Essential UK Pensions News

May 2020

Introduction

Essential UK Pensions News covers the latest pensions developments each month.

UK pensions: Regulator's annual DB funding statement urges collaboration to meet COVID-19 challenges

On **April 30, 2020**, the Pensions Regulator published its 2020 funding statement for defined benefit (DB) schemes with valuation dates between September 22, 2019, and September 21, 2020. However, these COVID-19 times are challenging for all businesses, and the effects of the pandemic are relevant to all DB schemes. The key points are set out below, with more detail to be found in our May 2020 pensions briefing.

The statement urges collaboration between trustees and employers to manage scheme funding impacts and to maintain a focus on the long term, particularly regarding planning and risk management. With the uncertainty of the COVID-19 crisis, effects will be marked on both the short-term business impact of the lockdown and the longer-term effect on the economy and stock markets. Heavy exposure to markets, and insufficient hedging, will mean a sharp fall in funding levels, and the Regulator expects contingency plans to be implemented where possible.

In all the current economic upheaval , the Regulator has made clear its intention to continue with its publication of a new DB funding code, although probably not until late 2021. We are holding a webinar on **May 28, 2020 at 11am** on the implications for schemes of the Regulator's annual funding statement and you can sign up here.

Trustee-employer collaboration

The Regulator sets out the five key areas of analysis for schemes from how post-valuation experience is taken into account, with a potential change to the valuation date, to benefit affordability, funding recovery plans and shareholder distributions. It clearly expects trustees to be front and centre of any employer plans made to deal with scheme funding and any actions taken in weathering the COVID-19 storm. It emphasises that trustee-employer collaboration is essential. It also warns that it fully expects trustees to ensure that the scheme is remembered as a creditor when employers begin to rebuild their balance sheets, having been supported financially by a deferment of scheme contribution payments.

Expectations of trustees

Having detailed its scheme specific considerations, the Regulator turns next to trustees. Paying the promised benefits is the key objective for all schemes, requiring both foresight and an integrated risk management framework. The Regulator expects trustees and employers to agree a clear strategy with this long-term goal in mind, recognising how balancing investment risk, contributions and covenant support may change over time. The first of the principal areas considered is the scheme's long-term funding target (LTFT) and the Regulator explains its expectations in advance of the future Pension Schemes Bill. The LTFT sits above the scheme's technical provisions, and will need to be considered for all schemes ahead of the appearance of the revised DB funding code, whenever that may now be.

Scheme covenant

The Regulator deals with covenant issues, and examines assessment, monitoring and covenant leakage in depth.

It makes clear that in return for the trustees' bolstering of employers under financial pressure by deferring scheme contributions, it does not expect the scheme ultimately to be disadvantaged. It recognises that ongoing employer support is essential to enable trustees to realise the scheme's objectives of paying all benefits to members but employers must play their part and compensate the scheme when their financial position improves in time.

Managing risks

Echoing previous statements, the Regulator continues to expect trustees to take an integrated approach to managing the three main areas of risk – investment, funding and covenant. This year, although this focus is continued, the Regulator expects scheme maturity to assume greater significance in setting future funding and investment strategies, as an increasing proportion of the membership reaches retirement age and draws benefits.

As before, the Regulator segments the DB scheme population into five categories in tabular form according to covenant strength, with each class then divided further according to scheme maturity. The table should be read in conjunction with both the current DB funding code and the Regulator's recently published guidance on COVID-19. In the current climate it is likely that the trustees' assessment of where their scheme now lies in the structure may well have changed from last year. Trustees should assess the impacts of both COVID-19 and Brexit so that they can judge which section of the table best reflects their scheme's situation, thus indicating future action.

What schemes can expect from the Regulator

Although the Regulator has suspended its other planned initiatives, the principles remain important and will be kept under review when the work is restarted. Focus is now on understanding and supporting trustees in responding to the impact of the pandemic, while ensuring the employer easements it has made are not abused.

The statement concludes by reminding trustees and employers that its suite of powers include directing how a scheme's technical provisions should be calculated, how a deficit should be funded and over what period. Such power can be used where there is a failure to agree the valuation assumptions or recovery plan, and investigations may be instigated where trustees or employers have not followed the expectations set out in the statement, codes and other guidance.

Comment

The Regulator is clear what its expectations are in trustees' and employers' approach to scheme funding during the current crisis and beyond. They are warned that they may well be called upon to justify their decisions on their current valuation process, providing evidence of robust negotiations having taken place.

