SLAUGHTER AND MAY

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Legal and regulatory developments in pensions

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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 Helena Davies.

New law

I. Equalisation of same sex survivor benefits: Government response

1. In a written statement on 4 July 2019, Guy Opperman, Pensions Minister, confirmed the basis on which same sex survivor benefits in public sector schemes will be equalised following:

   1.1 the Supreme Court decision in *Walker v Innospec* in September 2017. The Court ruled that the Equality Act exemption, which allowed pension schemes not to equalise survivor benefits for same sex spouses and civil partners in respect of pensionable service before 5 December 2005, was unlawful; and

   1.2 re-consideration of the Government's Review of same sex survivor benefits, originally published in June 2014.

2. The statement acknowledges that it is now clear, following the Supreme Court's decision, that same sex civil partners or spouses are entitled to survivor benefits in the same way as opposite sex spouses in respect of all periods of service, provided the benefit became payable after 2 December 2003. The Government will remove the 5 December 2005 limitation in public sector schemes. However, it will not make any further retrospective changes to legislation to equalise survivor benefits.

3. The statement notes that private sector schemes are individually responsible for ensuring they are compliant with the judgment in *Walker v Innospec* and equality legislation, and should take their own advice on compliance.

4. The way in which the Government is proposing to amend same sex survivor benefits in public sector schemes raises a separate inequality issue from the sexual orientation inequality that was the subject of *Walker v Innospec*. Broadly, to date in public sector schemes, same sex spouses and civil partners have been provided with benefits on the same basis as **widowers**. The Government has now decided that these same sex survivor benefits should be provided on the same basis as for **widows**.

5. In general, survivor benefits for widows (in both public and private sector schemes) have been more generous than those for widowers, mainly due to the fact that a widow's GMP is payable in relation to contracted-out service from 6 April 1978, whereas a widower's GMP is payable only in respect of contracted-out service from 6 April 1988.

6. The Government's decision to change the basis for same sex survivor benefits means that, in public sector schemes, men in an opposite sex marriage will potentially be entitled to lower values of survivor benefits than:

   - same sex survivors of either gender, and

   - women in an opposite sex marriage.

   The cost of eliminating all differences (which would involve equalising between widowers and widows and then providing same sex spouses and civil partners with identical benefits) was estimated in 2014 at £2.9 billion for public service schemes and £0.4 billion for private sector schemes. The Government recognises that its proposals for public sector schemes mean that some inequalities will remain, but suggests that these will "*work their way out of the system in time*".

Comment: Because the pensionable service that led to inequalities between widows and widowers took place prior to 17 May 1990, the date of the CJEU decision in *Barber*, there is no requirement to provide equal treatment for men and women. But the now-disadvantaged opposite sex male spouse may be able to argue sexual orientation discrimination based on a same sex male

spouse comparator who will get a (higher) widow's GMP.

Cases

II. Court of Appeal upholds Upper Tribunal ruling on FSD

A. Overview

The Court of Appeal has confirmed the Pensions Regulator's decision to issue Financial Support Directions (FSDs) to a number of companies (Targets) in relation to the Box Clever Pension Scheme.

B. Facts

1. The scheme was established to provide defined benefits for former active members of the Granada and Thorn pension funds who went on to work for a joint venture set up by the Granada and Thorn groups. Administrative receivers were appointed in 2003 and the scheme was closed to future accrual shortly afterwards. The Trustee asked the Regulator to consider issuing an FSD in 2005. The determination to issue an FSD was not made, however, until 2011. The scheme has been in a PPF assessment period since 2014, pending the outcome of this litigation.

2. The Upper Tribunal supported the Regulator's decision to issue the FSD. (To read about this, please see Pensions Bulletin 18/09).

3. Three issues were raised in the Court of Appeal:

   3.1 **Retrospective operation of FSD legislation** - when deciding whether to issue an FSD, could the Regulator take account of events which occurred before April 2005 (when the FSD legislation in the Pensions Act 2004 came into effect)?

   3.2 **Association** – Did the fact that the sponsoring employers were in administration mean they were "associated or connected with" the Targets at the "relevant time" – the date chosen by the Regulator as the "look-back date" (31 December 2009)?

   3.3 **Reasonableness** - was the Upper Tribunal's decision (that issuing an FSD would be reasonable) one which a reasonable tribunal could properly reach on the facts?

