BRIEFING

TRAVERS SMITH

What's Happening in Pensions

Issue 110 – July 2024

Travers Smith Pensions Sector Group

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In this issue:

New Labour Government: The King's Speech at the opening of the new Parliament announced a new Pension Schemes Bill, which will take up many of the last Government's unfinished pensions initiatives. There will also be a bigger picture pensions review, looking at how and where pension fund assets are invested and, later, member outcomes. Economic growth is the new Government's main priority and they will be looking to pension funds to help them with this. We still await news of various matters, including the laying of the Pensions Regulator's funding code of practice and regulations to resolve issues with the lifetime allowance abolition legislation.

Virgin Media amendment case: The Court of Appeal has dismissed Virgin Media's appeal in the case concerning the validity (or rather otherwise) of amendments to contracted-out benefits in respect of which no written actuarial confirmation has been found. It agreed with the High Court judge that a confirmation was required for amendments to future accruals.

BBC amendment power case: The Court of Appeal has upheld decisions of the High Court concerning the interpretation of a restriction in the BBC pension scheme's amendment power that protects active members' "interests". It agreed that the restriction severely limits the BBC's ability to use the amendment power to reduce future accrual rates or end accrual altogether.

ITV Box Clever anti-avoidance case settled: The Pensions Regulator has announced that it has agreed in principle a settlement with ITV in the Box Clever anti-avoidance case. All members of the scheme are expected to receive their benefits in full.

TPO IDRP requirement: A Pensions Ombudsman blog post has announced the mandatory use of a scheme's internal dispute resolution procedure (where applicable) before making a complaint to the Ombudsman.

DC scheme return: The Pensions Regulator has outlined details of new questions added to the DC scheme return this year. These concern transfers out, decumulation options, investment consultants and the primary contact for pensions dashboards.

TPR on master trusts: The Pensions Regulator has announced that it is evolving its supervision of master trusts to focus on investments, data quality and standards, and innovation at retirement. This will involve more two-way interaction.

DC chair's statement fines: The First-tier Tribunal has upheld a penalty notice imposed by the Pensions Regulator on a scheme for failure to produce a DC chair's governance statement. But it indicated that, in its view, such fines may not be mandatory in all cases.

BHS directors liable for breaches of duties to creditors and misfeasance: The High Court has handed down its judgment in a case brought by the BHS group liquidators against two former BHS directors. The case concerned actions taken by the directors when the BHS group was effectively insolvent. A key factor in the group's financial distress was the DB pension scheme deficit and in particular the lack of a plan for paying deficit repair contributions that were inevitably about to increase. The directors were found liable to pay significant financial penalties.

PENSIONS RADAR: You may also be interested in the latest edition of Pensions Radar, our quarterly listing of expected future changes in the UK law affecting work-based pension schemes. A new issue is due before the end of this month.

SUSTAINABILITY MATERIALS: Our Sustainable finance and Investment Hub includes a section on ESG and sustainable finance issues for pension schemes and their sponsors.

NEW LABOUR GOVERNMENT

Labour's victory in the General Election was not expected to result in the widespread abandonment of the last Government's ongoing pensions initiatives and this was confirmed at the opening of the new Parliament with the announcement of a forthcoming Pension Schemes Bill in The King's Speech.

The last Government of course had various initiatives underway as regards both DB and DC pension provision. We list these and indicate originally intended timescales in Pensions Radar (a new issue of which is due later this month). The Pension Schemes Bill will take up several of these. As noted in a Government briefing paper, these are:

- the automatic consolidation of small deferred DC pension pots;
- a value for money framework for trust-based DC schemes;
- a requirement for DC schemes to offer a retirement income solution or range of solutions, including default investment options where applicable;
- consolidating the DB market through commercial 'superfunds';
- legislation to provide that the Pensions Ombudsman is a 'competent court', so that schemes recouping overpayments from future instalments of pension with the Ombudsman's approval do not also need to go through a County Court process (following the *CMG* case: see WHiP Issue 106); and
- extending the definition of 'terminal illness' used for the purposes of the Pension Protection Fund and the Financial Assistance Scheme, to allow eligible members to receive benefits earlier.

Notably, there was no mention of a public DB consolidator scheme, access to surplus, or multi-employer collective DC schemes. And nor was there mention of Labour's manifesto promise to require pension schemes and others to develop and implement climate transition plans. The new Government clearly needs more time to think about those initiatives.

