Trustee Knowledge Update

August 2020

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LEGISLATION

Corporate Insolvency and Governance Act 2020

The Act came into force on 26 June 2020. It includes long-term changes to insolvency law as well as some temporary easements (up to 30 September 2020) to provide businesses with the flexibility and breathing space they need to continue trading during the difficult time caused by COVID-19. Key provisions in the Act include:

- a new moratorium regime for companies. The aim of the moratorium is to facilitate a rescue of the company, a restructuring or an injection of new funds. A company may apply to the High Court for a moratorium (initially for 20 business days but this can be extended in various ways). One effect of a moratorium is that it imposes a restriction on the enforcement of many debts. However, some debts including certain pension scheme contributions are excluded and remain payable. TPR and the PPF must, where relevant, be given notice of a moratorium and regulations give the PPF the power to exercise some creditor rights.
- a new restructuring plan regime whereby a plan can be proposed for the purpose of eliminating, reducing, preventing or mitigating the effect of a company's financial difficulties. Notice of any meeting to approve the plan must be sent to creditors and to TPR and the PPF where relevant and regulations allow the PPF to exercise certain creditor rights. If a number representing 75% in value of the creditors or class of creditors agree the plan, the court may, on application, sanction it.
- the temporary suspension of certain wrongful trading laws to support directors who continue trading through the COVID-19 emergency without the threat of personal liability and to protect companies from aggressive creditor action; and
- giving companies and other bodies temporary easements on company filing requirements and requirements relating to meetings.

More detail can be found in this CMS Law-now article.

CONSULTATIONS AND DRAFT LEGISLATION

Pension Schemes Bill amendments

The government suffered four defeats at the House of Lords Report Stage, with the Lords accepting amendments to including one to require the Secretary of State to ensure open schemes are treated differently from closed ones for funding purposes, balancing liquidity and investment risk with maturity and affordability, and not accelerating scheme closures. These amendments may not survive when the Bill is considered in the House of Commons (which is expected to be in early September).

In addition, the government laid new amendments allowing regulations to require that trustees explicitly consider climate change goals, including the Paris Agreement. The government also laid amendments to allow regulations to prescribe conditions about members obtaining information or guidance from MaPS before trustees can make a statutory transfer.

GOVERNMENT AND PARLIAMENT

Coronavirus Job Retention Scheme – next steps

From 1 July employers may bring a furloughed employee back to work on a part-time basis and the CJRS would then apply to the balance of the individual's normal working hours. The amount recoverable by employers from the CJRS will taper down each month until the end of October (when the scheme is due to end) as follows:

- June and July: CJRS will pay 80% of wages up to a cap of £2,500 as well as employer NICs and AE minimum pension contributions.
- August: CJRS will pay 80% of wages up to a cap of £2,500. Employers will pay NICs and pension contributions.
- September: CJRS will pay 70% of wages up to a cap of £2,187.50. Employers will pay NICs and pension contributions and 10% of wages to make up 80% total up to a cap of £2,500.
- October: CJRS will pay 60% of wages up to a cap of £1,875. Employers will pay NICs and pension contributions and 20% of wages to make up 80% total up to a cap of £2,500.

In welcome news, HM Treasury has confirmed that employees on furlough may still undertake work "*for the sole purpose of fulfilling their duties as a trustee*" of an occupational pension scheme. The exemption does not include employees who are acting as independent trustees or where the business activities of the employer include the provision of services as a trustee of the scheme.

Comment:

Trustees and employers should note that the provisions of the CJRS do not automatically change the employer's duties under contracts of employment or under pension scheme rules. Any changes to terms and conditions or to pension contribution rates for employees on furlough would have to be made in the usual way.

HMRC

Newsletter 120

This newsletter includes further information on temporary changes to pension processes as a result of COVID-19.

It also provides a reminder of the procedure for raising queries on the pensions tax rules. The first stage is to refer to the PTM and other HMRC guidance. If the question is not answered in the guidance then HMRC **Pension Scheme Service** may be able help clarify pension legislation. HMRC is unable to discuss individual or scheme specific information (if they do not have the appropriate authority) or answer hypothetical questions. If the question relates to a specific scheme or transaction then the **clearance process** should be followed. Here HMRC will only answer enquiries in cases of genuine uncertainty and where all the information required under the clearance service has been provided.

