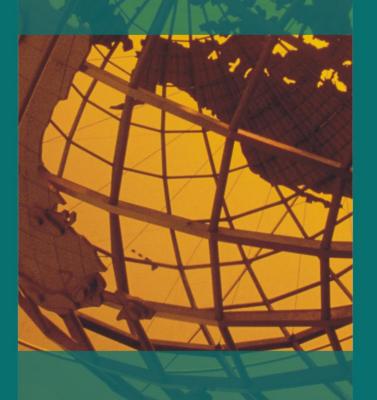
**Volume 92 – July 2020** 

### INTERNATIONAL

## PENSION LAWYER



Journal of the International Pension and Employee Benefits Lawyers Association



Contents	July 2020 – No 92
From the Editor	3
From the Chair	4
Journal Production Schedule and Representatives	6
IPEBLA Steering Committee 2019–2021	7
Theme: Effects of coronavirus disease (COVID-19) or	n pension arrangements
The COVID-19 Pandemic: The Initial Initiatives Taken Regulators	by Canadian Pension
Terra Klinck and Liam McCormick	
Canada	8
The Impact of the Corona Crisis on Belgian Occupational	Pensions
Jan Van Gysegem and Dorien Verstraeten	
Belgium	11
Impact of COVID-19 on UK Pensions Law	
Rosalind Conner and Aneliese Sweeney	
United Kingdom	14
Irish Pensions and the COVID-19 Pandemic	
Ian Devlin and Rebecca McEvoy-Martin	
Ireland	17
Pension and Employee Benefits Insights: France's Res	sponse to the COVID-19
Catherine Millet-Ursin and Sophie Yin	
France	21
ESG Implications of COVID-19	
Randy Bauslaugh	
Canada	24

The 'Lucky Country'?: The Australian Economic Response to COVID-19 and Impact on Australian Superannuation Funds	1
Andrew Bradley	
Australia	28
COVID-19 Measures for the Dutch Pension Sector	
Sijbren Kuiper and Wijnanda Rutten	
The Netherlands	39
COVID-19 and Pension Funds in Zimbabwe	
Nobert Musa Phiri	
Zimbabwe	43
Retirement Funds and COVID-19: Options for Payment of Contributions in South Africa	l
Leanne van Wyk	
South Africa	47
Theme: Sustainable investing	
Sustainable Investing of U.S. Retirement Assets	
Dana M. Muir	
United States of America	53
Theme: Comparative regulation	
A Comparison of the Regulation of Death Benefits in Occupational Pension Arrangements in South Africa, Germany and France	1
Naleen Jeram, Marco Maurer and Auriane Damez	
South Africa, Germany, France	59
	-



From the Editor ...

#### Dear Colleagues,

I hope you are all well in this difficult time of the COVID-19 pandemic, and that you have been able to be busy in this special area of law that we find so interesting.

One aspect of pensions law that is so important is its daily relevance in the lives of most people. That is why there is a response to be made in pensions law to something like the pandemic, because it affects everyone not only in respect of their health but also, amongst other areas, in the aspect of pension arrangements. Hence this edition which is focused primarily on the pension law response of various jurisdictions to the impact of the pandemic. I am grateful for those contributors from Canada (with an additional contribution from an investment aspect), Belgium, the UK, Ireland, France, Australia, The Netherlands, Zimbabwe (for the first time), and South Africa.

Then we also have two more articles: one on the latest developments on sustainable investments for pension plans in the USA, and the other a comparative analysis of the regulation of death benefits in occupational funds in South Africa, Germany and France. This last one is in fact what was to have been one of the workshops at the joint IPEBLA/PLA conference in Cape Town in March this year which, as you know, sadly was cancelled.

So there you have it, a bumper edition with twelve articles, put together by no less than twenty contributors. A special thanks to each of them.

Finally, Jessica Bullock has bowed out as co-editor for the time being and I would like to thank her for her support.

With best wishes,

Jonathan

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From the Chair ...

#### Dear Colleagues,

It certainly is a changed world since our last edition of the IPBELA Journal was published in January 2020. As most of you know, we unfortunately had to cancel the 2020 Joint Conference in Cape Town between the Pension Lawyers Association of South Africa and IPEBLA just as the COVID-19 pandemic was sweeping across the globe. Now, nearly all of us have been living among it for months, adjusting to our "new normal," and watching and waiting through various phases of re-opening.