As promised in the manifesto, there will also be a bigger picture pensions review, including how and where pension fund assets are invested and, later, member outcomes. Economic growth is the new Government's main priority and they will be looking to pension funds to help them with this in various ways. The report on investment is due to be published "in the next few months" and the report on member outcomes later this year.

Labour's manifesto also said that they would establish a National Wealth Fund, capitalised initially by Government but aimed at private investors including pension funds, to invest in "new industries of the future" and boost economic growth. An initial announcement was quickly made by the new Government about first steps, including the alignment of the UK Infrastructure Bank and the British Business Bank. A National Wealth Fund Bill will be introduced, which would put the Fund on a statutory footing (information on this is in the same briefing paper as mentioned above).

Labour also promised to retain the state pension 'triple lock'. But there was no mention of raising state pension ages or otherwise.

In opposition, Labour had pledged to reverse the abolition of the lifetime allowance. They have reportedly changed their mind about that but pensions tax was not mentioned at all in their manifesto, which may give them options in this regard. In any event, the pensions industry and affected individuals hope that they will quickly give HMRC the go-ahead for the regulations that we were expecting before Parliament was dissolved that will resolve issues with the abolition legislation.

The other step that the industry needs to be taken quickly is the laying before Parliament of the Pensions Regulator's code of practice on funding and investment. Legislation introduces the new 'funding and investment strategy' regime for valuations with effective dates on and after 22 September 2024. The code is needed in order for schemes to understand what is expected of them. We also need to hear from the Regulator on the required contents of the statement of strategy, their fast-track criteria, and guidance on covenant considerations.

The Labour win also means that the UK is likely to see significant changes to employment law and greater workers' rights. Our Employment team has produced a briefing summarising what Labour pledged to do.

The new Secretary of State for Work and Pensions is Liz Kendall MP and the new Pensions Minister (appointed to HM Treasury as well as to the Department for Work and Pensions) is Emma Reynolds MP. Ms Reynolds will be leading the pensions review.

VIRGIN MEDIA AMENDMENT CASE

The Court of Appeal has given its judgment in the Virgin Media case. This litigation concerns the validity of a rule amendment affecting benefits in a DB contracted-out scheme which was made without obtaining the actuary's written confirmation as required by section 37 of the Pension Schemes Act 1993.

The question appealed was whether a confirmation was required for changes to future service benefits or just past service benefits. The Court of Appeal has upheld the High Court's decision that such a confirmation was required for amendments to future accruals and not just for amendments affecting already accrued benefits. In the absence of this confirmation, the amendment was ineffective. The potential consequences of the judgment in this case are severe but further developments might help the scheme and other schemes that have similar issues.

In this case, a 1999 deed purported to amend the scheme's deferred pension revaluation provisions regarding future accruals. Under section 37 of the Pension Schemes Act 1993 and underlying regulations, the rules of a salary-related contracted-out scheme could not be altered in relation to any 'section 9(2B) rights' (broadly, all benefit rights in a salary-related contracted-out scheme other than from member voluntary contributions) unless the actuary had confirmed to the trustees in writing that they were satisfied that the scheme would continue to satisfy the contracting-out 'reference scheme test' applicable at that time. These provisions were a feature of the legislation between 6 April 1997, when the reference scheme test was introduced, and 5 April 2016, when contracting-out was abolished. From 6 April 2013, however, the legislation clearly only referred to amendments to future service benefits. Separate protections were introduced for changes to accrued benefits.

Assuming that no such confirmation was provided, Virgin Media asked the High Court to determine whether this meant that the 1999 revaluation amendment was void. And if so, was this only in respect of benefits accrued before the amendment or also to benefits accrued after the change (i.e. was the required actuarial confirmation only required in relation to benefits already accrued or also for future benefits)? It also asked if amendments beneficial to members would also be void or whether this would only be the case for adverse amendments.

In the High Court, Mrs Justice Bacon held in June 2023 that:

- The amendment is invalid and void if there was no written actuarial confirmation.
- Section 37, and so the above finding, applies to both accrued rights and future service benefits (before the 2013 change to the legislation noted above).
- Section 37, and so the above findings, does not only apply to amendments that are or might be adverse to beneficiaries.

This meant that the revaluation changes would, if no actuarial confirmation was provided, be ineffective. Benefit improvement amendments can also be void if no confirmation was provided. The judgment indicated that this outcome would cost the scheme around £10 million, in the absence of evidence of a written confirmation having been given.