The Regulator reminds trustees and employers of the extent of its moral hazard powers. Schemes must be treated fairly where employers seek to avail themselves of the Regulator's current easements, with no abuse of the these relaxations being tolerated.

The Regulator packs its usual punch in terms of setting out what will, or won't, be considered compliant. It explains how it envisages scheme treatment in circumstances of a weakened employer covenant. Trustees and employers need to take advice from their actuaries, lawyers and covenant advisers, in order to best cope with the economic fallout of the pandemic. Various forms of "covenant leakage" affecting the scheme's funding position may attract the Regulator's gaze, so decisions and approaches must be justifiable. It is likely that the eventual new DB funding code, together with the increased regulatory powers under the Pension Schemes Bill once it is enacted, will "up the ante" still further.

View the funding statement.

Regulator urges pensions industry to follow COVID-19 related easements and guidance to protect members' benefits

On **April 15, 2020**, the Pensions Regulator released a statement to urge the pensions industry to make use of its recently introduced easements and guidance to prevent members from making "hasty decisions" regarding their pensions.

Charles Counsell, the Regulator's chief executive officer, noted that the industry should focus on "heightened risk of members being targeted by scammers" following its recent joint warning (with the FCA) for pension savers, and aim to protect members' benefits.

Amid the ongoing pandemic, Counsell acknowledged that transfer requests may take longer to process, adding that the Regulator will not act against scheme trustees who need to reassess how transfers are calculated or prioritise making pension and bereavement payments in the next three months.

Furthermore, Counsell stated that since "providers and trustees are the first line of defence in protecting savers from pension scams", he encourages them to use the FCA's latest guidance to ensure savers make informed choices.

Government's CJRS extended and further guidance issued

On **April 20, 2020**, the Government's scheme of financial support for those companies that need to furlough some or all of their staff due to the COVID-19 emergency opened for grant applications.

On **April 17, 2020**, HMRC published an employer step by step guide to help employers with the application process along with related guidance on how to work out 80 per cent of wages, NICs and pension contributions. An online calculator is included, with further guidance on how to claim being added on April 20, 2020.

On **May 12, 2020**, HM Treasury published a press release announcing that the CJRS would be extended for a further four months to **October 31, 2020**, across all regions and sectors in the UK. There will be no changes to the scheme until the end of July 2020. From August 2020:

- Employees will be able to return to work on a part-time basis.
- Employers will be required to pay a percentage towards the salaries of their furloughed employees; and
- The employer's payments will substitute at least part of the Government's contribution under the CJRS, ensuring that any furloughed workers continue to receive 80 percent of their salary (up to the maximum of £2,500 a month).

The press release does not make clear whether the employer will be required to pay the full 80 per cent (up to £2,500) from August 2020, or whether they will continue to be able to reclaim a proportion of employees' furlough pay under the scheme, or what that proportion might be. More specific details of the changes and their implementation are due to be made available by the end of May.

Regulator issues guidance on salary sacrifice and DC auto-enrolment scheme certification for large employers

On **April 17, 2020**, the Regulator published its COVID-19 technical advice for large employers. It focuses on two specific areas of interaction between normal pension contribution calculations and the CJRS:

- Contributions where there is a salary sacrifice arrangement
- DC certification as a qualifying scheme for auto-enrolment purposes

and provides several practical examples.

Salary sacrifice – in summary, the Regulator makes the following points about salary sacrifice arrangements:

- For furloughed workers in salary sacrifice arrangements for pension contributions, contractual obligations and scheme rule provisions continue to apply; and
- As all of the grant claimed under the CJRS must be paid to the worker in the form of money, payroll processes may need to be amended to calculate the pension contribution due to the scheme under the CJRS.

The operation of salary sacrifice for pension contributions is separate from the auto-enrolment provisions and contributions set out under the scheme rules, and obligation is on the employer to pay the total contribution, however it is calculated.

The guidance for CJRS states that when calculating 80 per cent of a furloughed worker's salary or wage, employers should use the reference salary is the amount after the salary has been sacrificed. The pay during the furlough period should be treated as the post-sacrifice pay so that no further sacrifice is made on that amount. Government guidance on how to calculate both the reference salary and the grant is due shortly.

The Regulator warns that if an employer wants to claim a grant through the CJRS then it may have to agree a reduction in pay with their employee. This is because the grant only covers the lower of 80 per cent of furloughed workers' pay or £2,500 a month plus the associated employer's national insurance contribution costs and pension contribution up to the level of the auto-enrolment statutory minimum employer contribution.

