Wedlake Bell
IN COUNSEL
AUTUMN 2018

WELCOME

Welcome to the latest edition of our In Counsel publication.

Although the Brexit-related political temperature cooled over the summer while we sweltered through the hottest summer on record in England, it is certain to rise again over the next few months. Julia Jackson of our Employment team, specialising in immigration issues, therefore looks at the impact of Brexit and a possible no deal on EU nationals living in the UK.

We also outline other national and EU law developments affecting your business including:

- Claire McConway, new partner in our corporate and financial services and funds team, analyses the UK rules governing dividends and other distributions and approaches of popular common law jurisdictions (many of them offshore) when considering where to incorporate holding vehicles;
- Edward Craft and Camilla Wallace report on the draft legislation for the new "PSC in property" regime;
- James Castro-Edwards and Blair Adams, have prepared a guide for HR teams on how companies should deal with data breaches under GDPR; and
- Emily Matthews points out the importance of mental health at the workplace and the measures employers can engage to improve and promote positive mental health.

Rosalyn Breedy emphasises the benefits of adherence by the UK asset management industry to the key findings of the FCA Asset Management Market Study; and Jonathan Cornthwaite specialising in competition law, provides an analysis of the recent European Commission decision in the *Google Android* case.

Clive Weber and Katie Whitford look at the recent successful appeal by British Airways against the BA pension scheme Trustees' award of pensions increases, and Justin McGilloway reports on the implications for company directors and the Pensions Regulator of the government's response to its consultation on measures designed to improve corporate governance within companies which are in or approaching insolvency. Finally, Edward Craft and Harriet Forster comment on the Law Society's consultation aiming to identify and address legal uncertainties concerning electronically executed documents.

Wedlake Bell news

We completed our merger with Stitt & Co on the 30th July and the combined firm has 66 partners. Four partners from Stitt & Co alongside eight members of staff joined Wedlake Bell and the merger will reinforce the firm's already well-established practices particularly in commercial litigation, commercial and residential property as well as private client.

We are also very pleased to welcome **Claire McConway** who joined as a new corporate and funds partner in August. After a nine year career in UK and U.S. corporate and funds law practice in London, she spent several years practising offshore law (principally BVI, Bermuda and Cayman) and has recently returned to practising English law. She originally qualified as a solicitor in England and Wales in 2000 on completion of her training at Herbert Smith's London office. She is also admitted to practise in New York, California, the Republic of Ireland, Bermuda and the BVI.

Janice Wall, Head of Corporate

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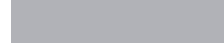

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BREXIT, EU NATIONALS AND NO DEAL

Julia Jackson

The first applications from EU nationals wanting to stay in the UK after Brexit were submitted to the Home Office on 28th August. The date marks the start of the private beta-testing stage of the new settlement scheme for EU nationals, initially open only to university students in Liverpool and NHS workers in the North-West of England.

This testing stage offers the Home Office the opportunity to consider if any adjustments are needed to the process, which Ministers have insisted will be simple with minimal paperwork. Following completion of the testing stage, the plan is to open up the settlement scheme to other EU nationals living in the UK on a phased basis from later this year to be fully opened by 30 March 2019.

However, the roll out of the scheme has been rather overshadowed in recent weeks by increasing discussion of the possibility of a no-deal Brexit. On 23 August the government published the first of its 80 technical notices setting out information on the impact of a no deal scenario designed to allow businesses and individuals to plan and prepare.

At the time of writing the technical notice regarding EU nationals living in the UK has not been published. However, there have been press reports of a leaked Cabinet Office paper appearing to confirm that EU nationals living in the UK will be given the right to stay in the event of a no-deal Brexit.

The leaked cabinet paper reportedly states that the Home Office offer is "not only important to provide certainty publicly, but will enable the UK government to take the moral high ground."

Whilst refusing to publicly guarantee the rights of EU nationals living in the UK, Brexit Secretary Dominic Raab is quoted as saying that it would be "inconceivable" that EU nationals would be asked to leave the UK regardless of the outcome of the Brexit negotiations.

Meanwhile citizens of EEA countries Norway, Iceland, Liechtenstein and of Switzerland living in the UK continue to wait for the outcome of discussions about their status in the UK after Brexit not currently covered by the Withdrawal Agreement or the settlement scheme.

For further information please contact Julia Jackson at jjackson@wedlakebell.com.

ONE FINE DAY: THE EUROPEAN COMMISSION'S DECISION IN THE *GOOGLE ANDROID* CASE

Jonathan Cornthwaite

The European Commission (**EC**) seems to be falling into the habit of imposing record-breaking fines on Google before packing up for its summer holidays. It happened last year when, at the end of June, the EC announced an eye-watering fine of €2.4bn in the *Google Shopping* case[1], more than twice as large as the biggest anti-trust fine[2] that the EC had previously imposed. And it has now happened again, for in the latter part of July of this year the EC imposed upon Google an even more massive fine of €4.34bn for having again breached EU competition law, this time in connection with illegal practices regarding Android mobile devices.

[1] Case 39740 *Google Search (Shopping)*

[2] The fine of €1.06bn levied against Intel Corporation in 2009 was (prior to the Google Shopping decision) the highest individual fine that the EC had then imposed, though the aggregate of the fine imposed by the EC on Microsoft in 2004 plus the non-compliance penalties subsequently imposed on it topped €1.67bn.

In this article we focus on the legal aspects of the EC's decision in *Google Android* (the **Decision**) in order to see what can profitably be learned from it.

What was the Decision in a nutshell?

As a result of two complaints to the effect that Google had abused its market dominance in relation to Android mobile operating systems, as well as an initial investigation carried out by the EC on its own initiative, the EC opened infringement proceedings in April 2015, issued a Statement of Objections in April 2016, and concluded in July 2018 that Google's conduct had indeed broken EU anti-trust law.

Was the Decision a surprise?

The EC's proceedings have been lumbering on for over three years, during which many pundits correctly forecast that it would find against Google. Few, however, accurately predicted the size of the fine, which didn't just break the pre-existing record but shattered it.

