SLAUGHTER AND MAY

Pensions Bulletin

7 September 2018 / Issue 12

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For more information, or if you have a query in relation to any of the above items, please contact the person with whom you normally deal at Slaughter and May or Bridget Murphy

New law

I. CMA proposals for pension investment reforms

1. Trustees may wish to take note of investment reform proposals put forward by the Competition and Markets Authority.

2. A provisional report[1] on the subject includes the following recommendations:

   2.1 trustees selecting their first fiduciary manager should run a competitive tender;

   2.2 trustees who have already appointed a fiduciary manager without a tender process should put the role out to tender within 5 years of that appointment;

   Comment: If this proposal is implemented, trustees close to the 5 year anniversary of their fiduciary manager's appointment may be faced with the need to put the role out to tender in short order.

   2.3 fiduciary management firms should provide clearer information on fees (including a break down) and how they have performed for other clients (industry standards would be introduced on how to report investment performance), to help trustees make meaningful comparisons between providers;

   2.4 trustees should set their investment consultants strategic objectives and firms should report against these; and

   2.5 the Pensions Regulator should issue guidance to advise trustees on how to choose and scrutinise providers.

3. The statutory deadline for the CMA's final report is 13th March, 2019.

II. PPF compensation consultation following Beaton ruling

1. Those involved in the running of DB schemes should note that the Government is planning to amend legislation[2] so that it can continue to calculate PPF compensation as it has previously, despite a recent High Court decision.

2. Under the proposals, pension derived from service in another scheme will continue to be aggregated with the member's other benefits under the scheme entering the PPF when calculating PPF compensation, including the cap on that compensation.

3. The DWP consultation was issued because of the October 2017 High Court decision in *Beaton*, which decided against the PPF's practice of aggregating transferred-in benefits with benefits earned by actual pensionable service under the scheme.

   Comment (1): The *Beaton* decision concluded that transferred-in benefits should not be aggregated with benefits earned by Mr Beaton with his new employer when applying the PPF compensation cap. The court considered that the transferred-in benefits were not 'attributable to pensionable service' with the new employer and the legislation[3]

[1] *Investment Consultants Market Investigation - 18th July, 2018*

[2] Pension Protection Fund (Compensation) regulations 2005 (SI 2005/670)

[3] paragraph 26(2)(b) of Schedule 7 to the Pensions Act 2004

requiring both sets of benefits to be aggregated did not, therefore, kick in. To read about the High Court ruling please see Pensions Bulletin 17/18.

Comment (2): It is understood that the Court of Appeal hearing for *Beaton* will be heard by 25th February, 2019.

III. Pensions cold calling ban planned for Autumn 2018

1. The Government's consultation on draft regulations[4] to ban pensions cold calling confirms that the ban is likely to be introduced in Autumn, 2018.

2. A ban on cold calling would cover unsolicited direct marketing calls about pensions products and services, but the ban would not apply in a range of situations.

3. For example, the ban would not operate in relation to firms regulated by the FCA or to trustees of occupational pension schemes where:

   3.1 the recipient of the call has given specific consent to receiving marketing calls on pensions from the organisation making the call; or

   3.2 the recipient of the call has an existing client relationship with the caller and the relationship is such that the recipient envisages receiving unsolicited calls for the purpose of direct marketing in relation to pension schemes.

4. The Information Commissioner's Office is to enforce the ban. The consultation paper confirms that the ICO will not be able to take action against firms located overseas but its arrangements with international regulators would enable enforcement action to be taken where companies operating wholly abroad make calls into the UK that would be unlawful if made in the UK.

5. Regulations to ban pension cold calling would be made under Section 21 of the Financial Guidance and Claims Act 2018.

Cases

IV. BA succeeds in Court of Appeal on pensions increase dispute

A recent Court of Appeal ruling serves as a reminder that trustees must use their powers for a proper purpose.

A. Facts

1. The Airways Pension Scheme ("**the scheme**") trustees used their unilateral power to amend the scheme, to grant themselves unilateral power to provide discretionary increases.

