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Essential UK Pensions News

Updater

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Introduction

Essential Pensions News covers the latest pensions developments each month.

FSHC Holdings Ltd v Glas Trust Corporation Ltd [2019]: Court of Appeal clarifies how to assess parties' intentions for rectification purposes

Usually in pension schemes where a mistake is identified, it has the effect of awarding greater benefits than intended to members and, therefore, the scheme amendment powers are of no assistance in this situation, as any changes would fall foul of section 67 of the Pensions Act 1995.

In order for a rectification claim to succeed, the parties to the document (usually, the scheme's trustees and the principal employer) must provide credible evidence that the document in question does not reflect their true and common intentions, and this has been judged objectively. The burden of proof falls on the party seeking the rectification, usually the scheme's employer. The mistake must also be of sufficient significance to justify the Court making a rectification order and in all the circumstances it must be appropriate and equitable to do so.

In *FSHC Holdings Ltd v Glas Trust Corporation Ltd* [2019], in a judgment handed down on July 31, 2019, the Court of Appeal held that it is wrong to apply the objective approach to assessing the parties' common continuing intention where rectification is sought for common mistake. The correct assessment is of the subjective intention of the parties. The objective approach was advocated by Lord Hoffmann in *obiter* (that is, non-binding) comments in *Chartbrook Ltd v Persimmon Homes Ltd* [2009], and these comments have since been the subject of extensive debate.

In *FSHC*, the Court of Appeal (Flaux, Leggatt and Rose LJJ) held that whether the parties had a common intention in respect of a particular matter should depend on their subjective intentions, as evidenced by an outward expression of agreement. If rectification was sought on grounds of a prior binding agreement, the terms of that agreement should be interpreted objectively, like all contracts. But that did not apply to a shared non-contractual intention.

In reaching this decision, the Court explained at length why the objective approach advocated by Lord Hoffmann in *Chartbrook*, and which has generated much uncertainty, was incorrect. The Court accepted that a document should be rectified to reflect an earlier binding agreement (interpreted objectively, as all contracts are interpreted), on the principle that parties should be held to what they have agreed. But an objective approach was not appropriate when rectifying a document to reflect a common intention which fell short of a binding agreement. In that case, rectification rests on the equitable doctrine that a party should not be allowed to enforce the terms of a written contract which is inconsistent with what both parties in fact intended those terms to be when the document was executed. The Court of Appeal also justified its ruling on the basis of precedent and policy.

Comment

Case commentators had predicted that the obiter comments of Lord Hoffmann in *Chartbrook* would not survive a Court of Appeal review. The *FSHC* judgment touches on the extensive debate on this issue and examines the doctrine of rectification from all angles. Its statement of the law now binds all lower courts and the Court of Appeal itself, so this is settled law – at least until the Supreme Court gets the opportunity to review.

Uncertainty on this point has led judges to make both an objective and a subjective assessment of whether there has been a common continuing intention and this decision should remove the need to do so in future.

The focus on the parties' subjective intentions is a good reminder of the importance of keeping records of negotiations.

DWP consults on regulations to implement CMA investment consultancy recommendations

The DWP is consulting on draft amending regulations incorporating new governance requirements for pension schemes. The Occupational Pension Schemes (Governance and Registration) (Amendment) Regulations 2019 will introduce changes to the way schemes manage their relationships with their investment consultants and fiduciary management providers.

Trustees will be required to run a competitive tender exercise for any agreement with a fiduciary manager provider that would result in 20 per cent or more of scheme assets being delegated. Trustees who appointed a provider prior to June 10, 2019 without conducting a competitive tender process will be required to conduct one within five years after the first appointment of a fiduciary management services provider. Where the five year period expires before, on or within two years of June 10, 2019, the competitive tender must be completed no later than June 9, 2021.

From April 6, 2020, trustees and managers will also be required to set objectives for their providers of investment consultancy (IC) services to enable them to better manage performance and to monitor value for money more closely. The DWP expects trustees to set objectives for their IC service that have regard to the statement of investment principles; review the performance of each IC provider against their objectives at least every 12 months; and review the objectives at least every 3 years and without delay after any significant change in investment policy.

The DWP expects that objectives will include a clear definition of the outcome expected to be delivered and the timescale over which it will be delivered, should be relevant to the services provided, and should also enable the trustees to measure the performance of the IC services provided.