Of course, as it has impacted all aspects of life, COVID-19 has affected not only our workplaces, but also the substance of our work. There have been legislative changes, impacts on markets and investments and challenges for employers and employees alike. This "super-sized" edition of the Journal has twelve articles from multiple jurisdictions addressing various responses to the pandemic as well as two other articles. I want to thank Jonathan Mort for his dedication to putting this edition together. I also want to thank David Powell for working with the Regulatory Liaison Committee in setting up jurisdictional COVID-19 "pocket summaries" on the IPEBLA website. Thank you also to the IPEBLA members that made contributions to these initiatives. Both the Journal and the website are valued resources by IPEBLA members, for IPEBLA members.

While we could not meet in person in Cape Town, the Membership Committee is working on virtual initiatives for members to stay in-touch through our next in-person conference. The Biennial Conference is one of the cornerstones of IPEBLA membership, and both the Steering Committee and the conference chair, Mitch Frazer, are actively discussing the various ways to continue the conference even with the uncertainty of the COVID-19 pandemic. To that end, if you have not already, please complete the Member Survey regarding the 2021 IPEBLA Biennial Conference, currently scheduled for 30 May to 2 June, 2021 in Amsterdam, Netherlands. (The link to the survey was sent via e-mail, but can also be found on the IPEBLA website.) The Steering Committee plans to make several key decisions as to the 2021 Biennial Conference in September, and will communicate with the IPEBLA membership regarding conference plans thereafter.

To continue with one of the initiatives IPEBLA began at the 2019 Biennial Conference in Lisbon, Mark Firman and members of the Executive Compensation Committee are sourcing articles for an executive compensation themed edition of the Journal. If you are interested in contributing an article on a non-pension, "compensation" topic – please reach out to Mark, Jonathan or your Journal country representative (the list is within this edition).

Finally, I wanted to thank Jessica Bullock for her contributions to co-editing prior editions of the Journal and note that Jonathan Mort is now the sole editor of the Journal. Thanks Jess! Until we meet again!

Carolyn

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## The COVID-19 Pandemic: The Initial Initiatives Taken by Canadian Pension Regulators





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#### Canada

The current COVID-19 pandemic has altered virtually every facet of daily life throughout the world, including the maintenance and administration of pension plans. This article provides a general overview of the actions taken to date by Canadian pension regulators and governments in response to the pandemic, including: (1) easing regulatory burdens, (2) allowing employers to curtail funding costs on a temporary basis, and (3) measures to ensure the benefit security of pension plan members.

#### Introduction

The current COVID-19 pandemic has altered virtually every facet of daily life throughout the world, including the maintenance and administration of pension plans. This pandemic has impacted global economies and markets and will invariably have a long-term impact on workplace pension plans.

In the shorter term, Canadian pension regulators have acted swiftly to respond to

the immediate needs of pension plan administrators, employers/sponsors and members. This article provides a high-level overview of these measures.

### 1. The Canadian Pensions Framework

In Canada, voluntary workplace registered pension plans<sup>1</sup> are governed by minimum standards legislation<sup>2</sup> enacted by our provinces, as well as a separate income tax regime. The pension minimum standards

Voluntary workplace pension plans are separate from the government sponsored "universal" workplace programs, the Canada Pension Plan (CPP) and the Quebec Pension Plan (QPP). There are also a variety of other workplace retirement and savings plan arrangements in Canada which are subject to a significantly less onerous legislative and regulatory regime.

With one exception; the province of Prince Edward Island has not enacted pension legislation. Additionally, the Federal government has adopted pension minimum standards legislation that governs workplace plans maintained by employers who perform certain inter-provincial undertakings such as banks, telecommunications, and airlines.

legislation of each Canadian province is similar in many respects, covering many of the same topics (e.g., minimum benefits, members' rights, funding requirements, etc.). However, Canadian pension minimum standards legislation includes province-by-province differences. Consistent with the framework, in the aggregate Canadian pension regulators have undertaken many similar COVID-19 response measures, but the precise measures taken by regulators have varied by iurisdiction.

### 2. The Canadian Response to Date

Throughout the COVID-19 pandemic Canadian pension regulators have remained open and have continued day-to-day operations. Most Canadian regulators are accepting electronic communications and filings as well as electronic signatures on documents, including in cases where paper filings and ink signatures were historically required.

#### Easing regulatory burdens

Most Canadian pension regulators have taken measures designed to address the upheaval of employers' and administrators' workplaces since the physical closing of many Canadian workplaces in mid-March. Most regulators have published policies providing extensions for various regulatory filing requirements (e.g., financial statements, annual information returns and actuarial valuation reports). In some jurisdictions the extensions are automatic and in other jurisdictions applications for extensions are required.

