

Pensions conference 2010

Legal Update

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Agenda

■ Regulatory Update

- IMG
- Cemex
- Ilford
- Houldsworth: DB or DC?
- s.251 PA 2004



Regulatory update



IMG case: HR Trustees v German



Overview

- Facts
- Decision
- Final salary linkage (*Courage*)
- Relying on contractual terms to override scheme rules (*South West Trains*)
- Ambit of s.91 PA1995



Facts

- DB scheme
- Convert benefits from DB to DC
- Change made in 1992 (prior to s.67 PA1995)



Facts – amendment powers

- 1977 Deed and 1981 Rules
- Fetter in 1977 Deed (old power)
 - “no amendment shall have the effect of reducing the value of benefits secured by contributions already made”
- Fetter absent in 1981 Rules (new power)
 - “except that no such alteration or addition shall operate so as to prejudice approval”



Facts – conversion

- Conversion DB → DC on 1 January 1992
- Member account credited with a transfer value for past service benefits to represent value of DB benefit
- Additional employer contributions to maintain expected retirement benefits (for accrued service)
- Value of benefit assessed at the date of conversion
- No underpin that DC benefit not less than DB



Facts – communication

- Member communications
 - memorandums
 - staff presentations
 - booklet
 - application form



Facts – implementation

- Deed of amendment executed: 3 March 1992
- Effective date of change: 1 January 1992
- Retrospective element to change



Decision – key questions

- Q1 Which was effective amendment power?
 - A1 Old power prevailed

- Q2 Could amendment (DB – DC) be made?
 - A2 Yes – subject to
 - underpin and
 - conversion to include benefits accrued to 3/3/92



Decision – key questions

- Q3 Could DB entitlements have been modified by consent, estoppel, waiver or other legal principle?
 - A3 Yes – but not on these facts

- Q4 Could member compromise / waive his pension rights on or after 6 April 1997 (s.91 PA 04)?
 - A4 No – surrendering by compromise agreement not within exception



Final salary linkage

- *Courage* case
- Secured benefit restriction – Millett J

“In the absence of express definition I see no reason to exclude any benefit to which a member is prospectively entitled if he continues in the same employment and which has been acquired by past contributions”

- IMG – restriction on amendment power protected final salary linkage



Getting around the rules

- Working outside the power of amendment
 - *South West Trains v Wightman*
 - pay increases from £22,950 to £25,000
 - pensionable salary £18,000
- Trustees bound to follow contract / adopt deed of amendment
- NUS Superannuation Fund



IMG case

- Was there a contract?
 - announcement about change to money purchase
 - presentations by Mr Wolanski
 - explanatory booklet
 - application form: “I wish to participate in the IMG Pension Plan...”
- All members ticked yes box, except Mr German



Why wasn't this enough?

- No intention to create legal relations (company to prove)
- On both sides
- Specifically, no intention to create contract
 - presented as fait accompli
 - booklet not comprehensive: no reference to giving up DB rights
- Cannot override fetter on amendment
 - breach of trust if trustees followed “contract”
- Pensionable salary determined outside scheme



What would have been enough?

- Informed consent to breach of trust
 - unaware of fetter on amendment
 - received no advice
 - no explanation about loss of DB rights
 - not told how CETV and contributions to be calculated
 - no real choice
 - received impression no adverse effect
- Is s.67 PA 1995 relevant?



But we relied on members' acceptance...

- Estoppel by representation
- High hurdle
 - clear representation or promise
 - act reasonably in relying
 - detriment if members not held to their representation
- Must be unequivocal representation
- Passive acceptance not enough
- Trust deed and rules prevail



But all parties shared same understanding...

- Estoppel by convention

- each and every member acted on agreed assumption that DB converted to DC
- passive acceptance not enough
- positive conduct or clear evidence of intention needed



But members gave up rights by compromise agreements...

- Waiver of claims in connection with reorganisation

- Clean break

- But an agreement to surrender entitlement or accrued rights is unenforceable

- s. 91 PA1995



A word about enhanced transfer values...

- “Caveat emptor”?
- Trend in favour of member
 - Regulator
 - IMG case



Other implications ?

