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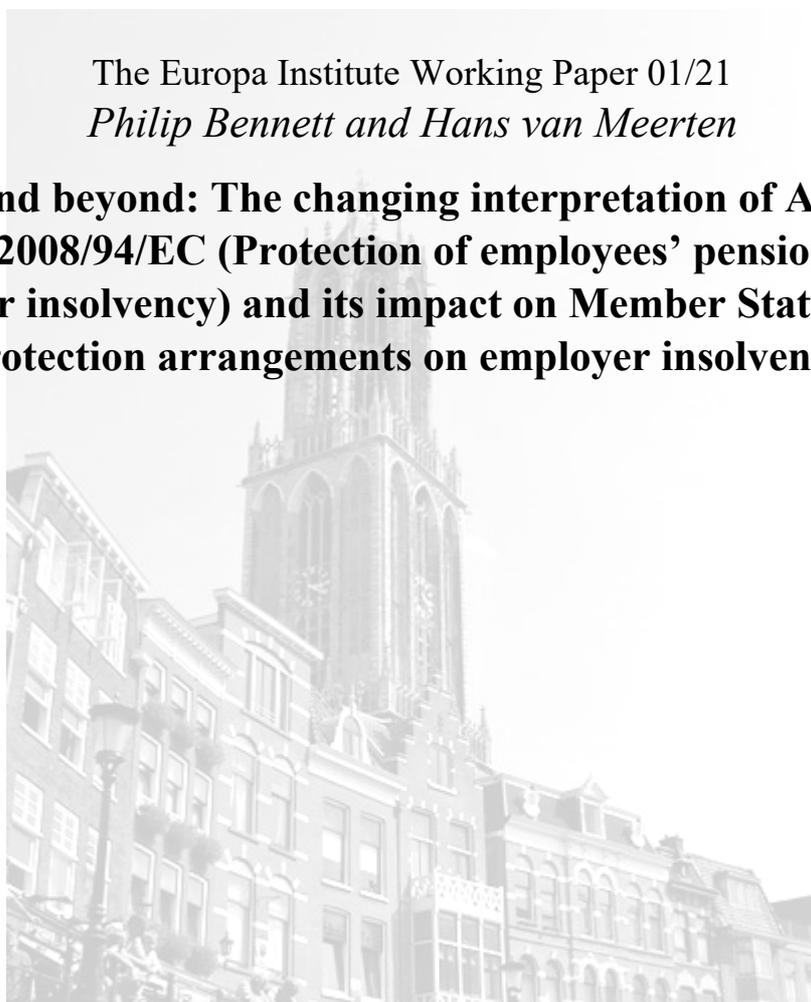
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‘Bauer and beyond: The changing interpretation of Article 8 of Directive 2008/94/EC (Protection of employees’ pension rights on employer insolvency) and its impact on Member State pension protection arrangements on employer insolvency’



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Bauer and beyond: the changing interpretation of Article 8 of Directive 2008/94/EC (Protection of employees' pension rights on employer insolvency) and its impact on Member State pension protection arrangements on employer insolvency

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Note: The law is stated as at 12th April, 2021.

Abstract

This Working Paper looks at the CJEU's changing interpretation of Article 8 of Directive 2008/94/EC (protecting pension rights on employer insolvency) over the last 14 years through its decisions in *Robins*, *Hogan*, *Webb-Sämann*, *Hampshire* and *Bauer*. The CJEU both decided that pension protection arrangements did not satisfy the Article 8 requirements and imposed a number of underpins as to the level of protection required. In *Bauer* the CJEU introduced an additional underpin of a 100% minimum protection level up to the Eurostat at-risk-of-poverty threshold (€14,767 pa after income tax in the Netherlands (for 2019) and £11,142 pa after income tax in the UK (for 2018)). This decision makes two errors in not recognising the time lag in index publication date and in not recognising its interaction with different tax years in different jurisdictions. It also suggests excessive judicial activism and creates legal uncertainty as to how the additional underpin can be administered. The Working Paper identifies gaps in compliance with Article 8 in the UK which are unaffected by Brexit (including unfunded (or direct pension promise) executive top-up schemes). It looks at the application of Article 8 to Dutch DB and CDC schemes. It identifies some issues with Article 8 compliance, although highly fact sensitive, in the Netherlands, particularly in the light of the *Bauer* underpin, where the employer has contractually committed to make good certain shortfalls. The Working Paper also questions whether Article 8 requires the protection of *Beckmann* early retirement (and certain other) benefits. The Working Paper discusses the use of an age discrimination argument to remove a compensation cap in the UK Pension Protection Fund for those who had not reached normal pension age. This argument (in *Hughes* -UK High Court) was based on Article 21 of the EU Charter of Fundamental Rights and Article 14 of the European Convention on Human Rights and may apply in other jurisdictions. Finally, the Working Paper notes that the CJEU has left the door open for further Article 8 underpins to be added.

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1. Introduction

Article 8 (“**Article 8**”) of Directive 2008/94/EC³ imposes an obligation on EU Member States (which, at the time in question, included the UK) to put in place a pension protection arrangement for the pension rights of employees of certain pension schemes on the insolvency of the employer of those employees. The interpretation of Article 8 has been considered by the Court of Justice of the European Union (the “**CJEU**”) in the cases listed in **Table 1** below.

This paper draws out some of the implications of those changes in the interpretation of Article 8 for the Pension Protection Fund in the UK (the “**PPF**”). In particular, it identifies gaps in the PPF coverage which demonstrate non-compliance with Article 8. The position is unaffected by Brexit (see below). This paper looks at some of the implications for The Netherlands (which does not have an Article 8 pension protection arrangement) of the cases listed in **Table 1** below. It also identifies areas of potential non-compliance with Article 8 in The Netherlands.

This paper, in addition, draws out some issues that may have ramifications in other EU Member States as to whether their State organised pension protection arrangements on employer insolvency that cover all of the pension rights which they are required to implement by Article 8.

The CJEU cases on Article 8 considered in this paper are:

Table 1

	Case Name	Case Reference	Date of CJEU Decision	Case abbreviation used in this Article
1.	<i>Robins v Secretary of State for Work and Pensions</i>	C-278-05	25 th January, 2007	Robbins
2.	<i>Hogan v Ireland</i>	C-398/11	25 th April, 2013	Hogan
3.	<i>Webb-Sämann v Seagon</i>	C-454/15	24 th November, 2016	Webb-Sämann
4.	<i>Grenville Hampshire v The Pension Protection Fund</i>	C-17/17	6 th September, 2018	Hampshire
5.	<i>Pension-sicherungs-verein Vvag v Bauer</i>	C-168/18	19 th December, 2019	Bauer

The reader of Article 8 (for text see **Section 2** below), without the benefit of the decisions of the CJEU, may well have reached the conclusion that Article 8 required, in general⁴, 100% of the pension rights⁵ referred to in Article 8, to the extent reduced by employer insolvency, of

³ This Directive (covering the protection of employees’ pension rights in the event of the insolvency of their employer) replaced Directive 80/987/EEC). In both Directives Article 8, dealing with protection of certain employee pension rights on employer insolvency, is unchanged.

⁴ Article 12(a) of the Directive permits Member States to take measures necessary to avoid abuses.

⁵ Consider Recital (3) “... while taking account of the need for balanced economic and social development in the Community” and Article 4 “1. Member States shall have the option to limit the liability of the guarantee institutions referred to in Article 3”. But Article 7 (effect on

employees and former employees to be protected by a pension protection arrangement under the laws of the Member State in question.

Such a reading would be in harmony with the rigorous analysis of Advocate General Kokott in *Robins* and the revisitation of the scope of Article 8 in the opinion of Advocate General Hogan in *Bauer*, both discussed below.

However, the CJEU was initially hesitant to impose a full level of protection given the potential economic cost of so doing. Instead, over the nearly 13 year period from *Robins* to *Bauer*, the CJEU:

- determined that the minimum level of protection required is 50% of the amount of the pension rights covered by Article 8 (subject to possible Member State discretion to impose a cap on the maximum amount protected).
- then removed the cap on the maximum amount of the pension to which the 50% test applied to the pension rights covered by Article 8.
- determined that the 50% test is a continuing test over the lifetime of the scheme member or survivor. This meant that guaranteed pension increases that would have been provided will increase the amount of the pension over time to which the 50% test applies. Note that the CJEU expressed this test as a value test taking into account those guaranteed increases.
- introduced a 100% minimum level of the pension covered by Article 8 based on the at-risk-of-poverty threshold as determined by Eurostat for the Member State concerned.

This paper will discuss, in **Section 12** below, whether all pension rights under the occupational pension schemes covered by Article 8 are protected by Article 8 or just old-age benefits, including survivors' benefits, provided under such a scheme. To draw this point out:

- does Article 8 protect rights to invalidity benefits and early retirement pensions (a distinction drawn by the CJEU in *Beckmann*⁶) provided by an occupational pension scheme within the scope of Article 8⁷, or
- are those rights protected by Article 3 (employees' outstanding pay claims) of the Directive but subject to the Member State option to limit those pay claims under Article 4 of the Directive, or
- are those rights outside the scope of the Directive and its protection?

benefits under national statutory social security schemes) and Article 8 are not subject to the Article 4 Member State option to limit benefit entitlements).

⁶ *Beckmann v Dynamco Whicheloe Macfarlane (C-164/00)* at paragraph 32.

⁷ Article 8 applies to “*supplementary occupational or inter-occupational pension schemes outside the national statutory social security schemes*”. Note these schemes may be unfunded book reserve schemes of the type identified in Articles 2(2)(c) and (e) of Directive (EU) 2016/2341 (the “**IORP II Directive**”) or may be funded IORPs (as defined in Article 6 of that Directive). The words “*supplementary occupational or inter-occupational pension schemes outside the national statutory social security schemes*” are also used in Directive 2001/23/EC (safeguarding employees' rights on transfers of undertakings) at Article 3(4).

It will also look at the ingenious use of an age discrimination related argument deployed to remove a further compensation cap imposed, in relation to compensation from the PPF, in *Hughes v The Pension Protection Fund*, a decision of the High Court in England on 22nd June, 2020⁸. The PPF does not impose a cap on the amount of compensation where the member had attained PPF normal pension age. But the PPF does impose a compensation cap in other cases which limited the level of compensation to more than 50% of the member's pension at time of employer insolvency. This topic is explored in more detail at **Section 13** below.

This age discrimination argument may also have application to pension protection arrangements in any EU Member State where the design of the pension protection arrangement imposes a monetary cap on the accrued pension of those employees and former employees who had not attained a particular age at the date of the employer insolvency.

For completeness, it should be noted that, despite Brexit, Article 8 and the associated pre-Brexit⁹ CJEU decisions (ie all those in **Table 1**) are all part of EU law retained by the UK which will continue in force until altered by Parliament or until a different interpretation to that of the CJEU is provided by the UK Court of Appeal or the UK Supreme Court¹⁰.

Note, however, that the ability to recovery damages against the UK under the rule in *Francovich*¹¹ for non transposition or incorrect transposition of an EU Directive which is part of retained EU law is no longer part of UK law¹². In addition, the European Charter of Fundamental Rights is no longer part of UK law¹³.

A point to draw out is the extent to which many of the provisions of the European Charter of Fundamental Rights were already part of UK law:

*“On appeal to the CA the Secretary of State has accepted that “the fundamental rights set out in the Charter can be relied on as against the UK...because the Charter simply restates rights that already formed part of EU law, and does not create new rights””*¹⁴.

⁸ [2020] EWHC 1598 (Admin)]. An appeal has been lodged by the PPF with the Court of Appeal in respect of the decision on this case.

⁹ The UK left the European Union on 31st January, 2020 at 11pm GMT. However, there was an implementation period which ended at 11pm GMT on 31st December, 2020. During that implementation period, in general, EU law continued to apply in full in the UK.

¹⁰ See the European Union (Withdrawal) Act 2018, (as amended by the European Union (Withdrawal Agreement) Act 2020) Sections 2,4,5, 5A, 6 and 7 and Schedule 1.

¹¹ [1991] C-6/90. *Francovich* was a case in relation to the Directive (the first version) 80/987 in respect of non-payment of wages following employer insolvency.

¹² The European Union (Withdrawal) Act 2018, Schedule 1, paragraph 4. There are some very limited transitional provisions in Schedule 8, paragraph 39.

¹³ The European Union (Withdrawal) Act 2018, Section 5(4).

¹⁴ *Saeedi* [2010] EWCA Civ 990, a decision of the Court of Appeal. See paragraph 7.

The European Union (Withdrawal) Act 2018¹⁵, initially, looks encouraging. Schedule 1, paragraph 2 says:

“No general principle of EU law is part of domestic law on or after [31st December, 2020] if it was not recognised as a general principle of EU law by the European Court in a case decided before [31st December, 2020] (whether or not as an essential part of the decision in the case)”.