2. They then decided to grant a 0.2% discretionary increase above CPI. The 0.2% increase amounted to 50% of the gap between RPI and CPI for 2013.

3. BA challenged the trustees' actions on a number of fronts, arguing that the member-nominated trustees did not give any active or genuine consideration to the exercise of the discretionary power and had fettered their own discretion. The High Court disagreed.

B. Decision

1. A majority of the Court of Appeal agreed with BA's argument that the trustees had acted for an improper purpose by setting, rather than delivering, the remuneration (in the form of pension) paid by BA.

2. The constitutional function of the trustees set out in the Trust Deed was to manage and administer the scheme, not to design the benefit structure. Managing and administering the scheme entitles the trustees to deal with assets which already form part of the

[4] Draft Privacy and Electronic Communications (Amendment) Regulations 2018

scheme (where there is a surplus), or to require additional contributions to be made in order to secure the benefits promised under the rules.

3. The power of amendment was not intended to give the trustees the right to remodel the balance of powers between themselves and the employer. Amending the pension increase rule resulted in a scheme with a different overall purpose, in which the trustees effectively added the role of paymaster to their existing responsibilities as managers and administrators.

   Comment (1): Trustees do not usually have a unilateral power to amend their scheme but this decision may be of relevance to how any trustee powers with funding implications under a DB scheme should be exercised.

Comment (2): This dispute is expected to continue in the Supreme Court, meaning that there will be a level of uncertainty until that judgment is handed down.

British Airways PLC v Airways Pension Scheme Trustee Limited

V. Scheme 'frozen' under Section 75 despite final salary link

Employers of DB schemes closed to future accrual, with final salary linked benefits, will be interested in a recent High Court ruling on whether a scheme in that position should be considered 'frozen' for employer debt purposes.

The court decided that deferred members of such a scheme who were still employees were not active members, despite the final salary link. This meant that the relevant sections of the scheme were 'frozen' for the purposes of Section 75 of the Pensions Act 1995.

A. Facts

1. The G4S Pension Scheme ('**the Scheme**') was made up of 3 sections which were treated as separate schemes for various statutory purposes.

2. An amendment in 2011 ended future accrual in 2 out of the 3 of the sections. Members kept their final salary link, however, because of a restriction in the Scheme amendment power.

   Comment: Some pension schemes contain an amendment power restriction prohibiting changes which prejudice the accrued rights of members in respect of pensionable service up to the date of the amendment. This kind of provision, often referred to as a *Courage* restriction, means that benefits remain linked to the member's final salary.

3. The court was asked to establish whether employees who became deferreds when the Scheme's sections closed to future accrual, with final salary linked benefits, were active members. The Scheme rules referred to these individuals as 'Employed Deferred Members' ('**EDMs**').

4. If the EDMs were not active members, the sections in question would be considered 'frozen' for the purposes of Section 75 of the Pensions Act 1995. In that scenario, an 'employment-cessation event' would not happen if an employer ceased to employ all of its EDMs and a Section 75 debt would not be triggered.

5. Conversely, if the sections in question were **not** 'frozen' then an 'employment-cessation event' would occur when an employer ceased to employ all of its EDMs, triggering a Section 75 debt.

B. *Decision*

1. The statutory[5] definition of an 'employment-cessation event' involves an employer ceasing to employ at least one active member and at least one other employer continuing to employ at least one active member. The term 'active member' means a person in 'pensionable service'.

2. The term 'pensionable service' means:[6]

   'service in any description or category of employment to which the scheme relates which qualifies the member (on the assumption that it continues for the appropriate period) for pension or other benefits under the scheme'.

3. The EDMs were not in pensionable service because their service after the closure date did not qualify them for further pension, it simply quantified the pension already earned by them before the closure.

4. The judge agreed with the *MNRPF* ruling which concluded that members who retained a right to a higher rate of revaluation if they remained in seagoing employment following the scheme's closure were not in pensionable service because the enhanced revaluation had already been earned by reference to service before the scheme closed.