Newsletter 121

This newsletter includes information on temporary processes during the COVID-19 crisis.

Newsletter 122

The latest Newsletter contains various reminder for scheme administrators items on reporting to HMRC and the need to issue 2019/20 annual allowance pension savings statements to members.

GMP Equalisation Newsletter

This newsletter concerns the tax treatment of lump sums following GMP equalisation. The guidance does not apply to GMP conversion, and HMRC indicates that it is unlikely to produce any further guidance relating to conversion (or at least not until wider issues on conversion methodology have been resolved).

The guidance includes helpful statements on past lump sum payments. HMRC accepts that the requirement to "*extinguish*" rights can be read as meaning only the benefits or rights that could reasonably have been known about at the time of the payment (to reflect the exceptional circumstances associated with GMP). This means that (other than trivial commutation) past lump sums subject to a payment limit (e.g. £10k) will not stop being authorised purely

because, due to GMP equalisation, a further entitlement is later identified.

Generally any future 'top-up' payments to a previous lump sum must satisfy the payment conditions in force when made (and are taxable when made).

Comment:

This second set of guidance from HMRC is generally helpful and addresses many of the tax uncertainties which could arise on an equalisation exercise. We are still awaiting the third judgment of the High Court in the *Lloyds Bank* case, which may resolve some issues relating to historic benefits and past transfers. In the meantime, trustees of affected schemes should be taking steps to prepare for equalisation. PASA has recently issued guidance on data and member communications to assist trustees and administrators.

THE PENSIONS REGULATOR

DC scheme management and investment: COVID-19 guidance for trustees

TPR has updated its COVID-19 DC guidance to include a section on diverting contributions to a different investment fund where the selected fund has been gated. In TPR's view, the only circumstances where a default arrangement would not be created are if either:

- members were made aware before they selected the original fund that contributions could be diverted to another fund in certain situations; or
- the trustees contacted the members before diverting contributions and obtained their consent.

TPR also warns that where contributions are redirected back to a previously gated fund, whether or not the member's previous expression of choice would still apply will depend on the circumstances. The pre-existing expression of choice will probably still apply where members have either:

- consented to the redirection of the contributions on a temporary basis, until the original fund reopens; or
- been informed by the trustees that their contributions are being diverted into a default fund but that this will be corrected as soon as the original fund reopens.

Comment:

If trustees discover that they have unintentionally created a default arrangement by diverting or returning funds they should immediately take steps to ensure this arrangement meets the legal requirements, including in relation to the charge cap.

DB scheme funding and investment: COVID-19 guidance for trustees

TPR has comprehensively updated its DB COVID-19 guidance, in particular in relation to requests for the deferral of DRCs. TPR now says it does not anticipate further updates to this guidance unless circumstances change "significantly".

A few points to note:

- trustees faced with a reasonable request for deferral should "*make an informed assessment of whether it is in members' best interests to agree, even if a request is part of a larger co-ordinated request across other stakeholders that may appear equitable*";
- given improved visibility of employers' financial situations TPR does "*not expect trustees to unquestioningly extend their original suspension arrangements on a three-month rolling basis based on limited information and for this to become the*

new normal'. Trustees should now be able to undertake due diligence first, although there is a specific paragraph addressing the rare scenario where information is genuinely unavailable;

- a clear distinction between covenant issues that might recede post-COVID, and those that won't. If there is good evidence that the covenant has materially worsened and is not expected to recover in a reasonably short timeframe, the guidance says trustees should consider whether to update the scheme's funding arrangements;
- trustees must still seek mitigation: there is now a list of options. One example given is stopping all dividends and shareholder distributions. Another emphasises the need to ensure that the effect of any wider refinancing is fully understood, and that wider lender protections are extended to the trustees;
- trustees should obtain focused advice as appropriate to their situation.

