited by the early exit charge restrictions and so any

MVA or terminal bonuses should be applied before calculating the value of a member's pot. Other exit charges derived from scheme investments in "with profits" funds will still be captured by the requirements of the cap.

The new guidance can be viewed here.

New corporate criminal tax evasion offence coming into force from 30 September 2017

A new corporate criminal offence of failing to prevent the facilitation of tax evasion, which is modelled on the UK Bribery Act, will come into force from 30 September 2017. Corporate trustees will be within scope of the new offence in the same way as any other corporate or partnership.

In a pensions context, the offence will apply where a pension scheme's employer or corporate trustee (or any of their associates):

- is knowingly concerned in, or takes steps with a view to, the fraudulent evasion of tax by another person;
- aids, abets, counsels or procures the commission of a UK tax evasion offence or foreign tax offence, or
- is involved in or part of the commission of an offence consisting of being knowingly concerned in, or taking steps with a view to, the fraudulent evasion of tax.

Associate is widely defined and includes an employees, as well as agents or any other person who provides services for or on behalf of the employer or corporate trustee.

Further detail about the offence can be found here.

It is a defence to have in place such prevention procedures as are reasonable in all the circumstances.

From a pensions tax perspective, it is relatively unlikely that potential infringement of the new legislation will occur. However, an area in which this new offence could potentially impact is in connection with any aggressive tax avoidance arrangements put in place (by either the employer or the member), for example, the aggressive use of arrangements to avoid breaching annual allowance or lifetime allowance limits. It is also conceivable that there could be circumstances in which the transfer by a corporate trustee to a pensions liberation vehicle which is being used to evade tax could potentially be caught. The legitimate use of statutory tax reliefs by both employers and trustees (e.g. tax relief on pension contributions and investment returns) should not give rise to any issues.

Employers and corporate trustees should take note of the new offence and remain vigilant to any potential cheating or tax evasion and, if they are concerned, should take steps now to review the position and put in place procedures to provide the strongest possible defence.

If you have any further questions about how you may be impacted by the new offence, please contact a member of the pensions team.

Pensions Disputes News

Benefit Changes - IBM succeeds on appeal - *IBM United Kingdom Holdings Ltd and others v Stuart Dalgleish and others* [2017] EWCA Civ 1212

This significant case was first heard in the High Court in 2014. In a weighty judgment, Mr Justice

Warren held that IBM had breached both its implied duty of good faith (the so-called *Imperial* duty), and its contractual duty of trust and confidence when making changes to its UK defined benefit pension plans (the "Plans"). The changes (under the heading "Project Waltz" in 2011) had three strands: (i) the closure of the Plans to future accrual (ii) the introduction of a new less favourable early retirement policy and (iii) the prevention of future salary increases from becoming pensionable.

The High Court found the changes were invalid because IBM had breached the relevant duties to members of the Plans by behaving "irrationally or perversely" when acting contrary to members' "reasonable expectations" and it did not consult meaningfully with members. Central to the High Court's findings was the importance of members' "reasonable expectations" as to continued benefit provision under the Plans, which had been engendered by statements made in relation to earlier benefit change exercises in 2005 and 2006. The effect was that IBM was faced with unwinding much of Project Waltz. IBM appealed against the High Court's decision.

The Court of Appeal has reversed the High Court's decision on all the material issues. Fundamentally, the Court of Appeal disagreed with the status accorded to members' "reasonable expectations" by the High Court. Although the Court of Appeal did not dismiss entirely the possibility that "reasonable expectations" could be relevant, they would need to meet minimum conditions of clarity and certainty. It said that the High Court had proceeded (wrongly) on that basis that, once a "reasonable expectation" was established, in implementing changes which would disappoint those expectations, the employer had to show that there was no other course open to it. That, in the Court of Appeal's view, is not the correct legal test. The correct test is whether the employer has acted in an irrational manner (i.e. reached a decision which no rational or reasonable decision-maker could have reached). The "reasonable expectations" of members may well be a relevant factor for a rational employer to consider but they should not be given greater weight than other relevant factors. As a result the Court of Appeal found that there had been no breach of the *Imperial* duty in relation to the Project Waltz changes and, on that basis, the changes were allowed to stand.