An appeal was lodged on the second of Mrs Justice Bacon's above findings but the Court of Appeal (Lord Justice Nugee giving the reasoned judgment and the other appeal judges agreeing) was wholly in agreement with "her impressive judgment". In particular, the Court placed significant weight on what it considered to be the purpose and policy intent of the relevant regulations, prioritising this over what might be considered a more natural interpretation of the definition of 'section 9(2B) rights'.

Clearly, this case has a potentially very significant impact on other schemes too, if required actuarial confirmations were not provided. The contracting-out legislation expressly allows the Government to make retrospective regulations to validate amendments that are void due to the absence of such written confirmation. Depending upon the outcome of any appeal to the Supreme Court, the Government is therefore likely to be asked by industry bodies to take action. For example, it could do this so as to avoid the granting of windfall benefits in cases where actuarial confirmation could have been obtained but appears not to have been. The Government may or may not agree to do that. We will, of course, report on future developments.

BBC AMENDMENT POWER CASE

The Court of Appeal has upheld decisions of the High Court in *British Broadcasting Corporation v BBC Pension Trust Limited and another*, concerning the interpretation of a restriction in the BBC pension scheme's amendment power that protects active members' "interests". It agreed that the restriction severely limits the BBC's ability to use the amendment power to reduce future accrual rates or end accrual altogether. But other options may be available.

The BBC is experiencing a very large pension cost differential between its DB member employees and DC member employees. This is notwithstanding the ability to cap the pensionable element of pay rises or declare them non-pensionable, using separate scheme provisions, as confirmed by the Court of Appeal in 2017 in *Bradbury v BBC* (see WHiP Issue 66). It is therefore exploring options for reducing or even perhaps terminating future service DB benefit provision. But it has stressed that it has not yet formulated any proposals in this regard.

First, the BBC needed to establish what could be done within the terms of the scheme's trust deed. The amendment power allows the trustee, with the BBC's consent, to alter benefits but a key proviso says that:

> *"no such alteration or modification shall … take effect as regards the Active Members whose interests are certified by the Actuary to be affected thereby unless –*
>
> *(a) the Actuary certifies that the alteration or modification does not substantially prejudice the interests of such Members; or*
>
> *(b) the Actuary certifies that to the extent to which the interests of such Members are so prejudiced, substantially equivalent benefits are provided or paid for by the BBC or the Trustees or provided under any legislation; or*
>
> *(c) the alteration or modification is approved by resolution adopted at a meeting of such Members convened by the Trustees"*

The question before the courts was what the word "interests" covers. In particular, does it include:

> *"(a) the rights earned by past service up to the date of any amendment;*
>
> *(b) any linkage of the value of those past service rights to final salary;*
>
> *(c) the ability of members to accrue future service benefits under the Scheme on the same terms as provided for under the Scheme immediately before the amendment;*
>
> *(d) the ability of members to accrue any future service benefits under the Scheme; and/or*
>
> *(e) those members' interests in some other (and if so what) right or benefit."*

The High Court held that it included all of (a) to (d) and decided it was not necessary to go further (see WHiP Issue 104). In the appeal, the parties agreed that question (a) should be answered in the affirmative and that question (e) did not require a separate answer.

The Court of Appeal (Lewison LJ giving the reasoned judgment) unanimously agreed with the High Court that the word "interests" in this context should be given its natural, broad meaning. It agreed with the High Court that it means "matters of relevant concern" and so includes all of (b), (c) and (d) (as well as (a)) from the above list of questions. Other cited uses of the word in the trust deed and rules were, Lewison LJ said, to be read in their own context and had narrower meanings.

The question also arose as to whether the rule amendment made in 2000 introducing the provision allowing the BBC to cap the pensionable element of pay rises or declare them non-pensionable, as considered in the *Bradbury* case, could have been validly made under the terms of the amendment power. An actuary's certificate under limb (a) of the amendment power restriction had been given in respect of that amendment. The High Court judge in the present case had decided that there was nothing in the judgments of the High Court or Court of Appeal in *Bradbury* that prevented him from reaching his conclusions: essentially they had been considering different questions - the judges in *Bradbury* had not been considering the scope of the amendment power. The Court of Appeal agreed.