However, Schedule 1, paragraph 3, goes on to provide:

“(1) There is no right of action in domestic law on or after [31st December, 2020] based on a failure to comply with any of the general principles of EU law.

(2) No court or tribunal or other public authority may, on or after [31st December, 2020] –

(a) disapply or quash any enactment or other rule of law, or

(b) quash any conduct or otherwise decide that it is lawful,

because it is incompatible with any of the general principles of EU law.”

The effect of Schedule 1, paragraph 3 would appear to reduce those retained general principles to interpretative tools.

However, the UK Supreme Court, in November 2019, gave the Human Rights Act 1998 more teeth¹⁶ by setting aside subordinate legislation which is incompatible with those provisions of the European Convention on Human Rights set out in Schedule 1 of that Act. It may well be that Article 14 and the First Protocol of the Convention will be deployed more broadly using those interpretative tools (and see **Section 13** below).

2. Setting the scene: Article 8 of Directive 80/987/EEC

The first version of Article 8 is in Directive 80/987/EEC of 20th October, 1980:

Article 8

*Member States **shall ensure** that the **necessary measures** are taken **to protect** the interests of employees and of persons having already left the employer's undertaking or business at the date of the onset of the employer's insolvency **in respect of rights***

¹⁵ As amended by the European Union (Withdrawal Agreement) Act 2020, Section 25(6)(a) and SI 2020/75.

¹⁶ *RR v Secretary of State for Work and Pensions* [2019] UKSC 52, 13th November, 2019.

conferring on them immediate or prospective entitlement to old-age benefits, including survivors' benefits, under supplementary company or inter-company pension schemes outside the national statutory social security schemes.” (emphasis added)

When reading Article 8, it is important to bear in mind the first Recital to this Directive:

“Whereas is necessary to provide for the protection of employees in the event of the insolvency of their employer and to ensure a minimum degree of protection, in particular in order to guarantee payment of their outstanding claims, while taking account of the need for balanced economic and social development in the Community.” (emphasis added)

This Directive was consolidated and replaced by Directive 2008/94/EC (but with no change to Article 8). The first sentence of Recital (3) is the same as the first Recital set out above.

In the rest of this paper references to the Directive and to Article 8 include, as applicable, the Directive 80/987/EEC or Directive 2008/94/EEC and Article 8 to each of those 2 Directives (depending on the Directive in force to which the CJEU case, referred to in **Table 1**, related).

3. What does ensuring the protection of certain pension rights on employer insolvency mean in Article 8: Preliminary

What types of schemes are covered by Article 8?

The types of pension scheme to which Article 8 applies are those that provide immediate or prospective entitlement¹⁷ to old age benefits, including survivor benefits, under supplementary occupational or inter-company occupational pension schemes outside the national statutory social security schemes.

Supplementary company or inter-company occupational pension schemes are not defined. But the same wording is used, for example, in the Acquired Rights Directive¹⁸.

Notwithstanding the lack of a definition, it is clear from the words used that they apply both to employer established funded Institutions for Occupational Retirement Provision (or IORPs)¹⁹ and unfunded book reserve or pay as you go occupational pension schemes which provide old-

¹⁷ The Directive, Article 1(2) says that “*This Directive is without prejudice to national law as regards the of the terms ... ”right conferring immediate entitlement” and “right conferring prospective entitlement”*”.

¹⁸ Directive 2001/23/EC (safeguarding employees’ rights on transfers of undertakings) at Article 3(4) “*supplementary occupational or inter-occupational pension schemes outside the national statutory social security schemes”*”.

¹⁹ As defined in the IORP II Directive, Article 6. In the UK this would include the usual private sector employer sponsored occupational pension scheme established under irrevocable trusts.

age benefits, including survivors' benefits. The cases in **Table 1** relate to one or other of the 2 types of scheme.

A scheme covered by Article 8 is referred to in the rest of this paper as an “**Article 8 OPS**”.

Protection for different types of benefit structures

Where the benefits concerned in an Article 8 OPS are money purchase (or defined contribution) benefits, the level of benefits should be unaffected by employer insolvency if the scheme is a funded scheme. Assets in a funded scheme would have been set aside and would be employer insolvency remote and ordinarily will equal the amount of the member's money purchase pension rights credited to their respective retirement accounts in the scheme. So employer insolvency has no effect²⁰ on those rights and Article 8 is not engaged (except in respect of unpaid contributions where Article 3 (Outstanding claims resulting from employment contract) of the Directive could apply).

However, if you have an unfunded money purchase Article 8 OPS where the member's rights to money purchase benefits may or may not be backed by notionally hypothecated pool of assets which are not employer insolvency remote, then such rights, if they are old age benefits, including survivors' benefits, (see below) would fall within the protection conferred by Article 8.

The same is true of an unfunded (or book reserve or pay as you go) defined benefit Article 8 OPS. These schemes include executive top up pension schemes of the type described in *Granada Group v Law Debenture*²¹ and unfunded direct pension promises in reasonably common use in Germany; see for example the pension arrangements in *Bauer*.

However, in a funded defined benefit occupational pension scheme, defined benefit rights which could lawfully be reduced on winding-up of the defined benefit funded pension scheme on grounds of insufficiency of assets (whether because of employer insolvency or otherwise), have been held by the CJEU to be within the scope of the Article 8 protection disregarding any such reductions. This is discussed in further in **Section 6** below.

Are all benefits provided by an Article 8 OPS protected by Article 8?

Article 8 applies to interests of employees and former employees “*in respect of rights conferring on them immediate or prospective entitlement to old-age benefits*”²², including survivors' benefits” under an Article 8 OPS.

²⁰ With the limited exception where scheme assets have been lost through fraud or negligence and there is a valid claim against the employer to make good the loss.

²¹ [2016] EWCA Civ 1289.

²² Contrast “old age benefits” with the definition of “retirement benefits” the IORP II Directive, Article 6.

“Benefits” for this purpose would include a pension for life payable from normal retirement date and a lump sum payable on retirement at normal retirement date. Such benefits are “old-age benefits” for Article 8 purposes.

Similarly, a survivor’s pension or lump sum payable on death of an employee (or former employee) in receipt of old-age benefits under an Article 8 OPS are “survivors’ benefits” for Article 8 purposes.

The same is not necessarily true for survivor benefits payable on death of an employee or former employee before that individual has started to receive old age benefits.

But what about an invalidity benefit or an early retirement benefit from an Article 8 OPS? Prima facie neither of these benefits is required to be protected under Article 8. This is discussed further in **Section 12** below.

4. What does protecting pension rights within the scope of Article 8 provided under an Article 8 OPS on employer insolvency mean for a UK DB pension scheme?

Private sector UK defined benefit pension schemes would, typically, be structured in one of two ways:

- as a funded scheme established under irrevocable trust (which would be treated as an IORP under the IORP I Directive and the IORP II Directive²³), or
- as an unfunded contractual promise directly enforceable by the member against the employer outside the scope of the IORP Directives²⁴.

Because of the more favourable tax treatment for funded UK DB schemes (together with the insolvency remoteness of the scheme assets if the employer were to become insolvent), the substantially more common legal form for a private sector UK defined benefit occupational pension scheme is for the scheme to be set up by the employer under irrevocable trusts²⁵.

For such a trust based scheme, it was usual to include one or more of the following “safety valves” to protect the employer from having any additional funding obligations if the scheme assets were not sufficient to provide the pensions which the trust deed governing the scheme granted to the members of the scheme:

²³ Directive 2016/2341, the IORP II Directive which replaced and consolidated the IORP I Directive (Directive 2003/41/EC).

²⁴ Neither the IORP I Directive nor the IORP II Directive apply to book reserve or pay-as-you-go pension schemes – see Article 2(2)(c) and (e) of each Directive.

²⁵ See, for example, this UK Office of National Statistics publication accessed on 22nd March, 2021:

<https://www.ons.gov.uk/economy/investmentpensionsandtrusts/articles/ukpensionsurveys/redevelopmentand2019results>

- a provision in the trust deed under which the trustee of the scheme could reduce benefits to balance the books if the scheme were in deficit following a valuation²⁶.
- a right for the employer to suspend or terminate contributions to the scheme (without any obligation to make good any shortfall in the scheme assets needed to provide the scheme benefits in full).
- a right for the employer to require the trustee to wind-up the scheme and use the available assets to secure the scheme benefits in the order specified in the winding-up clause in the trust deed (but with no obligation, under the trust deed or the contract of employment, for the employer to make up any shortfall).

A point to draw out is that, before 1st July, 1992, there was no obligation, under UK law, placed on the employer, whether solvent or insolvent, to make up any shortfall under a trust based scheme, structured as outlined above, in any of these situations. However, the position under UK law started to change from 1st July, 1992²⁷.

The new legislative provision included an obligation on the employer to make good a shortfall, upto a certain level, to scheme assets (but one that was less onerous than the cost of securing the benefits on the winding-up of the scheme in full by purchasing annuities from an insurance company).

Additional legislative provisions, in the Pensions Act 1995²⁸, came into force from 6th April, 1997 to invalidate the safety valve referred to above.

Furthermore, by 19th March, 2002, the obligations of the employer had been increased so that, on the employer's insolvency, a payment would be due to the scheme trustee (ranking as an

²⁶ An example of such a provision is illustrated in *Aon Trust Corporation v KPMG* [2005] EWCA Civ 1004 a decision of the Court of Appeal on 28th July, 2005.

²⁷ See Section 58B of the Social Security Pensions Act 1975 (as inserted by the Social Security Act 1990) and the Occupational Pension Schemes (Deficiency on Winding-up etc.) Regulations 1992. Note that the value of the liabilities under these Regulations and GN19 Version 1 in force from 1st April, 1993 <https://www.actuaries.org.uk/system/files/documents/pdf/GN19V1-0.pdf> read with GN11 as in force on 1st April, 1993 (Version 5.1) <https://www.actuaries.org.uk/system/files/documents/pdf/GN11V5-1.pdf> was based on the cost of buying out pensioners (at a time of high interest rates) and other members on their cash equivalent transfer basis (lower than the cost of the buy-out basis). So, at that point in time, even if the employer debt was paid in full (or there was no employer debt), the other members would not be able to purchase an identical benefit from an insurance company with the cash equivalent.

²⁸ Section 67 (Modification of accrued rights and entitlements void unless certain conditions met).

unsecured creditor) from the employer equal to the shortfall between the assets of the scheme and the cost of securing with an insurance company the scheme benefits in full²⁹.

In other words, it could be argued that these UK legislative changes brought UK funded DB occupational pension schemes within the ambit of Article 8, even before the IORP I Directive which was transposed into UK legislation by the Pensions Act 2004 (which Act introduced the statutory funding regime in Part 3 of that Act).

This point is worth bearing in mind when considering the *Hogan* case and the different legal position in Ireland. It also provides a contrast with the approach to Article 8 in The Netherlands discussed in **Section 11** below.

But let us start with the first CJEU decision on Article 8, the *Robins* case.

5. **Robins v The Secretary of State for Work & Pensions: The first Article 8 case**

Background

The background to this case is that a company called ASW Limited had 2 UK pension schemes established under irrevocable trust:

- the ASW Pension Plan, and
- the ASW Sheerness Steel Group Pension Fund.

The 2 pension schemes started to wind-up in July 2002. ASW Limited was placed in insolvent liquidation on 24th April, 2003. There was insufficient money in the 2 pension schemes to secure members' benefits in full.

An important point to draw out is the winding up rule applicable to the 2 pension schemes which required the scheme assets to be applied in a particular order:

*“The schemes were terminated in July 2002 and are in the process of being wound up. The trustees are now obliged to apply the assets of the schemes to secure the accrued benefits of the members according to certain priority categories laid down by the schemes' rules, as amended by legislation. **First**, the assets of the schemes are used to secure the benefits of those members whose **pensions had come into payment** at the date the schemes went into winding-up, and **then**, to the extent that there are any assets left in the schemes, to secure the **benefits of those members whose pensions had not yet come into payment** at the date the schemes went into winding-up.”³⁰*

²⁹ Section 75 of the Pensions Act 1995 and the provisions now in the Occupational Pension Schemes (Employer Debt) Regulations 2005 as amended. The position for a scheme with 2 or more employers is more complex and is outside the scope of this paper.

³⁰ *Robins* paragraph 28.

This resulted in members in receipt of pensions being paid in full, but the members whose pensions were not yet in payment, receiving benefits, in accordance with the scheme rules, which were less than 50% of their pre-scheme winding up benefits.

This winding up rule applied both where the employer triggered a winding up of the scheme while solvent and if the scheme were to be wound up because of employer insolvency.³¹

Miss Robins and 335 other members of the 2 schemes brought a claim that the UK Government had failed to implement Article 8 correctly.

The Advocate General's opinion

Advocate General Kokott gave her opinion in this case on 13th July, 2006³².