The draft regulations reflect the content of the Competition and Market Authority's (CMA) investigation into the investment consultancy services industry which led to the Investment Consultancy and Fiduciary Management Market Investigation Order being finalised on June 10, 2019, but adapted for occupational pension schemes. The requirement to report compliance with the new governance regime will now fall within a scheme's annual return to the Regulator, rather than requiring a submission to the CMA. The parts of the Order relating to mandatory tendering and investment consultancy "objective setting" are due to come into effect on December 10, 2019.

The DWP aims to lay the final form of the regulations before Parliament in either December 2019 or January 2020, with a coming into force date for the remainder of the provisions being April 6, 2020.

The consultation closes on September 2, 2019 and the short timescale for both this and the Regulator's consultation over the holiday period represent a challenge for those wishing to respond.

Pensions Regulator consults on trustee guidance following CMA investment consultancy recommendations

The Regulator has published a consultation paper on new guides intended to assist trustees in managing their responsibilities on the appointment and retention of investment consultancy and fiduciary management services. This follows the DWP's consultation (see above) on draft amending regulations.

The new regulations will require trusts to conduct a selection process when appointing a fiduciary manager. Trustees will also be required to set specific strategic objectives for their investment consultancy service providers to enable them to better manage performance and to monitor value for money more closely.

The Regulator's consultation includes the following draft guides:

- **tendering for fiduciary management services** – this guide provides a set of key principles to illustrate a good practice approach to tendering and how the principles may be applied. An illustrative case study outlines how it may work in practice
- **tendering for investment consultancy services** – this shorter guide outlines how the key principles of a competitive tender may be applied to the tender for investment consultancy services, again with an illustrative case study

- **setting objectives for providers of investment consultancy services** – this guide addresses how trustees can set objectives in line with the draft regulations, but also considers how to address the broader services such consultants provide
- **choosing an investment governance model** – this guide sets out the relevant matters which trustees should consider. It is aimed more at assisting trustees to understand investment governance rather than reflecting new legal requirements

The consultation closes on September 11, 2019.

DWP responds to consultation on changes to Pensions Ombudsman's jurisdiction

On August 8, 2019, the Department for Work and Pensions its response to its consultation on changes to the Pensions Ombudsman's jurisdiction. The DWP's December 2018 consultation focused on how best to provide an early resolution function that would allow the Ombudsman to resolve disputes informally before formal determination is necessary, as well as regularising the interaction with schemes' statutory internal dispute resolution procedure (IDRP). The consultation followed the transfer of TPAS' dispute resolution work to the Ombudsman in March 2018.

In its consultation, the DWP also proposed widening the Ombudsman's jurisdiction to permit employers using group personal pension (GPP) arrangements to make a complaint of maladministration or refer a dispute of law to the Ombudsman.

The key points set out in the DWP's consultation response are that:

- the early resolution process would be best suited to simpler complaints, allowing their speedy resolution in a more informal and cost-effective manner. The outcome would not be binding, but the parties would be free to enter into their own enforceable settlement agreement if they wished. The new process should be available both before and at any stage of the IDRP
- the DWP will work with the Ombudsman, the Financial Ombudsman Service and the Money and Pensions Service to consider how "signposting" on who can make complaints to the Ombudsman could be improved. Respondents were of the view that any early resolution process should be clearly detailed on the Ombudsman's website
- in a similar way to that governing employers' complaints and disputes relating to occupational pension schemes which are brought to the Ombudsman, the DWP is keen to ensure that this process should be available for GPP issues too. Again, signposting on the Ombudsman's website should be improved to reflect any such widening in jurisdiction.

These changes will require new legislation which the DWP says will be brought forward "in due course".

View the consultation response.

Pensions Regulator issues Single Code of Practice Statement

The Regulator has signalled a radical shake-up of its codes of practice and is reviewing the current line-up of its current 15 codes “to form a single, shorter code”. These changes, it says, are part of becoming clearer, quicker and tougher and will ensure that clear and consistent expectations are set for all types of scheme.

The review will take place “over the next year” and will reflect the Occupational Pension Schemes (Governance) (Amendment) Regulations 2018. The amalgamation of the 15 existing codes is intended to make them quicker to find, use and update, so that trustees and managers of all types of scheme can be more responsive to changes in regulation.