Most Canadian pension regulators have also provided time extensions for the delivery of various forms of member communications (e.g., annual member statements, notices of plan amendments) in recognition of difficulties faced administrators and their service providers in producing these communications in the current remote working environment. Again, in some jurisdictions the extensions are automatic and in other jurisdictions applications for extensions are required. In Canada, plan administrators must provide statutory member notices in writing. Electronic delivery of these statutory communications is generally permissible absent specific consent. Due to statutory constraints, the regulators have been unable to allow for the electronic delivery of member communications.

## Allowing employers to curtail funding costs on a temporary basis

In Canada, employers are required to fund defined benefit (DB) plan normal cost contributions (for current accruals) and special payments (for historic plan deficits). Significantly, the federal government has announced that it will be providing immediate, temporary funding relief to sponsors of federally-regulated plans through a moratorium on solvency special payments for the remainder of 2020. Employers will be required to continue to make normal cost contributions for current accruals. In contrast to historic solvency relief initiatives introduced in the past (in response to the 2008 economic crisis for example), it is anticipated that the federal COVID-19 solvency relief regime will not be an opt-in program, and member and/or union consent will not be required. Rather, the statutory regime will be revised to provide that no further solvency instalment payments must be made in 2020. The federal government has also stated that it will be consulting with stakeholders over the coming months regarding options to provide funding relief in 2021, as necessary. In the coming months we expect provincial governments to introduce pension funding relief initiatives in various jurisdictions through statutory changes. Whether provincial governments will follow the federal government's proposed 2020 COVID-19 solvency moratorium model or a more traditional solvency funding relief regime is not yet known but will, of course, be of great interest to the Canadian pension industry over the coming months.

Other Canadian provincial minimum standards regulators have signalled a willingness to consider on a case-by-case basis extensions to the amortization periods for the funding of deficits, as well as extensions to the deadlines for the remittance of employer and employee contributions.

In respect of defined contribution (DC) registered pension plans, a number of regulators are permitting a temporary full suspension of employer and employee contributions to plans on a prospective basis. In order to implement changes to employee and/or employer contribution rates, the contribution formula under the DC pension plan text must be amended and filed with the applicable regulators. Member notices are required and vary by jurisdiction.

### Ensuring the benefit security of plan members

Under Canadian minimum standards legislation, when a member of a DB plan ceases employment prior to retirement age the member must be given "portability options", i.e., the ability to transfer the commuted value ("CV") of their pension entitlement out of the plan to a locked-in

vehicle. Pension legislation across the has different CV transfer country rules/requirements (e.g., employer top-up payments in order to allow 100% CV payments if a plan is underfunded, restrictions on transfer amounts when a plan is underfunded, etc.). Due to the significant declines in asset values and increased market volatility resulting from the COVID-19 pandemic, a number of Canadian regulators have imposed additional new restrictions on CV transfers to protect the funded status of plans and the rights and interests of plan members and beneficiaries who continue to hold benefit entitlements under a plan. By way of example, the Federal pension regulator has issued a directive temporarily prohibiting all CV transfers without specific regulatory approval. Restrictions on buy-out annuity purchases have also been implemented, for the same reason.

### Member withdrawals have not been expanded

In Canada, minimum standards legislation provides that members' pension entitlements are locked-in subject to limited exceptions (e.g., shortened life expectancy, small benefits). In contrast to initiatives taken in other countries, Canadian laws have not been revised to give members broader access to their pensions to alleviate immediate needs for cash.

#### 3. What's Next?

While Canadian employer and plan administrators have faced challenging economic conditions in the past, the COVID-19 pandemic is presenting unique and unprecedented challenges. We expect extensive further relief and reform initiatives to be introduced over the coming months.

### The Impact of the Corona Crisis on Belgian Occupational Pensions

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#### **Belgium**

#### Introduction

below We discuss the Belgian government's reactions to the Corona crisis in the field of pensions. The government's initiatives focused on (1) pension accrual during temporary unemployment, (2)prudential supervision, and (3) the operation of pension funds.

# 1. Pensions and Risk Coverages During Temporary Unemployment due to the Corona Crisis

In Belgium, temporary unemployment is a social security system which makes it possible to suspend the employment contract of certain employees in the event of force majeure or for economic reasons. Due to the Corona crisis, the government has softened the conditions and procedures of this system. As a result of the suspension of the employment contract, the employer no longer pays remuneration

and benefits. Instead, the temporary unemployed receives compensation from the government. A suspension of the employment contract does, however, impact the occupational pension in many cases. During the suspension, most occupational pension plan rules do not provide any further accrual of pension rights, and the risk coverages (such as death, disability, health insurance etc.) are suspended.