DC auto-enrolment certification – some employers certify that their scheme meets an alternative auto-enrolment statutory minimum contribution requirement and can therefore be treated as a qualifying scheme. In such cases, the definition of pensionable pay under the scheme rules is likely to be different from qualifying earnings. Pensionable pay may include basic pay without overtime or bonuses and may require contributions to be deducted from the first penny earned. The provisions of the pension scheme rules are unaffected by the CJRS. The employer calculates, deducts and pays the pension contribution under the scheme provisions as normal.

Where employers have a mixture of furloughed and non-furloughed staff, they may need to recertify in respect of the non-furloughed staff.

The Regulator's April 9, 2020 general guidance on COVID-19 and auto-enrolment was updated on **May 6, 2020**. The updated guidance now includes a section titled "Automatic enrolment duties for furloughed staff", which includes practical guidance for employers on three key issues:

- Enrolling employees who become eligible during furlough leave. The guidance confirms that employers must still enrol (or postpone) employees if they meet the eligibility requirements, irrespective of whether the employee is furloughed or not. If an employee's pay increases after the furlough has ended, the employer must continue to assess them and enrol them if they are eligible.
- Automatic re-enrolment. If the third anniversary of an employer's staging or duties start date falls during the furlough period, it can choose a date up to three months after its third anniversary to assess staff.
- Requests to join a pension scheme. The guidance states that any furloughed member of staff can ask to be put into the pension scheme at any time including during the furlough period.

Regulator expands its COVID-19 guidance for DC schemes

On **May 13, 2020**, the Regulator published expanded COVID-19 guidance for DC scheme trustees, which has now been renamed *DC scheme management and investment: COVID-19 guidance for trustees*.

The updated guidance now reflects the Regulator's separate guidance for employers on reducing auto-enrolment contributions to the statutory minimum, which was updated on **May 6, 2020**. This provides that, if certain conditions are met, including that the reduction applies only in relation to workers who have been furloughed under the CJRS, a regulatory easement will apply under which the Regulator will take no action where an employer fails to consult with affected members for the 60-day period required by law.

The expanded guidance adds that if a rule change is needed to reduce employer contributions and trustees are responsible for exercising their scheme's amendment power (either solely or jointly with the employer), they must be mindful of their duty to act in members' best interests. According to the Regulator, this could include factoring in the likelihood of the employer no longer continuing as a going concern without a reduction in contributions, provided this risk is genuine and the trustees have considered whether any change could be temporary.

The expanded guidance also covers transfers. The Regulator says it expects trustees and their administrators to prioritise these as core financial transactions, notwithstanding the pandemic. Given the risk that delays in making payment may cause reductions in transfer values if investments fall, the guidance emphasises that it is important for transfers to be processed within a reasonable timeframe, making sure due diligence has been undertaken.

Consultation on reform of RPI extended to summer 2020

Chancellor of the exchequer Rishi Sunak has extended until August the consultation on how the retail price index should be reformed, to give businesses more time to respond. In a letter to Sir David Norgrove, Chair of the UK Statistics Authority, published on **April 16, 2020**, the Chancellor said he was extending the consultation period by four months to **August 21, 2020** in light of the coronavirus crisis.

The extended date will also depend on coronavirus-related developments, with the Government's response due in the autumn.

The consultation seeks views on the proposal to align the RPI with the consumer price index including housing costs, which is expected to lower its annual rate by an average of one percentage point.

HM Treasury publishes Direction on CJRS

On **April 15, 2020**, HM Treasury published a 12-page Direction on the Coronavirus Job Retention Scheme, and it is possible that further updates will be issued.

The Direction deals with employment issues relating to the CRJS and requires HMRC to pay the amounts set out under Sections 71 and 76 of the Coronavirus Act 2020.

The CJRS applies to all employers with an HMRC registered (on the real time information system) PAYE scheme by **March 19, 2020** (the date was previously **February 28, 2020**). Eligibility will depend on when an employer submitted pay information to HMRC. If an employer has more than one scheme, a claim must be made in respect of each PAYE scheme. The CJRS has effect only in relation to earnings paid or payable to furloughed employees for the period **March 1, 2020** to **June 30, 2020** (the original end date was May 31, 2020 but an extension was announced on April 18, 2020), together with employer NI contributions and "directed pension payments" in relation to such earnings.