Comment:

It is vital that trustees faced with an employer request to reduce DRCs carefully consider this guidance and take appropriate advice. The guidance has been supported in a recent blog from TPR's Chief Executive stressing the importance of early engagement with the employer and managing any conflicts of interest.

COVID-19: an update on reporting duties and enforcement activity

TPR has updated its reporting duties guidance. The general principle is that TPR expects trustees, wherever possible, to comply with reporting requirements from 1 July 2020. The exception is that providers will continue to have 150 days to report late payments of DC contributions instead of 90 days, with this remaining easement to be reviewed at the end of September.

The guidance does specifically mention a few reporting areas:

- although trustees must report any breaches of transfer obligations from 1 July there is a reminder that they can apply to TPR to use the 3-month easement for delays to CETVs caused by factors outside their control. Trustees should also continue to issue TPR's letter template for members requesting a CETV quote, and monitor the pattern of requests;
- TPR does not plan regulatory action where review of a Statement of Investment Principles (or default arrangement SIP) is not delayed beyond 30 September;
- although trustees will be asked to report failures to prepare audited accounts, TPR will not look to take enforcement action on late accounts signed off by 30 September 2020;
- TPR still does not expect to review Chair's Statements until the autumn (but they must still be produced in time);

THE PENSION PROTECTION FUND

Need help paying this year's levy invoice?

The PPF has announced that schemes or businesses struggling to meet PPF levy invoices within 28 days can now apply for up to 90 days to pay. Applicants will on receipt of an invoice, need to complete an online form explaining how COVID-19 has caused financial hardship justifying an extension.

There is more detail here (including the PPF's proposal to charge zero interest for the first 90 days, a reduced rate of 3% for the next 60 days and the normal rate of 5% above Bank of England base rate after that). The PPF also confirms that employer credit scores will not be affected, as liability for the levy falls on the trustees.

For schemes that may require extra time to pay the levy but cannot use COVID-19 as their justification, it remains possible to apply to pay by instalments.

CASES

Univar UK Ltd v Smith High Court - *rectification*

The sponsoring employer of a scheme sought rectification of the pension increase provisions in its 2008 Deed & Rules. These required indexation and revaluation based on RPI and not, as per the previous rules, statutory minimum increases (which later changed to CPI). The effect of the drafting was to increase the funding cost of the scheme by £23m.

The High Court noted that the mistakes had been made at an early stage in the drafting process and then neither identified nor corrected. After considering extensive evidence, the judge was satisfied that neither the employer nor trustees intended the relevant rules to have the legal effect that they did. Had that been the intention, he was satisfied that the change in approach would been included in the schedule of agreed changes provided by the solicitors involved.

The case shows that rectification may still be available where:

- the parties intended to use a particular form of words, but misunderstood its legal effect;
- the drafting error, at the time it was made, had no immediate implications for the scheme;
- the mistaken wording was down to negligence by one of the parties to the rectification or their legal advisers.

Comment:

This is another welcome decision where the court has come to a practical and sensible decision on the intention of the parties when granting rectification.

Hughes v The Board of the Pension Protection Fund High Court - *PPF compensation cap*

This claim challenged the PPF's approach to implementing the CJEU judgment in Hampshire (which decided that all members should receive at least 50% of the value of their accrued pension benefits). The claimants also challenged the existence of the PPF compensation cap. The questions considered by the court included:

Was the PPF compensation cap unlawful? Yes. Imposing the cap amounted to unlawful age discrimination under EU law. The provisions involved differential treatment on grounds of age, as members above normal pension age were not subject to the cap.

Did the PPF's method for ensuring 50% PPF compensation comply with the Insolvency Directive? Yes. The PPF could properly adopt an approach under which the overall compensation payable during retirement equalled 50% of the benefits the member would have received from the pension scheme during retirement (rather than applying an annual test). It was a matter for the PPF as to which method it employed to achieve that.

Was there a limitation period for claims against the PPF for payment of arrears of compensation? Yes. A six year limitation period applied for claims to the PPF under section 9 of the Limitation Act 1980.