- Capping pensionable pay
- Closure to accrual bypassing trustees
- Meaning of “consent”
- Collective bargaining
- Override wording in communications can backfire
- Compromise agreements

- Due to go to Court of Appeal



Cemex case: UK Marine v MNOPF Trustees



Cemex UK Marine v MNOPF Trustees

- Merchant Navy Officers' Pension Fund
- S.75 and "employment cessation event"
 - old definition (pre 4/08)
 - when does ECE happen?
- Not a historic case



Cemex – definitions

■ ECE

- cease to employ “persons in the description of employment to which the scheme relates” while someone else continues to

■ Active member

- in “pensionable service” = “service in ... employment to which the scheme relates which qualifies the member ...for pension ...”



Cemex – definitions

■ Employer

- “employer of persons in the description ... of employment to which the scheme .. relates”



Cemex – facts

- MNOPF closed to new members but trustees retained discretion to admit
- 5 employees
 - 1 active member
 - reached NRD 28/11/05 but postponed pension and remained employed until 1/06 when he left and drew his pension
 - 4 non members



Cemex – facts

- Non members
 - had all had option to join
 - two declined and joined Cemex Fund
 - two joined but took refunds and joined Cemex Pension Fund



Cemex – arguments

- Cemex argued no ECE
 - always employed someone in ... description of employment to which the scheme relates
 - anyone employee with scheme benefits
 - or eligible non members
 - wide reading
- Trustees argued there was ECE
 - ceased to employ actives
 - narrow reading



Cemex – decision

- Judge held: wide reading correct
- ECE doesn't happen if continue to employ
 - anyone with scheme benefits
 - or eligible non members



Cemex – practical effect

- To have ECE, employer must cease to employ
 - actives
 - deferreds (early leavers)
 - late retirees
 - pensioners
 - anyone “eligible” to join
 - = can apply?



Cemex – possible criticisms

- Narrowly based decision that may not be correct
- Apparently no examination of scheme rules e.g.
 - when employer’s participation ends
 - detail of eligibility rule
- Relies on loose notion of “eligible”
 - includes using amendment power or discretionary benefits rule?



Cemex – possible criticisms

- Law “clarified” in favour of narrow reading in 4/08
 - but transitionals preserve old definition in some cases
- Policy angle
 - crystallisation of s75
 - (long) delayed
 - how to know when?



Cemex – possible criticisms

- TPR’s 11/05 guidance on withdrawal arrangements took narrow reading
 - “the main question ... is whether you have ceased to employ ... all your active members If this happens and [another employer continues to have actives] this will be a cessation event”



Not a historic case

- 4/08 transitionals mean old style ECE can happen today
 - *NB ignoring for now changes to transitionals in 4/10*
- Old ECE definition continues to apply to employer after 6/4/08 where, before that date,
 - it ceased employ actives while someone else still had people in “employment to which ... scheme relates”
 - was not an ECE



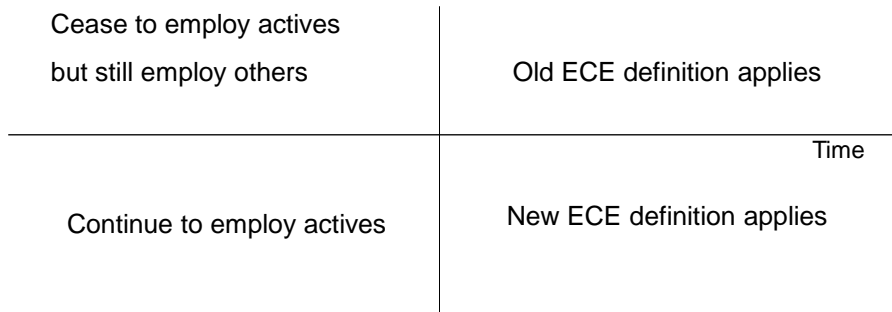
Cemex – potential problems

- Thought you’d triggered, but you hadn’t
 - paid but still liable
 - restitution?
- Thought you hadn’t triggered, but you had
 - can have ECE even if no actives



Transitionals – which ECE definition applies?