Furloughed employees – the Direction makes clear that the CRJS is not limited to employees who would otherwise have been made redundant. An employee is furloughed if:

- They have been instructed to cease all work for the employer;
- The period of cessation is 21 calendar days or more; and
- The instruction is given by reason of coronavirus.

Employers should keep a clear written record to evidence each of these points and are due to be able to submit claims via the HMRC portal from **April 20, 2020**.

Pension payments are reclaimable under CJRS if they are paid in respect of an amount of gross earnings not exceeding the lower of £2,500 pm and the employee's reference salary (detailed in paras 7.1-7.15). An employer's auto-enrolment duties continue under furlough, and employers can claim the statutory minimum pension contribution – 3 per cent – under the CRJS.

An employer may have to pay more than the statutory minimum auto-enrolment contribution included under the CJRS where, for example, it tops up salary or where pension scheme rules provide for a contribution rate of above 3 per cent of qualifying earnings. Any excess above the minimum contribution will not be met by the CRJS and employers should continue to make the correct contributions under the scheme, meaning an employer could have to pay some of the pension contribution itself. Grants for pension contributions can be claimed up to this cap provided the employer will pay the whole amount claimed to a pension scheme for the employee as an employer contribution.

The guidance acknowledges that employers may wish to decrease auto-enrolment contributions to the statutory minimum and the Pensions Regulator will not take regulatory action in respect on a failure to consult "for the full 60 days".

UK Pensions: Regulator's warning that members requesting transfers during the pandemic may be making a poor decision

On April 29, 2020, the Regulator added to its already impressive library of COVID-related publications with new guidance for trustees on Communicating with members when they request a transfer or to access benefits.

The Regulator says that scheme members might consider transferring their pension due to the current financial uncertainty around investments, or to access their funds by retiring from the scheme when they wouldn't otherwise have done so. This is a critical moment for them. They are irreversible actions that will have a lasting impact on the member's retirement benefits.

Trustees should be alert to the risks and support members to make an informed decision in the following ways:

- Provide appropriate warnings of the risks and implications of their chosen option (this is required where members are seeking to access DC benefits);
- Read the guidance from the Financial Conduct Authority (FCA) which can help them to outline the types of risks members should keep in mind;
- Encourage members to take regulated independent financial advice to understand their options;
- Encourage members to ask questions of their financial adviser to identify any increased risks associated with how the member has decided to access their pension funds; and
- Highlight the free and impartial pensions guidance offered by Pension Wise, including telephone appointments and online information.

Specific guidance on DB to DC transfers

The Regulator reiterates that transferring out of a DB pension scheme into a different type of pension arrangement is unlikely to be in the member's best long-term interests, as a DB scheme promises a pre-determined level of benefits that is underwritten by an employer, usually with an additional layer of protection offered by the PPF.

A template letter (prepared jointly by TPR, the FCA, and the Pensions Advisory Service) is provided, which the Regulator says should be issued to all members requesting a CETV quote. It contains information on points the members should consider before making a decision and where they should go for impartial guidance. Trustees should actively monitor the number of requests for CETV quotes received and which advisers are supporting the members' request. If trustees identify unusual or concerning patterns, such as spikes in CETV requests or the same adviser across a multitude of requests, they should contact the FCA on DBTransferSchemeInformation@fca.org.uk.

There is a reminder that where a DB transfer value is more than £30,000 and members want to transfer benefits to a DC scheme, they are required by law to take advice from a financial adviser firm who is authorised to advise on transfers by the FCA. Trustees are reminded to refer to the Regulator's DB to DC transfer guidance on the communications they need to give members when managing DB transfer requests.

PPF reassures levy payers of minimal impact on levy due to pandemic

On **April 28, 2020**, the PPF published a statement aiming to reassure levy payers that the COVID-19 pandemic will have very little impact on the amount of levy it expects to charge in the autumn.

Although there has been speculation that the levy will be raised, the PPF has said that the impact of the crisis on the amount of levy it will collect this year will be minimal because the rules used to calculate the levy were fixed before the current pandemic. It added that in calculating the levy invoices it will be using information that was largely collected before the economic impact of COVID-19 became significant.