Some have commented that the quantum of this fine, huge though it was in absolute terms, was a relatively small change for Google given that the assets of its parent company, Alphabet, are astronomical. But such comments overlook the EC's power to impose further back-dated fines, in the event of Google's non-compliance, of up to 5% of Alphabet's average *daily* turnover. If the duration of that non-compliance were to be lengthy, the aggregate of those further fines could be such as to make even Google feel the pain. Having said that, Google may be troubled more by the bad publicity – abusing a dominant position isn't entirely consistent with its corporate moto *"Don't be evil"*! – and (unless it successfully appeals against the Decision, as to which see below) by the need to alter its business model, for the Decision obliges Google to cease and desist from its infringing practices.

What was the legal basis for the Decision?

The Decision was grounded on Article 102 of the Treaty on the Functioning of the European Union (**TFEU**), which prohibits the abuse of a dominant market position, and which has been copied by other EU member states (**Member States**) in their respective domestic laws (for example, the UK's Competition Act 1998 contains at section 18 an almost *verbatim* equivalent). Article 102 is probably the most fearsome weapon in the EC's anti-trust arsenal for, unlike Article 101 of the TFEU (which prohibits anti-competitive agreements and practices), it can be infringed by purely unilateral conduct, and is subject to almost no exceptions. Furthermore, although the Article contains a list of four particularly heinous examples of abuse, that list is non-exhaustive only, which means that the prohibition is dangerously open-ended.

The task of assessing whether a business has contravened Article 102 by having abused market dominance is a composite one, involving various steps that need to be taken in the correct order. The first is to identify the markets in question, and to decide whether the business under investigation is dominant in any of them. In this particular case the EC came to the conclusion that there were three relevant markets to be considered, namely the worldwide (excluding China) markets for:

- general internet search services;
- licensable smart mobile operating systems; and
- app stores for the Android mobile operating system.

Step number 2 was to assess whether Google was dominant in any of those markets, and the EC found dominance to have been established in all three. One reason for that finding was the high entry barriers obtaining in all of them. But even had those barriers been lower, the likelihood is that dominance would still have been established, as a result of Google's sky-high market shares, which exceeded 90% in each of the three markets.

But, infuriating though it may be to the competition, market dominance – even the extreme level of dominance wielded by Google – does not itself break the law. As the EC succinctly put it in its press release, *"[m]arket dominance is, as such, not illegal under EU anti-trust rules"*. The problem, rather, occurs where that dominance is abused, which was the subject of the third and final step in the EC's legal analysis. And that step was crucial, for the analysis uncovered multiple abuses.

Of which abuses was Google guilty?

The EC found that Google had engaged in not just one but three separate types of abuse, all of which had the aim of cementing its dominant position. One of them was the illegal tying of its search app and of its Chrome browser, namely by ensuring that both were pre-installed on practically all Android devices sold in the EEA. The result was to reduce the incentives of manufacturers to pre-install competing search and browser apps, as well as the incentives of users to download them.

A second type of abuse was the making of illegal payments conditional on exclusive pre-installation of Google Search. Some of the largest device manufacturers, as well as mobile network operators, received significant financial incentives from Google on condition that they exclusively pre-installed Google Search across their entire portfolio of Android devices, which dissuaded them from pre-installing competing apps.

And a third illegality was the obstruction of the development and distribution of alternative Android operating systems, often known as "Android forks". In order to be able to pre-install Google's proprietary apps on their devices, manufacturers had to agree contractually not to develop or sell even a single device running on an Android fork.

To what extent does the Decision set a precedent?
In terms of substantive law the Decision breaks little new ground: after all, the prohibition of abuse of a dominant position in Article 102 (and its predecessors) has been a major plank of EU competition law for some sixty years, and it is already well-settled by cases such as Microsoft[3] that the prohibition can be breached if a player leverages its dominance in market A (in this case the market for Android operating systems) in order to exploit market B (in this case the market for general internet search). However, in terms of the quantum of the fine (both in relative and absolute terms) the Decision breaks new ground, and arguably accords more publicity than ever before to the EC's readiness and willingness to punish the abuse of a dominant position.

What kind of alterations to Google's business model may result from the Decision?
In cases such as this it is the duty of competition law regulators to enforce compliance and punish breaches, rather than to dictate how compliance is to be achieved; that is why the EC's press release said that *"[i]t is Google's sole responsibility to ensure compliance with the Commission decision"*, though it is already clear that the EC will not necessarily be taking Google's explanations at face value, and will be monitoring it closely. The relative lack of specificity in the Decision about remedies is therefore unsurprising. Having said that, the Decision obliges Google to cease and desist from each of the three types of abuse explained above, though it does not prevent Google from putting in place a reasonable, fair and objective alternative system to ensure the correct functioning of Android devices using Google proprietary apps and services.

Is the Decision likely to stimulate civil actions before Member States' courts?
We are already seeing a rising tide of civil actions before the courts of Member States by victims of anti-competitive practices, due to a range of factors, including two principal ones. One of them is the growing familiarity with competition law on the part of businesses, who are gradually wising up to the opportunities for extracting compensation for damage inflicted on them by anti-competitive conduct. The other is the way that the law is (belatedly) making it easier for them to do so, and in this respect the EU's Antitrust Damages Directive[4] was a milestone.[5] The Decision – and the major publicity accorded to it – will inevitably add fuel to the fire.

What about the EC's other outstanding formal investigations into Google?
The Decision is not the only euro-headache that Google has. The EC's ruling in *Google Shopping* has been mentioned above; and the EC is also investigating *AdSense* (Google's search advertising model), having already reached the preliminary conclusion that that practice breaches EU competition law. If this conclusion is confirmed, another thumping fine will follow as certainly as night follows day, although it is too early to speculate whether its amount would equal or exceed the one imposed this July.

Is the Decision "game over"?
Unlikely. Google has until the autumn in which to appeal against the Decision, and few companies in the world have a deeper war-chest with which to fund the costs of an appeal. If it decides to appeal, it is perfectly possible that it could succeed. After all, just because the EC is in charge of EU competition law doesn't mean that it is infallible; on the contrary, it has got the law wrong on various occasions, and some pundits are already predicting that the Decision would be reversed in the event of an appeal.