The High Court had also ruled that the amendment power, which was exercisable by the trustee with the employer's consent, would not be being exercised for an improper purpose if it were used, subject to its terms, to change benefits without agreement having been reached between the BBC and affected members (whether by consent or collective bargaining). This point was not argued in the Court of Appeal.

This is not necessarily the end of the matter. As well as the possibility of a further appeal, at the beginning of the judgment Lewison LJ says (without further explanation):

> *"Although the precise scope of the power raises a number of potential questions, it has been agreed between the parties that some of those questions should be answered (if at all) in later proceedings. We are asked to consider very specific questions, and nothing I say should be taken as applying more widely than the specific questions we have been asked."*

ITV BOX CLEVER ANTI-AVOIDANCE CASE SETTLED

The Pensions Regulator has announced that it has agreed in principle a settlement with ITV in the Box Clever anti-avoidance case. All members of the scheme are expected to receive their benefits in full.

The Regulator had issued financial support directions to ITV and associated entities in 2020, after years of litigation. Agreement on reasonable financial support was not reached, so the Regulator sought a contribution notice for the scheme's full buy-out deficit (most recently estimated as around £76 million). ITV has always considered it wrong that (among other things) it should be held responsible for more than its proportionate share of liabilities in respect of the joint venture.

The agreement in principle will see all of the 2,800 members (both ex-Granada and ex-Thorn) transferred to the ITV Pension Scheme after (and to an extent subject to) a data cleanse exercise. Members have been receiving benefits at PPF levels since 2014 but can now receive full scheme benefits and arrears. No information about the additional funding to be provided by ITV has been disclosed.

The settlement is supported by the trustees of the Box Clever scheme and the PPF.

TPO IDRP REQUIREMENT

A Pensions Ombudsman (TPO) blog post has announced the mandatory use of a scheme's internal dispute resolution procedure (where applicable) before making a complaint to TPO. This follows TPO's recent review of its operating model, which looked at how to address the issue of demand for their services outstripping their capacity (see WHiP Issue 109).

Going forward, TPO will be requiring all complainants to exhaust the respondent's formal complaints process before it will consider investigating a complaint. In the case of a dispute with an occupational pension scheme, this means the internal dispute resolution procedure.

Pensions Ombudsman Dominic Harris explained:

> *"… our legislative framework sets out that, generally, TPO will not investigate complaints until the IDRP process has been exhausted. However, that requirement was relaxed in 2018 when the Pensions Advisory Service moved its (informal) dispute resolution function to TPO. Individual complainants could choose to use our informal resolution service, which could include engagement before, or during, the scheme's own IDRP process. …*
>
> *Although our Resolution Team will only consider investigating complaints that have completed an internal resolution process, our team of volunteer advisers … will continue to offer their impartial support to individuals prior to, or during, the IDRP process. This will be focused on supporting vulnerable members and cases, for example where the risk of financial harm is high or where there is a time-critical situation. …*
>
> *As one of our priority workstreams, we will be moving from piloting some aspects of the change to full implementation by autumn this year."*

Further blog posts on other changes are promised over the next few months.

TPO have also updated their factsheet 'Signposting to The Pensions Ombudsman'.

DC SCHEME RETURN

In advance of 2024 DC scheme returns being issued next month, the Pensions Regulator has outlined details of new questions added to the return this year. These concern transfers out, decumulation options, investment consultants and the primary contact for pensions dashboards.

For 2024, there are new questions about scheme leavers (by which they mean transfers out) in the 12 month period leading up to the date at which the most recent membership information is provided. These ask for:

- The number of members who have left the scheme and are taking decumulation benefits outside a trust-based pension scheme.
- The number of members who have left the scheme and are taking decumulation benefits with another workplace pension scheme or pension provider via a partnership arrangement.
- The number of members transferred to a master trust due to the scheme winding up or considering winding up.
- The number of members who have initiated a transfer to another workplace pension scheme as an active or deferred member.
- The number of members who have left the scheme for any other reason.

In all cases, schemes with 12 or more members must also declare the amount in pounds of sums transferred in respect of the members in each category.

Regarding investment consultants, which the Regulator first asked about last year, there are the following three new questions:

- When did the trustees last review the performance of the provider against objectives?
- If there has not been a performance review, explain why.
- If there has not been a review of the objectives, explain why.

For schemes with 12 or more members, there will also be new questions about some benefit types under the scheme, including the number of members receiving each benefit and the asset value the members received. This appears to relate to schemes that offer decumulation options within the scheme. Details are yet to be finalised but interested schemes can ask to see the current draft of this question set.