Several employers promptly took the necessary steps to modify the pension plan rules in order to guarantee further accrual of pension rights and/or risk coverages during periods of temporary unemployment due to the Corona crisis. At the end of March 2020, the insurance industry presented a global position announcing they would assimilate every period of temporary unemployment and guarantee further pension benefits (including risk coverages such as death cover, disability cover, collective health insurance), except in cases where the employer explicitly wishes not to do so (an opting-out system). This position is now being translated into law so that it would become applicable to all insured pension plans, but also to funds or institutions pension occupational pension provisions (IORPs). This law organises continuity of rights, regardless of what the pension plan rules provide. This does not require any amendment of the pension plan rules or the agreement with the pension provider (IORP or insurer). The employer/organiser can opt out and decide to follow the existing pension plan rules. However, the law provides that at least the death cover must be maintained, even when opting out.

The continuation of the pension plan means that the contributions and benefits will be calculated as they existed right before the beginning of the period of temporary unemployment. The contributions will thus be calculated on the basis of the remuneration of the plan member right before the period of suspension of the employment contract as a result of temporary unemployment.

However, to take the financial situation of the employers/organisers into account, the employers/organisers have the option to postpone the payment of contributions until 30 September 2020 at the latest, by simply informing the pension provider, without impact on the plan members.

In order to provide sufficient protection for the plan members, the employer also has an information obligation.

These rules apply from 13 March 2020 until 30 September 2020.

Although an answer has been given to the question of how to deal with pension rights in the event of suspension of the employment contract due to temporary unemployment, a number of outstanding questions remain. For example, it is unclear

how to deal with personal contributions. Unless the employer/organiser requested a postponement of the payment of the contributions, they must be paid. Normally, personal contributions deducted from the net salary, but due to the suspension of the employment contract, there is no net salary. In practice, the contributions will sometimes be deducted from the extra allowance paid by the employer on top of the unemployment benefit or they will be deducted from salary when the employee returns to work. It is also not entirely clear how the law can be applied to industry sector pension plans.

## 2. Regulatory Supervision **During the Corona Crisis**

Pension funds (IORPs) have certain obligations with regard to their funding level, obligations which they may not be able to meet in the context of the Corona crisis. This may mean that they will have to implement and monitor financial recovery plans. In addition, IORPs are also under the strict supervision of the Belgian regulator, the FSMA.

The Belgian regulator has announced that it will take account of the current situation in its supervision. For example, there is a twomonth postponement for annual reporting. It has also been announced that, in view of the unprecedented difficult and circumstances confronting the today, IORPs will not be unnecessarily burdened and the supervision will be limited to measures that are strictly necessary in view of the current circumstances. The Belgian Regulator is also prepared, where possible, to show flexibility for the practical application of the rules, including with regard to the deadlines for the regular updating of key documents,

such as the Statement of Investment Principles. However, the Belgian regulator also stresses that the rules and obligations remain unchanged and that the IORPs must pay additional attention to the continuity of their services.

Likewise, the National Bank of Belgium has published specific provisions for insurance companies in the context of the Corona crisis. For example, insurers are required to communicate on a regular basis to the regulator in order to closely monitor the impact of the Corona crisis on insurance companies. In addition, the insurance companies also received a postponement of two months for annual reporting.

## 3. Operation of Institutions for Occupational Pension Provisions (IORPs)

In addition to the postponement of the annual reporting and requirement to pay additional attention to the continuity of their services, a new Act was introduced in order to facilitate the organisation of the general assembly meeting, the board of directors meeting and meetings of other operational bodies of IORPs.

The Act introduces three temporary flexibilities for the organisation of the general assembly. (The general assembly of a Belgian IORP is composed of all sponsors, and. in some cases, representatives of the plan members.) Firstly, it is possible to postpone the ordinary general assembly meeting until 31 August 2020 at the latest, even if the has already been general meeting convened and without having to repeat the formalities for convening and participating. Secondly, the general assembly may be organised electronically video by teleconference. Thirdly, the board of directors may require the participants of the general assembly to vote remotely by means of a form drawn up by the board of directors and/or by working with proxies. The form or proxy must then be signed and returned to the IORP, this can be done by any means, including by returning a scanned or photographed form/proxy by email.