The aim is to develop the new overarching code in phases, with the early focus being on those codes most affected by the regulations. Codes of Practice 9 (internal controls) and 13 (defined contribution) will be first, including content from Codes of Practice 14 (public service schemes) and 15 (master trusts), as the Regulator sets out the features of effective governance that will apply to all types of pension scheme. Trustees will need to be able to demonstrate that they have an effective system of governance within 12 months of publication of the updated code.

A formal consultation is planned for later in the year, in advance of which the Regulator will engage with stakeholders for feedback on the proposed design and content.

In advance of this intended streamlining though, the Regulator has recently published further information for those involved in applying for master trust authorisation. One of the five authorisation criteria is the effective running of the scheme, and confirmation that its systems and processes are sufficient. The extra guidance is aimed at new master trusts that intend to use an external administration and investment platform. The Regulator expects trustees to provide evidence of the scheme’s functionality and maintenance of IT systems, as well as evidence from any third party administrator that their IT systems meet the Regulator’s expectations regarding record-keeping, reconciliations and maintaining contributions.

Comment

This is an ambitious project as the Regulator has vast amounts of material on its website. Anyone who has tried to navigate their way through the large number of codes, guides, statements, forms and research papers in order to ensure their scheme’s compliance will wish the Regulator every success with its review and re-organisation. With such an enormous task ahead, it is probably unlikely that any draft of the new, single code will be available before 2020.

Pensions Regulator publishes 2018/19 annual report and accounts

One year on from becoming “clearer, quicker and tougher”, the Regulator has published its annual report and accounts for the 2018/19 financial year. As a result of the new focus, new supervision and enforcement teams have increased regular contact with schemes and enabled a cycle of one-to-one interactions with some of them throughout the year.

The report reveals there has been a 32 per cent increase in the use of the Regulator’s frontline powers, a 24 per cent increase in caseload and an 11 per cent increase in the use of trustee appointment powers. There were 154 uses of the Regulator’s information-gathering powers, while 286 mandatory penalty notices were issued over failures in preparing a trustee chair’s statement. Overall, 14.7 per cent of schemes were subject to risk-targeted regulatory intervention and this figure has increased every year since 2015/16.

Specific focus areas included:

- driving compliance with auto-enrolment duties (seeing increased whistle-blowing)
- implementing the authorisation and supervision regime for master trusts
- campaigning to improve trusteeship standards

The Regulator states that 18 of the 22 key performance indicators set out in its 2018-21 Corporate Plan were achieved, with those missed relating to refocusing priorities and issues with staff development. As to budget, actual expenditure in 2018/19 was £85.4 million, £2.6 million lower than budgeted, largely due to a reduction in enforcement costs, with fewer high-cost cases. Next year the budget is due to increase to £98.4 million and further still to £110.2 million in 2020/21, reflecting increases agreed with the DWP for the implementation of the Regulator’s new approach.

However, there is no mention of the new powers which the DWP intends to bestow upon the Regulator following the publication of the DWP’s White Paper and the long-term funding targets outlined in the Regulator’s annual statement in March 2019.

View the 2018/19 annual report and accounts.

The Pensions Ombudsman’s 2018/19 annual report and accounts

In the first report published since the Early Resolution Team joined the Ombudsman’s office from the Pensions Advisory Service in 2018 it is revealed that demand for pension dispute resolution services continues to grow but that the informal resolution of disputes has been a success.

The report confirms the aim to maintain an average time of 5.3 months to complete investigations even though the volume of early resolution cases was 50 per cent higher than anticipated, in addition to a continued rising trend in complaints accepted for formal investigation. Overall, 28 per cent of complaints decided by an Ombudsman were upheld or partly upheld. A record level of nearly 90 per cent of investigations and cases were resolved without an Ombudsman’s involvement.

The report highlights the Ombudsman's more proactive policy of intervention in appeals, and emphasises his concern to be notified of appeals, to "support the smooth and fair running" of those cases. Referring to the High Court's obiter comments in Burgess v Bic [2018], the Ombudsman reported receiving "positive industry comment" to his fact sheet positioning the Ombudsman as a "competent court" for the purpose of trustee recoupment in overpayment cases.

In future, the Ombudsman expects to engage with the DWP to progress legislative changes to extend his early resolution powers, following an initial consultation published in December 2018. He also expects the DWP to report on its tailored review of the Ombudsman's governance and accountability, conducted in January 2019. Additionally, a new complaints portal will be launched shortly for applications and documents to be submitted online, with this functionality extended to respondents next year.