HMRC publishes Pension schemes newsletter no. 119

On **April 30, 2020**, HMRC published its latest edition of the Pension schemes newsletter, which includes:

- Confirmation that protected pension ages will not be lost where individuals aged between 50 and 55 who are re-employed within six months of retirement, where the individual has returned to work in relation to COVID-19 (for example, to work in the NHS);
- HMRC will not be issuing "notices to file" pension scheme returns for 2019 to 2020, due to the difficulty administrators are experiencing in obtaining the valuations needed to complete the return;
- TTransfers made to Gibraltar following the UK's exit from the EU will be treated as they were before the UK left the EU. When the position after the transition period becomes clear, HMRC will update the Pensions Tax Manual;
- Confirmation that where a member designates funds for a drawdown pension and the administrator needs to value the benefits against the lifetime allowance, alternative methods of valuation may be used where trading has been suspended or closing prices do not reflect proper market value of shares as a result of coronavirus; and
- For other valuations of pension scheme assets, normal methods should be used, but where this is not possible, the administrator must be able to demonstrate and support any alternative method used.

HMRC also confirms that the annual allowance calculator has been updated to reflect the changes to the threshold and adjusted income allowances, as well as the minimum tapered annual allowance for the 2020/21 tax year.

View the newsletter.

Legislation

LGPS regulations amend exit credit provisions – the Local Government Pension Scheme (Amendment) Regulations 2020

Changes to the regulations governing the Local Government Pension Scheme (**LGPS**) have been finalised. The LGPS (Amendment) Regulations 2020 came into force on **March 20, 2020**, but have partial retrospective effect to **May 14, 2018**.

The regulations amend the LGPS Regulations 2013 making changes to the mechanism for calculating exit credits payable to employers ceasing to participate in the LGPS. In particular, the amending regulations create a discretion for administering authorities to determine the amount of the exit credit. In exercising this discretion, the authority must have regard to a list of factors including:

- The extent to which there is an excess of assets over liabilities in the fund relating to the employer;
- The proportion of this excess of assets which has arisen because of the value of the employer's contributions;
- Any representations to the administering authority made by the exiting employer and, where the employer participates in the LGPS by virtue of an admission agreement, any body providing an indemnity or bond for it; and
- Any other relevant factors.

The amending regulations provide that an administering authority should exercise its discretion in determining the amount of an exit credit within six months of the employer exiting the scheme, unless a longer period is agreed between the authority and the exiting employer. Although the amending regulations are stated to apply retrospectively to **May 14, 2018**, a transitional provision specifies that the amendments do not apply to exit credits that have been paid on or after **May 14, 2018** and before **March 20, 2020**.

New criminal investigatory powers for the Pensions Regulator: Investigatory Powers (Communications Data) (Relevant Public Authorities and Designated Senior Officers) Regulations 2020

The draft Investigatory Powers (Communications Data) (Relevant Public Authorities and Designated Senior Officers) Regulations 2020, published on **April 21, 2020**, propose amendments to the Investigatory Powers Act 2016 to give the Pensions Regulator new powers which include the right to harvest communications data.

Under the proposed provisions, the Regulator "is given the power to obtain communications data, where it is wholly or partly events data, for the purpose of preventing or detecting serious crime, and in any other case, for the purpose of preventing or detecting crime or of preventing disorder". A spokesperson for the Regulator said that scammers are a key target of the new powers.

The Regulations will give the Regulator the power to obtain communications data for an "applicable crime purpose". This means preventing or detecting serious crime, where the data is wholly or partly "events data", and preventing or detecting crime or preventing disorder in any other case. Events data is defined in the Act to mean any data which identifies or describes an event (whether or not by reference to its location) on, in or by means of a telecommunication system where the event consists of one or more entities engaging in a specific activity at a specific time. The senior officers at the Regulator who may authorise the obtaining of communications data in urgent cases are listed as a "Head of Department in an enforcement or intelligence role".

The draft Regulations are due to be made under the "enhanced affirmative procedure", which provides for draft regulations to be made 40 days after they have been laid before Parliament, following approval by both Houses, and so long as an explanatory document has also been laid. In a report published on May 7, 2020, the House of Lords Scrutiny Committee suggested that the explanatory memorandum accompanying the draft Regulations should be revised to incorporate the contents of the separate document, which it noted had been laid before Parliament, but not made publicly available.

Cases

High Court upholds Ombudsman's decision that RPI "hard-coded" into scheme rules: *Carr v Thales Pension Trustees Ltd* [2020]

In a judgment handed down on **April 22, 2020**, the High Court has upheld a determination of the Pensions Ombudsman on the interpretation of the Thales UK Pension Scheme's pensions increase rule.

