ALLEN & OVERY

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Pensions: what's new this week

Welcome to your weekly update from the Allen & Overy Pensions team, bringing you up to speed on all the latest legal and regulatory developments in the world of occupational pensions.

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Equalising pensions for GMPs? High Court says 'yes'

The High Court has ruled that since pension benefits, including any Guaranteed Minimum Pension (GMP) element, are pay; and since it is not lawful to pay unequal benefits as between men and women, trustees have a duty to equalise scheme benefits for the effects of unequal GMPs: ***Lloyds Banking Group Pensions Trustees Ltd v Lloyds Bank plc and others***.

This is a landmark ruling and will have consequences for all schemes that were contracted out of the State Earnings-Related Pension Scheme in the period from the date of the *Barber* judgement (17 May 1990) up to the end of GMP accrual (5 April 1997).

Mr Justice Morgan also ruled that where more than one method produces equality of benefits, the trustee should choose the method which results in 'minimum interference' with the rights of any party – in this case, the sponsor was entitled to insist on the use of the least costly method.

In relation to correcting underpaid pension, the Court ruled that there was no applicable limitation period under legislation, but that scheme rules which provide for forfeiture of unclaimed benefits after six years may operate so as to restrict the ability of beneficiaries to claim back payments. This will depend on the specific wording of scheme rules.

We acted for the trustee of the Lloyds schemes in this very significant case. **Click here** for our briefing setting out more details and action points.

Morrisons vicariously liable for data leak

Morrisons has lost its appeal against a ruling that it is vicariously liable for a former employee leaking personal information about 100,000 members of staff, in the UK's first data protection class action (***Wm Morrison Supermarkets plc v various claimants***).

The leak was a deliberate action by a senior IT internal auditor at Morrisons who had a grudge against his employer; the individual has been jailed for eight years. However, Morrisons has been held vicariously liable for his actions in leaking the data on the basis that they were 'in the field of activities assigned to the employee' because he was entrusted with the payroll data. Morrisons intends to appeal the latest ruling, which leaves it facing a compensation bill to over 5,000 current and former employees.

Most data breaches are internal, so this decision serves as a reminder that trustees and sponsors, as data controllers under the Data Protection Act 2018 and as holders of vast quantities of personal data for members and employees, must be alert to the risk of insider breach and ensure that they are adequately managing this risk. Regulators and the market increasingly expect trustees and sponsors to do all they reasonably can to prevent cyber attacks and to deal with them effectively, but there remains very little firm guidance about what this means in practice. If you are interested in hearing first hand from our specialists who advise clients in relation to cyber security breaches, please get in touch. We have advised clients in relation to a broad range of cyber breaches and can share key practical lessons and tips for incident planning and response.

IORP II: scheme governance and cross-border schemes

Regulations to transpose the IORP II Directive (the revised EU Directive on the activities and supervision of institutions for occupational retirement provision) have been laid before Parliament. The regulations, which come into effect on 13 January 2019, address scheme governance and the cross-border scheme authorisation process.

IORP II governance requirements

The first set of regulations amends the Pensions Act 2004 to require trustees to have an effective system of governance in place that is proportionate to the size, nature, scale and complexity of their scheme. The detail will be set out in an updated Code of Practice on internal controls. A key change is the requirement for trustees of schemes with more than 100 members to have a risk management function and conduct regular own-risk assessments of their systems of governance.

The revised Code of Practice will include detail about:

- effective systems of governance (from management and organisational structure to business continuity and the role of environmental social and governance (ESG) factors in investment decisions);
- key functions including the actuarial and risk-management functions, the internal evaluation of the scheme's governance system and outsourcing of activities, plus the requirement for written trustee-approved policies on these functions (to be reviewed triennially);
- remuneration policies; and
- the running and documenting of an own-risk assessment of the scheme's system of governance.

Schemes with fewer than 100 members will only have to comply with the requirements on effective systems of governance (the first bullet point above).