Comment: Employers will welcome this decision. Over a number of years, several schemes in a similar situation have sought Opinions from Counsel on the point. The court noted that it had been asked to construe the legislation and that the particular facts relating to the Scheme were not likely to make a difference, making this ruling of wider application than would otherwise be the case.

G4S PLC v G4S Trustees Ltd - 12th June, 2018

VI. Ombudsman decides no transfer discharge following pensions liberation transfer

The Pensions Ombudsman has upheld a complaint against the Northumbria Police Authority ('**the Authority**') regarding a transfer made to a pensions liberation scheme. The Ombudsman considered that the Authority was not discharged from liability to pay the member's pension, ordering it to reinstate the benefits.

A. *Facts*

1. Mr N was a deferred member of The Police Pension Scheme, which featured a normal pension age of 60. At the age of 39 he decided to seek advice on transferring to another pension arrangement which would allow him to access his pension from age 55. He did this a few months after the February, 2013 pension scams action pack was issued by the Pensions Regulator.

2. The Regulator's action pack contained a leaflet for members, about which the action pack stated '*you may want to include a copy with any member correspondence*'. The Authority sent a link to the leaflet via a message on its intranet newsfeed for employees.

3. Mr N was referred to a firm of financial advisers by an unregulated introducer. Those financial advisers recommended an occupational DC scheme called the London Quantum Retirement Benefit Scheme, which had been registered with HMRC for 2 years.

[5] Occupational Pension Schemes (Employer Debt) Regulations 2005 (SI 2005/678), regulation 6ZA

[6] Section 124(1) of the Pensions Act 1995

4. Confirmation that the transfer had taken place was received by Mr N in August, 2014.

5. The Regulator later appointed an independent trustee (Dalriada Trustees Limited) to the receiving scheme, in 2015.

6. Mr N subsequently complained to the Pensions Ombudsman and an oral hearing was held early in 2018.

B. Decision

1. The Authority's failure to engage directly with Mr N, its failure to send him the Regulator's scam warning leaflet, and the extent of its enquiries regarding the receiving scheme amounted to maladministration.

2. By failing to carry out reasonable checks before the transfer, the Authority had not *'done what is needed to carry out what the member requires*' and it was not, therefore, statutorily[7] discharged from the obligation to provide Mr N's benefits. The Authority was ordered to reinstate Mr N's benefits (less whatever he could recover from the receiving scheme trustees).

   Comment: This stands in stark contrast to a decision (*PO-10365*) reached in 2017 in which the Ombudsman ruled that failure to provide the complainant with a pension scam warning amounted to maladministration. The Ombudsman considered that £1,000 was an appropriate penalty, after concluding that the complainant would have gone ahead with the transfer anyway. To read more about *PO-10365* please see Pensions Bulletin 17/15.

3. The Regulator's scam warning leaflet was designed to be sent to members individually, not via a link on an intranet newsfeed accessible to all employees. Mr N's motivations for a transfer were not so strong or pressing that he could not have been deterred by appropriate warnings or further information about the possible risks.

   Comment (1): The Ombudsman also noted in *PO-10365* that pension scam warnings had not put a stop to people transferring their benefits.

   Comment (2): The Regulator's approach regarding the distribution of its scam warning leaflet has been one of encouragement, rather than attempting to impose an obligation to distribute.

   Comment (3): Compliance with the Pension Scams Industry Group Code of Good Practice on pension scams (updated 22nd June, 2018) is voluntary, although trustees may find it useful to look at tips on how to conduct due diligence when considering a transfer request. The Code contemplates scheme administrators including some wording of their own in pre-retirement letters, for example, as an alternative to providing members with the Regulator's scam leaflet.

4. The Authority should have picked up on 'red flags' raised in relation to the receiving scheme, including the sponsoring employer's dormant status and its registration at an address far removed from Mr N, who was still employed as a policeman in Northumberland and still living in that county.