The case was originally brought before the Ombudsman by pensioner member Mr Carr, after Thales sought to adjust the way it calculated inflation in line with the consumer price index, which runs about one percentage point lower than RPI. CPI is generally considered to be the more accurate reflection of real inflation, but compounded over the years this less-generous index could result in retirees each losing substantial amounts of pension benefits.

The Scheme's rules stated that pensions in payment would be increased on April 1 each year by:

"... the percentage increase in the retail prices index…..subject to a maximum of 5 per cent as specified by order under Section 2 of Schedule 3 of the Pensions Schemes Act."

At the time that the rule was drafted, the revaluation order under the Pension Schemes Act 1993 specified RPI, but from 2010 onwards the order referred to CPI following the Government's decision to switch to CPI, and consequently the two limbs in the increase rule were inconsistent.

The Ombudsman determined that the ordinary and natural meaning of this provision was that the rate of pension increases should be RPI, meaning that the first limb of the rule prevails. He directed that the switch (which had already been made) be unwound and affected members put back where they would have been, with interest. The employer appealed to the High Court, contending that on a true construction of the pension increase rule, the trustee was right to adopt CPI.

The High Court judge acknowledged that a key issue was to identify which of two inconsistent provisions in the scheme rules should prevail, He agreed with the Ombudsman and held that a "natural and ordinary" reading of the relevant rule gave primacy to the limb that provided for increases to be in line with the RPI, subject to a maximum of 5 per cent. The judge commented that "it is not always easy to articulate with precision why one reading of a disputed phrase seems more natural and ordinary than another", noting that this was "an accumulation of experience of how language is ordinarily used".

Comment

This is another in a string of cases on the way pension increase rules are interpreted. Under the Thales rules, pensions increases must now be measured in line with RPI, which will prevent the employer saving in the region of £20 million in liabilities. The case highlights the difficulties experienced by employers in trying to move from RPI to CPI as the measure for inflation where scheme rules are in the slightest ambiguous.

Earlier this year the UK Statistics Authority proposed aligning RPI, which is used by the Treasury but consistently overstates inflation, with CPI, including housing costs. However, as noted above, chancellor Rishi Sunak has announced an extension to the consultation, originally due to end on April 22, 2020 to **August 21, 2020** amid the coronavirus pandemic.

High Court considers what happens when the composition of the applicable index changes: *Ove Arup & Partners International Ltd v Trustees of the Arup UK Pension Scheme* [2020]

In *Ove Arup & Partners International Ltd v Trustees of the Arup UK Pension Scheme* [2020], "The Index" was defined in the scheme rules as "subject to Rule H1.03 (Changes in the Index), the Index of Retail Prices (All Items) published by the Office for National Statistics". Rule H1.03 stated:

"If the composition of the Index changes or the Index is replaced by another similar index, the Trustees, after obtaining the Actuary's advice, may make such adjustments to any calculations using the Index (or any replacement index) as they consider to be fair and reasonable".

The employer applied for Court declarations on whether the trustees were obliged, or at least had the power for the future, either to change the relevant index from RPI to CPI or CPIH or, if this were not permitted, to make adjustments to calculations using RPI that would achieve the same effect. It argued that RPI had been "functionally" replaced by CPI and CPIH because those indices were regarded as the main measure of consumer price inflation from March 14, 2013.

Alternatively, the employer sought adjudication on whether three changes to RPI made between 2010 and 2017 amounted to a change of composition in the index, entitling the trustees to make adjustments to their annual pension increase calculations.

The Court considered two trigger events:

- Had the Index been replaced? The judge concluded that the Index had not been replaced because (following the Supreme Court in Barnardo's,) the "…RPI is "replaced" only if it is discontinued and another similar index is introduced or declared by the responsible body to be in its place, and that the Rule does not contemplate any form of "functional" replacement". So, the question of the powers and duties of the Trustees did not arise; and
- Had the composition of the Index changed? The judge's view was that "a substantial change must be produced in the end result" and that any such change could not be at a date earlier than the adoption of the latest set of Rules, as the relevant wording implied a future change. Therefore, each time a new set of rules was adopted, it re-set the clock and the "Index" as defined was the RPI as it existed at the adoption of the latest version of the rules in 2013.

