

Court of Appeal upholds High Court's *Virgin Media* decision on failure to obtain a s37 confirmation



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Introduction

On 25 July 2024, in the case *Virgin Media v NTL Pension Trustees II Limited (and others)*, the Court of Appeal upheld the High Court's 2023 decision on the correct interpretation of historic legislation governing the amendment of contracted-out DB schemes.

Key points

- The Court of Appeal has upheld the High Court's decision that, based on the relevant legislation at the time, a written actuarial confirmation was required where an alteration to a scheme's rules affected pension benefits attributable to past or future service benefits related to section 9(2B) rights. Without such a confirmation, an amendment would be void.
- This decision is relevant for schemes which were contracted-out on a DB basis on or after 6 April 1997.
- Overall, our view is that the decision does not expose any new risks for schemes. The issue will be whether schemes can demonstrate that they complied with section 37 when changes were made. The decision does not give any guidance on what evidence would (or would not) be sufficient.
- Many within the pensions industry have suggested that the DWP should provide a legislative solution, but whether they will do so remains unclear.

Background

With effect from 6 April 1997 until contracting-out on a DB basis ended on 6 April 2016, contracted-out schemes had to satisfy an overall quality test known as the "reference scheme test" in relation to contracted-out rights known as "section 9(2B) rights". Whether that test was met had to be assessed and certified by the scheme actuary. In addition, section 37 of the PSA93 provided that the rules of contracted-out schemes "cannot be altered" in relation to section 9(2B) rights except amendments of a "prescribed description" made in "prescribed circumstances", as set out in regulations.

From 6 April 1997, regulation 42 of the Occupational Pension Schemes (Contracting-out) Regulations 1996 (“the Regulations”) permitted alterations to section 9(2B) rights in salary-related contracted-out schemes where:

- the trustees “informed the actuary in writing of the proposed alteration”
- the actuary “considered the proposed alteration” and “confirmed to the trustees in writing” that they were satisfied that the scheme would continue to meet the relevant statutory standard if the alteration were made (“Section 37 Confirmation”), and
- the alteration did not otherwise prevent the scheme from satisfying the requirements for a contracted-out scheme.

The Regulations have since been amended, but the parties in this case agreed that the effect of regulation 42 at the relevant time was to require alterations to section 9(2B) rights to be preceded or accompanied by a Section 37 Confirmation.

“Section 9(2B) rights” were defined in the Regulations as, broadly, “rights to the payment of pensions and accrued rights to pensions (other than rights attributable to voluntary contributions)” under a contracted-out scheme, attributable to pensionable service after 6 April 1997. The Regulations were later amended, with effect from 6 April 2013, to specifically refer to both past and future service rights.

Facts

The case concerned the validity of a second definitive trust deed and rules dated 8 March 1999 (“the 1999 Trust Deed and Rules”) in relation to the National Telecommunications Limited Pension Plan (“the Plan”), a contracted-out DB scheme.

The 1999 Trust Deed and Rules sought to reduce the rate of revaluation of deferred benefits under the Plan. Crucially, no Section 37 Confirmation had to date been located for the 1999 Trust Deed and Rules, and the case was determined on the assumption that it was not obtained.

A third definitive trust deed and rules dated 21 June 2010 (“the 2010 Trust Deed and Rules”) closed the Plan to new members and, for existing members, provided for revaluation of deferred benefits to continue on the same basis as under the 1999 Trust Deed and Rules. A copy of the Section 37 Confirmation was available for this deed.

Due to a restriction in the Plan’s amendment power, the parties agreed that the reduction in the rate of revaluation could only apply to future accrual of benefits from the date of the amendment. The claim therefore concerned pensionable service between 8 March 1999 (the date of the 1999 Trust Deed and Rules) and 21 June 2010 (the date of the 2010 Trust Deed and Rules). If the changes to the 1999 Trust Deed and Rules were ineffective, benefits accrued during that period would improve at an estimated cost to the Plan of around £10m.

High Court’s judgment

The judge considered the versions of the legislation in force during the relevant period, and found that:

- amendments to the rules of a contracted-out scheme which related to section 9(2B) rights were void and ineffective to the extent that the amendment was introduced without the required Section 37 Confirmation. The legislation was “plain and unambiguous” in this respect

- the words "section 9(2B) rights" included both past service rights and future service rights. Taking into account the wording of the legislation and the Regulations as a whole, the judge dismissed the principal employer's argument that the Regulations did not protect future service benefits until they were amended in 2013, and
- there was nothing in the legislation to limit the effect of section 37 to alterations that would or might have an adverse effect. It applied to all alterations to section 9(2B) rights.

Court of Appeal's judgment

The parties agreed that, if a Section 37 Confirmation was not obtained, a purported amendment in relation to any section 9(2B) rights would be void. However, the principal employer brought an appeal concerning one limited issue: whether the words "section 9(2B) rights" and the requirement for a Section 37 Confirmation applied to both past service rights and future service rights. The High Court judge gave permission to appeal, recognising that "the question of construction was a difficult one and that the decision had potentially wide-ranging implications for many similar pension schemes".

Based on a detailed review of the purpose of the legislation, the Court of Appeal considered "rights" to be a "very general word" and agreed with the High Court's "impressive judgment" that the legislation at the relevant time did not confine the requirement for a Section 37 Confirmation to amendments affecting past service benefits only. Changes to both past and future service benefits relating to section 9(2B) rights would therefore be void if a Section 37 Confirmation was not given.

The wider implications

Like the High Court judgment before it, overall, our view is that this decision doesn't expose pension schemes to any new risks. The requirement for a Section 37 Confirmation for amendments relating to reference scheme benefits was well known, and decisions should have been taken at the time changes were being made as to whether or not it was engaged.

Importantly, because of the limited scope of the appeal, the Court did not need to consider what evidence might be enough to demonstrate that a Section 37 Confirmation was in fact received. The legislation did not require confirmation to be given in any particular form so, for example, the Section 37 Confirmation could have been wrapped up as part of written advice given at the relevant time. As such, a deed making specific reference to a Section 37 Confirmation (or not as the case may be) will not necessarily be conclusive either way.

Neither did the Court have to consider whether other types of actuarial confirmations might "fix" the absence of a Section 37 Confirmation for a particular amendment. In particular, schemes had to carry out a recertification process at least every three years to retain their contracted-out status. The Court was not asked to consider whether the amendment could have become valid when the actuary next recertified the scheme.

Given the potential for historical scheme amendments, including those which were beneficial to members, to be rendered void due to a lack of evidence of a Section 37 Confirmation, it is possible the DWP might exercise its power to make regulations to validate such changes. This could help address some of the issues faced by trustees and employers in relation to imperfect records of historic scheme documents, and the industry has already asked for such legislation to be considered.

In the meantime, we consider that whether or not a Section 37 Confirmation was given is part of the wider question of whether all the necessary formalities (eg execution requirements, section 67 certificate) were

satisfied when a scheme amendment was made. Whether trustees should take steps to investigate such issues will depend, we think, on their scheme's specific circumstances.

If you have particular concerns following this decision and/or would like to understand the potential impact for your scheme, please speak to your usual Sackers contact.

Sacker & Partners LLP
20 Gresham Street
London EC2V 7JE
T +44 (0)20 7329 6699
E enquiries@sackers.com
www.sackers.com

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