In conclusion
Cases such as this can reinforce the belief that it is only massive multinationals that really need to fear the Article 102 prohibition. But such a belief is erroneous…and dangerously so. They may not command banner headlines, but there is no shortage of cases in which organisations far smaller than Google have fallen foul of Article 102 or its national equivalents.[6] The only safe conclusion is that no business, great or small, can afford to disregard the consequences of abusing market dominance.

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[3] Case T-201/04, *Microsoft Corporation v Commission*, judgment of 17 September 2007

[4] Directive 2014/104/EU of the European Parliament and of the Council of 26 November 2014 on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union.

[5] Once Member States get around to transposing it into their respective national laws, that is – the EC has been obliged to institute infringement proceedings against several of them for having failed to do so!

[6] For example, organizations recently found to have infringed section 18 of the Competition Act 1998 (the UK's equivalent to Article 102 of the TFEU) have included entities as modestly-sized as Flynn Pharma Limited and The Law Society of England and Wales.

CAPITAL MAINTENANCE FOR HOLDING COMPANIES: A COMPARATIVE LOOK AT DIVIDENDS AND OTHER DISTRIBUTIONS

Claire McConway

When it comes to deciding where to incorporate a company, it is not uncommon for cross border holding structures to have multiple options on the table. Although the available choices for operating companies are often narrowed due to the need for compliance with local regulatory regimes or tax treatment, there is often a wider choice available higher up in a holding structure. Typical factors include tax structuring and a jurisdiction's market reputation in the relevant sector. When setting up a new holding vehicle, the ability to move funds and assets between group companies is an important factor that is usually overlooked.

The ability to return income and capital to investors is a cornerstone of the planning of any investment structure. Company and insolvency laws generally protect the creditors of financially unhealthy or insolvent companies by prohibiting or reversing the transfer of corporate assets to shareholders. Beyond this common thread, the rules on distributions vary widely between jurisdictions. This article looks at the UK rules and then considers briefly the approaches of popular common law jurisdictions for the incorporation of holding vehicles – many of them offshore. Whilst all of these require a basic solvency test to be met, the applicable test varies widely and once solvency has been established, the rules governing what is and is not distributable to shareholders also differ.

Before a UK company can lawfully pay a dividend, it must have "profits" available for the purpose (often referred to as distributable profits or distributable reserves), calculated by reference to formal accounting methods. A company's undistributable reserves are: (i) its share premium account; (ii) its capital redemption reserve; (iii) the amount by which its unrealised uncapitalised profits exceed its unrealised losses not written off; and (iv) any other reserve that the company is prohibited from distributing either by statute or by its constitutional documents. The distribution must also be justified by reference to "relevant accounts". Relevant accounts are always individual (not group) accounts and may be:
(i) the company's most recent annual accounts;
(ii) specially prepared interim accounts; or
(iii) specially prepared initial accounts.

The form of these accounts may vary, depending on whether the company produces its accounts under UK GAAP or IFRS (IAS).

The profits rule for dividends is tempered by recent reforms making it easier for private companies to return capital to shareholders. Private companies may now make out of court non-dividend distributions out of capital if a cash flow solvency test is met and shareholder approval is obtained. Further streamlining was later added by allowing private companies to make small buy-backs out of capital (up to a maximum of £15,000 per financial year) without complying with the formal solvency and shareholder approval requirements. These routes are not available to public companies, who must use the court approval route.

Offshore jurisdictions in particular are typically seen as interchangeable by practitioners sitting in London or New York. Whilst this is often the case from a tax planning perspective, their corporate and regulatory regimes vary widely in many other respects. In particular, their rules on distributions differ and this information can be vital at the planning stage.

The British Virgin Islands (BVI), Guernsey and the Isle of Man now apply a single unified solvency test for dividends and all other distributions (at least for newer companies). The solvency test combines a balance sheet (net assets) test and a liquidity (cash flow) test: it requires that the value of the company's assets will exceed its liabilities and the Company will be able to pay its debts as they fall due. Provided that the solvency test has been

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satisfied, dividends may be paid and shares may be redeemed or repurchased out of any capital or profits of the company. These tests follow the simple "one size fits all" double-pronged balance sheet and cash flow test first introduced in the ABA's Revised Model Business Corporation Act. They allow the directors to take a flexible look at balance sheet values based on their good faith assessment of the valuation principles most appropriate to the company's circumstances.

Bermuda also combines a cash flow test with a balance sheet test, but Bermuda companies may not pay dividends or make other distributions out of the share capital account or the share premium account. Dividends and other distributions may be paid out of the "contributed surplus" account, to which must be allocated, among other things, shareholder capital which is unrelated to any share subscription and which is reduced to the extent that dividends or distributions exceed net income. The net assets part of the test requires that the "realisable value" of the company's assets will be less than its liabilities. "Realisable value" is not defined and is a matter for the directors, who may need to seek a valuation if value is not determinable by way of a ready market.

Subject to a cash flow test, Cayman and Jersey companies may pay dividends out of profits and share premium, but not share capital. However, the share capital account and capital redemption reserve can (subject to solvency) be utilised for share redemptions and repurchases. Since there is no net assets test, there is no need to consider asset values. Jersey differs slightly from Cayman and its other competitors in applying a 12 month forward-looking requirement for its cash flow test.

On the other hand, the UK's current or former approaches to capital maintenance rules are still broadly followed in countries across Europe, Asia and Africa with a common law tradition. For example, Ireland's rules are virtually identical to those of the UK, with the only difference of note that Ireland has not adopted the UK's more recent exemption allowing private companies to make small buy-backs out of capital. Malta, Cyprus and Gibraltar continue to apply the profits rule. The original core principles remain in relation to dividends even in the jurisdictions which have updated the rules for other types of distributions (e.g. Hong Kong and Singapore).

