



ITV FAILS TO BOX CLEVER IN COURT DETERMINATION ON PENSIONS DEFICIT

The Pensions Regulator (TPR) recently indicated that it will not hesitate to use its anti-avoidance enforcement powers under the Pensions Act 2004 (PA 2004) against any connected or associated company where it believes that it would be reasonable for that company to provide financial support to an underfunded defined benefit pension scheme. TPR was no doubt emboldened by the Upper Tribunal's decision last month in the Box Clever case which confirmed the very broad scope of TPR's jurisdiction and the considerable latitude that it enjoys when applying the statutory "reasonableness" test.

In this briefing we focus on the legal issues considered in the Box Clever decision in terms of when TPR can exercise its power to issue a financial support direction (FSD). As a starting point it is worth noting that whilst the powers derive from the anti-avoidance provisions of the PA 2004, an FSD can in fact be imposed on a party on a "without fault" basis, as indeed occurred in ITV's case (where the Tribunal did not attribute any blame to ITV neither as to the way in which the pension scheme deficit arose nor more generally as to the way in which the Box Clever joint venture was structured). The key issues in the case were whether: (i) TPR had jurisdiction to issue an FSD to ITV (which included considering whether ITV was connected or associated with the sponsoring employers of the Box Clever defined benefit pension scheme and whether the PA 2004 was retrospective in effect); and (ii) if TPR did have jurisdiction, whether it was reasonable to impose an FSD in the circumstances of the case.

As a result of the decision, ITV is required to provide financial support pursuant to the FSD, with the exact amount of support to be determined. The scheme deficit of £115m is a result of a failed joint venture entered into in 2000 between the Thorn Group and the Granada Group, which is now part of the ITV Group. The joint venture was an attempt to consolidate operations in what was recognised as a declining market for television rentals.

Now almost 18 years later, ITV has been unsuccessful in challenging TPR's ability to issue an FSD, although we understand that ITV has been granted permission to appeal.

Key issues

- First judicial decision on whether an FSD should be made
- Whether it is reasonable for only one of two joint venture partners to be compelled to provide financial support to address the £115m deficit in the Box Clever defined benefit pension scheme
- Administrative receivers were appointed to Box Clever in 2003 after which time ITV has had no involvement with the business in any real commercial sense. However, the Tribunal considered whether ITV was still in technical "control" of Box Clever for the purposes of establishing its own jurisdiction to issue against ITV.
- Whether it is reasonable for TPR to look back at events that pre-date even its own existence as a regulator (TPR was established in 2005)
- ITV to appeal

This case is significant because it is the first judicial determination on whether an FSD can be issued. TPR justified its decision to proceed against ITV by reference to its statutory objectives which include protecting pension scheme members' benefits and reducing the risk of calls on the Pension Protection Fund (PPF). However, one can see how ITV may feel aggrieved at the result, especially given that TPR is not taking any action against the other joint venture partner (due to the fact that, following a formal application for clearance, TPR had previously issued a letter of comfort to that party based on what TPR now considers was an incorrect view of the law) but also noting that the anti-avoidance provisions of the PA 2004 were not even in effect at the time the joint venture was formed (indeed the provisions were only enacted after the joint venture had collapsed).

LEGAL ASPECTS

No one could accuse the Tribunal of lacking in thoroughness as the decision runs to over 140 pages and examines in forensic detail the facts giving rise to the deficit (see below a summary timeline.) The majority of the judgment is devoted to an analysis of the factual pattern and an assessment of the reasonableness to impose an FSD in such circumstances.

From a legal perspective there are a number of key takeaways:

- The appointment of an administrative receiver does not break the chain of control for the purposes of s43 PA 2004 between a parent company (who might be the target of an FSD) and an insufficiently resourced employer of a defined benefit pension scheme.
- Following a close analysis of the terms of a debenture, the Tribunal held that a security trustee, with legal and equitable security over shares in the Box Clever group, had not assumed voting rights so as to become associated with the pension scheme employers (under the debenture, the security trustee was obliged to serve a notice before it would assume voting rights and it had not served any such notice). This reaffirms the importance for lenders and security trustees, where there are concerns around defined benefit pension schemes, of having clear provisions relating to when rights and powers become exercisable under security documents and being aware of the potential for liability if they assume control or possession of an asset. In particular, lenders and security trustees should ensure that assumption of voting rights is not automatic on the occurrence, or declaration of, an event of default because there may be unintended consequences.
- Having said that, even if a lender or security trustee put itself within the scope of the regime by exercising voting rights, we remain of the view that it is unlikely in most cases that it would be reasonable for TPR to issue an FSD against the lender/ security trustee. However, lenders should note that the Tribunal was very clear that the fact that a target had not received any substantial benefit from the employer was not a bar to the issue of an FSD, if, taking into account other factors, it was reasonable for an FSD to be issued.
- Liability under an FSD is not fault-based and there is an unlimited look-back period when considering reasonableness. ITV's defence based on retrospectivity failed. The Tribunal said that "*s43 is not truly retroactive or retrospective legislation, but is legislation which can alter prospectively the rights and obligations arising from pre-existing legal relationships*".

