

The Actuarial Profession
making financial sense of the future

Actuaries and the Law Seminar
Michael Hayles



The employer's perspective

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Agenda

- Who is the “employer”?
- Employer’s role
- Duty of good faith
- Duties owed by the trustees to the employer
- Key statutory employer obligations
- Defences to “Moral Hazard”

Who is the “employer”?

- Which legal entity is the “employer”?
- There can be a difference between:
 - the actual or “statutory” employer
 - a “TD&R” or “contractual” (principal) employer
- tPR guidance “*Identifying your statutory employer*” (July 2011)

Who is the “employer”?

- Organising “statutory pension liability” with a group:
 - creation of “employer” through employment of an active member
 - employment (albeit limited) should not be a “sham”
 - apportionment (with trustee agreement)
 - orphan liabilities

Who is the “employer”?

- Separation of business from statutory liability:
 - transfer of business (TUPE transfer) (NB: appropriate value paid for “business”)
 - apportionment (subject to revision)
- “Moral hazard”

Who is the “employer”?

- Consider the “statutory employer”:
 - a substitution of principal employer
 - a service company arrangement
- Consider scheme funding:
 - whose covenant are we testing?
 - who should sign the schedule of contributions?

Employer's roles (per tPR)

- tPR guidance (non-exhaustive):
 - make employer contributions and deduct member contributions
 - provide information to trustees
 - provide information and support to employees
 - work with tPR

Employer's roles

- BUT Employer does have a self interest:
 - design of benefit package
 - liability management (employers should operate PIE and ECETV exercises with care)

Duties/powers arising from scheme governing documentation

Duties/powers arising from scheme governing documentation

- Pay employer contributions
- Participate with running of scheme:
 - retirement
 - incapacity
- Amendment
- Discretionary increases
- Use of surplus (subject to legislation)

Duty of Good Faith

Discretions, powers and fiduciary powers

- What kind of power does the employer hold?
 - fiduciary powers
 - beneficial powers
- Employer's discretion or power should have regard to:
 - the extent of the power
 - implied duty of good faith

Implied duty of Good Faith

- Derives from employment law
- 1991 - *Imperial Tobacco*
- 1998 - *Edge*
- 2001 - *National Grid*
- 2011 - *Prudential*

Implied Duty of Good Faith – Imperial Tobacco

- Judgement
 - Duty not to damage the relationship of confidence and trust between employer and employee extended to the exercise of employer's rights and powers under the pension scheme
- Principle
 - A duty of good faith exists in the employer's exercise of its pensions law rights and powers

Implied Duty of Good Faith - Prudential

- Facts
 - Pru. changed its policy on granting discretionary pension increases
 - Trustee challenged the decision
- Key arguments
 - Trustee asked Court to consider obligation to act in good faith
- Conclusion
 - all points found in favour of employer
- Principles
 - the implied duty of good faith will not be breached unless employer's conduct is irrational or perverse in a serious manner

What is the limit of the concept of good faith?

- Prudential – avoid “irrational” or “perverse” behaviour
- What is “irrational” or “perverse” behaviour:
 - “[potentially] *decision to override expectations which an employer has engendered*”
- Does the concept of “good faith” have any relevance where:
 - employers take advice
 - employers have an audit trail for decisions

What duties do trustees owe to employers?

- Trustees duty to act in beneficiaries' best interests
 - what if the employer is an express beneficiary?
 - is the employer a beneficiary (even where not express)?
- Trustee discretions and powers
 - are the interests of the employer a “relevant factor”?

What duties do trustees owe to employers?

- What could this mean?
 - how far should the influence of the employer go?
 - where are the limitations of influence?
- Trustees obliged to consult on statement of investment principles

Directors' Duties

Directors' Statutory Duties

- S172 CA 2006:
 - “*duty to promote the success of the company*” for the benefit of shareholders
- S172(b)
 - “*have regard to the interests of ...employees*”

Employers' Statutory Duties

Key Statutory Duties – Scheme Funding

- Part 3 (scheme funding) Pensions Act 2004
- Obligation for employer to fund scheme to meet the SFO
- Section 229 - to be agreed with trustees:
 - technical provisions
 - recovery plan
 - schedule of contributions
- When does the consultation requirement apply?
- What is consultation? – *Pitmans [2004]*

Key Statutory Duties – Scheme Funding

- Code of Practice: “reasonably affordable”
 - *“Trustees should aim for any shortfall to be eliminated as quickly as the employer can reasonably afford. What is possible and reasonable, however, will depend on the trustees’ assessment of the employer’s covenant.”*
- What is the employer business plan?
 - Trustee involvement
- Employer covenant
 - engagement and presentation

Key Statutory Duties - Consultation

- Consultation of members required before ‘listed changes’ are made to the scheme
- A listed change is essentially any change to the benefit structure
- Employer must provide information to affected members/their representatives
- “Spirit of co-operation”
- Duty to consider the responses to the consultation

“Moral Hazard”

Corporate activity around the Scheme

- Pre 2004:
 - corporate law and duty of good faith
 - no strong regulatory powers
- Post 2004:
 - “moral hazard”
 - potentially powerful regulatory powers

Moral Hazard

- FSD
 - tPR can require the employer (and those associated and connected) to put in place financial support for the scheme
- CN
 - tPR can require the employer (and those associated and connected) to pay a specified sum into the scheme

Moral Hazard

- Type 'A' Event: (materially detrimental)
- Example employer related events: (need a relevant deficit)
 - change in priority
 - return of capital
 - change to group structure
 - change to employer
 - sale and leaseback transactions (reduction of assets)
 - inter-company loans
 - business/asset sales
 - phoenix events
 - increase/reallocation of debt

Moral Hazard

- Defence to CN
 - reasonable to conclude (having considered the point) that the act was not materially detrimental
 - unreasonable to impose
- Defence to FSD
 - do not satisfy the tests
 - unreasonable to impose

Questions?