The following are selected paragraphs (emphasis added) from that opinion which provide an insight into the careful and rigorous way the Advocate General was analysing Article 8.

*“36. The degree of protection afforded by Article 8 thus falls to be determined through the interpretation of the terms '**protection of interests in respect of rights conferring immediate entitlement to old-age benefits and 'necessary measures'**'. The degree of protection afforded by Article 8 will also be determined by a further condition, **namely the requirement of insolvency as the causative factor in the adverse effect on rights to old-age benefits.**”*

...

“38. If Article 8 thus seeks to protect the interest of employees in regard to their immediate or prospective entitlement to old-age benefits, this means, in other words, that it seeks to protect the interest of employees in securing payment of their pension claims.”

...

*“61 Furthermore, the claimants in the main proceedings correctly point out that these various bodies of rules differ significantly in terms of substance and are also not based on comparable interests. Non-payment of wages or salaries will be manifest to employees and most instances of such non-payment are usually of brief duration. In any event, employees can react to such matters relatively quickly. **Pension schemes, by contrast, are in the main of almost impenetrable complexity, and the effects of the non-materialisation of expected pension payments will be serious, long-term and scarcely amenable to correction.** Application of*

³¹ Section 73 of the Pensions Act 1975, as amended, sets out a statutory order of winding up priorities that overrides the terms of a scheme's governing legal documentation. From 6th April, 2005, when the PPF opened for business, it required the scheme assets backing defined benefits to be used, after expenses (and some very limited exceptions) first to provide benefits for all members at the level corresponding to the PPF compensation that would apply if the scheme were to enter the PPF. If the scheme cannot meet this test, then its assets are taken over by the PPF which provides compensation in place of the scheme benefits.

³² C-278/05.

Article 4(3)³³ to Article 8 by way of analogy is thus from the outset precluded by the lack of comparability between the areas of interest underlying those rules.”

...

“70. As an interim conclusion, it may therefore be held that Article 8 of Directive 80/987 **demands full protection for the interests of employees in regard to their rights to occupational old-age benefits should their employer become insolvent.**

“71 It is unnecessary to determine in the present case whether a restriction on this comprehensive protection may be justifiable in exceptional situations. The first recital in the preamble to **Directive 80/987** may suggest that exceptions to this generally comprehensive protection are possible. **That recital states clearly that protection of employees is to be provided for while at the same time account is taken of the need for balanced economic and social development in the Community; protection is thus not absolute.** Particular relevance in this connection attaches to the economic repercussions of safeguarding employees' claims. **Protective measures of this kind obviously involve considerable costs, which in turn affect the national economy.**“

“**In determining the level of protection under Article 8, however, the emphasis must be placed on the particularly extensive need of employees for protection with regard to their pension entitlements, as already outlined, in such a way that it can only be in a limited number of exceptional scenarios that consideration may be given to a diminution of what must in principle be full protection of employees' claims.** Should there be merely a reduced need for protection on the part of employees and if, on the other hand, comprehensive safeguarding will give rise to disproportionate costs, this may conceivably constitute an exceptional case in which, after a balance has been established which takes account of both aspects, a lower level of protection may be appropriate.”

“Moderate restrictions may, for instance, be envisaged with regard to the prospective rights of employees who are still well off pensionable age and can benefit from possibilities of compensation, **or in the case of elevated benefit claims that are significantly above the average**³⁴. There is, however, no evidence of any such exceptions here. Moreover, any such lowering in the level of protection would have to be statutorily prescribed on grounds of legal certainty.”

...

“83. As an interim conclusion, it may be held that Article 8 of Directive 80/987 in principle requires **full protection of employees' interests in regard to their acquired and prospective rights to benefits under an occupational old-age benefits scheme.** Under a benefits system characterised, as in the present case, by a **balance of costs scheme**, this protection also extends to the consequences for pension entitlements flowing from **under-financing of the scheme.** Article 8 does not, however, place Member States under an obligation to ensure this protection

³³ Which allows Member States to restrict the level of compensation for non-payment of wages (and other claims covered by Article 3) within certain parameters.

³⁴ This restriction is considered in *Hampshire* discussed in **Section 8** below.

by providing their own payments in the sense of imposing on them liability in respect of deficits.”

“100. On the basis of the foregoing considerations, I propose that the Court reply as follows to the questions referred to it by the High Court of Justice of England and Wales, Chancery Division:

- 1) Article 8 of Directive 80/987/EEC in principle requires full protection of employees' interests with regard to their acquired or prospective rights to benefits under company or inter-company old-age benefits schemes. The protection afforded by Article 8 of Directive 80/987 also extends to adverse effects resulting from the under-financing of the benefits scheme, if those adverse effects are attributable to insolvency.*
- 2) Article 8 of Directive 80/987 does not oblige Member States to guarantee the protection of employees' interests by means of their own payments.”*

(emphasis added)

It is worth drawing out the point made by the Advocate General in paragraph 100(1) of Opinion that Article 8 is to extend to the *“adverse effects resulting from the under-financing of the benefits scheme, if those adverse effects are attributable to insolvency”*.

This is consistent with the concept that, if the employer could wind-up the scheme, while the employer is solvent with no obligation to pay additional contributions to make good the shortfall, then, on the employer's insolvency, the members should not be placed in a better position than would otherwise have been the case.

Where the employer has not paid contributions to the scheme which it had agreed to pay, because of impending insolvency, it is possible to undertake a factual analysis to identify the amount by which the scheme assets were reduced and the impact on the level of benefits the scheme could provide.

Consider the example where the employer has paid all contributions it has agreed to pay to the scheme up to the scheme winding up trigger. The scheme is underfunded on a winding-up basis (because of the higher cost of securing benefits by buying annuities from an insurance company). In that case benefits are adjusted to have a value equal to the scheme assets in accordance with the scheme winding up rule.

The logical interpretation of Article 8 is that it should not require a greater level of protection on insolvency of the employer than if the employer while solvent had, in exercise of legal rights reserved to it, reduced scheme benefits or served a notice to wind up the scheme which had the same result.

A point to draw out is that the usual term of an employment contract in the UK is that the employee has the right to be a member of the pension scheme established under irrevocable trust subject to the employer's reserved right to terminate the scheme by notice to the trustee of the scheme. Apart from payment of any unpaid contributions, the employer assumes no contractual obligation under the employment contract to make up any shortfall relative to the amount by which the cost of securing the unreduced scheme benefits with an insurance

company exceeds the available scheme assets. However, as discussed above, additional obligations have been imposed on the employer by overriding legislation.

CJEU decision in Robins on 25th January, 2007

The CJEU did not follow Advocate General Kokott's opinion. The CJEU decided:

“54 According to unchallenged statements in the documents before the Court, two of the claimants in the main proceedings will receive only 20 and 49% respectively of the benefits to which they were entitled.

55 There being no obligation to guarantee entitlement to benefits in full, it remains to determine the minimum level of protection required by the Directive.

...

57 Nevertheless, having regard to the express wish of the Community legislature, it must be held that provisions of domestic law that may, in certain cases, lead to a guarantee of benefits limited to 20 or 49% of the benefits to which an employee was entitled, that is to say, of less than half of that entitlement, cannot be considered to fall within the definition of the word 'protect' used in Article 8 of the Directive.”

59 It must therefore be concluded that a system such as that established by the United Kingdom legislation does not ensure the protection provided for by the Directive and does not constitute proper implementation of Article 8 thereof.

60 That conclusion is not shaken by the introduction from 1 September 2005 of a scheme such as the FAS, even though that scheme is applicable to winding-up procedures initiated between 1 January 1997 and 5 April 2005.

61 It is apparent from unchallenged information contained in the documents before the Court that the FAS:

- does not cover members of the scheme who were more than three years away from retirement on 14 May 2004;*
- helps only about 11 000 of the non-pensioner members of the schemes concerned, that is to say, less than 13% of the total number of members.*

62 The answer to the second question must therefore be that a system of protection such as that at issue in the main proceedings is incompatible with Article 8 of the Directive.”

By way of context, the UK Government had put in place, from 1st September, 2005, a scheme called the Financial Assistance Scheme to protect pension rights for scheme winding-ups that occurred between 1st January, 1987 and 5th April, 1995.

The UK Pension Protection Fund was established by the Pensions Act 2004 and applied to employer insolvencies occurring after 5th April, 2005³⁵.

ASW Limited went into insolvent liquidation on 24th April, 2003. In contrast, the Rover Group went into insolvency on 8th April, 2005 (and so its pension scheme members were covered by the new Pension Protection Fund).

The reasoning of the CJEU set out above does not reflect the reduction in scheme benefits as discussed above that would apply whether or not the employer were insolvent and the scheme were to be wound up.

The next CJEU case is *Hogan* in April 2013

By way of additional context, it is important to remember that the IORP I Directive, which provided for funding obligations on employers where an IORP included a guarantee of benefits or cover against biometric risks (but excluding “regulatory own funds”), was required to be transposed into Member States’ domestic legislation by 23rd September, 2005³⁶.

The employer in relation to the 2 Irish defined benefit schemes the subject of *Hogan* became insolvent in 2009, after the IORP I transposition date.

6. Hogan v Ireland, decision of the CJEU on 25th April, 2013

Background

Waterford Crystal Limited became insolvent in 2009. This led to the winding up of 2 Irish defined benefit pension schemes (the “**Waterford Schemes**”) which it had set up.

Mr. Hogan and other members of these 2 pension schemes would, on their actuary’s evidence, see their benefits reduced to between 18% and 28% of the promised entitlements (if the scheme were not to be wound up).

The Irish Government’s actuary said the reductions would be between 16% and 41%. However, whichever way you do the numbers, the members would be receiving less than half of their promised entitlement (if the scheme were not to be wound up).

The CJEU in *Hogan* described the rights of a member of an Irish Article 8 OPS, such as the Waterford Schemes, as follows:

³⁵ See the Pensions Act 2004, Section 127 and SI 2005/275.

³⁶ See the IORP I Directive, Article 22(1).

“8 In such a scheme, the employees are entitled to a pension only on condition that their scheme has sufficient assets. Those assets are protected by the use of a trust, which segregates them from the assets of the employer.

*9 Under the national rules, the supplementary pension schemes are funded by contributions from both employer and employees. In the case of the employees, a fixed percentage of their salary is paid to the pension fund, while the employers make an annual contribution in order to ensure that **in the long term the supplementary pension scheme has sufficient assets to meet its liabilities.***

10 In order to determine the amount of the employer’s contribution, the Pensions Act 1990, as amended, requires an actuary to calculate the employer’s contribution in accordance with a specified standard known as the ‘Minimum Funding Standard’. It follows that the supplementary pension schemes are ‘balance of cost’ schemes, where the employer contributes annually the amount needed in addition to the employees’ contributions to balance the assets and liabilities in the long term.

11 The rules of the pension fund allow the employer to wind up the supplementary pension schemes at any time and thus to terminate its obligation to contribute to the schemes. Those rules provide that, in the event of the fund’s being wound up, whether because of the employer’s decision to terminate its liability, because of the insolvency of the employer or for any other reason, the employees are to receive a share of the assets of the fund.

12 In Ireland a defined benefit supplementary scheme may take account of the State pension. Such a scheme is called an ‘integrated pension’.

The transposition of Article 8 of Directive 2008/94 into Irish law

13 The national court states that the only measure of national law adopted for the express purpose of transposing Article 8 of Council Directive 80/987/EEC of 20 October 1980 on the approximation of the laws of the Member States relating to the protection of employees in the event of the insolvency of their employer (OJ 1980 L 283, p. 23), now Article 8 of Directive 2008/94, is section 7 of the Protection of Employees (Employers’ Insolvency) Act 1984, which provides that any contribution deducted by an employer, or due to be paid by that employer, during the 12 months preceding insolvency is to be paid into the supplementary occupational pension scheme.” (emphasis added)

Given the description of the rights of a member under an Irish Article 8 OPS, such as the Waterford Schemes, as determined by the CJEU (see above), the logical conclusion would appear, at this point in the analysis, to be that employer insolvency had no effect on the immediate or prospective entitlement to old-age benefits, including survivor benefits, under the 2 pension schemes. The only exception would be any unpaid employer contributions which would be protected under Article 3 or Article 8 depending on the choice made by the Member State under Article 6 of the Directive.

Mr. Hogan and others brought proceedings against the Irish Government for non-transposition of Article 8 into Irish law.

The decision of the CJEU

There was no Advocate General's opinion written in this case.

The CJEU's judgment included the following discussion of the nature of the pension rights of the members of the 2 defined benefit Irish pension schemes of Waterford Crystal Limited:

“22 By its first question the national court asks, in essence, whether Directive 2008/94 is to be interpreted as meaning that it applies to the entitlement of former employees to old-age benefits under a supplementary pension scheme set up by their employer.

