

# Pensions Legal Update

## Legal Update Contents

## Page

1. TUPE transfers: early retirement provisions
3. Capping pensionable pay increases: contractual agreement

## TUPE transfers: early retirement pensions

**Summary:** The High Court has provided some clarification on the transfer of early retirement rights under occupational pension schemes under the Transfer of Undertakings (Protection of Employment) Regulations 2006 (*SI 2006/246*) (TUPE 2006).

**Background:** On the relevant transfer of an undertaking, employees, together with the rights and liabilities connected with their employment contract, automatically transfer from the selling employer to the buyer (*regulation 4, TUPE 2006*). However, there is an exception for any terms relating to an occupational pension scheme to the extent that they relate to “benefits for old age, invalidity or survivors” (the carve out).

The European Court of Justice (ECJ) has held that early retirement benefits under an occupational pension scheme on redundancy or agreed voluntary severance were not within that carve out because the employee became entitled to them before reaching normal retirement date (NRD) (*Beckmann v Dynamco Whicheloe Macfarlane Limited; Martin v South Bank University*). In both cases, the obligation to provide those benefits transferred from the seller to the buyer.

The scope of *Beckmann* and *Martin* is unclear and buyers of businesses where employees were members of occupational pension schemes often seek an indemnity from the seller against the risk of liability for early retirement rights transferring to them.

**Facts:** This case arose from the sale of a business by P to S. The asset sale and purchase agreement provided for the purchase price to be adjusted to take account of any accrued pension liabilities that transferred to S under TUPE 2006.

P’s pension fund (the fund) was a defined benefit scheme that allowed early retirement from service with employer consent. The transferring employees became deferred members of the fund on the sale to S. On early retirement as deferred members, they would miss out on two “enhancements” that were available to members retiring from service, namely:

- A bridging pension payable until state pension age.
- For those without 15 years’ continuous service, the ability to accrue further service to bring them up to 15 years (at which point more generous early retirement reduction factors would apply to the pension).

The questions for the court were:

- Whether liability to provide any early retirement rights under the fund transferred to S under TUPE 2006.
- If so, whether it was the liability to provide the full early retirement pension which passed, or just liability to provide the enhancements.
- Whether a pension that came into payment before NRD would always be outside of the carve out even if it continued to be paid after NRD.

**Decision:** The court held that:

- Because the member could have the enhanced early retirement benefits only with employer consent, what transferred under TUPE 2006 was the right to be considered for early retirement. It was therefore open to S to decide not to give consent (provided it acted in good faith in taking that decision).
- The liability that transferred to S was the liability to provide the enhancements, rather than the full early retirement benefit. The deferred pension to which the member was already entitled from the fund satisfied the liability for standard level of benefits and S did not have to duplicate those benefits. Otherwise, the employee will get a windfall benefit.
- The pension instalments payable after the member reached NRD should be categorised as “old age benefits” and therefore apparently within the carve out, even if the pension had come into payment before that date.

**Comment:** The decision provides some useful clarification, but leaves open important issues such as: how to put a value on early retirement enhancements where these are not provided as of right; how a buyer should exercise the power to consent to early retirement; and, if an enhanced early retirement benefit becomes an old age benefit after NRD, who is liable to provide the enhanced element of the benefit after NRD. We understand that the case is to be appealed.

*Case: The Procter & Gamble Company v Svenska Cellulosa Aktiebolaget SCA and another [2012] EWHC 1257 (Ch).*

## Capping pensionable pay increases: contractual agreement

**Summary:** The High Court has held that a cap on pensionable pay that had been achieved by an extrinsic contractual agreement with the employees rather than by amendment of the scheme rules, was valid.

**Background:** Where an employer wishes to amend the terms of employees' benefits under an occupational pension scheme, it can be done either:

- By amending the scheme rules (which will generally require the consent of the trustees).
- By entering into an extrinsic contractual agreement with the employees whose benefits will be affected by the proposed amendment.

While case law has upheld the validity of amendments made by an extrinsic contractual agreement (such as *South West Trains v Wightman* [1998] PLR 113), the precise scope of an employer's ability to effect amendments to pension benefits in this way is by no means clear.

**Facts:** B was employed by the British Broadcasting Corporation (BBC) and was a member of the "new benefits" section of the BBC pension scheme (the scheme).

The BBC decided that, in order to reduce the scheme's deficit, it would limit the extent to which future pay increases for members of the new benefits section would be pensionable. The following options were put to the members:

- To remain in the new benefits section subject to a 1% cap on future pensionable pay increases.
- To opt out of the new benefits section and join a new career average section under which there would be no similar cap.
- To opt out of the scheme altogether and join a defined contribution arrangement.

Where members chose the first option, the cap on pensionable pay was achieved via an extrinsic contractual agreement whereby pay increases were conditional upon the member agreeing that only the first 1% would be pensionable (the prescribed terms).

B made an unsuccessful complaint to the Pensions Ombudsman and appealed to the High Court arguing, among other things, that the BBC's conduct in seeking to impose a 1% cap on pensionable pay via the contractual mechanism was contrary to the scheme's trust deed and rules.

The BBC argued that the definition of pensionable salary gave the BBC the discretion to determine that only an element of basic salary would be pensionable. Alternatively, the BBC argued on the basis of the *South West Trains* case that, if the member accepted the pay award on the prescribed terms, that would amount to a contract that would be binding on the member concerned and to which the trustees would be required to give effect.

**Decision.** The court held that:

- The BBC's interpretation of its discretion to determine a member's basic salary was too wide. If the definition entitled the BBC to determine what elements of future pay increases were pensionable, it could equally entitle the BBC to determine that, in future, elements of pay which had been pensionable would cease to be so.
- While an extrinsic contractual agreement could not override a contrary provision in the rules of a pension scheme, there was nothing in the scheme rules that prohibited the level of pensionable pay increases being capped. Subject to any breach of the implied terms of trust and confidence and good faith between the members and the BBC, acceptance of a pay award on the prescribed terms would therefore be binding on the member concerned notwithstanding the scheme rules.

**Comment:** This decision will be welcomed by employers wishing to rely on extrinsic contractual agreements to make changes to pension benefits that would otherwise require an amendment to the scheme rules. However, employers will need to ensure that members are fully informed about the proposed change and its implications, and that they are given a genuine choice whether or not to accept the proposed change. In addition, any use of an extrinsic contractual agreement will be subject to the implied terms of trust and confidence and good faith; in this case, the court did not make a decision as to whether or not the BBC had complied with these duties as the point had not been argued before the Pensions Ombudsman.

*Case: John Bradbury v British Broadcasting Corporation [2012] EWHC 1369 (Ch).*

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