View the annual report and accounts.

HMRC publishes Countdown Bulletin no. 47 and Pension schemes newsletter no. 112

Further issues of the Countdown Bulletin and Pensions Schemes Newsletter have been published.

Published on July 30, 2019, the Countdown Bulletin highlights administrative issues relating to the re-running of the Scheme Financial Billing and Reconciliation refund exercises. Letters to administrators of schemes in debt will be issued shortly after 15 August 2019.

Published on July 31, 2019, the Newsletter reminds administrators that where the deadline for submitting annual return information has not been met, any subsequent interim repayments will be withheld until the outstanding return and declaration are received by HMRC.

There is also a reminder that annual allowance pension savings statements for the 2018/19 tax year must be issued to members exceeding the annual allowance by October 6, 2019. A link is provided for members with DC savings to HMRC's annual allowance calculator.

Cases

Corsham v Police and Crime Commissioner for Essex [2019] and *Hazell v Chief Constable of Avon and Somerset* [2019]: potential trap for employers re-employing members with protected pension age

Pensions and tax legislation provides that members with a protected pension age of under 55 are subject to penal tax levels if benefits are taken between that protected pension age and age 55, where the member is re-employed with six months by the same employer (or one month by the same employer in essentially the same role).

These two cases involved former police officers from two constabularies (constabulary V and constabulary E) who appealed against the Pensions Ombudsman's dismissal of their complaint of breach of duty in relation to their pensions.

Background

The officers were entitled to retire after 30 years' service and did so in 2010/11, although they were under age 55 and the normal minimum retirement age was 55. Taking pension benefits before reaching 55 ordinarily produced adverse tax consequences, but the Finance Act 2004 enables avoidance of the consequences in certain circumstances. For the officers to benefit from those provisions, it was critical that they did not take employment within one month of retirement. Each was re-employed in a police civilian post within one month of retiring and such re-employment was a widespread practice as a means of retaining senior officers' skills. Each became subject to the adverse tax consequences. They claimed that their respective chief constables and police authorities had encouraged them to take up re-employment straight away and failed to inform them about the tax consequences. The Ombudsman held that there had been no breach of duty by V, E or the chief constables.

The officers' main claims were the level of the constabularies' knowledge about the one-month rule with its attendant adverse tax consequences, and the application of *Scally v Southern Health* and *Social Services Board*, where a term was implied into a contract of employment, requiring the employer to take reasonable steps to inform the employee of a valuable right conferred by the contract of which the employee could not be expected to be aware.

High Court decision

In the High Court, Morgan J allowed the appeal. He found that the Ombudsman had not made the findings of fact necessary to enable disposal of the appeals. He did not conduct a hearing, so there was no oral evidence, cross-examination, or much evidence by way of witness statements. There needed to be a more thorough exploration of the facts potentially relevant to liability, particularly the state of the police authorities' knowledge at the critical times.

The cases against the police authorities (V and E)

The police authorities, the Court said, should have known about the one-month rule as they were administrators of the scheme. The 2004 Act made significant and widely-publicised changes to the tax treatment of pensions. V knew the retirement dates of its officers and knew of the offer to re-employ them within one month, yet it still sent written confirmation to them that their lump sums would be tax free when it should have appreciated this was not the case. Those sums, if paid, would have been unauthorised payments and the authorities had made negligent misstatements about the tax position. The relationship between the authorities and the officers was sufficiently proximate to impose liability.

Scheme administrators had specific statutory duties to notify HMRC of the making of unauthorised payments and would have been liable for scheme sanction charges. V had assumed a responsibility not to make statements that it should have foreseen would be highly misleading, and which were misleading. Nowhere in the letter was a disclaimer of responsibility for the information given. The officer had no reason to suppose that there could be a problem and nobody warned him or raised the possibility with him. The relationship between V and the officers was sufficiently proximate to justify imposing liability on V for its negligent misstatements. V was not entitled to assume that the officers would seek independent advice, and the officers' failure to do so was not unreasonable. The officers had also acted reasonably in relying on the statements. Had they been given the correct information, they would have postponed the date of their re-employment to avoid the tax liability. V was therefore liable for their loss.