23 In that question the national court refers to Article 1(1) of that directive and states that, in Irish law, in such a situation, there is no legal basis for a claim to be made by the plaintiffs in the main proceedings against their employer.

24 In that regard, it must be pointed out that, having regard to the fact that the plaintiffs were required, when they started work, to join the occupational pension scheme set up by their employer, their entitlement to old-age benefits under that scheme must be regarded as arising from the contracts of employment or employment relationships linking them to their employer, within the meaning of Article 1(1) of Directive 2008/94.

25 Article 8 of Directive 2008/94 imposes a specific obligation on the Member States in favour of employees. The Member States may fulfil that obligation by various means. That may be done by ensuring either that the employer is able to meet the obligations arising out of a supplementary occupational pension scheme or that the institution for occupational retirement provision, which is separate from the employer, is able to do so.

26 It is common ground that the plaintiffs in the main proceedings are former employees of a company who claim that their interests, as regards rights conferring on them immediate entitlement to old-age benefits under a supplementary occupational pension scheme, were not protected by Ireland in the event of the insolvency of their employer.

27 Consequently, the answer to the first question is that Directive 2008/94 must be interpreted as meaning that it applies to the entitlement of former employees to old-age benefits under a supplementary pension scheme set up by their employer.”

This then brings us to the issue of whether insolvency of the employer was the cause of the underfunding. The analysis and conclusion of the CJEU was as follows:

35 By its fourth question, the national court asks, in essence, whether Article 8 of Directive 2008/94 is to be interpreted as meaning that, in order for that article to apply, it is sufficient that the pension scheme is underfunded as of the date of the employer's insolvency and that, on account of his insolvency, the employer does not have the resources to contribute sufficient money to the pension scheme to enable the pension benefits owned to the beneficiaries of that scheme to be satisfied in full, or whether it is necessary for those beneficiaries to prove that there are other factors giving rise to the loss of their entitlement to old-age benefits.

36 *It must be pointed out that the purpose of Directive 2008/94 is the protection of employees in the event of the insolvency of their employer. It does not deal in any way with the causes of that insolvency.*

37 *There may be various causes for the underfunding of a supplementary occupational pension scheme, such as non-payment of contributions by employees or by the employer, unfavourable developments in the capital markets, poor management of the scheme's funds or insufficiently stringent prudential rules.*

38 *Nevertheless, Article 8 of Directive 2008/94 does not distinguish between those possible causes, but lays down a general obligation to protect the interests of employees and leaves it to Member States to define, in accordance with European Union law, **in particular Directive 2003/41/EC**³⁷ of the European Parliament and of the Council of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision (OJ 2003 L 235, p. 10), the methods by which they fulfil that obligation.*

39 *Therefore, in order for Article 8 of Directive 2008/94 to apply, **it is not necessary to identify the causes of the employer's insolvency or of the underfunding of the supplementary occupational pension scheme.***

40 *Consequently, the answer to the fourth question is that Article 8 of Directive 2008/94 must be interpreted as meaning that, in order for that article to apply, **it is sufficient that the pension scheme is underfunded as of the date of the employer's insolvency and that, on account of his insolvency, the employer does not have the resources to contribute sufficient money to the pension scheme to enable the pension benefits owned [sic]**³⁸ to the beneficiaries of that scheme to be satisfied in full. It is not necessary for those beneficiaries to prove that there are other factors giving rise to the loss of their entitlement to old-age benefits.*

(emphasis added)

It is, perhaps, worth noting the logical non sequitur from paragraphs 11 and 37 of the judgment to the conclusion in paragraphs 39 and 40. There may be a better argument for the conclusion based on the requirements of the IORP I Directive as to the funding of an IORP which provides a guarantee of benefits or cover against biometric risks or a guarantee of a given level of benefits as referred to in Articles 15 and 16 of the IORP I Directive. But, again, it disregards the scenario where an IORP is in balance, or surplus, on an ongoing technical provisions basis, at time of employer insolvency but the assets are insufficient to secure the full benefits on the winding up of the IORP by buying annuities from an insurance company.

The CJEU went on to decide:

*"51 As soon as the judgment in *Robins and Others* was delivered, namely on **25 January 2007**, the Member States were informed that correct transposition of Article 8 of Directive 2008/94 **requires an employee to receive, in the event of the***

³⁷ i.e. the IORP I Directive.

³⁸ Should read "owed".

insolvency of his employer, at least half of the old-age benefits arising out of the accrued pension rights for which he has paid contributions under a supplementary occupational pension scheme.

52 In those circumstances, it must be held that, although the nature and extent of the obligation incumbent on the Member States under Article 8 of Directive 2008/94, which is intended to confer rights on individuals, were clear and specific, at the latest as of 25 January 2007, Ireland had not correctly fulfilled that obligation, which constitutes a sufficiently serious breach of that rule of law in the context of any examination which might be carried out in respect of that Member State's liability for damage caused to individuals.

53 Consequently, the answer to the seventh question is that Directive 2008/94 must be interpreted as meaning that the fact that the measures taken by Ireland subsequent to Robins and Others have not brought about the result that the plaintiffs would receive in excess of 49% of the value of their accrued old-age pension benefits under their occupational pension scheme is in itself a serious breach of that Member State's obligations." (emphasis added)

The CJEU decision does not follow logically from the description of the legal rights of members of an Irish Article 8 OPS of the type before the CJEU in *Hogan* even deploying an argument based on the employer funding obligations deriving from the IORP Directive. Following *Hogan* an employee can be better off on employer insolvency than if his or her Irish Article 8 OPS were wound up before the employer became insolvent.

In this context Article 14(2) of the IORP II Directive provides as follows:

"(2) The home Member State may allow an IORP, for a limited period of time, to have insufficient assets to cover the technical provisions. In this case, the competent authorities shall require the IORP to adopt a concrete and realisable recovery plan with a timeline in order to ensure that the requirements of paragraph 1 are met again. The plan shall be subject to the following conditions:

(a) the IORP shall set up a concrete and realisable plan to re-establish the required amount of assets to cover fully the technical provisions in due time. The plan shall be made available to members or, where applicable, to their representatives and/or shall be subject to approval by the competent authorities of the home Member State;

(b) in drawing up the plan, account shall be taken of the specific situation of the IORP, in particular the asset/liability structure, risk profile, liquidity plan, the age profile of the members entitled to receive retirement benefits, start-up schemes and schemes changing from non-funding or partial funding to full funding;

*(c) in the event of winding up of a pension scheme during the period referred to in the first sentence of this paragraph, the IORP shall inform the competent authorities of the home Member State. **The IORP shall establish a procedure in order to transfer the assets and the corresponding liabilities of that scheme to another IORP, an insurance undertaking or other appropriate body.** This procedure shall be disclosed to the competent authorities of the home Member State and a general outline of the*

procedure shall be made available to members or, where applicable, to their representatives in accordance with the principle of confidentiality.”³⁹ (emphasis added)

A point to draw out is that if, at the time of insolvency of the employer, the IORP was fully funded on a technical provisions basis (or in surplus on a technical provisions basis), then there would be no requirement for a recovery plan.

A further point to draw out is that there is a distinction between an IORP funded on a long term ongoing basis and being fully funded, at any point in time, if the IORP has to wind up and benefits have to be secured by the purchase of annuities from an insurance company.

It is not possible, unless the provision of the benefits is to become unaffordable, for an IORP to be fully funded at all times on an ongoing basis and a winding up basis in all economic scenarios:

- in times on high inflation and high interest rates, the nominal value (or purchasing power) of the pension falls (assuming no guaranteed pension increases) but the cost of providing the nominal amount of the pension is low. In such a scenario the ongoing technical provisions may be higher than the cost of securing the benefits with an insurance company; particularly if they include provision for discretionary non-guaranteed pension increases.
- in times of low long term interest rates and low inflation, the cost of providing the nominal amount of the benefit is high (because the contribution towards meeting that cost from the investment return on the IORP assets is so much lower).

The next case involving Article 8 was a decision of the CJEU in *Webb-Sämann v Seagon*.

7. Webb-Sämann v Seagon, decision of the CJEU on 24th November, 2016

Background

Mr. Webb-Sämann was employed by Baumarkt Praktiker. Baumarkt Praktiker became insolvent in 2013 and Mr. Seagon was appointed to act as liquidator.

The claim related to contributions to an occupational old age pension scheme which Baumarkt Praktiker should have paid into the account of Mr. Webb-Sämann’s occupational pension scheme, Hamburger Pensionskasse.⁴⁰

³⁹ Article 14(2) corresponds to Article 16(2) of the IORP I Directive.

⁴⁰ A point to draw out is that Mr Webb-Sämann’s pension was provided under a different structure to that provided to Mr Bauer (see **Section 9** below) even though the Hamburger Pensionskasse was involved in both cases.

The unpaid amount of the employer contribution was €1,017. The effect of the non-payment of the contribution of €1,017 was that Mr. Webb-Sämann's monthly pension rights would be reduced by between €5 and €7 per month.

The CJEU decided that a reduction of between €5 and €7 a month was not within the scope of Article 8 on the fact pattern of the case. However, Mr. Webb-Sämann could claim in the liquidation of his employer for the non-payment of contributions like any other ordinary creditor.

The judgment contained the following important paragraph as a sign of change in the CJEU thinking on how Article 8 is to be applied.

“35 Although the Member States thus enjoy a wide margin of appreciation when implementing Article 8 of Directive 2008/94, they are nonetheless obliged, in accordance with the objective pursued by that directive, to ensure a minimum degree of protection for employees as required by that provision.

In that regard, the Court has already held that a correct transposition of Article 8 of that directive requires an employee to receive, in the event of the insolvency of his employer, at least half of the old-age benefits arising out of the accrued pension rights for which he has paid contributions under a supplementary occupational pension scheme (see, to that effect, judgments of 25 January 2007, Robins and Others, C-278/05, EU:C:2007:56, paragraph 57, and of 25 April 2013, Hogan and Others, C-398/11, EU:C:2013:272, paragraph 51), although that does not mean that, in other circumstances, the losses suffered could also, even if their percentage differs, be regarded as manifestly disproportionate in the light of the obligation to protect the interests of employees, referred to in Article 8 of that directive.” (emphasis added)

This brings us on to the *Hampshire* case.

8. Hampshire v The PPF, decision of the CJEU on 6th September, 2018

Background

Mr. Hampshire was employed by Turner & Newall Plc (“T&N”). He was made redundant in 1998 and took an early retirement pension at age 51. His normal retirement age under the pension scheme was age 62. His early retirement pension was £48,782 a year, before tax with annual increases of at least 3%.

The sponsoring employer became insolvent in July 2006 when Mr. Hampshire was aged 58. This was after the PPF had been established and was available to protect employees whose employers became insolvent after 5th April, 2005⁴¹. The T&N pension scheme assets were not

⁴¹ See Section 5 above.

taken over by the PPF as its assets were sufficient to provide benefits at at least the PPF level of compensation.

However, the T&N pension scheme was required to reduce pensions to a level assessed by the PPF to be affordable. In consequence, Mr. Hampshire's pension was reduced from £60,240 a year, which he would have received from the T&N pension scheme if his employer had not become insolvent, to £19,819 a year. He was below his PPF normal pension age of 62. £19,819 is 33% of £60,240. He also lost most of his rights to annual increases to his pension (as nearly all of his pensionable service was pre 6th April 1997⁴²).

Mr Hampshire claimed that the effect of the PPF rules was to reduce his pension below 50% and that, in calculating the 50%, full account should be taken of his level of guaranteed pension increases on pension derived from all of his pensionable service.

The PPF argued that the *Robins/Hogan* 50% minimum level of compensation was 50%, on average, across the affected employees and former employees and not on a minimum of 50% per such affected employee or former employee.

Decision of the CJEU

The CJEU decided that:

*“50 Consequently, Article 8 of Directive 2008/94 requires Member States to guarantee each individual employee, without exception, compensation corresponding to at least 50% of the value of their accrued entitlement under a supplementary occupational pension scheme in the event of his employer’s insolvency, although that does not mean that, in other circumstances, the losses suffered, even if less than 50%, could also be regarded as manifestly disproportionate in the light of the obligation to protect the interests of employees, referred to in that provision (see, to that effect, judgment of 24 November 2016, *Webb-Sämann*, C-454/15, EU:C:2016:891, paragraph 35). [see G1.8 above for text]*

51 Moreover, as stated, in essence, by the Advocate General in points 48 to 53 of her Opinion, in order to ensure the full effectiveness of the minimum protection afforded to employees in the event of their employer’s insolvency by Article 8 of Directive 2008/94, which requires that that protection lasts for the entire pension period, the compensation corresponding to at least 50% of the value of their accrued entitlement must be calculated taking into account the envisaged growth in the pension entitlement throughout that period, in order to prevent, as a result of the passage of time, the amount guaranteed falling below 50% of the initial value accrued for one pension year.