The judge also noted that counsel for both the trustees and the employer had drawn his attention to the "numerous" cases that have addressed whether RPI could be replaced by CPI in other schemes, including several which considered what constitutes the "replacement" of an index. Bearing in mind the Barnardo's approach to the proper interpretation of pension scheme rules, he did not refer to them in his judgment, on the basis that:

"…they do not lay down general principles and even to the extent they indicate what the judge considered to be the normal or ordinary meaning of a word, it would be so necessary to expand on the particular context that it would be questionable whether any real assistance could be derived for this case."

Comment
Given that there are many variations on increase and revaluation rules, it is likely that questions such as those outlined above will continue to come before the Courts. Whilst some general principles can be drawn from these cases, they may be of only limited use for schemes with as yet untested RPI definitions.

However, depending on the outcome of the consultation on the future of RPI, it is possible the issue may fall away entirely if there is no eventual differentiation between the RPI and CPIH measures.

High Court decides coincidence of parties' intentions satisfied rectification test – *Lloyds Bank Plc v Lloyds Banking Group Pensions Trustees Ltd and others* [2019]

In a judgment from December 11, 2019, although it has only recently become available, the High Court has granted a summary judgment application for rectification of a secretarial error in the Lloyds Bank Pension Scheme No. 1 in *Lloyds Bank Plc v Lloyds Banking Group Pensions Trustees Ltd and others* [2019]. This was to correct a mistake made upon the consolidation of the scheme rules in 2005, whereby a provision was omitted regarding a state pension deduction from the payable benefits. The effect was to appear to confer a very substantial benefit to deferred members.

The Court applied the test for rectification confirmed recently in 2019 in *FSHC Group Holding Ltd v GLAS Trust Corporation Ltd*. Not only did this decision clarify that the intentions of the parties must be assessed subjectively, but it also accepted that in such pensions cases it was sufficient for the parties to have a "coincidence of intention" that could be separately demonstrated rather than an outward expression of accord.

In the Lloyds case, the Court was satisfied that the scheme rule consolidation exercise was clearly intended to reflect changes by previous amendments and legislation. The evidence was clear that there was "no intention" to alter the SPA provisions and "no sensible basis" on which the Bank or trustee could have intended this.

The scheme had been administered as if the error had not occurred and the case provides a good example that conduct after the date of the relevant document can constitute evidence of the intention of those executing it. As to later deeds containing the same error, following Warren J in *IBM United Kingdom Pensions Trust Ltd v IBM United Kingdom Holdings Ltd and others* [2012], it was held that the claimant need only show that the parties intended the scheme members to have their lawful benefits.

Procedurally, the Court approved of the use of the confidential opinion procedure on behalf of the representative beneficiary, as a "helpful and worthwhile exercise". It was also confirmed that it was good practice for the scheme members to be notified of the proposed application, but this was not a strict requirement.

Pensions Ombudsman: GMP equalisation and trivial commutation – Mrs S

The Pensions Ombudsman has dismissed a complaint brought by a member of an occupational pension scheme who argued that the scheme had failed to fulfil a commitment to pay her benefits in the form of a trivial commutation lump sum (TCLS).

Background

Although a guaranteed minimum pension (GMP) can be commuted as part of a TCLS, since the decision in Lloyds Banking Group Pensions Trustees Ltd v Lloyds Bank Group plc in 2018, many schemes have suspended such payments where they include commutation of GMPs pending confirmation by HMRC of the impact of subsequent GMP equalisation adjustments on the requirement to discharge all benefits. This is because the conditions applying to a TCLS include that the payment must extinguish the member's entitlement to defined benefits under the scheme and that the £30,000 limit must be met at a specific "nominated date", which must be a date within three months of the first TCLS payment. The receipt of a GMP equalisation top-up would, on the face of the tax legislation, undo the previous satisfaction of these conditions and could risk the whole payment attracting an unauthorised payments charge.

Facts of the case

Following the *Lloyds Bank* judgment, the member was informed that if any additional benefit payments were due after GMP equalisation, there was a risk that the TCLS could constitute an unauthorised payment and result in tax charges from HMRC as it might not extinguish the member's entitlement to benefits under the scheme. After obtaining legal advice, the scheme's trustee suspended all trivial lump sum payments.

The member argued that she had signed and completed all the necessary paperwork to require the scheme to pay the TCLS, so the administrator should make the payment (of just under £5,000) in full as promised.

The Ombudsman found there was no maladministration, as the trustees had a duty to protect the scheme and its members from potential tax charges that could arise following GMP equalisation. Completing the paperwork for the trivial lump sum did not provide the member with an entitlement to receive her benefits, as the process had been incomplete. The FA 2004 did not make TCLS payments mandatory, thus the trustee's decision to withdraw the option was not incorrect and it had done so for valid reasons.