Whether or not local tax is levied at a corporate level, special care should be taken in planning for the overseas tax treatment applicable to distribution payments. This is especially so in the case of distributions from sources other than profits, which may in some countries be taxable in the hands of the shareholder as a return of capital rather than income. This was highlighted in the Court of Appeal decision in *First Nationwide v The Commissioners for HMRC*.[7] The court held that it is the legal machinery under the laws of the jurisdiction of incorporation of the company paying the dividend, and not the source of the funds, that is determinative of the nature of the payments (i.e. as capital or income) in the recipient's hands. Because the payment was made by way of dividend (and was made otherwise than in the course of a winding up), then it had to be treated as a dividend, and was therefore income, even though it was paid by a Cayman company out of its share premium account. Whilst this appears to settle the immediate position for UK shareholders, appropriate tax advice should be taken wherever the recipient of a distribution will be liable to tax.

Capital maintenance rules serve a worthy purpose rooted in a desire to protect creditors and lower ranking shareholders from bad management decisions or, at worst, asset stripping. Critics of more rigid distribution policies note that placing too much reliance on accounting principles can artificially prevent financially sound companies from returning value to shareholders. A more liberal regime gives boards and investors the flexibility to adopt policies most fitting for their company's evolving operating and financial circumstances. Those who oppose the wholesale dismantling of the older rules argue that the ability to call directors and shareholders to account for their actions after the fact may be of little value in practical terms. Both sets of arguments have their merits and their critics. What is best for the investors in a cross border holding company is unlikely to be suitable for a large trading company with employees, pension liabilities, lenders and business creditors. In a world of many different options, the most suitable vehicle in any given set of circumstances needs to be an educated one based on all relevant factors, of which the distribution rules can form an important part.

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[7] [2012] EWCA 278

PSC IN PROPERTY IS ONE STEP CLOSER

Edward Craft and Camilla Wallace

As it committed to do, BEIS has issued draft legislation for a new regime for "PSC in property", in the form of the Overseas Entities Bill.

This bill has only been published in draft and has not been read in Parliament. Indeed, it is not provided for in the current session. The regime is expected to be operational by 2021.

However, it is clear that BEIS intends to proceed with the new regime which will require disclosure of the persons behind overseas entities owning real estate across the UK. The original proposal was for England and Wales, but the devolved administration of Scotland has since got on board and, with no operating executive in Northern Ireland, it is easy for the UK government to include that part of the UK.

The trust industry has been awaiting clarification of whether trusts will be within scope and will be pleased that, whilst "overseas entities" is defined to include companies, partnerships and other entities with legal personality, it does not include overseas trusts that directly hold UK real estate. The beneficial owners of such trusts are already subject to the UK's "Trust Register" regime and disclosable to HMRC and law enforcement agencies and, with the regime to be extended with the upcoming introduction of the Fifth Anti-Money Laundering Directive, this has been deemed sufficient from a transparency perspective given the legitimate need to protect minor and vulnerable beneficiaries. Trusts that hold UK real estate via an offshore company are subject to the regime but will only need to disclose those with significant influence or control (not ownership) of the trust.

The good news is that the regime is, very sensibly, built upon the infrastructure for the registers of people with significant control (**PSC**) regime inserted into the Companies Act 2006 with effect from 30 April 2016. The register will be maintained at Companies House and not the Land Registry. In a similar way to the sanctions under the PSC regime, an overseas entity will not be able to acquire registered title or dispose of registered title without being on the register. Just as in the PSC regime, one can expect that there will be significant negligent or deliberately misleading filing and it will be interesting to observe if the regulatory and enforcement bodies take action to maintain the quality of the register.

However, in publishing the draft legislation, BEIS seems to have missed a fairly obvious and fundamental point, namely the required review of the registers of the PSC regime which must take place by the early part of 2019 is a legal obligation of the Secretary of State.

Whilst one can expect that the registers of the PSC regime (the UK's gold-plated and slightly non-compliant implementation of the EU Fourth Anti-Money Laundering Regulation) will remain despite Brexit, the errors and inconsistencies within the regime remain and surely the triennial review is the right time for the Secretary of State to take on board all of the comments it has received in order to deliver an effective regime which will be able to stand the test of time.

Only once the defects and oddities of the registers of the PSC regime are fixed should a revised Overseas Entities Bill be introduced to Parliament. At the moment, BEIS has fallen into the trap of transposing across the errors.

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THE FRC IN THE BALANCE

Edward Craft

Sir John Kingman, chairman of Legal and General plc has been charged by the government with carrying out a root-and-branch review of The Financial Reporting Council (the **FRC**), that rather odd beast in the corporate reporting and governance landscape.

The review is welcome because the position of the FRC is confusing. Key areas of confusion include the name, its jurisdiction and its enforcement powers. Whatever substantive conclusions are reached, greater clarity is welcome.

It is a reality that, over time, responsibilities have been allocated to the FRC in a rather haphazard manner. It would benefit all if it was placed on a clearer statutory footing, probably following the model of the Financial Conduct Authority or the Takeover Panel.

The FRC's key competencies fall into the following areas:

Regulation of accountants and actuaries	Noting that the FRC is hoping to see this jurisdiction and the ability to censure extended to all directors
Audit regulation	A direct statutory power derived from the EU Audit Directive
Issue and enforcement of accounting standards	Under the Companies Act 2006 (section 464)
Drafting of the UK Corporate Governance Code and the Stewardship Code	Plus support for the Coalition Group responsible for the Wates Principles for privately held companies
Regulation and Enforcement of its corporate governance codes	To date this has been weak, with much enforcement left to the London Stock Exchange and to shareholders

It remains to be seen if Sir John's review will conclude that these competencies should all be carried out by the same body. Whilst the author is no advocate of additional regulatory bodies, there does seem to be a powerful case for greater focus and clarity as to the functions, legal basis and responsibilities of a re-badged "Corporate Reporting and Governance Authority".

For further information please contact Edward Craft at ecraft@wedlakebell.com.

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REPORTING DATA BREACHES – A GUIDE FOR HR TEAMS

Blair Adams and James Castro-Edwards

Having spent weeks or even months making your HR processes, systems and documents GDPR-compliant, you will realise that there is no let-up and that the focus of your efforts will now extend to dealing with data breaches.

What is a data breach under GDPR?
Any breach of security leading to the accidental or unlawful destruction, loss, alteration, unauthorised disclosure of, or access to, personal data.