52 In the light of the above, the answer to the first and second questions is that Article 8 of Directive 2008/94 must be interpreted as meaning that every individual employee

⁴² The PPF does not provide pension increases from pension derived from pensionable service before 6th April, 1997. It only provides inflation related increases (capped at 2.5% a year) on pension derived from post 5th April, 1997 pensionable service. The Pensions Act 2004, Schedule 7, paragraph 28.

must receive old-age benefits corresponding to at least 50% of the value of his accrued entitlement under a supplementary occupational pension scheme in the event of his employer's insolvency." (emphasis added)

There is no discussion in the Advocate General's opinion or in the judgment of whether Mr. Hampshire's pension contained any element of enhancement amounting to an early retirement pension (rather than an actuarially neutral rearrangement of an old age pension to allow it to be drawn early).

So it is unclear from the facts:

- whether Mr Hampshire's early retirement pension was an actuarial equivalence of his old age pension payable from his normal pension age of age 62 (so it remained an old age pension), or
- whether it contained any elements of enhancement. If it contained any elements of enhancement, those elements of enhancement would not amount to an old age pension but would amount to an early retirement pension.

A ground for exclusion from Article 8 protections of the early retirement enhancement element (or of the early retirement pension element as distinct from the rearranged actuarially cost neutral old age pension) is discussed in **Section 12** below.

Direct effect of Article 8 of the Directive

Remember that Directives can have direct effect between the individual and a state or an emanation of the state if not correctly transposed⁴³.

The PPF is an emanation of the state for these purposes:

"In the light of the above, the answer to the third question is that, in circumstances such as those in the main proceedings, Article 8 of Directive 2008/94 has direct effect and may, therefore, be invoked before a national court by an individual employee in order to challenge a decision of a body such as the Board of the PPF." (emphasis added)

This brings us on to the most recent of the CJEU decisions on Article 8- *Bauer*.

9. Pension-sicherungs-verein Vvag v Bauer, a decision of the CJEU on 19th December, 2019

⁴³ See, CJEU decisions referred to in *Farrell*, C413/15, paragraphs 32 and 33, a decision of the CJU on 10th October, 2017. Those decisions include *Marshall* and *Foster v British Gas* (the State, and emanations of the State, are prevented from pleading incorrect transposition/non-transposition of a requirement of a Directive into domestic legislation). Brexit should not affect the application of the *Bauer* Underpin as the CJEU decision pre-dates 31st December, 2020. See **Section 1** above.

Background

Mr. Bauer was granted, by a former employer, an, in general, unfunded occupational old age pension within the meaning of the German law on occupational pensions. However, part of Mr. Bauer's unfunded pension was paid by the Hamburger Pensionskasse. The amount paid by the Pensionskasse reduced the amount of Mr. Bauer's unfunded pension paid by his former employer on a Euro for Euro basis.

The Pensionskasse experienced financial difficulties and the pension paid from it was reduced each year from 2003 to 2013 by approximately 1.25% to 1.4% a year with a cumulative loss of approximately 13.8%. The loss corresponded to 7.4% of the total of Mr. Bauer's total unfunded pension. Mr. Bauer's former employer became insolvent in January 2012.

Pension-sicherungs-verein Vvag (the "PSV") is the German equivalent of the UK Pension Protective Fund. It took over full payment of Mr. Bauer's unfunded pension following the insolvency of his employer but excluding the amounts that should have been payable in full by the Pensionskasse. The Pensionskasse continued to pay Mr. Bauer a reduced pension as outlined above.

Opinion of Advocate General Hogan in Bauer on 8th May, 2019

Advocate General Hogan revisited the prior interpretation of Article 8 of the Directive by the CJEU and proposed a more generous interpretation:

*"75. To that extent, therefore, I believe that **the Court should move on** from decisions such as *Robins* and answer the second question to the effect that the circumstances to which the Court referred in **paragraph 35** of the judgment of 24 November 2016, *Webb-Sämann* (C-454/15, EU:C:2016:891), are those in which the claimant proves that the Member State has not fulfilled its obligation to ensure that the necessary measures were taken to protect the interests of employees or of persons having already left the employer's undertaking and **where the reduction in pension rights is at a level which is either not de minimis or which otherwise impairs the essence of the occupational pension entitlements which, but for the employer's insolvency, the retiree had every reason to anticipate receiving.**" (emphasis added)*

He concluded (at paragraph 98(2)) that "protection" in Article 8 is **not** provided:

*"where the **reduction** in pension rights is **at a level** which is **either not de minimis or which otherwise impairs the essence** of the occupational pension entitlements which, **but for the employer's insolvency, the retiree had every reason to anticipate receiving.**" (emphasis added)*

The CJEU did not follow the Advocate General's approach. But it did pull a rabbit out of a hat.

Decision of the CJEU in Bauer

The CJEU, on 19th December, 2019, decided:

"36 It follows from the above considerations that the answer to the first question is that Article 8 of Directive 2008/94 must be interpreted as applying to a situation in which an employer, which provides occupational old-age pension benefits through an inter-

occupational institution, cannot, on account of its insolvency, offset losses resulting from a reduction in the amount of those benefits paid by the inter-occupational institution, a reduction which was authorised by the State supervisory authority for financial services which is the prudential regulator for that institution.”

...

*“46 In the light of the above considerations, the answer to the second question is that Article 8 of Directive 2008/94 must be interpreted as meaning that **a reduction in the amount of occupational old-age pension benefits** paid to a former employee, on account of the insolvency of his or her former employer, is regarded as being manifestly disproportionate, even though the former employee receives at least half of the amount of the benefits arising from his or her acquired rights, where, as a result of the reduction, the former employee is already living, or would have to live, below the at-risk-of-poverty threshold determined by Eurostat for the Member State concerned.”*

(emphasis added)

It is difficult to see how anyone could have deduced the at-risk-of-poverty threshold determined by Eurostat as one of the levels of protection required under Article 8. This has the look and feel of the CJEU assuming a legislative role and not a judicial role. It is not consistent with the concept of legal certainty.

There is no temporal limitation on the judgment. So affected scheme members can claim for arrears of compensation subject only to any applicable laws imposing a time limit on bringing claims in the jurisdiction in question.

What is the UK’s at-risk-of-poverty threshold?

For the calendar year ended 2018, for an individual to be at risk of poverty, he or she had to live in a household which had an annual equivalised household disposable income of £11,142 pa⁴⁴. This figure uses a single adult household as the base unit.

The Eurostat figure for the UK for 2018 is €12,878⁴⁵. No later figure is available as at 22nd March, 2021.

As an aside, it would be interesting to see whether Eurostat will continue to produce these figures for the UK post Brexit. However, the working assumption is that, if there were

⁴⁴ The £11,142 comes from an email dated 20th December, 2019 from the UK Office of National Statistics to Philip Bennett.

⁴⁵ Source: This Eurostat weblink: https://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ilc_li01&lang=en# accessed on 22nd March, 2021.

challenge in the UK court, the court would identify an equivalent. The counter argument would be that the Bauer Underpin would be void for uncertainty.

What is the Netherland's at-risk-of-poverty threshold?

On the assumption that the CJEU was referring to a single person household, for 2019 the at-risk-of-poverty threshold in the Netherlands was €14,767⁴⁶. The provisional 2020 figure for the Netherlands is €15,404⁴⁷.

Implications of Bauer

The consequence of the decision in *Bauer* is that Article 8 requires a pension protection arrangement to include an underpin equal to the lower of:

- the at-risk-of-poverty threshold applicable to the member (an ongoing annual test), and
- what would have been the member's pension from the pension arrangements of the insolvent employer had the employer insolvency not occurred,

(the “**Bauer Underpin**”).

Where a Member State pension protection arrangement (including, for this purpose the UK ⁴⁸) does not have that Bauer Underpin, then that Member State's pension protection arrangement will need to provide a Bauer Underpin. As noted in **3.3** above, affected members will have claims for arrears subject to any limitation periods under the laws of the jurisdiction in question.

The practical operation of the Bauer Underpin should not be underestimated.

In brief, a scheme would need to collect the following data each year in respect of the member whose pension is in payment:

- the member's after tax income from all sources, and
- the at-risk-of-poverty threshold amount for the year,

and then calculated retroactively whether the member needs an additional top up payment calculated on an after tax basis for that year upto the amount required to satisfy the Bauer underpin.

There will be a time lag in that figure being available for that year unless it is permissible to use the latest published threshold figure. For example, the figure for 2020 will not be available until some time in 2021.

⁴⁶ Source: This Eurostat weblink: https://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ilc_li01&lang=en# accessed on 22nd March, 2021.

⁴⁷ Ibid.

⁴⁸ See discussion in **Section 1** above.

The normal drafting solution is to specify the reference period figure to use; for example the latest Eurostat published figure at the time the test is being applied and to use the member's after tax income for the previous year.

But it looks as if the CJEU made an elementary mistake of not realising that there is always a time lag between the end of a year and the threshold figure for that year being published by Eurostat and that after tax income for a year will not be known until the following year (and that the tax year may not run on a calendar year -in the UK, it runs from 6th April in year 1 to 5th April in year 2).

If the benefit is a combination of a taxable defined benefit pension and a defined benefit tax free lump sum, it remains unclear how credit for the lump sum would be provided.

In the normal legislative process, consultation with interested parties might be expected to take place so that some of the practical problems could be resolved in advance (and an elementary mistake avoided).

10. Overview of the UK Pension Protection Fund

What types of schemes are covered?

The PPF was established by the Pensions Act 2004⁴⁹. It covers eligible schemes which, in brief, are tax approved funded occupational pension schemes set up under irrevocable trust by employers in the UK.⁵⁰ A point to draw out is that it does not cover unfunded schemes.⁵¹

Trigger events for possible entry into the PPF

If the employer in relation to an eligible scheme becomes insolvent⁵², then that is the trigger for an assessment of the scheme. If it is underfunded on the valuation measure used by the PPF:

- the scheme assets are transferred to the PPF,
- members' claims to pension rights from the scheme are extinguished, and
- those rights are replaced by rights to compensation from the PPF.

The position is more complex for schemes with 2 or more employers and is outside the scope of this paper.

⁴⁹ See Part 2 of that Act.

⁵⁰ The Pensions Act 2004, Section 126 and the Pension Protection Fund (Entry Rules) Regulations 2005

⁵¹ For example, of the type described in *Granada Group v Law Debenture* [2016] EWCA Civ 1289.

⁵² Special rules outside the scope of this paper apply to multi-employer schemes.

How is the PPF financed?

The PPF is financed by a levy on eligible schemes. That levy is payable by the trustee of the scheme out of the scheme assets. But it is, in economic terms, borne by the employer in relation to the scheme, as an increase to the amount of the employer's contribution.

PPF compensation levels

If the member has reached normal pension age for PPF purposes⁵³, compensation is:

- equal to the pension in payment, but no increases will be provided in the future on the part of the pension derived from pre 6th April, 1997 pensionable service, and
- pension increases on pensions derived from post 5th April, 1997 pensionable service are increased each year are in line with inflation (measured using the Consumer Prices Index) capped at 2.5%⁵⁴

If the member has not reached normal pension age for PPF purposes, then:

- a 10% reduction applies to the accrued pension.
- if after the 10% reduction the pension still exceeds the compensation cap, the pension is further limited to the compensation cap (but see below).
- future pension increases are limited to the same extent as for the member who has reached normal pension age for PPF purposes (see above).

Compensation cap: position before decision in Hughes on 22nd June, 2020

Prior to the decision of the High Court in *Hughes* (discussed in **Section 13** below), PPF compensation in respect of a pension with a normal pension age for PPF purpose of 65 and which was not in payment at the time of the employer insolvency was limited to 90% of the compensation cap.

The compensation cap for age 65 for the year starting 1st April, 2021 is £41,461 (so 90% of £41,461 equals £37,315)⁵⁵. However, for members with 21 or more years' pensionable service, the compensation cap is increased by 3% for each full year of pensionable service over 20 upto a maximum of 2x compensation cap applicable to the member⁵⁶.

Following the CJEU's decisions in *Hampshire* and *Bauer* the compensation for a member who had not reached normal pension age for PPF purposes was also subject to 2 further underpins:

- a minimum of 50% of what the pension would have been but for employer insolvency at any point in time (so taking account of revaluation of deferred pensions and increases to in payment pensions required to be provided by law

⁵³ The earliest age at which the member may draw benefits as of right unreduced and ignoring special circumstances such as ill-health see Pensions Act 2004, Schedule 7, paragraph 34.

⁵⁴ The Pensions Act 2004, Schedule 7, paragraph 28.

⁵⁵ The Pensions Act 2005, Schedule 7, paragraphs 26 and 26A. The compensation cap varies actuarially by reference to the normal pension age in question.