The High Court's finding that, in failing to properly consult on the Project Waltz changes, IBM had breached it contractual duty to members (and its statutory duty under the consultation regulations) was not challenged on appeal. However, the Court of Appeal refused to grant an injunction restraining IBM from implementing the changes without rerunning the consultation. It said that an injunction would "*change the position of IBM and of the members…far too radically*". The Plan members will, in principle, be able to claim damages for breach of the contractual duty in relation to conduct of the consultation but that may present a number of difficulties (not least being able to show a causal link between the failure properly to consult and any loss suffered by the relevant member).

The original High Court decision gave rise to a number of concerns that benefit change exercises could be open to greater risk of challenge (particularly where they followed earlier exercises in which statements may have been made regarding the sustainability of future DB pension provision). The Court of Appeal's decision, overturning much of what the High Court said, will therefore bring some comfort to those employers who may have been concerned about current or future exercises. However, it is still the case that, when looking at making changes, employers should communicate carefully with members and trustees, present an appropriate business case and, where relevant, consider any "reasonable expectations" of Plan members as a relevant factor.

It is understood that the decision will not be appealed to the Supreme Court.

Validity of pensionable pay caps - *Bradbury v BBC* [2017] EWCA Civ 1144

This decision of the Court of Appeal will prove interesting for any employers considering the imposition of a pensionable pay salary cap. Mr. Bradbury was a member of the final salary “New Benefits Section” of the BBC Pension Scheme (the "Scheme"), which was significantly in deficit. In an attempt to reduce this deficit, the BBC introduced a 1% pensionable pay cap for active members.

The cap was introduced through a contract (as opposed to amending the Scheme Rules directly). When offered a pay rise, members were informed that the pay rise was conditional upon the acceptance of pensionable pay being limited to an increase of 1%. If members chose not to accept the cap, they would receive no pay rise. Alternatively they could choose to join the new career average section of the Scheme with no cap or join an entirely separate defined contribution scheme.

In this long-running case, Mr Bradbury has raised a number of complaints before the Pensions Ombudsman and High Court challenging the validity of the pensionable salary cap exercise. The Court of Appeal agreed with the BBC on all the relevant issues:

- It found that the BBC had the power under the Scheme rules to determine what proportion of any future pay rise was pensionable (this finding was based on the specific wording of the Scheme and so was case-specific). This was a departure from the finding of the High Court, which held that the rules did not confer such a power. The Court also found that the Cap did not breach section 91 of the Pensions Act 1995, which only protected the accrued pension, since Mr Bradbury had no right to future increases in salary (or pensionable salary).

- Mr. Bradbury argued that, through the process by which the BBC had introduced the cap, it had breached the contractual duty of trust and confidence which exists between and employer and its employees. The Court of Appeal disagreed, noting that the test for a breach of duty was one of "irrationality or perversity".

When assessing whether the BBC breached the duty of trust and confidence, the court gave particular consideration to the financial difficulties faced by the BBC, and the need for the BBC to act quickly to improve its position. This pragmatic, though perhaps unsurprising, analysis will be welcomed by employers considering these types of benefit changes to manage the costs of their DB schemes.

Can advantageous treatment still lead to unlawful discrimination? - *Williams v The Trustees of the Swansea University Pension and Assurance Scheme and another* [2017] EWCA Civ 1008

The Court of Appeal has considered the question of whether a disabled pension scheme member who receives an enhanced pension on ill health early retirement can nevertheless claim to have been treated unfavourably on the basis of their disability. The claim was made by a disabled member of the Swansea University Pension and Assurance Scheme (the "Scheme").

The Scheme rules required the pension for a part time worker (including an enhanced pension on ill health) to be calculated by reference to a full time equivalent salary but with a reduction to pensionable service to reflect the part time working arrangement. The member argued that, if he had been suffering from a disability which entitled him to retire immediately from full time work, as opposed one which led to him transitioning to part time working before taking his pension, he would have received a higher enhanced pension.

The member had succeeded at the Employment Tribunal, although the Employment Appeal Tribunal had dismissed the claim. The member then appealed to the Court of Appeal.

The Court of Appeal said that the critical question was whether treatment which confers advantages on a disabled person, but would have conferred greater advantages had his disability arisen more suddenly, amounts to "unfavourable treatment" under the Equality Act 2010. The Court held that it did not and dismissed the member's appeal. The Court considered the example of an employee who had requested and been granted part time work because of a disability. It cannot have been Parliament's intention in passing the legislation, the Court said, for that employee then to claim that the part-time salary was unfavourable treatment or (similarly) claim an entitlement to the same pension he would have received if he had worked full time.

Contact us

If you wish to discuss any of these issues further, please contact your usual Baker McKenzie lawyer.

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