Can a breach be "internal" e.g. where personal data never leaves the organisation but is accidentally shared internally?
Yes. For example, if an employee's health records were accidentally sent to another employee, that would amount to a data breach.

Do we need to record details of all breaches?
Yes, you have an obligation to do so under GDPR, whether or not the breach is reportable.

In any event, by analysing and recording the causes, extent and impact of the breach and documenting the organisation's response to it, you should be in a better position to persuade the ICO and any affected parties that you have reacted appropriately.

We can help you to put in place a detailed risk assessment process and documentation.

Which breaches must be reported to the Information Commissioner's Office?
Any breach that is likely to pose a risk to any person's rights and freedoms. This is a very wide definition that requires the exercise of judgement in each case, but also a full understanding of the circumstances of the breach, which is why a detailed risk assessment process is so important.

What is the time limit for notifying the ICO?
You must notify without delay, and not later than 72 hours from becoming aware of the breach.

Should we notify the ICO even if our internal investigations are not complete?
Yes, that is advisable. The GDPR allows you to provide the necessary information in phases if necessary.

What information do we have to give to the ICO when notifying a breach?
The GDPR requires you to provide:

- a description of the nature of the personal data breach including, where possible:
  - the categories and approximate number of individuals concerned; and
  - the categories and approximate number of personal data records concerned;
- the name and contact details of the data protection officer (if your organisation has one) or other contact point where more information can be obtained;
  - a description of the likely consequences of the personal data breach; and
  - a description of the measures taken, or proposed to be taken, to deal with the personal data breach, including, where appropriate, the measures taken to mitigate any possible adverse effects.

This is why you must have a good internal system for recording the nature of the breach and your response to it.

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Do we also need to tell affected individuals?
Yes, if there is a "high" risk to their rights and freedoms. Again, this requires an exercise of judgement based on a complete understanding of the circumstances.

In the HR context, if another employee's data is the subject of the breach, you should consider your other legal obligations to them in addition to those under the GDPR.

Should we also notify our insurers?
Yes, without delay. We are aware of cases where an organisation has preferred to complete an internal investigation first, before notifying insurers, and has found itself to be in breach of its insurance policy conditions.

Should we have a DPO in order to deal with breaches?
One of the advantages of having a DPO is that they act as point of communication between your organisation and the ICO, particularly in relation to breaches.

We provide an outsourced DPO service through our ***ProDPO business***.

What are the penalties for failure to notify a breach?
They are significant: a fine of up to 10 million Euros or 2 per cent of your organisation's global turnover. In addition, the ICO can impose other corrective measures.

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MENTAL HEALTH IN THE WORKPLACE

Emily Matthews

The economic cost of mental illness in the workplace is now well documented. Mental ill health at work is estimated to cost UK employers £26 billion per year, which on average equates to approximately £1,035 per employee.

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The problem is not going away. According to a recent survey conducted by the British Chambers of Commerce and Aviva, almost 30% of businesses have seen an increase in the number of staff taking time off for mental health reasons. In part, this increase may reflect growing awareness around mental ill health problems; however, it also indicates that businesses need to do more to tackle the issues and promote positive mental health and wellbeing in the workplace.

What is the cost of mental ill-health?

In addition to the cost of sickness absence, employers suffer losses from those who are at work and should not be (presenteeism). Presenteeism causes problems such as a loss of productivity, damage to relationships between colleagues and clients and potentially serious mistakes.

According to the Stevenson/Farmer report, *"Thriving at Work – a review of mental health and employers"*, approximately 15% of people at work have symptoms of an existing mental ill health condition. Research carried out by the Chartered Institute of Personnel and Development (CIPD) found that 97% of respondents with poor mental health said it affected their performance at work. In total, it is estimated that presenteeism costs UK businesses £15.1 billion per year or £605 per employee.

Businesses may also experience difficulties in retaining staff as a result of mental ill-health in the workplace. It is estimated that UK employers spend £2.4 billion each year in replacing staff who have left their jobs due to mental ill health.

What are the causes?

Mental ill health problems are largely concentrated among people of working age. Excessive workloads, a lack of support, perceptions of job insecurity, relationships at work (bullying/harassment), and difficulties in finding a balance between work and home life have all been identified as common causes of mental ill health in the workplace.

Although research published last week by the British Chambers of Commerce and Aviva suggests that we may be making inroads into fighting the stigma associated with mental health, there is still a way to go. Employees are still likely to find it much more difficult to tell their employer about a mental health issue than a physical one.

What can employers do?

ACAS has published Guidance for employers on how to improve mental health in the workplace and fight the stigma around mental ill health. Employers should look to:

- develop an action plan to change attitudes in the workplace;
- create a mental health policy;
- train senior managers to ensure they champion awareness and fight stigma;
- tackle work-related causes of mental health; and
- educate the workforce in the importance of promoting good mental health.

It is estimated that by improving and promoting positive mental health within the workplace, employers could potentially save 30% or more of the associated costs of mental illness within an organisation.

According to research carried out by the London School of Economics, every £1 **invested in workplace stress prevention** results in an estimated saving to society of £2.00 (over 2 years).

What we do

Wedlake Bell offer an innovative training, education and engagement package with separate elements tailored to HR, staff and managers, including the policy documents recommended in the ACAS guidance.

Our training and documentation is provided by employment law specialists who are experienced in dealing with disability, absence management and performance issues and are also certified in Mental Health First Aid.

Our Charity of the Year

This year, our firm is proud to be supporting The Matthew Elvidge Trust as our charity of the year. The Matthew Elvidge Trust aims to promote the importance of wellbeing and good mental health whilst working to fight the stigma around mental illness. If you would like to find out more information about this fantastic charity, please see the website www.thematthewelvidgetrust.com.