FSDs and Contribution Notices (CNs) explained

Under the PA 2004, TPR has wide powers to extend defined benefit pension liabilities beyond actual employing companies, to their "associates" and "connected persons". These terms are broadly defined. As well as including group companies, shareholders and individuals such as directors, they can also extend to anyone entitled to exercise, or control the exercise of, one third or more of the voting rights in group companies, which is where the concern lies for lenders and security trustees taking share security.

There are two main powers – TPR can issue FSDs and Contribution Notices (CNs). FSDs can be used to extend pension liabilities to so called "target companies" associated with an employer of the scheme, without any fault on their part. An FSD requires the person to whom it is issued to put in place financial support for the scheme (which could include, for example, making all members of the group jointly and severally liable for the pension liabilities).

If a person fails to comply with an FSD, the Pensions Regulator is empowered to issue a CN to that person requiring that a contribution be made to the scheme. The conditions for imposing a CN directly are stricter (generally but not always there must be some "avoidance" or a specific act or omission to which TPR can point), but the consequences are more severe – a CN can be used to attach personal liability to directors and also to accelerate pension liabilities and require large one-off payments. Both powers have been exercised only rarely. Although with some high-profile collapses and the resultant increased political pressure, this may be set to change.

- Whilst it is a general rule of law that TPR as a public body should treat like cases alike, there may be an objective justification which permits TPR to treat different potential targets differently. The legislation does not require TPR to pursue every person who falls within the scope of its FSD powers; it can "choose only one or two without needing to devote resources to investigating the other candidates". In this case TPR proceeded against ITV but not Thorn.

NEXT STEPS

As mentioned above, the Tribunal's decision is not the last word on the case and the Court of Appeal's judgment will be keenly awaited. If the appeal by ITV is unsuccessful, then the amount of financial support that ITV needs to provide to the scheme will fall to be determined. TPR may not seek the full amount of the scheme's buy-out deficit (which as of this year is approximately £125m). The Tribunal acknowledged that relevant factors in determining the quantum will include the actions of the pension scheme trustees in delaying the closure of the scheme to future accrual and in postponing the winding-up of the scheme (both actions which have caused the deficit to increase), as well as the fact that the other joint venture partner (Thorn) has not been compelled to provide any financial support.

Generally speaking, the case may signify a new era in the use of anti-avoidance powers by TPR, as the regulator itself has come under the spotlight and been criticised for a failure to exercise such powers in some very high-profile cases. From a structuring and financing perspective the decision is an important reminder of the need to take into account the potential liabilities and consequences associated with underfunded defined benefit pension schemes. This may include taking steps to avoid unwittingly or unnecessarily being "connected" or "associated" with pension scheme employers, or to cease such connections or associations where they are not required for other commercial purposes. It may also include considering an application for clearance from TPR, but in any event it should always include considering whether a given proposal may in the future lead TPR to conclude that it would be reasonable to issue the FSD.

TIME LINE

1999 - 2000	Box Clever joint venture formed between Granada Group (now ITV) and Thorn Group
2001	Box Clever established the defined benefit scheme with Box Clever companies as employers of the scheme (the shareholders were clear that financial commitments created by the pension scheme were and would remain the responsibility of Box Clever and that the shareholders would not provide additional support)
2003	Administrative receivers appointed to the Box Clever group (below the joint venture holding company)
2003	Defined benefit scheme closed but not wound up
2004 - 2009	Negotiations on possible transfer of pension scheme members back to Granada/ ITV scheme
2009	ITV applied for clearance, which was refused (Thorn had earlier applied for clearance and was also refused but did instead get the benefit of a comfort letter).
2009 - 2011	TPR investigations into ITV (but not Thorn)
2011	Warning Notice issued, and later the Regulator's Determinations Panel determines to issue an FSD
2012	Reference by ITV to Upper Tribunal in January 2012 to challenge TPR's determination to issue an FSD
2012 - 2016	A number of preliminary hearings followed, including a strike-out application which is appealed to the Court of Appeal
2018	First substantive hearing in the Upper Tribunal

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