The Ombudsman had made no findings about the state of E's knowledge. That element of the case was remitted to him to do so.

The case against the chief constables

The claimants accepted that they had no contract of employment with their chief constables and that *Scally* could not directly apply to their situation. However, they did claim that as the relationship between a police officer and a chief constable was akin to an employment relationship, the Court should find that the chief constables owed a duty of care in tort broadly similar to the effect of the *Scally* implied term.

However, the Court found that *Scally* had been decided on narrow grounds. Even if it was possible to re-express its principle as a duty of care in tort, such a duty did not arise here. There was no right arising under the officers' quasi-employment by the chief constables of which they were unaware, as there had been in *Scally*. Even assuming that their pension benefits could be said to have arisen under their quasi employment, they were aware of those rights. The adverse issue for the officers was the tax consequences upon their re-employment by V and E. It would be a major and unjustified extension of the decision in *Scally* to hold that the chief constables had a duty to warn the officers about those consequences, as they were not responsible for administering the pension scheme or for the re-employment.

Comment

This decision relates to the specific circumstances of the retirement and re-employment of police officers, and the relationships between the constabulary and the chief constable with officers of the force. It is difficult to draw exact parallels with the situation in the private sector where the employer and the trustee are separate, as a police officer is an officer of the Crown and is a public servant but is not an employee of the police authority or the Police and Crime Commissioner. However, Courts have held previously that the relationship of the chief constable and the officer is closely analogous to that of employer and employee.

Nevertheless, the judgment is an interesting consideration of the decision in *Scally* and the status of member communications. Here, the police constabulary, as administrator of the scheme, was held liable for the officer's loss as it had stated misleadingly that his lump sum would be tax free. However, the Court found that it would be a major and unjustified extension of *Scally* to hold that the chief constable (in a quasi-employer role) had a duty to advise, inform or warn the appellants of those tax consequences.

While the case does not go as far as imposing on trustees and administrators a duty of care to inform members with a protected pension age of potential tax disadvantages where they are re-employed and take benefits early, it serves as a reminder that care is needed to ensure that protected pension ages are not lost.

In his judgment, Morgan J cited the Court of Appeal decision in *Crossley* [2004] that there was no standard legal obligation for a term in contracts of employment requiring an employer to take reasonable care for the economic well-being of his employee and that the imposition on employers of such a general duty would impose an unfair and unreasonable burden. Nevertheless, trustees should be on their guard against including in member communications incorrect information on which individuals may rely.

Issues in the pensions pipeline

October 31, 2019 – the UK withdraws from the EU, although it is (currently) unclear exactly what form Brexit will take.

October 1, 2019 – new SIP requirements beginning to come into force relating to environmental, social and governance (ESG) factors.

GMP Equalisation – DWP conversion guidance has now been published. The cross-industry working group has now published its Call to Action paper and guidance is expected throughout the rest of 2019.

Revised Funding Regime – consultation on a revised Code of Practice is expected "in the summer" with technical provisions expected to remain broadly as they are, with the main change being the addition of a secondary long-term funding target.

New Pensions Bill is now unlikely before the Autumn 2019, as the Queen's Speech has been postponed. It is expected to include provisions covering the Pensions Dashboard, the Regulator's powers, the revised Funding Regime, DB Consolidators and the Money and Pensions Service.

EMIR – new requirements to the exchange variation margin relating to derivatives applied from March 1, 2017. A further EMIR temporary exemption extension for pension scheme arrangements applied to 16 August 2018 and has now expired. On May 28, 2019, the EMIR amending regulation was published and was implemented on June 17, 2019. Under the amendments, the clearing requirement is not activated for the first two years, and the exemption may also be extended twice more, each time by a further year if "*... no viable technical solution has been developed and that the adverse effect of centrally clearing derivative contracts on the retirement benefits of future pensioners remains unchanged.*" The UK Government has confirmed that, as far as possible, the regime set out in the EMIR legislation will not change after the UK has left the EU.

October 1, 2020 – new disclosure obligations apply for trustees in relation to scheme's Statement of Investment Principles under the Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019 following the transposition into UK law of the revised Shareholder Rights Directive (SDR II).

October 1, 2021 – new requirements apply for trustees to publish information on a publicly available, free website relating to voting and capital structure of investment companies under the Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019 following the transposition into UK law of the revised Shareholder Rights Directive (SDR II).

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