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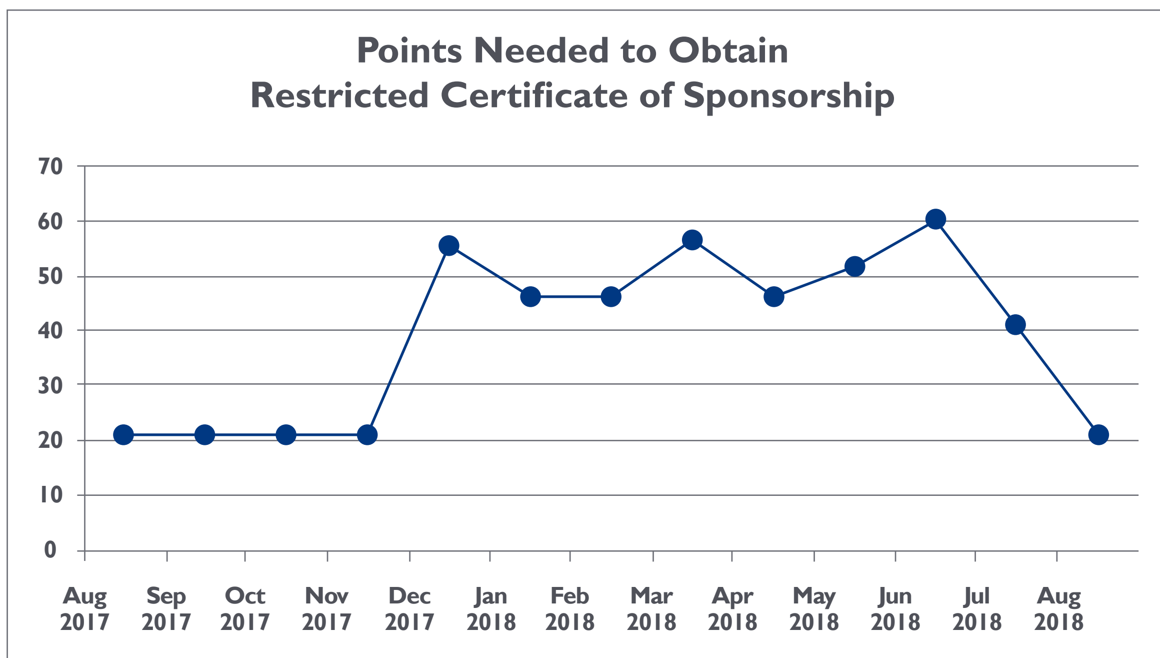
RELIEF FOR EMPLOYERS SEEKING TO OBTAIN RESTRICTED CERTIFICATES OF SPONSORSHIP

Julia Jackson

In the last In Counsel, we reported on the problems being encountered by employers trying to obtain restricted certificates of sponsorship for new recruits from overseas (see ***the article*** Recruitment Blocked by Immigration Bottleneck).



We are pleased to see that, as predicted, the removal in July of roles for doctors and nurses from the allocation of restricted certificates has had an immediate and clear effect. The number of points needed to secure a restricted certificate dropped from a high in June of 60 (equivalent to a minimum salary of £60,000) down to 41 in July and to just 21 in August (equivalent to a salary of £20,800) as illustrated by the table above.

It is hoped that in the coming months the number of restricted certificates of sponsorship available will continue to meet demand and that employers will be able to fill vacancies by recruiting from overseas when roles cannot be filled locally.

Where employers have previously been unsuccessful in a request for a restricted certificate of sponsorship, the request can be resubmitted at any time provided that the test of the resident labour market is still valid and less than six months old.

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EMPLOYMENT

ISN'T IT TIME THE UK ASSET MANAGEMENT INDUSTRY EMBRACED THE FCA ASSET MANAGEMENT MARKET STUDY?

Rosalyn Breedy

"Drive thy business or it will drive thee" **–**
Benjamin Franklin (**1706 to 1790**)

The FCA Asset Management Market Study, published June 2017, acknowledged the vital role the UK asset management industry plays in managing the savings and pensions of millions of people, allocating capital, performing corporate governance and contributing positively to the UK economy.

The report states that 'the UK asset management industry is the second largest in the world, managing around £6.9 trillion of assets. Over £1 trillion is managed for UK retail (individual) investors, and £3 trillion on behalf of UK Pension funds and other institutional investors. The UK asset management industry also manages around £2.7 trillion for overseas investors.'

The FCA launched its investigation of the industry in November 2015 because it wanted to ensure that the market worked well and the investment products consumers use offer value for money.

Key findings of the final report include:

- A finding of weak price competition in a number of areas of the asset management industry with a particularly adverse effect for retail investors. It found evidence of high levels of profitability with an average profit margin of 36% amongst firms sampled.

- On average, neither actively managed and passively managed funds for retail and institutional investors outperformed their benchmark after fees. No clear relationship between charges and the gross performance of active retail funds in the UK was identified. Not all persistently poorer performing funds were merged or closed and it could take a long time for the worse performing funds to be merged or closed.

- There were concerns about the communication of fund objectives to retail investors with many active funds offering similar exposure compared to passive funds but some charging significantly more for this. The FCA considers value for money for asset management products typically to be some form of risk adjusted net return. This can be broken down into performance achieved, the risk taken to achieve it and the price paid for investment management services.

- Investors' awareness and focus on charges was mixed and poor, with many retail investors not aware they are paying charges for their asset management services. However, many institutional investors and some retail investors are increasingly focused on charges.

- Significant differences in both the behaviour and outcomes of institutional investors were identified. A number of larger institutional investors were able to negotiate effectively and to achieve good value for money. A long tail of smaller institutional investors, typically pension funds, found it harder to negotiate with asset managers and generally relied upon investment consultants when making decisions.

- Concerns were identified in the investment consulting market including relatively high and stable market shares for the three largest providers; a weak demand side; and conflicts of interest.

- A concern that retail investors do not appear to benefit from economies of scale when pooling their money through direct-to-consumer platforms. Concerns were also raised about the value retail intermediaries provide.

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An overall package of remedies has been proposed by the FCA which is designed to improve competition, and protect those least able to actively engage with the asset manager. The FCA considers that these measures are proportionate and will increase the efficiency and attractiveness of the UK asset management industry. The intention is to develop a coherent framework of interventions which would sit with Markets in Financial Instruments Directive (**MIFID**) II, Packaged Retail and Insurance-based Investment Products (**PRIIPS**), and the Senior Managers and Certification Regime (**SMCR**).