C. Decision

1. **Retrospective operation**

   1.1 The Court confirmed that the Regulator could consider events which occurred before April 2005. Retrospective measures have to be assessed against the unfairness which they may produce. When examining unfairness in the context of FSD legislation, one important factor was that the Regulator must assess whether it would be reasonable to issue an FSD in the situation in question.

   1.2 There was no error of law in the Upper Tribunal's assessment that the retrospective operation of FSD legislation did not breach the Targets' right to peaceful enjoyment of a "possession" (the "possession" being the money payable under the FSD), under Article 1 Protocol 1 of the European Convention of Human Rights. The Court agreed that a fair balance had been struck between achieving the aim of the legislation and the interference with the possession. There was symmetry between the PPF's liability to address a shortfall even if the scheme deficit can be traced to events long ago, and the liability of connected persons to contribute to an FSD.

2. **Association**

   Given the highly technical factual matrix involved in this case (which centred around the impact of a default under a debenture), the Court agreed with the Upper Tribunal's view

that the Targets were associates of the scheme's sponsoring employers at the relevant time, even though administrative receivers had been appointed in respect of the companies. It was immaterial that it would have been the administrative receivers rather than the directors of the companies who would have decided how voting rights would be exercised.

3. **Reasonableness**

3.1 The Court rejected the assertion that the Upper Tribunal's decision was one which no reasonable tribunal could properly reach on the facts. In looking at whether it would be reasonable to issue an FSD, the Upper Tribunal had considered the various arguments raised by the Targets concerning retrospectivity, and the impact on them if an FSD were to be imposed, and concluded that the factors in favour of an FSD outweighed those against it.

3.2 The Court described the test for reasonableness as whether *"fairness requires that an insufficiency of funding should be borne by the levy payers of the PPF and the scheme members on the one hand, or the target on the other"*.

Comment (1): The Court of Appeal decision confirms the wide scope of the Regulator's FSD powers. They are potentially applicable to activities prior to the date the anti-avoidance legislation was introduced in 2005; they can cover employers and those connected or associated (even after the appointment of administrative receivers); and they are not dependent on a finding of fault on the part of the target companies.

Comment (2): The willingness of the Court to allow the Regulator to consider conduct prior to the introduction of the moral hazard regime raises the possibility that the same element of retrospectivity might apply to any future changes to the regime.

Comment (3): It is reported that the Targets have been refused permission to appeal by the Court of Appeal, but will now apply to the Supreme Court for permission to appeal.

Granada UK Rental and Retail Ltd v Pensions Regulator – 20 June 2019

Points in practice

III. Investment Governance guidance updated for SIPs new requirements

1. The Pensions Regulator has updated its Investment Governance Guidance for DC schemes to reflect the fact that changes to legislation from 1 October 2019 will require Statements of Investment Principles (SIPs) to include additional information about ESG/climate change, stewardship, voting behaviour, and details of the scheme's arrangement with its asset manager.

2. The legislative changes are being introduced by two sets of regulations, made in 2018 and 2019 (see Pensions Bulletin 18/13 and Pensions Bulletin 19/06).

3. SIPs must state the trustees' policy on "financially material considerations", including ESG factors. The revised guidance lists considerations for trustees when identifying whether a financial factor of their investment plan is material or not - such as the proportion of scheme membership impacted; the proportion of a fund that is owned by the scheme; and the appropriate time horizon for the members. The guidance also fleshes out what the ESG factors might encompass and urges trustees to consider their scheme demographic when applying their policy in relation to ESG issues in their investments. Trustees are encouraged to involve their advisers and asset managers, as well as engaging with investee companies, policymakers, and collaborative industry initiatives.

4. The extent to which "non-financial matters" (broadly, members' and

beneficiaries' views, including their ethical views and opinions on social and environmental impact) are taken into account must also be specified.

Comment: There is a difference between making a statement on the extent to which members' views have been taken into account and in fact taking those views into account. Case law[1] is clear that the latter is permitted only in very limited circumstances.

5. Other changes to the guidance include sections on:

5.1 **Stewardship** – trustees are encouraged to become familiar with their managers' stewardship policies.

5.2 The **implementation report** that trustees need to draw up (from 1 October 2020), showing how they have followed and acted upon the investment policies stated in their SIP. The report should set out where decisions have diverted from the policy and explain how the policy has been followed and the extent to which its objective has been achieved. Where this has not been successful, the report should set out what actions the trustees will take to rectify the situation. By 1 October 2021, the report must also describe the trustees' voting behaviour during the year; the guidance suggests that this might include detail on how policies on voting and engagement have been developed and implemented in practice.