   Comment: The Government plans to restrict the statutory right to transfer to certain situations, once the authorisation regime for master trusts is rolled out. Under those restrictions, where the receiving scheme is an occupational pension

[7] Pension Schemes Act 1993, Section 99(1)

scheme it must either be an authorised master trust or there must be a genuine employment link to the receiving scheme, demonstrated by evidence from the member of regular earnings from that employment. To read more about this please see Pensions Bulletin 17/15.

Mr N (PO-12763)

Points in practice

VII. EMIR pensions clearing exemption timing gap - FCA statement

1. The FCA has confirmed (by email, on 4th July, 2018) that it will not require pension schemes and their counterparties to start putting processes in place to clear derivatives during the timing gap between the expiry of the latest clearing exemption and the re-introduction of that exemption.

2. The exemption for pension schemes from the central clearing requirement expired on 16th August, 2018. The European Parliament announced (on 12th June, 2018) that the exemption should be extended to apply for a further 2 years '*for a large majority of PSAs [pension scheme arrangements]*', with small pension schemes being granted an extension of 3 years instead. Further extensions are also in contemplation.

Comment (1): The pensions exemption was introduced because pension schemes typically minimise their allocation to cash, holding higher yielding investments such as bonds or shares, in part to try to match more closely to the way their liabilities are valued and, in part, to try to reduce the cost of funding the scheme's benefits.

Comment (2): Requiring pension schemes to clear over the counter derivative contracts centrally would therefore lead to divesting a significant proportion of their assets for cash in order for them to meet the ongoing margin requirements of central counterparties, with a consequential increase in cost.

VIII. Master trusts draft Code - Regulator response to consultation

1. Those involved in running master trusts should note that the Pensions Regulator has published (on 2nd July, 2018):

   1.1 the response to its consultation on the draft Code of Practice 15: Authorisation and supervision of master trusts (to read about the consultation please see Pensions Bulletin 18/06), and

   1.2 the final version of the Code, which has been laid in Parliament.

2. The Regulator acknowledges that it may be appropriate to provide new or revised information for an application which has already been submitted, for example where the Regulator is considering a recommendation to refuse authorisation, or where something significant happens that impacts the master trust's ability to meet the requirements.

3. In that event, the Regulator would decide whether to accept new or different information based on whether it would be fair and reasonable to do so.

4. The Regulator expects external assessments of a master trust's systems and processes to be less than 6 months old when submitted but where that is not practical it '*will want to understand how the trustees have satisfied themselves that no changes have impacted the report's conclusions*'.

5. Master trusts will now be expected to hold financial reserves of at least £150,000 (the figure suggested previously was £75,000). Financial reserves are expected to cover the costs arising from a triggering event.

6. As regards independent trustees, the response confirms that their presence on the independent trustee register would not be a suitable proxy for the 'fit and proper' assessment required under the new master trusts regime, '*as it does not have the same focus or breadth*'.

7. The Regulator plans to publish:

7.1 checklists for the business plan and continuity strategy requirements; and

7.2 information on how and when the list of authorised master trusts will be published and updated.

IX. Master trusts - draft supervision and enforcement policy

1. The Pensions Regulator has consulted on its draft Master Trust Supervision and Enforcement Policy. The draft Policy lacks detail in number of areas.

2. The draft Policy includes a section on 'additional supervision', to be conducted in relation to master trusts 'with higher perceived risk'. When monitoring risk the Regulator plans to consider a range of issues, including:

   2.1 external factors impacting master trusts, (such as the socio-economic environment, political and legal environment and competitive landscape); and

   2.2 member and employer experience (for example, complaints received).

3. Under the draft Policy, the Regulator would give consideration to a number of factors when reaching a decision on whether to withdraw a master trust's authorisation. One of those issues would be the '*circumstances of the wider market as a whole*'.

4. The draft Policy includes a section on pause orders, to be issued during a triggering event period if the Regulator is '*satisfied that it will help trustees carry out their implementation strategy or there is an immediate risk to members' interests and the order would be in the interests of the generality of members*'.