Comment:

This decision has serious implications for the design of PPF compensation. It will also have a knock-on effect for pension schemes which have entered PPF assessment but wind-up outside the PPF due to being funded above PPF compensation levels. Until the government has indicated its intentions there will continue to be uncertainty in the provision of PPF compensation for those members whose benefits are affected by the compensation cap.

Safeway Limited v Newton **Court of Appeal - *scheme's 'Barber window' could be treated as closed from date of UK equality amendments***

This Court of Appeal ruling followed last year's CJEU decision which decided that the Safeway scheme did not equalise retirement ages with effect from 1 December 1991 (the date of a letter to members confirming the purported equalisation) but only from 2 May 1996 (when a deed formally amending the rules was executed). This was despite the scheme amendment power allowing, as permitted by UK law, deeds to have retrospective effect to the date of an earlier announcement to members.

These proceedings dealt with the effect on this analysis of section 62 of the Pensions Act 1995. Section 62, introduced from 1 January 1996 to implement the CJEU's equal treatment rulings into UK law, provided for all occupational pension schemes to be treated as including an "equal treatment" rule. The Court decided that section 62 expressly provided for "levelling up" and this meant that from 1 January 1996, UK law applied instead of EU law to determine member rights. The Court therefore accepted the employer's argument that the UK law effect of the 1996 deed was only nullified by EU law insofar as it related to the period from 1 December 1991 to 31 December 1995. The deed remained effective to level down scheme normal pension age to 65 with effect from 1 January 1996.

Comment:

This decision will come too late for many schemes who have completed their Barber equalisation. It may be relevant to any schemes with outstanding equalisation issues who had purported to amend their scheme rules retrospectively in the period between 1 January 1996 and 6 April 1997 (after which section 67 of the Pensions Act 1995 restricts amendments to accrued rights).

Facebook Ireland & Schrems **– CJEU - *data protection: EU-US Privacy Shield struck down, but controller to processor standard contractual clauses permitted***

In the original Schrems case in 2015 the CJEU struck down the "Safe Harbor" provisions for sharing data with the United States. In 2016 the EU Commission adopted the Privacy Shield, designed as a more robust replacement of the Safe Harbor framework with added oversight and enforcement. In the new *Schrems* case the CJEU has now declared the Privacy Shield invalid too, although confirming that Standard Contractual Clauses ("SCCs") can still lawfully be used as an alternative to transfer personal data from the EU.

The ICO issued an initial statement on "*Schrems II*" to confirm that it is reviewing its Privacy Shield and SCCs guidance. Its advice to those currently using the EU-US Privacy Shield framework for data transfers to the US is to continue to do so until new ICO guidance becomes available (but for nobody to now start using the Privacy Shield). A further statement on 27 July refers to updated European Data Protection Board FAQs on the Privacy Shield and SCC implications, which apply to UK data controllers and processors. It advises parties to *"take stock of the international transfers you make and react promptly as guidance and advice becomes available".* However, the ICO assures stakeholders that it will continue to apply a risk-based and proportionate approach. For more information, see the CMS LawNow here.

Comment:

Trustees who transfer scheme data to the US should carefully consider the ICO guidance and take expert advice. Data transfers between the UK and EU are currently allowed without additional protections but this may change from 1 January 2021 when the transition period after Brexit ends.

MISCELLANEOUS

FCA – Pensions transfer advice

The FCA has published a package of measures designed to address weaknesses in the DB transfer market. This includes a ban on contingent charging in most circumstances (including where the employer is paying for the advice). The FCA will also implement proposals allowing advisers to provide an abridged advice process which will help consumers access initial advice at a more affordable cost. The abridged process can only result in a recommendation not to transfer or a statement that it is unclear whether a consumer would benefit from a pension transfer without giving full advice. Where only abridged advice has been provided, a firm may not provide a confirmation for the purposes of section 48 Pension Schemes Act 2015 that appropriate independent advice has been provided.

The new rules come into effect on 1 October 2020 with transitional arrangements for those firms with clients that have agreed contingent charges terms before 1 October and started work before 1 October. In this situation they may charge contingently, provided a personal recommendation is given before 1 January 2021.