5.3 **Fiduciary management** – the guidance notes the changes that will come into force by the end of 2019 as a result of the CMA investigation into investment consultancy and fiduciary management (see Pensions Bulletin 19/06). The key change is mandatory tendering where over 20% of the scheme assets are delegated to a fiduciary manager. A checklist for trustees includes carrying out due diligence on the proposed fiduciary manager; ensuring that measures are in place to identify and manage conflicts of interest; and establishing reporting relationships.

5.4 Two new concepts currently gaining profile in the market - **impact investment** (which aims to deliver tangible, positive impacts on society/the environment alongside generating investment returns) and **patient capital** (long-term finance for firms which have potential to grow).

The guidance points out the risks of impact investment, including liquidity and a lack of common standards. With patient capital, trustees need to complete sufficient due diligence to understand the main drivers of the expected return and how risks are managed and mitigated. Again, illiquidity of the investment in the context of the scheme's objectives and member profile can be an issue.

IV. TPR consultation on future of trusteeship and governance

1. The Pensions Regulator has launched a consultation about the shape of pension scheme trusteeship, and the removal of barriers to consolidation.

2. The Regulator intends to set out expected implementation timings in its response. The consultation closes on 24 September 2019.

A. Trusteeship

1. TKU

1.1 The consultation proposes that the Regulator's 21st Century

[1] See *Cowan v Scargill* [1985] and *Harries v Church Commissioners* [1992]

Trusteeship campaign run in 2017/18 could be the starting point for defining a clear minimum standard for trustee knowledge, and asks whether trustees should be required to demonstrate a minimum level through training or qualification. A continuing professional development programme is also mooted.

1.2 The Regulator plans to revisit its TKU Code and guidance, suggesting a move away from a broad, generic TKU syllabus towards more measurable competency-based standards. Trustees would be expected to demonstrate how they meet TKU requirements. The paper also suggests that the TKU Code should be revised so that more is expected from all professional trustees.

2. Whether every scheme should have a professional trustee

The Regulator thinks that "*the vast majority*" of pension schemes would benefit from having an accredited professional trustee on the board. Whilst noting that the numbers of schemes and professional trustees at present would not make it feasible to mandate this, the consultation asks whether such a legislative change ought to be introduced "*in the future*".

Comment (1): Although the paper does not say when a requirement for a professional trustee could be brought in, the Regulator highlights the relevance of the expectation that the number of schemes in existence in five years' time will be much smaller than now.

Comment (2): The reference to accreditation relates to work done by the Professional Trustee Standards Working Group, culminating in Professional Trustee Standards (published March 2019) to which a voluntary accreditation framework will attach (expected to be launched later in 2019).

3. Diversity

3.1 Views are sought on whether schemes should be required to report on what they are doing to ensure that their board has "'*the necessary diversity of skills and reflects the membership of the scheme*". The paper also asks whether such a requirement should apply only to schemes of a certain size and what the reporting mechanism might be.

3.2 An industry working group to pull together tools, guidance and case studies on diversity is also mooted.

4. Sole trusteeship

4.1 The Regulator is concerned about DB schemes with an **individual** who solely performs the trustee role "*including sole trustee directors or other individuals acting on behalf of a corporate trustee*".

4.2 The paper refers to anecdotal evidence that some employers appoint a sole trustee in the belief that it will enable them to negotiate an employer-friendly funding agreement. Other concerns relate to diversity and to the sole trustee's ability to engage in robust decision-making.

4.3 The Regulator asks whether the governance standards should be strengthened by, for example, requiring at least two trustees (or, in the case of a sole trustee company, at least two directors) to be present at meetings. Views are also sought on the advantages and disadvantages of different types of corporate trustee model, and how sole trustees manage potential conflicts of interest.

B. Governance and DC consolidation

1. The Regulator intends to use "*targeted regulatory activity*" which

will involve asking trustees to demonstrate that they have met certain basic governance requirements. Where trustees are unable to do that, the Regulator will "*dig deeper into the general running of the scheme*".

2. The Regulator wants to encourage and facilitate DC consolidation, the aims being to enable schemes to achieve greater efficiency and to address situations where the trusteeship and governance of a scheme is sub-standard.