   Comment: The draft Policy simply summarises the legislation[8] on the pause orders. Given that a pause order may have a significant impact on the master trust concerned (by, for example, directing the scheme to stop contributions or benefit payments), some level of detail about how the Regulator might come to decide that a pause order should be issued would have been of greater assistance.

X. Late valuation submission results in £25,000 penalty

1. The Pensions Regulator has issued a press release (on 11th July, 2018) announcing that it has imposed a £25,000 penalty[9] for the late submission of 2 valuations which were due in 2013 and 2016.

2. The Regulator had been told that the delays were due to a planned merger with another scheme run by the employer. According to the press release, the Regulator told the trustee that the proposed merger was not a valid reason for failure to submit the valuations. When the proposed merger did not happen and the valuations had not been submitted by the end of 2017 the Regulator decided to take action.

3. The press release states that the Regulator has issued 9 Warning Notices for late valuations since April, 2017.

   Comment (1): The Regulator's Compliance and enforcement quarterly bulletin (April-June 2018) includes the following statement: '*we are coming down harder on those trustees who put their members' benefits at risk by failing to agree an appropriate valuation within the statutory deadline*'.

   Comment (2): We have observed that the Regulator is taking a tougher stance where valuations are submitted later than the deadline of 15 months after the valuation's effective date. Trustees and employers heading towards a scheme valuation deadline should therefore make every effort to finalise and submit their valuation on time if they are to avoid engagement from the Regulator.

[8] Section 31 of the Pension Schemes Act 2017

[9] under Section 10 of the Pensions Act 1995

XI. Pension scheme financial statements - PRAG guidance

1. The Pensions Research Accountants Group (**PRAG**) has issued guidance for trustees and auditors concerning the requirement for pension scheme financial statements to comment on the appropriateness of the ‘going concern’ basis of accounting for the scheme in question.

2. The guidance emphasises that this does not represent a change to trustees’ responsibilities.

3. Audit reports must:

   3.1 state whether the use of the ‘going concern’ basis of accounting is inappropriate, and

   3.2 refer to any undisclosed material uncertainty that may cast significant doubt over its use for a period of at least 12 months from the date of approval of the financial statements.

4. This applies to DB, DC and hybrid pension scheme financial statements.

5. The guidance lists examples of circumstances that may lead trustees to conclude that the ‘going concern’ basis is not appropriate, or that there are material uncertainties about the scheme’s ability to continue as a ‘going concern’. One example listed is where the employer fails to comply with its duties under the scheme trust deed and rules, or its current behaviour leads the trustees to believe that it will do so in the next 12 months.

6. The guidance also notes that the timing of financial statement ‘going concern’ disclosures can give rise to sensitivities in relation to:

   6.1 member communications – this could therefore influence the timing of the approval of the annual report and accounts, within statutory time limits; and

   6.2 the employer’s financial position, for example if it is in negotiations with creditors, the PPF or the Pensions Regulator – the guidance recommends that trustees engage with the employer, and other parties if appropriate, at an early stage.

   Comment (1): The guidance has been put together following the 2018 version of the Statement of Recommended Practice (‘**SORP**’) on Financial Reports of Pension Schemes. The SORP applies for all scheme years starting on or after 1st January, 2019, although early adoption is permitted.

   Comment (2): The revised SORP includes changes to the ‘going concern’ section, designed to clarify:

   - that disclosures may still be required even if there is no material uncertainty in relation to ‘going concern’ - for example, where a scheme is expected to end its PPF assessment period and continue as a closed scheme; and

   - which ‘going concern’ disclosures might be appropriate where the scheme is in a PPF assessment period.

Watch List

The Watch List is a summary of some potentially important issues for pension schemes which we have identified and where time is running out (or has recently run out), with links to more detailed information. New or changed items are in **bold**.