The own-risk assessment of the systems of governance will include reviewing how the trustees assess various scheme risks, including: management and decision making; conflicts of interest with the employer where key scheme functions are outsourced to the employer or to an employee; the scheme's funding needs; operational risks; payment of members' benefits; the mechanisms

protecting benefits (e.g. the employer covenant, insurance or a guarantee); and where ESG factors are considered, how trustees assess new or emerging risks in relation to investments.

The first own-risk assessment must be prepared within 12 months after the last day of the first scheme year after the updated Code of Practice on internal controls is issued or, if later, within 15 months from the date of the next actuarial valuation or annual governance statement. After this, the risk assessment must be prepared at least every three years.

The government's view is that well-run schemes should not have to make onerous changes to comply with these regulations and the new code of practice; it may only be a case of documenting existing practice. Schemes that have been following and implementing the governance standards set out in the Regulator's **21st Century Trusteeship** guidance may find they have already covered some of the ground. We understand that the Regulator intends to consult on an updated Code of Practice on internal controls next year.

Cross-border schemes

Separate **regulations** make changes to the existing authorisation process for cross-border schemes and update the process for schemes wanting to carry out a bulk transfer to a scheme located in another EEA state. The process will include ensuring that the transfer is approved by a majority of members and beneficiaries concerned, and authorised by the Regulator.

TPR: updated DC communications guide

The Regulator has updated its DC 'How to' **guide to communicating and reporting**. The new version supports the use of the new industry 'Simplified Annual Benefit Statement' template (see **WNTW**, 22 October 2018); and contains links to other resources including:

- the new **pension scams leaflet** (other resources available **here**, including an updated version of the Regulator's scheme transfer checklist which cross-refers to the updated Code on Combating Pension Scams); and

- TPR's quick guide to the Chair's statement and technical appendix (to read more, see **WNTW**, 17 September 2018). TPR has also updated the guidance for schemes in wind-up to clarify the circumstances in which a Chair's statement must be prepared.

The new document also updates the downloadable PDF version to remove discrepancies between this and the web version of the guide that have existed since summer 2018.

Brexit: draft pensions regulations before Parliament

The government has published **draft regulations** which would affect numerous items of pensions legislation in connection with the UK's exit from the EU in the event that there is no withdrawal agreement. They are intended to ensure that retained EU law continues to operate effectively post-Brexit, by correcting legislation in areas that will become obsolete (for example, where the UK is referred to as an EU or EEA Member State, or where the UK is obliged to share data under reciprocal arrangements that will no longer apply). Proposed changes include:

- altering the requirements for scheme investments – currently, under the Investment Regulations, scheme assets must be predominantly assets traded on 'regulated markets' (defined by reference to EU Directives). The draft regulations propose to amend this to assets traded on UK regulated markets only (by reference to the Financial Services and Markets Act 2000); and

- repealing the framework for cross-border pension schemes. This removes the requirement for UK occupational pension schemes to obtain authorisation from TPR for cross-border activities. The **explanatory memorandum** states that UK private occupational pension schemes will remain subject to the obligation to treat non-UK workers in the same way as members who work wholly in the UK in relation to contribution and membership entitlements, and that TPR will provide guidance to UK pension schemes currently authorised for 'cross-border activity' within the EU.

Implementing Welsh income tax rates

Welsh rates of income tax will be introduced from April 2019. HMRC is **consulting** on consequential changes to legislation, including provisions of the Finance Act 2004 which deal with relief at source and the annual allowance charge. HMRC has also published a **technical note** which explains that where net pay arrangements are used for pension scheme contributions, the tax relief should automatically be at the Welsh rate where applicable. Where relief at source is used, pension schemes will claim relief at the Welsh basic rate for Welsh taxpayers who are members. HMRC is currently developing a tool to assist schemes with this (it has been developing the tool for the Scottish rate of income tax, but also intends this to be used for Welsh taxpayers). Further details are expected in due course.

The consultation closes on 5 November 2018.

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