3. Recognising that the bulk transfer relaxations introduced on 6 April 2018 (see Pensions Bulletin 18/05) do not apply where a guarantee or promise attaches to the DC pension, the Regulator suggests possible solutions (such as assigning policies with guarantees to the individuals affected without crystallising their benefits, or increasing the pot size of members who surrender their guarantees).

V. PASA guidance on transfers from DB schemes

1. On 8 July 2019, the Pensions Administration Standards Association (PASA) published Part 1 of best practice guidance about "standard" transfers from DB schemes. The guidance, designed to promote faster, safer transfers, has been welcomed by Pensions Minister Guy Opperman and the Pensions Regulator. The guidance has been reviewed by the FCA, among others.

2. Part 2 (scheduled for publication towards the end of 2019) is expected to cover more complex types of transfer, such as suspected scam cases, partial transfers, overseas transfers, non-statutory transfers, and cases requiring significant manual intervention.

3. While PASA notes that compliance with the guidance is voluntary, it anticipates that the Pensions Ombudsman will refer to it as "good industry practice" when addressing complaints.

4. In a standard case where there is no referral to an actuary, PASA expects the guaranteed quote to be issued to the member within seven working days. Where the transfer does involve referral to the actuary, PASA expects this to happen within eight working days. The settlement process is then expected to take up to nine working days.

5. A Transfer Template for members and their advisers is attached to the guidance. PASA expects use of the template to result in fewer follow-up data requests from advisers, and better quality advice through an improved understanding of safeguarded rights.

6. Other appendices to the guidance include a sample letter of acknowledgement for the quote request, a transfer forms checklist, and a consumer factsheet on the Pension Transfer Gold Standard (a voluntary code of good conduct for financial advice relating to DB transfers).

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	6 April 2016 and ongoing requirement	Pensions Bulletin 16/03
2.	Ban on member-borne commissions in DC schemes used for auto-enrolment	5 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.	Money purchase annual allowance, which applies to individuals who have flexibly accessed their money purchase pot on or after 6 April 2015, has dropped from £10,000 to £4,000 under Finance (No.2) Act 2017	Retroactive effect from 6 April 2017	Member communications should include a warning note about this, highlighting the retroactive effect.
4.	GMP equalisation		
4.1	Part 8 action brought by female staff, trustee and Lloyds Trade Union Judgment published Clarificatory judgment published	15 May 2017 26 October 2018 6 December 2018	We will continue to monitor developments in this litigation, which has implications for all schemes with GMPs accrued in the period 17 May 1990 to 5 April 1997. Pensions Bulletin 18/15 Pensions Bulletin 18/17
4.2	Government response to consultation on GMP equalisation published	13 March 2017	Pensions Bulletin 17/7
5.	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
6.	DC bulk transfers without member consent: introduction of easements	6 April 2018	Pensions Bulletin 17/18 Pensions Bulletin 18/05 Pensions Bulletin 18/08
7.	Bulk transfers of contracted-out rights without consent: introduction of easements	6 April 2018	Pensions Bulletin 18/01 Pensions Bulletin 18/05
8.	Deferred debt arrangements became available	6 April 2018	Pensions Bulletin 18/05
9.	Disclosure of costs, charges and investments - new requirements Chair's statement and website must publish costs and charges information	Mostly in force 6 April 2018 Within 7 months of scheme year end falling on or after 6 April 2018	Pensions Bulletin 18/05
10.	Existing EMIR exemption extension for pension scheme arrangements ended	16 August 2018	Pensions Bulletin 17/01 Pensions Bulletin 18/12
	EU Parliament confirms further extension of pensions exemption, with further extensions possible	12 June 2018	Pensions Bulletin 18/10
11.	CJEU decides PPF compensation must equal at least 50% of each recipient's benefit (*Hampshire - Case C-17/17)*	6 September 2018	Pensions Bulletin 18/13
12.	Master trusts new authorisation and supervision regime introduced	1 October 2018	Pensions Bulletin 18/12 Pensions Bulletin 18/13 (note: SI later re-issued as SI 2018/1030)
13.	IORP II transposition deadline	12 January 2019	Pensions Bulletin 16/11
14.	Trustees must ensure Statement of Investment Principles meets new requirements on ESG and stewardship	Various requirements phased in: 1 October 2019, 2020, and 2021	Pensions Bulletin 18/13 Pensions Bulletin 19/06
15.	Pensions Regulator consultation on draft DB Funding Code of Practice expected	Spring 2020	

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 Charles Cameron or your usual Slaughter and May adviser.

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