No.	Topic	Deadline	Further information/action
1.	Put in place register of persons with significant control (“PSC”) for trustee company where trustee is a corporate	6th April, 2016 and ongoing requirement	Pensions Bulletin 16/03
2.	Ban on member-borne commissions in DC schemes used for auto-enrolment	5th July, 2016 at the latest and ongoing requirement	Trustees must notify “service providers” if the scheme is being used as a “qualifying scheme” for auto-enrolment purposes and some or all of the benefits are money purchase. Pensions Bulletin 16/04.

No.	Topic	Deadline	Further information/action
3.	Cyclical re-enrolment	Within 6 month window by reference to third anniversary of employer's staging date	For example employers with a 1st July, 2015 staging date must complete cyclical re-enrolment process between 1st April, 2018 and 30th September, 2018. Publication available to clients on request from usual pensions contact.
4.	Money purchase annual allowance, which applies to individuals who have flexibly accessed their money purchase pot on or after 6th April, 2015, has dropped from £10,000 to £4,000 under Finance (No.2) Act 2017	Retroactive effect from 6th April, 2017	Member communications should include a warning note about this, highlighting the retroactive effect.
5.	GMP equalisation		
5.1	Part 8 action brought by female staff, trustee and Lloyds Trade Union	15th May, 2017	We will continue to monitor developments in this litigation, which has implications for all schemes with GMPs accrued in the period 17th May, 1990 to 5th April, 1997.
		Trial commenced	5th July, 2018
5.2	Government response **to** consultation on GMP equalisation published	13th March, 2017	Pensions Bulletin 17/7
6.	HMRC's existing practice on VAT and pension schemes to continue indefinitely		Employers should consider taking steps to preserve, or even enhance, their pensions-related VAT cover. Pensions Bulletin 17/18
7.	DC bulk transfers without member consent: introduction of easements	6th April, 2018	Pensions Bulletin 17/18 Pensions Bulletin 18/05 **Pensions Bulletin 18/08**
8.	Bulk transfers of contracted-out rights without consent: introduction of easements	6th April, 2018	Pensions Bulletin 18/01 Pensions Bulletin 18/05
9.	Deferred debt arrangements become available	6th April, 2018	Pensions Bulletin 18/05
10.	Disclosure of costs, charges and investments - new requirements	Mostly in force 6th April, 2018	Pensions Bulletin 18/05
11.	Auto-enrolment total minimum DC contributions increase to 5% (of which minimum employer contribution of 2%)	6th April, 2018 to 5th April, 2019	
12.	Auto-enrolment total minimum DC contributions will increase to 8% (of which minimum employer contribution of 3%)	6th April, 2019 onwards	
13.	Data protection: New Regulation: EU General Data Protection Regulation in force	25th May, 2018	Pensions Bulletin 16/05 Employment Bulletin 16/15 As data controllers, trustees will need to ensure that compliance with the EU General Data Protection Regulation is achieved by this date. A compliance checklist for trustees is available to clients from their usual Slaughter and May contact.
14.	Existing EMIR exemption extension for pension scheme arrangements ends	16th August, 2018	Pensions Bulletin 17/01 **See Item VII above.**
	EU Parliament confirms further extension of pensions exemption, with further extensions possible	12th June, 2018	Pensions Bulletin 18/10
15.	**Master trusts new authorisation and supervision regime starts**	**1st October, 2018**	**See Items VIII and IX above**
16.	IORP II transposition deadline	12th January, 2019	Pensions Bulletin 16/11

No.	Topic	Deadline	Further information/action
17.	Brexit	By 29th March, 2019, unless extended	UK leaves EU from effective date of withdrawal agreement or, failing that, 2 years after giving Article 50 notice unless: (a) European Council and UK unanimously decide to extend period, or (b) UK withdraws, if able to do so, its Article 50 notice before 29th March, 2019.

If you would like to find out more about our Pensions and Employment Group or require advice on a pensions, employment or employee benefits matters, please contact Jonathan Fenn or your usual Slaughter and May adviser.

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