The FCA has also recommended to the HM Treasury that investment consultants are brought into the regulatory perimeter pending the outcome of the provisional market investigation reference to the Competition and Markets Authority (**CMA**).

Concerns have been raised by the industry as to whether the new regulations proposed would be good for the UK investment market or whether this new regime will be too tough on asset managers. The added pressure of Brexit is creating new challenges for asset managers such as high compliance costs and changes to how funds can be sold to non-UK investors.

These concerns are misplaced, when the focus of attention in the industry should be the findings not the proposed remedies. In essence, the findings show that the retail and smaller customers most dependent on the industry are the least well served and that the industry is not practising what it preaches which is efficiency, effective allocation of capital and the winnowing out of poor performance.

Common sense dictates that these issues should be tackled in a coherent manner and embrace the new rules, though it is true that recent years have seen an overwhelming pace of regulatory interventions which have been a strain on asset managers.

The UK asset management industry should focus on addressing the efficiency of its operating model; strategic and appropriate use of technology and outsourcing; refining and improving its product range; and simplifying and driving down distribution costs. A gold standard could be achieved by the voluntary adoption of a fiduciary standard for those seeking to develop brands with significant and long standing value.

Just as the automotive and publishing industries have had to adapt to market disruption, so the UK asset management industry could embrace these changes and tackle its operating model to develop financial firms fit for the 21st century. Not only would the UK retain its position as the second largest asset management industry in the world, but it could also become a mighty barrier to disruptors.

First published in Investment Week on 21 July 2017.

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BRITISH AIRWAYS: COURT OF APPEAL DEFINES THE PROPER PURPOSE OF AN OCCUPATIONAL PENSION SCHEME AND NARROWS THE ROLE OF PENSION SCHEME TRUSTEES

Clive Weber and Katie Whitford

British Airways (BA) has successfully appealed against the BA pension scheme Trustees' award of pensions increases. The Court of Appeal reversed the High Court decision in favour of the Trustees by a two to one majority. We discussed the High Court judgment in our June 2017 edition of Pensions Compass.

Recap
The BA litigation concerns the exercise of a unilateral power of amendment by the Trustees, in response to the scheme's change from RPI to CPI-based increases in line with public sector schemes in 2010. This change was forced on the scheme because of the particular wording of the scheme rules which stemmed from the scheme's public sector origins.

Under their unilateral powers, the Trustees introduced:

- a duty for the Trustees to review the scheme's pension increases annually; and

- a unilateral power to award additional discretionary increases on top of the statutory-based increases required under the scheme rules.

The Trustees then awarded members a discretionary pension increase of approximately half the difference between RPI and CPI (0.2% in 2013).

The High Court held the Trustees had exercised their powers properly and had not acted unreasonably.

Appeal to the Court of Appeal
BA's appeal concerned two particular aspects of the High Court judgment. It argued that:

- the introduction of the discretionary increase power was beyond the scope and contrary to the *purpose* of the scheme's power of amendment; and

- the discretionary increase was a "benevolent or compassionate" payment and therefore prohibited by the scheme's objects clause.

BA was unsuccessful on the second ground of appeal (the increase was not "benevolent or compassionate"), but the first ground was upheld by a majority of the three judges, with Lord Justice Patten dissenting. The two judges in the majority, Lord Justice Peter Jackson and Lord Justice Lewison, held that the Trustees had not acted in line with the "proper purposes" of the scheme, and therefore the Trustees' amendment to introduce the discretionary increase power and subsequent award of discretionary pension increases were invalid.

The Trustees' *method* of decision-making (an area of law which is the subject of much litigation) was in fact not called into question in the Court of Appeal. Lord Justice Patten noted that the High Court found the Trustees had balanced the interests of the employer against those of the employees or former employees and had taken the funding implications into account. This was not the subject of BA's appeal.

PENSIONS & EMPLOYEE BENEFITS

Where the Trustees fell foul (according to the majority of the Court of Appeal) was in relation to whether the Trustees were acting beyond the purposes of the scheme and therefore not entitled to make those decisions in the first place.

Proper purposes: scope of the Trustees' amendment power

The scheme's power of amendment, exercisable only by the Trustees, contained a caveat that no amendment could be made which *"would have the effect of changing the purposes of the scheme"*. The Court of Appeal therefore had to consider whether the Trustees' actions had changed the purposes of the scheme and breached this caveat. This involved first finding what the purposes of the scheme really were.

The scheme rules helpfully contained an objects clause which provided that the main object of the scheme was *"to provide pension benefits on retirement… The scheme is not in any sense a benevolent scheme and no benevolent or compassionate payments can be made therefrom"*. The Trustees argued that this objects clause set out the purpose of the scheme, and the discretionary increase power fell within these boundaries.

BA argued that the Court shouldn't limit itself to looking at the scheme rules to discern the purpose, but should consider a wide variety of materials and factors, including the business context of occupational pension schemes and the funding level of the BA scheme. BA's position was that the Trustees had taken on a role akin to a trade union to improve members' benefits, going beyond their proper role to administer the scheme to fulfil the purpose of delivering promised benefits.

If the Trustees' decisions were upheld, BA argued that it would be forced into paying additional contributions *"not for the purpose of funding benefits already promised but for funding additional benefits decided upon by the Trustees"*.

Lord Justice Jackson adopted a test drawn from the important 1997 High Court decision in the *Courage* case to determine the validity of the Trustee's actions:

Were the Trustees' actions required *"by the exigencies of commercial life"*?

He found that they were not, and agreed with BA that the Trustees had effectively added the role of paymaster to their duties. However, it was central to this finding that the scheme was in deficit. Had the scheme been in surplus, the decision may well have been in favour of the Trustees.

Unusually, Lord Justice Patten's dissenting judgment is the longest and most closely reasoned of the three judgments, taking up about 2/3rds of the written decision. We understand that the Trustees have been granted permission to appeal to the Supreme Court and we can see plenty of scope for debate on both sides – indeed the judiciary itself is split.