For the board of directors and the other operational bodies, any decision can be taken by a unanimous written procedure, even for the approval of the annual accounts and regardless of whether this possibility is provided for in the by-laws, and meetings can be held by video or teleconference.

These measures apply from 1 March 2020 up to and including 30 September 2020 and to all meetings of the general assembly, the board of directors or other operational bodies organised during this period. The end date may be extended if necessary.

#### 4. Other Developments

It is too early to tell what the long-term impact of the crisis will be, in particular on the financing of pension plans and the regulatory supervision of the financing levels. As employees are gradually getting back to work, the questions that arise deal with the impact of temporary salary reductions, increased flexibility in working time, and, regrettably, company reorganisations and collective dismissals.

#### Impact of COVID-19 on UK Pensions Law

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#### Introduction

There is no doubt that the impact of COVID-19 has been substantial from an economic point of view. However, the impact on UK pensions law has been much more limited.

## 1. The Coronavirus Job Retention Scheme and UK Pensions

Drawing on similar initiatives in place across the continent, the UK Government has introduced the Coronavirus Job Retention Scheme (CJRS) to support employees in these difficult economic times. Employers that choose to use the CJRS can 'furlough' their employees — this means that although the employees cannot do any work for their employer, the Government will provide a grant of 80% of the employee's salary (up to a maximum of £2,500 a month).

Given the success of automatic enrolment in getting more people saving into a pension in the UK, in addition to salary, the CJRS also covers the employer's pension contribution. However, the employer's pension contribution covered by the CJRS is capped at 3% of qualifying earnings (the minimum an employer is required to pay under UK automatic enrolment laws). This is fundamental to allowing employers to continue to pay pension contributions and encouraging employees to do the same.

That is the good news. Things get more complicated when you start to look at how the CJRS interacts with pensions. From a lawyer's perspective, the CJRS is not straightforward. The legal framework is set out in a short direction from the UK Treasury, in addition to guidance from HMRC (the UK tax authority) which changes on an almost daily basis. As the guidance and legal framework have inevitably had follow political to announcements, the CJRS does pose some difficulties from а pensions perspective.

For example, some employers may be required to pay more than the 3% contribution they can receive under the CJRS. This may be because of the terms of an employee's contract or the governing documents of a pension scheme, which the employer may have a limited ability to

change. Also, the minimum total pension contribution required to be paid under UK automatic enrolment law remains at 8% of qualifying earnings. Employers that agreed to pay more than the 3% minimum employer contribution must therefore continue to top-up the contributions they pay to furloughed employees, even though the employer can only recover the 3% minimum contribution under the CJRS.

An added complication is for pension contributions made by salary sacrifice. By salary sacrifice we mean an employee who has agreed to reduce their salary in exchange for their employer paying that amount on their behalf into the pension scheme (which gives a potential tax saving for both the employee and employer). Salary sacrifice causes a number of issues for employers using the CJRS:

- Where contributions are made by way of salary sacrifice, as the entire contribution is made by the employer, the employer must continue to make a contribution in excess of the 3% minimum it can recover under the CJRS. This is because to meet the minimum total automatic enrolment contribution set by law, the employer must be paying a contribution of 8% of qualifying earnings.
- As the 80% of salary available under the CJRS is based on the employee's (lower) salary after the sacrifice has been made, employees who use salary sacrifice will be worse off, unless their employer makes a voluntary top up to compensate the employee for this loss.
- Employers are having to look carefully at how their salary sacrifice arrangements are structured, as it may be that the employee has agreed to sacrifice a fixed figure, rather than a percentage of the

employee's salary (as it varies from time to time). If an employee has agreed to sacrifice a fixed figure, the pension contributions will remain the same (and therefore more expensive for the employer), despite the reduction in the furloughed employee's salary.

In summary, although the CJRS is a fundamental support mechanism for the UK economy in these times, it does pose some practical issues for employers to deal with from a pensions perspective.

### 2. Guidance from the UK Pensions Regulator

The UK Pensions Regulator (TPR) has been very responsive throughout this crisis, releasing guidance aimed at supporting both employers and trustees of UK pension schemes. However, as TPR has to work within the existing legal framework, the main changes it has made are in respect of enforcement and its guidance for dealing with distressed employers (as TPR cannot make changes to UK pensions law).

TPR has addressed some of the issues with the CJRS. For example, as employers try to reduce their pension contributions to the 3% minimum covered by the CJRS, TPR is waiving enforcement of the 60 day consultation requirement that would usually apply to such reduction (provided that certain conditions are met).