⁵⁶ The Pensions Act 2004, Schedule 7, paragraph 26A.

and the scheme rules of the scheme in question) – but see the next paragraph below, and

- the Bauer Underpin.

For completeness note that the specific requirement in the CJEU judgment in *Hampshire* is a reference to value (not an amount at each point in time through the life of the member):

52 In the light of the above, the answer to the first and second questions is that Article 8 of Directive 2008/94 must be interpreted as meaning that every individual employee must receive old-age benefits corresponding to at least 50% of the value of his accrued entitlement under a supplementary occupational pension scheme in the event of his employer’s insolvency.” (emphasis added)

The meaning of paragraph 52 of the CJEU’s judgment in *Hampshire* was considered in *Hughes*- see **Section 13** below.

11. Ramifications of the CJEU cases on Article 8 of the Directive for Dutch pension schemes⁵⁷

Legal form of Dutch pension funds: the IORP

Direct pension promise pay as you go book reserve schemes of the type in *Bauer* are prohibited under Dutch law.⁵⁸

All Dutch pension funds established after 2015 are required to have the legal form of a Stichting. However, prior to 2016 it was possible for a Dutch pension fund to have a separate legal personality (e.g a BV) although not established as a Stichting. That said, even before 2016, pension funds in The Netherlands were typically established as Stichtings. This section discusses the position on the basis that the legal form of the pension fund is a Stichting (although, as a practical matter, little turns on this point).

Under Dutch law, a “Stichting” is a body corporate which has its own separate legal personality (ie. just like any other company). But a Stichting set up to provide pension benefits has a limited purpose under its constitutional documents of using the assets of the Stichting to provide those benefits to the members of the Stichting (ie. the employer’s employees and the former employees and their respective survivors). The members derive their rights as against the Stichting from the memorandum and articles of association (or the Pension Regulations) of the

⁵⁷ This Section draws heavily on an article by the authors “How do CDC schemes qualify under the IORP II Directive?” in *VUZF Review*, (2), 67.

⁵⁸ The so called ‘DGA’ – where a ‘director-major shareholder’ could build up pension rights in his own company, was allowed under Dutch law. This has been abolished in 2017.

Stichting which confer legally enforceable rights to the pension benefits on the member against the Stichting⁵⁹.

The relationships between the interested parties in relation to the Stichting can be analysed as a triangular relationship:

- **Relationship 1:** Employer to employee (under the contract of employment including any terms incorporated via the collective bargaining agreement between the employer or the employer's association and the recognised trade union) which provides for the terms on which the employer will make available, via the Stichting, pension benefits. This agreement is called a "*pensioenovereenkomst*" or a Pension Agreement⁶⁰.
- **Relationship 2:** Between the employer and the Stichting under which the employer has agreed with the Stichting under a funding agreement as to the amounts (or "premiums") it will contribute to the Stichting to fund the retirement benefits to be provided by the Stichting to the employees of the employer (and their surviving dependants), which such benefits are more particularly described in the memorandum and articles of association (or Pension Regulations) of the Stichting. This agreement is called a "*uitvoeringsovereenkomst*" or an Administration Agreement.
- **Relationship 3:** Between the employee/member (including surviving eligible dependants) and the Stichting. The Stichting is required by the memorandum and articles of association (or Pension Regulations) of the Stichting to make payments to the member (and his or her eligible surviving dependants) of the benefits as determined in accordance with the terms of the memorandum and articles of association (or Pension Regulations) of the Stichting. These arrangements are referred to as the "*pensioenreglement*" or Pension Regulations.

In The Netherlands, it is possible, as an alternative to using a Stichting, for the retirement benefits to be provided:

- by an insurance company (ie. premiums are paid to the insurance company by the employer to purchase retirement benefits for the employee under an insurance contract), or
- by a premium pension institution⁶¹.

⁵⁹ Lutjens, 2016: Mr. C. Assers Handleiding tot de beoefening van het Nederlands Burgerlijk Recht. 7. Bijzondere overeenkomsten. Deel XI. Pensioen, Alphen aan den Rijn: Wolters Kluwer.

⁶⁰ Lutjens 2013: Pensioenwet: Analyse en commentaar, Alphen aan den Rijn: Wolters Kluwer / Commentaar op Voorontwerp Wet invoering reële ambitieovereenkomst', Tijdschrift voor Pensioenvraagstukken, 4, 31-39.

⁶¹ Borsjé, H. van Meerten, 2015: 'A EU Pensions Union', in Pennings, F. et al. (eds) Research Handbook on European Social Security Law, Cheltenham: Edward Elgar Publishing.

As set out in previous research⁶², there must be a distinction between two archetypes of pension frameworks. In the first archetype, the IORP is an independent legal entity, at some distance from the employer, with full recourse to its own funds. The IORP has up-front provisions on its balance sheet to bear biometric risks or to guarantee a certain investment performance or level of benefits. This IORP is the most common in The Netherlands⁶³. It is classified as a regulatory own fund for the purposes of the IORP II Directive, Article 15.

In the second archetype, the sponsor and the IORP are closely related and the IORP may have been set up by the sponsor. The sponsor provides the ultimate pension security to its employees and stands ready to supply financing in the event of an adverse shock to the IORP. This type of IORP is, in our view, not a regulatory own fund for the purposes of the IORP II Directive (because of the employer support).⁶⁴

The pension schemes

The pension schemes serviced by the IORP can, in principle, be either of a Defined Benefit (DB) or a Defined Contribution (DC) nature.

A DB pension plan guarantees to deliver benefits at retirement that are predefined in the accumulation phase, and are usually based on an employee's final or average pensionable pay and length of service.

In a DC pension plan, contributions paid by employers (and/or employees), determine the amount of benefits that are delivered on retirement. The accumulated pension assets (and, therefore, the actual benefits that can be delivered at retirement) depend on the level of contributions and the financial returns from investing those contributions (and the charges and expenses paid out of those pension assets).

In addition a range of hybrid schemes are possible. The most publicised ones are Collective Defined Contribution (“CDC”) schemes.

The first CDC schemes started in The Netherlands in the beginning of 2000. The benefit structure is, in general, an average salary benefit structure with conditional revaluation before the pension comes into payment and conditional indexation once the pension is in payment.

In this paper a distinction is drawn between the increase of the accrued but not in payment pension (referred to as revaluation) and the increase to the pension in payment referred to as

⁶² Borsjé, Van Meerten, 2016: ‘Pension Rights and Entitlement Conversion (‘Invaren’): Lessons from a Dutch Perspective with Regard to the Implications of the EU Charter’, *European Journal of Social Security*, 18, 46-73.

⁶³ Van de Griend, Van Meerten, 2017: ‘Hervorming pensioenstelsel: degressieve opbouw in uitkeringsovereenkomsten en vlakke premies in premieovereenkomsten’, *SEW: Tijdschrift voor Europees en economisch recht*, 5, 189-198.

⁶⁴ However, in the Netherlands, some of these pension funds fall under Article 15 of IORP II, because there is no statutory obligation to make good the deficits.

indexation. The rates of revaluation and indexation may be identical or they may differ depending on the benefit design.

CDC schemes were introduced in The Netherlands by way of response to changes in accounting standards which had the effect of bringing the deficits in Dutch defined benefit schemes on to the balance sheet of Dutch companies. So the CDC scheme provided a similar benefit structure to a traditional Dutch defined benefit pension scheme providing average salary benefits, but with the employer contribution rate being fixed as a percentage of pensionable pay (but for a period of no more than 5 years⁶⁵. The key point is that, even if the employer contribution rate is re-negotiated after the end of that period, of up to 5 years, there would be no legal requirement to pay any deficit make up contributions).

However, the funding regime and other attributes of regulation of the Dutch CDC scheme, including in relation to conditional revaluation and conditional indexation, seem similar to those for a “traditional” Dutch defined benefit pension scheme.

A point to draw out is that, in many ways, the “traditional” Dutch defined benefit pension scheme which provides average salary benefits with conditional revaluation and conditional indexation is the same as the Dutch CDC scheme.

In terms of outturns for members, if the liabilities of the scheme (ie. the technical provisions) plus the solvency margin exceed the value of the assets of the scheme, then:

- there is no future conditional revaluation and no future conditional indexation granted (because it is conditional on the revaluation and indexation being affordable (measured by reference to the margin by which the value of the scheme’s assets exceeds the value of the scheme’s accrued “nominal” or “guaranteed” liabilities plus a buffer)).
- if the deficit is not made good along with the required “buffer” or “solvency margin” within a 5 year period (to restore the funding position back to the Minimum Required Funding Level), then it will be necessary to reduce the “nominal” benefits (whether in payment, in deferment or accrued for active members) in order to balance the books usually over a period of 10 years by equal reductions.

A common feature of a CDC scheme is that risks and rewards are shared, in accordance with the risk sharing rules provided for under the scheme’s governing legal documents, amongst the members of the scheme whether within a generation of members or a particular group. For example, this group could be a 5 year cohort of a generation of members. Alternatively, the risks and rewards could be shared across generations of members. The key point is that the employer has no greater obligation than to pay the contributions it has agreed to pay to the scheme to finance the non-guaranteed benefits.

Using this conceptualisation, it becomes clear that a CDC scheme, unlike a DB scheme, does not offer guarantees but instead in these schemes the participant, rather than an external sponsor, bear the risks of any shortfalls between the assets of the pension fund and the target

⁶⁵ DNB, 2015: See for more details the explanation of the Dutch Central Bank (DNB, 2015) of this 5 year requirement: <http://www.toezicht.dnb.nl/3/50-228388.jsp#>.

benefits of the pension fund. These Dutch schemes have evolved from traditional defined benefit (DB) schemes with employers as external risk sponsors⁶⁶.

Therefore, no buffers are required. Hence it seems clear that CDC schemes cannot be DB schemes, not even if the way pension accrued is similar or even alike as in DB schemes.

Article 10 of the Dutch Pensions Act says that there are three types of pension scheme:

- (a) *een uitkeringsovereenkomst* (a DB scheme).
- (b) *een kapitaalovereenkomst*; (a hybrid scheme, in which the amount of capital that can be accrued is agreed).
- (c) *een premieovereenkomst* (a DC scheme).

A Dutch CDC scheme is not defined in law. It is not defined as being category (a), (b) or (c).

The Explanatory Memorandum relating to Article 10 of the Dutch Pensions Act 2007⁶⁷ says (translated):

“In a CDC scheme too, therefore, one of these three forms of (declining) risks will always be present for the members of a pension scheme, based on the content of the pension scheme (and not on the basis of the name) and the communication about this with the participants, it will be necessary to assess the type of pension scheme”

In other words, if the Pension Agreement qualifies the CDC scheme as an uitkeringsovereenkomst, it is a DB scheme.

Protection of accrued rights under a Dutch pension scheme: Protection against reducing accrued rights

Article 20 of the Dutch Pensions Act includes protection for accrued rights but does not prevent those accrued rights being amended in accordance with the terms of any reserved rights to do so (or in accordance with any mandatory obligation on the pension fund to do so). Articles 76, 78, 83 and 134 of the Dutch Pensions Act allow for pension rights of beneficiaries to be restricted or reduced (i.e. they are not fixed).

Under Pensions Regulations of the Stichting (and Article 134 of the Dutch Pension Act), provision will be made for benefits to be reduced if the scheme is underfunded and cannot recover its Minimum Required Funding Level (see below) over a recovery period (currently on average, depending on the facts, 5 years).

The Pensions Regulations of the Stichting must contain information about the possibility of benefit reductions in accordance with Article 134. In the context of good governance, it is

⁶⁶Bovenberg, Mehlkopf, Nijman, 2014: 'The Promise of Defined Ambition Plans: Lessons for the United States', Pension Research Council The Wharton School, University of Pennsylvania, PRC WP 2014-15.

⁶⁷ Dutch Pension Act 2007, Kamerstukken II 2006-2007, 30 413, nr. C, <https://zoek.officielebekendmakingen.nl/kst-20062007-30413-C.html>.

important adequately to inform the (former) participants that accrued entitlements and rights can possibly be reduced.

Where benefits are cut, this is a uniform reduction applied to:

- all pensions in payment,
- all deferred pensions, and
- all accrued pensions.

As noted above, there is an initial permitted 5 year recovery period before any cuts to accrued pension benefits (including those in payment) have to be made. Thereafter cuts to accrued benefits in payment (including those in payment) have to be made on a uniform basis over a 10 year period to bring the value of the scheme's liabilities back in to line with the value of the scheme's assets to at least the Minimum Required Funding Level.