The Ombudsman held that the member had not lost her benefits in the scheme but was simply not permitted to receive them in the manner she had originally requested. He indicated that the member could transfer her benefits to another provider that offered trivial commutation.

Comment

The member deserves some sympathy for having her payment request refused after complying with the scheme's requirements. However, the impact of the Lloyds Bank case made the trustee's decision to suspend such payments the most prudent option given that there was the potential for any GMP top-up to invalidate the entire payment. Balanced against possible punitive tax charges, the decision to suspend such payments was justifiable.

Pensions Ombudsman: Mr N (PO-22730) – employer responsible for failure to notify member of changes to late retirement factors affecting his benefits

The Pensions Ombudsman has given his determination in Mr N's complaint against Police Scotland.

Facts

Mr N was a member of the Lothian Pension Fund (the **Fund**), which was part of the Scottish Local Government Pension Scheme. The scheme's administrator, Scottish Public Pension Authority, issued a circular which indicated that the new actuarial guidance concerning late retirement factors would come into effect on June 24, 2017, by which time, Mr N was aged 68 years and 7 months. The normal pension age under the scheme was 65, thus Mr N was classified as a late retirement member.

Although the circular stated that scheme members considering late retirement should be informed about the changes as soon as possible, Mr N argued that he had not been made aware of the changes until he accidentally discovered the circular in March 2018.

Mr N raised an enquiry with the Fund, which responded that their February 2017 employer bulletin had been issued to Mr N's employer, Police Scotland. However, Police Scotland claimed that the Chief Constable had not been included in the Fund's distribution list, thus the information was not available via its intranet.

Police Scotland also rejected Mr N's complaint, noting that it was not a matter for its grievance procedure, and failed to respond to his subsequent complaints.

Determination

The Ombudsman upheld Mr N's complaint, agreeing with the Adjudicator's opinion. He held that the employer, Police Scotland, had undoubtedly received the February 2017 bulletin, and the employer had a reasonable time to implement the new late retirement factors.

Police Scotland argued that since the changes to the calculation of late retirement factors constituted an administrative change rather than a benefit change, the obligation to notify Mr N fell to the scheme manager instead. The Ombudsman disagreed, concluding that as a reasonable employer, Police Scotland had a duty of care to notify Mr N of the implications of the changes on his retirement benefits.

Ombudsman's directions

The Ombudsman directed Police Scotland to request the administrator to calculate Mr N's late retirement benefits on the assumption that Mr N would have elected to take his pension on June 23, 2017. Police Scotland was also ordered to pay any arrears of pension Mr N was entitled to, including any tax-free cash, plus interest from June 23, 2017 to the date of payment. Future pension payments were to be calculated on the late retirement basis provided by the administrator.

Mr N was also awarded £2,000 for the severe distress and inconvenience caused by Police Scotland's action and its failure to respond to his complaints.

Comment

This seems rather a harsh decision from the employer's (Police Scotland's) point of view. The starting point is that an employer has no general common-law duty to inform employees of their rights under the contract of employment. However, this case re-examines the issue of an employer's duty of care to employees as pension scheme members. It is not the first time this issue has been considered by the Courts and the Ombudsman.

In *Corsham v Police and Crime Commissioner for Essex* [2019] (an appeal from an Ombudsman's determination) the High Court held that police authorities, as the administrators of police pension schemes, should have known about the provisions in the Finance Act 2004 regarding taxation of pensions, and about the adverse tax consequences arising where police officers were re-employed into civilian roles within one month of retirement. The Court found that the employer had a duty of care regarding the impact of re-employment on a protected pension age.

In *Corsham*, the judgment took into account the decision in Scally and the status of member communications. The police constabulary, as administrator of the scheme, was held liable for the officer's loss where 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.

The *Corsham* decision related to the specific circumstances of 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.

While the *Corsham* case did 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 served as a reminder that care is needed to ensure that protected pension ages are not lost. The Corsham case also involved an incorrect statement that lump sums would be tax free.

In Mr N's case, the Ombudsman did not include any consideration of previous authorities on the employer's duties, although Mr N's case did not involve a misstatement by the administrator of benefit entitlements.

In *Corsham,* the judge 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 and employers should be on their guard to ensure that member communications are readily available to all members as soon as possible after they are issued and that they contain accurate information.

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