PLSA - DC Chair's Statement drafting template

This Chair's Statement template for 'standard' occupational DC schemes is designed to reflect the Charges & Governance Regulations requirements to produce an annual governance statement in trustee annual reports. It has been designed in conjunction with a number of law firms to be used alongside TPR's detailed guidance and quick guide. The initiative is supported by TPR.

PLSA - Engaging the engagers: a practical toolkit for schemes to achieve effective stewardship through their managers

This toolkit is a joint initiative from the PLSA and the Investor Forum. It looks to provide a framework for pension schemes (and other asset owners) to better understand the asset managers they use, and to demonstrate the value of effective stewardship and engagement across investment portfolios. The aim is to ensure that schemes can effectively use asset managers to achieve their long-term obligations.

The guidance focuses on how schemes should communicate with their asset managers, and how to assess the quality of asset managers' own engagement and stewardship work. It therefore includes definitions of stewardship and engagement, suggestions for broad scheme stewardship strategies, and an overview of how the PLSA sees effective engagement working in practice.

PLSA - Implementation Statement guidance for trustees

The PLSA has published guidance for DB and DC trustees on the new requirements on them to produce an implementation statement, publicly disclosing the scheme's investment and responsible investment activity over the previous year. The guidance has been produced by the PLSA's cross-industry Voting and Implementation Statement Working Group to cover a summary of the legislation, and timing requirements; principles for producing good statements; considerations around voting behaviour disclosures; and 'top tips' for relevant communications. There is also a useful flowchart of the requirements.

The guidance captures the fact that DC and hybrid schemes will have to disclose against all parts of their SIP, with DB schemes only having to disclose in relation to voting and engagement behaviour. In answer to a frequently raised question, it notes that unlike Chairs' Statements, implementation statements are subject to discretionary (not mandatory) civil penalties.

In relation to ESG disclosure requirements, the guidance also reminds trustees that there is no obligation on trustees to take non-financial matters into account; that legal tests must be met before trustees are permitted to do so; and that legal advice should be sought.

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Pension scheme reports and financial statements, and related matters in the context of the COVID-19 pandemic

This guidance for auditors of private sector occupational schemes is also designed to be useful to trustees and those preparing accounts.

Trustees should reflect on the effect of the crisis on the content of annual reports and Chair's Statements, even when reporting for accounting periods that ended on 31 December (as the subsequent COVID-19-related impact may be relevant). Schemes with accounting periods ending after 31 December must decide how much of the impact of COVID-19 should be attributed to 'non-adjusting events' such as a significant decline in the value of investments; the reduction or suspension of employer contributions; delay in completing Part 3 scheme funding documents; or employer insolvency.

CMA update on investment consultants market investigation – compliance statements

The CMA has issued an update on the submission of compliance statements under the Investment Consultancy and Fiduciary Management Market Investigation Order 2019. Compliance statements must be submitted to the CMA within 12 months and 4 weeks beginning with the date on which each of the relevant applicable Articles come into force. The parts of the Order which impose requirements on pension scheme trustees came into force on 10 December 2019 and so compliance statements must be submitted by 7 January 2021. Compliance statements should be sent to the CMA at RemediesMonitoringTeam@cma.gov.uk.

The pensions aspects of the Order had been expected to be transposed into regulations by 6 April 2020 these have been delayed.

This document reflects the law as at 12 August 2020.

Dates for diaries: Trustee training remains one of the most important ways of ensuring that trustees have the knowledge and understanding required to perform their duties. CMS runs regular trustee training days. If you would like to be updated of upcoming dates or have any other enquiries about this course please contact Megan Thorogood (megan.thorogood@cms-cmno.com).

If you are interested in any additional trustee or employer training please contact Kieron Mitchinson (kieron.mitchinson@cms-cmno.com) who can provide you with a list of our current training topics or discuss any particular training needs you might have.

Note: The information in this document is for general purposes and discussion only and does not purport to constitute legal or professional advice. It is not an exhaustive review of recent developments or relevant law and must not be relied upon as giving definitive advice. It is intended to simplify and summarise the issues which it covers.