Article 134 of the Dutch Pensions Act says as follows:

- “1. A pension fund may only reduce acquired pension entitlements and pension rights if:*
- a. the technical provisions and the minimum funding requirements are no longer completely covered by assets;*
 - b. the pension fund is not able, to cover the technical provisions and the minimum funding requirements by assets within a reasonable term without disproportionately comprising the interests of scheme members, deferred beneficiaries, pensionable persons, other entitlement beneficiaries or the employer; and*
 - c. all other available steering instruments, with the exception of the investment policy, have been deployed as developed in the short-term recovery plan referred to in Article 140.*
- 2. A pension fund will inform the scheme members, deferred beneficiaries, pensionable persons and the employer in writing concerning the resolution to reduce pension entitlements and pension rights.*
- 3. The reduction referred to in the first paragraph may not be effected earlier than one month after scheme members, deferred beneficiaries, pensionable persons, employer and supervisory body have been informed thereof.”*

Points to note on protection of accrued rights

Under this approach, the Stichting, prima facie, cannot (in principle) become insolvent for its pension liabilities because it has a mechanism for “balancing its books”.

Whether the employee has a claim against the employer if there is a reduction in benefits in the Dutch DB or CDC scheme in this underfunding situation will primarily depend on the applicable terms of the contract of employment (including any collective bargaining agreement) applicable to the employee in question (ie. the Pension Agreement).

It is possible that the terms of the Administration Agreement between the employer and the Stichting may make provision for additional payments in this situation (or the funding

agreement may just be limited to an agreement to pay contributions for a specified period and to agree, thereafter, separately, the contributions to be paid for another specified period).

Application of the IORP Directive to CDC schemes

A Dutch “*pensioenfond*s” is treated, under Dutch legislation, as a regulatory own fund (falling within Article 15 of the IORP II Directive). In other words, a conscious decision by The Netherlands to treat such a pension scheme as if it provided a guarantee of benefits and cover against biometric risk – even though the benefits may be reduced to reflect underfunding⁶⁸ (and see also above).

This means that, under Dutch legislation, the “buffer” capital requirements for a regulatory own fund specified in Articles 16-18 of the IORP II Directive are applied. Under the “*Financieel Toetsingskader*” or “FTK”, a pension fund must value its assets and liabilities at fair value. These provisions are transposed into Dutch law by the Dutch Pensions Act, Articles 125a-150 which provides for the Financial Assessment Framework.

Article 13(5) of the IORP II Directive says that the home Member State:

‘May make the calculation of technical provisions subject to additional and more detailed requirements, with a view to ensuring that the interests of members and beneficiaries are adequately protected.’

The Dutch legislation referred to above as implemented by De Nederlandsche Bank (the “**Dutch Central Bank**”) has set out in a prescriptive manner the way in which discount rates are to be determined (under the FTK), ex article 134 of the Dutch Pensions Act.

In particular, under the FTK, it is necessary to use a discount rate for determining the value of future “nominal pension benefits” (ie. excluding conditional revaluation and conditional indexation) based on the “Ultimate Forward Rate” (ie. the risk free rate derived from the capital markets applicable to the expected duration of the pension in question). This is the rate used within The Solvency II Directive (Directive 2009/138/EC [recast]) for insurers who are also supervised by the Dutch Central Bank.

The pension fund must set its funding requirements so that:

“The probability of the pension fund having less assets at its disposal than the amount of the technical provisions within a year is reduced to 97.5%”

This particular requirement will feed into the risk management process of the pension fund and the investment strategy of the pension fund.

⁶⁸ Van Meerten, 2008: ‘De premiepensioeninstelling; van, maar ook op alle markten thuis?’, *Nederlands tijdschrift voor Europees recht*, 12, 347–355 / 2009: ‘Pension reform in the EU: recent developments after the implementation of the IORP Directive’, *Pensions: An International Journal*, 14(4), 259–272.

There are 2 funding tests that apply to the pension fund:

- the fair value of the assets of the pension funds is equal to at least, in summary, 104.2% of the amount of its pension obligations (this would not include future conditional revaluation or conditional indexation) valued using the Ultimate Forward Rate as the discount rate – call this the “**Minimum Required Funding Level**”.
- that the fair value of the assets of the pension fund is equal to at least its capital requirement (based on its risk profile): approximately 125% (for an average pension fund) of the amount of its pension obligations (this would not include future conditional revaluation or conditional indexation) valued using a discount rate which depends on the risks involved in its assets and the liability profile of the pension fund – call this the “**Higher Required Funding Level**”.

The Higher Required Funding Level is relevant to whether the pension fund can grant conditional revaluation and conditional indexation (see further below). The amount by which the Higher Required Funding Level exceeds the Minimum Required Funding Level can be viewed as a further “solvency buffer”.

Where the funding level of the pension fund has fallen below the Minimum Required Funding Level, the pension fund must submit a recovery plan to the Dutch Central Bank which increases the funding position of the pension fund back to the Minimum Required Funding Level within a fixed 10 year period.

If the funding level has not recovered on 5 subsequent consecutive annual valuation dates from the valuation date showing that the Minimum Required Funding Level is not met, then accrued pensions (ie. both in payment and not yet in payment) are to be reduced on a proportionate basis spread over period of 10 years.

Conditional revaluation and conditional indexation cannot be granted during any period when the funding level of the pension fund is below the Minimum Required Funding Level. Where the funding level of the pension fund is at least 110% of the Minimum Required Funding Level but not above the Higher Required Funding Level, then conditional indexation may be granted on a proportionate basis.

In The Netherlands it is the benefits that are reduced rather than the employer that has to pay more contributions to make good the deficit. The exceptions are where the employer:

- has agreed under its Administration Agreement (or funding agreement) with the Stichting to make good the shortfall (which would not be the case in multi-employer (this term is used in the sense of employers operating, for example, in the same industry sector but where those employers are not in the same corporate group) traditional defined benefit scheme or in the case of some CDC schemes)⁶⁹, or

⁶⁹ The Dutch Court of Appeal held in 2008 that the Dutch Pension Act does not contain an unconditional obligation for, in casu, Akzo Nobel to make up a deficit of the pension fund of Akzo Nobel. See: ECLI:NL:GHARN:2008:BE9201.

- has agreed, directly or indirectly, with its employees under the contract of employment (or Pension Agreement) to procure that a particular level of benefits is provided, in which case the employee would have a right for breach of contract to claim damages. This happened in the case of *Pensioenfondsen Alcatel-Lucent/Alcatel-Lucent*⁷⁰.

**Protection of pension benefits on an employer’s insolvency in The Netherlands:
Amount of claim on the employer**

The Stichting will claim on employer for any arrears of contributions payable under the Administration Agreement (or funding agreement) in place between the Stichting and the employer.

The Stichting will rank as an unsecured creditor for contributions falling due for payment prior to the insolvency of the employer. Until the employer’s participation in the pension scheme is terminated by the trustee in bankruptcy, contributions falling due for payment after insolvency are claims on the assets held by the trustee in bankruptcy which will be paid out ahead of liabilities relating to periods prior to the date of insolvency of the employer.

The Dutch Employee Insurance Agency (the “*Uitvoeringsorgaan Werknemerverzekeringen*” or “**UWV**”) will take over the employer’s obligation to pay pension contributions in a situation where the employee would otherwise lose his or her pension rights because of the employer’s non-payment of the pension fund contributions. This type of payment would be covered for the period of no longer than 1 year. This legislation gives effect to Article 3 of the Directive.

There is no Dutch equivalent to Section 75 of the UK Pensions Act 1995 which imposes, where a defined benefit pension scheme is in deficit, on the happening of certain trigger events, a statutory debt on the employer equal to the pension scheme deficit (which has to be calculated on a “buy-out basis”, i.e. the cost of insuring the defined benefit benefits of the members with an insurance company).

Benefit obligations of pension scheme are adjusted so as to match available assets of pension scheme (ie. so the stichting continues to pay the (reduced) benefits).

Unless the employer has agreed to make up the deficit under its Administration Agreement (or funding agreement), there is no substantive claim on the employer by a Stichting (reflecting that any underfunding results in not granting (or reducing) future conditional indexation and, if necessary, reducing the members’ accrued pension rights (whether or not in payment).

Is a pension protection fund required in respect of a Dutch Article 8 OPS to comply with the Directive?: Preliminary

Under Dutch legislation, no provision is made for a pension protection fund as member benefits reduce on a pro rata basis to make good any underfunding whether before or after employer insolvency. The Stichting can, of course, become insolvent for its ‘normal’ (ie. non-pension) liabilities.

⁷⁰ Dutch Supreme Court on 10th June, 2016, ECLI:NL:HR:2016:1134, NJ 2016/450.

Reliance, instead, is placed on the strict funding standards for delivery of the nominal pension benefits (with the additional solvency buffer and with the conditional revaluation and conditional indexation serving as further buffers where that is part of the benefit design).

The analysis is that there is no requirement to have a pension protection fund in order to comply with Article 8 where there is no legally binding obligation on the employer to make good any deficit in relation to the pension scheme (as would be the situation for a Dutch industry wide defined benefit pension scheme or a Dutch CDC scheme).

Instead, benefits are reduced where the assets of the pension fund are insufficient to cover the liabilities of the pension fund after allowing for the recovery mechanisms referred to above. This, in part, is a function of the employer having no mandatory obligation under Dutch legislation to make up a deficit in the pension fund in contrast to the position in the UK.

The reason for this conclusion is that the solvency or insolvency of the employer is not related to whether benefits are or are not reduced. That said the ECJ has not drawn such a clear distinction in its analysis- see *Hogan* at paragraphs 22 to 27 set out in **Section 6** above.

That said, the impact of the financial crisis on traditional Dutch defined benefit pension schemes has included the following: the average cut in pensions during the financial crisis was 2-6%; some schemes' pensions had to be cut by grosso modo 20% (although this can be done gradually over a 10 year period⁷¹). In other schemes there has been no conditional indexation granted for many years. This is a consequence of the change from an average nominal coverage ratio (the Minimum Required Funding Level) of these pension funds of around 150% (before the crisis) to the average of around 95% in 2013⁷².

Different considerations apply where employer has agreed, in legally binding terms, to make good the deficit in the pension fund, and has become insolvent. This position is discussed below.

Is a pension protection fund required in respect of a Dutch Article 8 OPS to comply with the Directive? The application of the cases of Hampshire and Bauer to Dutch pension schemes

What seems to be reasonably clear is that:

- where the employer has entered into a funding obligation to make good a deficit,
- the employer becomes insolvent,
- scheme benefits are reduced in consequence, and
- the benefit reduction is below the minimum amount required by the CJEU's interpretation of Article 8,

⁷¹ See Blake, 2016: 'Independent Review of Retirement Income: Report', available at <https://www.pensions-institute.org/IRRIRreport.pdf>

⁷² See Van Meerten, 2016: 'European Ruling on Pensions: second warning for The Netherlands', in Goudappel, F.A.N.J., Hirsch Ballin, E.M.H. (eds), *Democracy and Rule of Law in the European Union. Essays in Honour of Jaap W. de Zwaan*, Den Haag: Asser Press

then The Netherlands would have failed correctly to transpose Article 8 of the Directive. In consequence, it would be exposed to a *Francovich* claim.⁷³

The minimum amount referred to in the preceding paragraph above required by Article 8 of the Directive is:

- at least 50% of what would have been the benefit had the employer been able to pay the contributions which it failed to pay because of its insolvency, measured on an ongoing basis, (the “**50% Underpin**)), and
- if greater, the Bauer Underpin.

Where, as is more common in the Netherlands, the employer had no obligation to pay additional contributions to make good any deficit (**and has paid all contributions due to date of insolvency**), then the more logically coherent argument is, because of the consequence of the regular approach to adjusting benefits to balance the books in a Dutch pension scheme (as outlined above), there is nothing to be protected by Article 8.

However, if the employer has not paid all contributions due from it to date of insolvency, the Bauer Underpin will apply as will the 50% Underpin (even if the 50% Underpin is highly unlikely to bite in practice).

12. Are invalidity benefits and early retirement benefits provided in an occupational pension scheme covered by Article 8?

Directive 2001/23/EC on the approximation of the laws of Member States relating to the safeguarding of employees’ rights in the event of transfers of undertakings of businesses or parts of undertakings of business (the “**Acquired Rights Directive**”) consolidates and replaces Directive 77/1874/EEC.

Article 3(1) provides:

*“The transferor's rights and obligations arising from a contract of employment or from an employment relationship existing on the date of a transfer **shall, by reason of such transfer, be transferred to the transferee.**”*

Member States may provide that, after the date of transfer, the transferor and the transferee shall be jointly and severally liable in respect of obligations which arose before the date of transfer from a contract of employment or an employment relationship existing on the date of the transfer.” [emphasis added]

⁷³ The Dutch Court of Appeal held in 2008 that the Dutch Pension Act does not contain an unconditional obligation for, in casu, Akzo Nobel to make up a deficit of the pension fund of Akzo Nobel. See: ECLI:NL:GHARN:2008:BE9201.