It is very unusual for scheme trustees to have power to amend unilaterally. Nonetheless, the discussion in the Court of Appeal judgment of a scheme's "proper purposes" is important to all occupational schemes. Even where powers are vested jointly in the employer and the trustees, trustees still need to take into account the "proper purposes" of the scheme in their decision making. We eagerly await the next instalment in the Supreme Court – probably next year!

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£800M BUYOUT OF NEW BHS PENSION SCHEME

Katie Whitford

Pensions Insurance Corporation has announced an £800m buyout of the new BHS pension scheme, BHS2, on 12 August. BHS2 members were approximately 9,000 BHS pension scheme members who did not take a cash lump sum or transfer to the PPF, opting to transfer to the new sponsorless scheme under the terms offered by the predecessor BHS schemes.

This buyout represents a more secure position for the membership, guaranteeing the BHS2 benefits in full. The news comes against the backdrop of a predicted record-breaking year for the bulk annuity market. Hymans Robertson predict pension scheme buy-in and buy-out volumes to reach a record £18bn in 2018, the result of a combination of attractive pricing by insurers and de-risking following recent improved funding levels.

Trustees and employers of schemes which are moving towards a buy-out or bulk buy-in the near future should be aware of steps they can take to ensure their scheme is well placed in the current market conditions. Carrying out a scheme documents "health check" and putting together a benefit specification is an important first step and will allow trustees to identify potential issues and stumbling blocks at an early stage. Insurers are likely to favour well-prepared schemes as it will lead to a more straightforward transaction, and getting this preliminary housekeeping underway as early in the process as possible will allow trustees to watch market movements and time their approach to insurers. Equally important is having the right team of advisers on board who can guide trustees through the many technicalities inherent in the process – a factor which helped to secure the BHS2 benefits sooner than had been anticipated.

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PENSIONS & EMPLOYEE BENEFITS

INSOLVENCY AND DIRECTORS DUTIES: CHANGE IS COMING...

Justin McGilloway

On 26 August 2018 the Department for Business, Energy and Industrial Strategy (**BEIS**) published the government's response to the consultation on measures designed to improve corporate governance within companies which are in or approaching insolvency.

A string of prominent pre-pack insolvency arrangements whereby pension schemes are off-loaded to the Pension Protection Fund (**PPF**) whilst at the same time permitting struggling businesses to be sold have led many to comment that action is needed sooner rather than later to prevent continued abuse of the PPF.

With the House of Fraser's pension schemes due to enter the PPF's assessment period after the company was purchased as part of a pre-pack this topic is under the spotlight more than ever before.

Crackdown on reckless directors

A press release from BEIS on the same date as the consultation response entitled "Crackdown on reckless directors" confirms that:

- boardrooms will be expected to explain to shareholders how they can afford to pay dividends alongside capital investment, workers' rewards and pension schemes;
- struggling companies will be given more time to try to rescue the business and help safeguard jobs; and
- directors who have dissolved companies to avoid paying workers or pensions could be disqualified or fined by regulatory authorities for the first time.

These and other measures designed to protect workers and small suppliers will be set out in further detail in the autumn.

Role of the Pensions Regulator

Many in the industry are hoping that the Pensions Regulator will be given enhanced powers to ensure that, where there is a material scheme deficit, the payment of dividends or the sale of a company will not jeopardise the solvency of the fund. One suggestion in the consultation response is that where there is a deficit, directors should have to make a statement before declaring a dividend that the company will continue to be able to comply with the terms of any contribution agreement negotiated with the trustees.

The idea of providing fuller disclosure of details of a deficit reduction plan was also floated – this would go some way to providing stakeholders with useful additional information with which to hold management to account for decisions on pay out policy.

Wedlake Bell comment

As the title to this piece states – "change is coming". This consultation follows hot on the heels of this year's White Paper "Protecting Defined Benefit Pension Schemes" (March 2018) and the " Protecting defined benefit pension scheme – a stronger Pensions Regulator" consultation (June 2018). Measures to ensure there are clearer funding standards for all pension schemes and that the Pensions Regulator has enhanced powers to obtain the right information when it is needed and new powers to strengthen existing safeguards are on their way, and the majority will say, rightly so. However, any new measures must also be balanced to ensure that legitimate commercial transactions are now unduly hampered by restrictive pensions red tape. Watch this space.

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ELECTRONIC SIGNATURES

Edward Craft and Harriet Forster

Commercial parties are becoming more familiar with electronic signatures. In the summer of 2016, the Law Society produced a practice note summarising the current legal position and supporting the use of electronic signatures.

However, many concerns continue to subsist in relation to this, particularly in the real estate industry.

For this reason the Law Commission has turned its mind to the issue.

A lot of contracts do not need to be signed, or even written, in order to be valid. However, in relation to real estate section 2, Law of Property (Miscellaneous Provisions) Act 1989 is problematic. That states that contracts for the sale of land must:

1. be in writing;
2. contain all the agreed terms; and
3. be signed by or on behalf of all the parties.

The law does not expand upon the meaning of writing or the meaning of signed and pre-dates today's web-powered digital world. Is it possible to fulfil the statutory requirement for "signature in writing" without wet ink?

The Law Commission's consultation notes widely diverging views and practices from routine use of electronic signatures to those who will not entertain them in any circumstance. The Law Commission wants to cut through all this uncertainty, which is very helpful. Perhaps less helpfully, it has concluded that there is no need to change the law. We think that the fact that the current law regarding real estate raises profound and fundamental issues of interpretation presents a strong case for greater clarity and a debate over whether real estate should be treated differently to all other contracts?

The current consultation paper will not change the mind of any professional still committed to wet ink. For change to happen, the law needs to state clearly what is acceptable in an electronic world, and put the issue beyond debate and this must come from either Parliament or the appellate courts.

There is a strong case for an Act of Parliament to place the validity of electronic signatures on all types of contract beyond any doubt and demonstrate that English law is looking forward to a digital future. The Law Commission is reluctant to propose investing Parliamentary time on unnecessary legislation, but on this occasion, we can't help feeling it would be worthwhile and should not require significant debate.

Until the law is absolutely clear and any debate amongst legal professionals stops, adoption of electronic signing protocols will remain limited. Commercial parties should be allowed to contract in whatever manner they deem fit.

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