6/4/08



Cemex – example

- In 2002, ceased to employ actives
 - mistakenly believed triggered but no debt (MFR)
 - employer thought it was clear of s.75 liability
- In 2009, ceased to have any employees
 - 2008 transitionals maintain old ECE definition
 - buy-out debt triggered



Cemex – potential problems

- Close to accrual for all employers before 4/08 doesn't extinguish possibility of ECE
 - but 4/08 transitionals produce unexpected outcomes
 - already addressed by 4/10 changes to transitionals but further legislation or court decisions may be needed



Cemex – potential problems

- 4/10 change to transitionals
- Old ECE definition continues to apply to employer after 6/4/10 where, before 6/4/08,
 - it ceased employ actives while someone else still had people in “employment to which ... scheme relates”
 - was not an ECE and
 - scheme had not ceased to have actives



Cemex – potential problems

- Past restructuring: M&A in particular
 - warranties and indemnities
 - have claim?
 - in time?
 - share v. asset sales
- Future restructuring without knowing whether employer triggered in past
 - M&A or group reorganisation



Cemex – potential problems

- Wider issue in background
 - meaning of “employer” in Pensions Acts
 - different meanings in different contexts?



Cemex – good news?

- Pilots National Pension Fund v Taylor
 - who's an "employer"?
 - what's an ECE?
 - judgment soon?
 - Warren J
 - could well go to appeal
- Cemex not being appealed



Iford case: ITS v Hope



Ilford case – an improper proposal

- How far can trustees take PPF into account?
- Wide implications for DB schemes
- DB scheme in deficit (buy out £45m; PPF £15m)
- Employer in administration
- Trustees about to take steps to enter PPF
- Highly paid managers retired early on unreduced pension
 - asked trustee to buy out in full before entering PPF



PPF compensation

- 100% PPF compensation for members who have attained scheme NRD, members in receipt of a survivors or ill health pension before the assessment date
- Otherwise, 90% PPF compensation
- Subject to compensation cap
 - 09/10 £31,936.32 at age 65



Issue

- Could trustee agree to members' request?
- Trustees' advisers: no
- High earners' advisers: yes
- Trustee applied to Court for directions
- PPF and TPR represented



Impact on scheme

- Would use disproportionately large share of assets
- Better result for high earners
- No negative impact on other members
- Unjustifiable if PPF did not exist



Impact on PPF

- Would receive almost zero assets to support balance of scheme liabilities
- In effect, meets cost of securing high earners' benefits
- But for the PPF, would we make this decision?



Judgment – proper purpose

- Trustees must act for proper purpose
- PPF compensation not scheme asset, so could not be taken into account when allocating a fair share of the assets
- Contrary to purpose of scheme for trustees to use assets so disproportionately
- Prejudice remaining members
- Need for actuarial advice
 - no more than fair share of fund should be used



Judgment – is PPF a relevant factor?

- In making a decision, trustees need to take account relevant factors and disregard irrelevant factors
- PPF not a relevant factor
 - policy of legislation: PPF is last resort fund for insolvent schemes



Issues for trustees

- Keeping a scheme open to future accrual
- Investment
- Buying out benefits
- Pay unreduced CETVs
- Long recovery plans – TPR clearance?



When is acceptable to take PPF into account?

- Legitimate aims
- Entry to PPF
 - qualifying secondary insolvency events
 - compromise agreements
- Members have received permission to appeal



DB or DC?
Houldsworth v Bridge (CA)
(was Bridge v Yates)



DB or DC?

- CA determined not to be purist (contrast KPMG)
- Held following to be DC benefits
 - members' accounts on which GMP was first call (inc. where investment return was notional)
 - where scheme provided the annuity
 - where scheme guaranteed minimum level of benefit from member's account
 - where employer matched member's contributions



DB or DC?

- More schemes now escape SSF, s. 75, PPF levy etc.
- CA careful not to define "DC"
 - open to schemes to argue their case
- DWP wants to appeal to Supreme Court



S.251 Pensions Act 2004



S.251 – power to refund surplus

- Pass resolution before 6/4/11 to keep power alive
- Attempt to help schemes shed onerous conditions on their refund powers drawn from old legislation
 - but misfired
- Other jobs before 6/4/11
 - HMRC limits
 - HMRC approval for amendments





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