However, Member States have the option not to permit certain pension rights to transfer under Article 3(4):

*“4. (a) Unless Member States provide otherwise, **paragraphs 1 and 3 shall not apply in relation to employees' rights to old-age, invalidity or survivors' benefits under supplementary company or intercompany pension schemes outside the statutory social security schemes in Member States.***

*(b) Even where they do not provide in accordance with subparagraph (a) that paragraphs 1 and 3 apply in relation to such rights, Member States **shall adopt the measures necessary to protect the interests of employees and of persons no longer employed in the transferor's business at the time of the transfer in respect of rights conferring on them immediate or prospective entitlement to old age benefits, including survivors' benefits, under supplementary schemes referred to in subparagraph (a).**” [emphasis added]*

The point to draw out is that the Member State option under Article 3(4) only applies to old age, invalidity and survivors' benefits under supplementary company or inter-company pension schemes.

The UK exercised the option to exclude old age, invalidity and survivors' benefits. Its implementation of the protections required under Article 3(4) are to be found in the Pensions Act 2004, Sections 257 and 258⁷⁴.

The Transfer of Undertakings (Protection of Employees) Regulations 2006 (“**TUPE 2006**”)⁷⁵ are the current UK regulations transposing the Acquired Rights Directive into UK law.

Previous versions of these predecessor regulations did not distinguish between early retirement benefits and old age, invalidity and survivor's benefits (see below).

The TUPE 2006, Regulation 10 carves out pension rights:

10. (1) Regulations 4 and 5 shall not apply—

*(a) to so much of a contract of employment or collective agreement as relates to an **occupational pension scheme** within the meaning of the Pension Schemes Act 1993; or*

*(b) to any rights, powers, duties or liabilities under or in connection with any such contract or subsisting by virtue of any such agreement and relating to **such a scheme** or otherwise arising in connection with that person's employment and relating to **such a scheme.***

⁷⁴ And the Transfer of Employment (Pension Protection) Regulations 2005.

⁷⁵ And its predecessors.

(2) For the purposes of paragraphs (1) and (3), any provisions of an **occupational pension scheme** which do **not** relate to benefits for **old age, invalidity or survivors** shall **not** be treated as being part of the scheme.

(3) An employee whose contract of employment is transferred in the circumstances described in regulation 4(1) shall not be entitled to bring a claim against the transferor for—

(a) breach of contract; or

(b) constructive unfair dismissal under section 95(1)(c) of the 1996 Act,

arising out of a loss or reduction in his rights under an occupational pension scheme in consequence of the transfer, save insofar as the alleged breach of contract or dismissal (as the case may be) occurred prior to the date on which these Regulations took effect.” [emphasis added]

The distinction between:

- old age, invalidity and survivors’ benefits, and
- other rights under an occupational pension scheme (e.g. early retirement pensions),

was drawn out in the CJEU decision in *Beckmann* of 4th June, 2002⁷⁶, where the CJEU held:

“32. The answer to the first question must therefore be that **early retirement benefits and benefits intended to enhance the conditions of such retirement, paid in the event of dismissal to employees who have reached a certain age, such as the benefits at issue in the main proceedings, are not old-age, invalidity or survivors’ benefits under supplementary company or inter-company pension schemes within the meaning of Article 3(3) of the Directive.**” [emphasis added]⁷⁷

It can be argued that some early retirement pension rights under an occupational pension scheme do not fall within the ambit of Article 8 of Directive 2008/94/EC (because they are not old age benefits – as, indeed, was decided on similar wording on the Acquired Rights Directive, Article 3(4) as interpreted by the CJEU in *Beckmann* and subsequently *Martin*).⁷⁸

⁷⁶ *Beckmann v Dynamco Whicheloe McFarlane* (C-164/00).

⁷⁷ See also *Martin v Southbank University* (C-401) a decision of the CJEU on 6th December, 2003 and also the UK High Court decision in *Proctor & Gamble SCA* [2012] EWHC 1257 (Ch).

⁷⁸ Baugnet, The protection of occupational pensions under European Union law on the freedom of movement for workers, Thesis submitted for assessment with a view to obtaining the degree of Doctor of Laws of the European University Institute Florence, November 2014. Online at: https://cadmus.eui.eu/bitstream/handle/1814/33869/2014_Baugnet.pdf;sequence=1 .

This then leads on to the next question – does that mean that these early retirement pensions are not only outside the protection of Article 8 but also outside the protection of Article 3 of the Directive. Or does it mean that those early retirement rights in fact fall to be covered by the protection in Article 3 of that Directive?

A point to draw out is the difference between:

- an old age pension which is drawn early but which is actuarially reduced on a cost neutral basis. Logically, such a pension retains its classification as an old age pension.
- a pension payable on retirement before normal pension age, which is not reduced for early payment, will be an early retirement pension in respect of the period from the date it comes into payment until the member's normal pension age. This is the type of pension which was not classified as an old age pension in *Beckmann*.

Similarly, since Article 8 only refers to old age benefits and survivors' benefits, an invalidity pension does not, on the words of Article 8, fall within the ambit of Article 8.

The argument would be that claims for early retirement benefit or invalidity benefit should fall to be covered under Article 3 of the Directive. It is then down to the Member State in question as to what limits it puts on those benefits to the extent permitted by Article 4. Equally, it is open to the Member State (including the UK for this purpose) to treat early retirement benefits and invalidity benefits as if they were old age benefits.

The key point is that, if this distinction is valid, then it is open to the Member State to determine the level of protection it provides to employees in respect of early retirement pensions, invalidity pensions and, potentially also, survivor pensions which are payable on death of the employee prior to obtaining normal pension age.

However, such a differential treatment may raise discrimination questions which leads us onto *Morgan*.

13. Age discrimination overlay: Hughes v The Board of the Pension Protection Fund, a decision of the High Court on 22nd June, 2020

Background

This was a case that followed on from the CJEU decision in *Hampshire*.

The main issue in this case was whether the UK Pension Protection Fund compensation cap, referred to in **Section 10** above amounted to unlawful discrimination on grounds of age contrary to:

- EU law, such as Article 21 of the EU Charter of Fundamental Rights and the general principles of non-discrimination in EU law⁷⁹, or

⁷⁹ See, for example, *Mangold v Helm* C-144/04, a decision of the CJEU on 22nd November, 2005, at paragraph 75 “*The principle of non-discrimination on grounds of age must thus be*

- Article 14 of the Convention on the Protection of Human Rights and Fundamental Freedoms (the “**Convention**”) read with Article 1 to the First Protocol⁸⁰.

The other substantive issue, within the scope of this paper, is whether the method adopted by the UK Pension Protection Fund to ensure that an employee receives at least 50% of the value of accrued entitlement complies with the requirements of Article 8 as interpreted by the CJEU in *Hampshire*.

What did the High Court decide on the question whether the compensation cap gave rise to unlawful discrimination on the grounds of age?

The High Court decided that the compensation cap (which only applied to those below normal pension age⁸¹ for pension protection fund purposes at the time of employer insolvency) did amount to discrimination on grounds of age against those who had not attained normal pension age at the date of the employer insolvency.

The Court also decided that such discrimination, applying EU law (see above) amounted, on the facts before the Court, to discrimination which could not be justified. The compensation cap, although included to pursue a legitimate aim, was not appropriate and necessary to achieve that aim.

The Court reached the same conclusion in relation to the alternative argument based on the Human Rights Act 1998 together with Article 14 of the Convention read with Article 1 of the First Protocol (both of which are set out in Schedule 1 to that Act). Again, the Secretary of State could not demonstrate that the compensation cap could be objectively justified.

A point to draw out is that the 10% reduction that applied to the accrued pension rights of members who had not attained a normal pension age for PPF purposes was not challenged in *Hughes*. That 10% reduction was accepted as a proportionate means of achieving a legitimate aim (although it was also an example of age discrimination).

Lawfulness of the PPF approach to ensuring that a person receives 50% of the value of their accrued entitlement as required under the CJEU decision in Hampshire

The Court decided that the PPF would need to put in place appropriate measures to make sure that, throughout the lifetime of the member receiving compensation from the Pension Protection Fund, the level of compensation was at least equal to 50% of what the member’s

regarded as a general principle of Community law.” And also Küçükdeveci v Swedex C-555/07, a decision of the CJEU on 19th January, 2010, at paragraph 50: “the principle of non-discrimination on grounds of age is a general principle of European Union law in that it constitutes a specific application of the general principle of equal treatment (see, to that effect, Mangold, paragraphs 74 to 76).”

⁸⁰ Article 14 of the Convention and Article 1 to the First Protocol are incorporated into UK domestic legislation under the Human Rights Act 1998 (but within the parameters of that Act).

⁸¹ See **Section 10** above.

pension would have been had the pension continued to be paid in full under the employer's pension scheme throughout the member's lifetime.

A cautionary note

It should be noted that both the Pension Protection Fund and the Secretary of State are appealing the High Court decision. So this may not be the final word on this topic.

It is also worth noting that the case considered a number of other interesting points relating to the interaction between Article 8 and UK domestic legislation which are outside the scope of this paper.

14. Further expansion of the Bauer Underpin?

Webb-Sämann, *Hampshire* and *Bauer* all refer to the possibility of a higher level of protection being required under Article 8 over and beyond:

- the 50% Underpin, remembering that its value is to be determined by reference to what the benefits would have been in the employer's Article 8 OPS had the employer not become insolvent on continuing basis (eg reflective of future revaluation to deferred pensions and future increases to pensions in payment), and
- the Bauer Underpin.

The test is what level of reduction (after meeting the 50% Underpin and the Bauer Underpin) and in what circumstances would be regarded as “*manifestly disproportionate*” in the language of the CJEU in *Webb-Sämann*, *Hampshire* and *Bauer* in the light of the obligation under Article 8 of the Directive to protect the interests of employees.

At this stage, future developments can only be a matter of speculation and it leaves open the question of the extent to which the CJEU is exercising a legislative function rather than a judicial function. One can but reflect that Advocate General Kokott's analysis as to the level of protection in the *Robin*'s case was correct⁸².

But from a UK perspective, post Brexit any such further decision of the CJEU will only have persuasive effect which the UK courts may or may not choose to follow.

15. Conclusions

Implications in the UK

⁸² At paragraph 100(1) of her opinion in *Robins* (set out at **Section 5** above).

The required Article 8 protection only applies to PPF eligible schemes. So, for non PPF eligible occupational pension schemes, despite Brexit, it seems reasonably clear that the PPF would be required to provide:

- the 50% Underpin, and
- the Bauer Underpin,

to such excluded schemes (subject to the possibility of an option to deploy Article 12(a) (measures necessary to avoid abuse) of the Directive).

Where, before *Hampshire*, *Bauer* and *Morgan*, an occupational pension scheme has been wound up, following employer insolvency, and had sufficient assets to secure benefits above the PPF level of compensation through the purchase of annuities from an insurance company (e.g. under a buy-out policy), it will be necessary to revisit such buy-out policies (and the discharge given to the trustees of such schemes on their winding-up) to see whether the benefits secured met as applicable:

- the 50% Underpin,
- the Bauer Underpin, and
- the compensation level required after applying the age discrimination based argument for disapplying the PPF compensation cap in *Hughes*⁸³.

Similar considerations to those in the immediately preceding paragraph apply to schemes which are being wound-up following employer insolvency and which have assets that are sufficient to cover liabilities at the PPF compensation level (as adjusted to allow for the Bauer Underpin and the decision in *Hughes*).

There may also be some outturns where a scheme appeared to have sufficient assets to meet the at least the then understood level of PPF compensation, but which should, on the revised understanding of the required level of PPF compensation, have gone into the PPF.

It remains to be seen whether the UK courts will continue to look at the required level of protection under Article 8 and the extent to which they may have scope to build on the “manifestly disproportionately” line of argument referred to in **Section 14** above.

There are also the practical ramifications of administering the Bauer Underpin which involve:

- the process for collecting data from members as to their various sources of income, and
- the requirement to do an annual check for members who may benefit from the Bauer Underpin (or who do benefit from the Bauer Underpin) to update their benefits.

⁸³ Albeit that the *Hughes* decision is subject to the results of the appeal to the Court of Appeal.

In addition, affected members who have been underpaid the required level of compensation referred to above will have claims for arrears of compensation. However, some claims may be barred, in whole or in part, depending on whether they are out of time⁸⁴.

Implications in the Netherlands

The ramifications for the Netherlands are:

- those outlined in **Section 11** above, and
- the risk of further CJEU judgments as to the meaning of “manifestly disproportionate” and the circumstances where a required level of protection under Article 8 is higher than that referred to in **Section 14** above.

Other EU member states

Depending on the nature of the pension protection arrangement put in place by the Member State in question, the points identified in the preceding sections of this paper may have similar ramifications for the pension protection arrangements in that Member State.

⁸⁴ Discussion of limitation periods is outside the scope this paper. But see the decision on this point in *Hughes v the Pension Protection Fund* [2020] EWHC 1598 (Admin) starting at 197.