The return will also ask for information about the scheme's pensions dashboard primary contact.

TPR ON MASTER TRUSTS

The Pensions Regulator has announced that it is evolving its supervision of master trusts to focus on investments, data quality and standards, and innovation at retirement. This will involve more two-way interaction.

Neil Bull, the Regulator’s Executive Director of Market Oversight, told a Pensions Regulator master trust event that the move would see master trusts become the "gold standard for pension provision". This follows on from the master trust authorisation and supervisory regime, which he said has resulted in high levels of governance and administration.

Mr Bull added that he wanted master trusts to see their relationship with the Pensions Regulator as a partnership, which mitigates harms, identifies opportunities for savers and delivers value. He also called on master trusts to share their thoughts candidly so that the Regulator can explore concerns and build sophisticated evidence bases to understand the bigger picture.

He also said that many master trusts will have already seen a difference in how the Regulator engages with them on investments. This includes expert-to-expert conversations where a multi-disciplinary team from the Regulator engages with a master trust’s investment and strategic experts as well as its trustees.

Finally, he said TPR will:

- *"probe and challenge more on how a master trust’s approach to investments delivers for savers*
- *investigate how a master trust is seeking the best possible long-term risk-adjusted returns*
- *look more broadly at master trust investment governance practice and investment decision making*
- *request deep dives into the systems and processes of master trusts"*

And he added: “Our visits need not be cause for concern but seen instead as a learning opportunity for us both.”.

DC CHAIR'S STATEMENT FINES

In Caldwell (Trustee of the Smith & Wallace & Co 1988 Pension Plan) v Pensions Regulator, the First-tier Tribunal upheld a penalty notice imposed by the Pensions Regulator on a scheme for failure to produce a DC chair's governance statement. But it indicated that, in its view, such fines may not be mandatory in all cases.

The trustee of the scheme in question had failed to produce a chair's statement. The legislation says that in such circumstances the Regulator "must" impose a penalty notice, so the Regulator argued that it had no discretion in the matter, regardless of the circumstances.

The Tribunal disagreed in principle. It did not accept that "mere use of mandatory language without more excludes from consideration any explanation offered for the breach, however compelling". Rather, it considered that Parliament's intention was that the Regulator ought not to fine trustees where "wholly exceptional circumstances fully explained and excused their non-compliance and imposition of a penalty would be manifestly unjust". But the Tribunal accepted that the circumstances of this case were not exceptional and upheld the penalty notice.

Decisions of the First-tier Tribunal do not set a precedent for other cases but may be considered.

BHS DIRECTORS LIABLE FOR BREACHES OF DUTIES TO CREDITORS AND MISFEASANCE

The High Court has handed down its judgment in *Wright v Chappell*, a case brought by the BHS group liquidators against two former BHS directors. The case concerned actions taken by the directors when the BHS group was effectively insolvent. A key factor in the group's financial distress was the DB pension scheme deficit and in particular the lack of a plan for paying deficit repair contributions that were inevitably about to increase. The directors were found liable to pay significant sums.

The two directors found liable were Dominic Chandler and Lennart Henningson, who will have to pay a combined £18 million. The trial of the third and best known, Dominic Chappell (who is in prison), has been deferred as he successfully argued that the case against him should be held over as he did not have the time to prepare for his case nor the opportunity to instruct counsel. But it has been reported more recently that Mr Chappell will be found liable on the same bases to pay more than £50 million including costs, if a draft order is approved by the judge.

Our Restructuring and Insolvency Team have produced a briefing for their sector clients.

FOR FURTHER INFORMATION, PLEASE CONTACT

Susie Daykin
Partner, Head of Pensions
susie.daykin@traverssmith.com
+44 (0)20 7295 3247

Daniel Gerring
Partner
daniel.gerring@traverssmith.com
+44 (0)20 7295 3341

Niamh Hamlyn
Partner
niamh.hamlyn@traverssmith.com
+44 (0)20 7295 3287

David James
Partner
david.james@traverssmith.com
+44 (0)20 7295 3087

Dan Naylor
Partner
dan.naylor@traverssmith.com
+44 (0)20 7295 3454

Chris Widdison
Partner
chris.widdison@traverssmith.com
+44 (0)20 7295 3604

Nick White
Knowledge Counsel
nick.white@traverssmith.com
+44 (0)20 7295 3472