TPR is also effectively giving extra time for employers to pay pension contributions. Although TPR cannot change the law, it has stated that it does not expect late payment of contributions to be reported, unless the contributions are 150 days late.

More specifically for final salary pension schemes, TPR has set out guidance for employers in financial difficulty, including an ability to ask for the suspension or postponement of deficit contributions. An employer cannot change deficit repair contributions unilaterally the consent of the scheme's trustees is required to defer or suspend any contributions. Although this continues to be the case. TPR has set out how trustees can (and to extent encourages trustees to) consider such requests. Given that deficit repair contributions can be very substantial, this mechanism allows employers some breathing space and additional liquidity at a time when this can be hard to come by. However, this does come with strings attached. To secure the trustees' agreement, the employer may have to agree to suspend company dividends, put more security and share information about how the company's lenders are extending its finance terms.

#### Conclusion

Given the speed at which the CJRS was introduced (and continues to change) this support mechanism continues to cause a headache for pensions lawyers, as we try to deal with the unintended pension consequences which the UK Government did not have time to consider. In formulating its response, the UK Government appears to have chosen to not to make any changes pensions law to deal with the consequences of COVID-19. Instead, it has left the task of dealing with the pensions fallout mainly to TPR (who have to operate within the existing legal framework) by way enforcement of easements encouraging action through its guidance.

#### Irish Pensions and the COVID-19 Pandemic

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#### Introduction

The COVID-19 pandemic has resulted in shut downs, restrictions on movement and the enforcement of strict social distancing measures across the world. businesses are facing acute financial difficulties as a result. In Ireland, we have seen many businesses implement a range of cost cutting measures, including making changes to their pension arrangements. Against this backdrop, we examine the challenges that employers and trustees of Irish pension schemes have been grappling with. We also look at some of the government and regulatory responses relevant to the Irish pension sector.

## 1. Business Continuity, Governance and Administrative Issues

#### **Business continuity**

The Irish pensions regulator, the Pensions Authority ("Authority") issued guidelines for trustees in late March on how to deal with some of the more immediate issues arising from COVID-19. It recommended that trustees contact their administrators to confirm that:

- pension payments to retired scheme members are paid as they fall due; and
- that payments from members and employers are remitted to the scheme without delay.<sup>1</sup>

To date, administrators have successfully implemented business continuity measures and we have not seen trustees having to deal with disruptions to pension or contribution payments at an administrative level.

### Trustee meetings and executing agreements

Social distancing restrictions have meant that trustee and other types of board meetings are now taking place remotely in Ireland via video or telephone conferencing. This transition to meeting remotely has been surprisingly smooth. However, the same cannot be said for signing pension deeds.

Certain legal documents in Ireland,

The Pensions Authority, Press Release issued 27 March 2020.

including pension deeds, must be executed under seal. Unlike many jurisdictions, Irish law still requires Irish corporate entities to physically impress their corporate seal on any deed they execute. This must then be counter-signed by two authorised signatories, usually company directors, using wet-ink signatures. In most cases, it is still physically possible for Irish corporates to execute deeds during lockdown. It is however proving to be a cumbersome and time-consuming process. Some of the legal solutions being deployed to ease these difficulties include putting in place powers of attorney to enable a duly authorised attorney to execute deeds without the need for a corporate seal.

#### Administrative issues

The European Insurance and Occupational Pensions Authority ("EIOPA") on 15 April 2020 suggested that national competent authorities in the European Union (such as the Authority), should allow pension schemes flexibility in the collection of contributions from employers liquidity pressures and should be flexible about deadlines for publication in the current documents and data circumstances.2

Interestingly, the Authority, unlike some pension regulators in other European jurisdictions, has not formally relaxed any of the regulatory requirements it is tasked with policing. In late April 2020, the Authority emphasised that it has no power to waive statutory requirements but acknowledged that it would "take into account current circumstances" when

assessing compliance. It also confirmed that it expected trustees and their service providers to be able to demonstrate that they made "reasonable efforts to meet their statutory obligations".<sup>3</sup>

What amounts to "reasonable efforts" and how flexible the Authority will be in having regard to "current circumstances" is currently unclear. This is causing concern for many trustees and scheme administrators, who are struggling to deal with some of the logistical issues statutory associated with disclosure requirements as result of the pandemic.

Separately, in relation to the collection of statistical reporting data for the European Central Bank, the Central Bank of Ireland ("CBI") has also indicated a willingness to be flexible when it comes to the satisfaction reporting obligations by pension schemes. It has helpfully committed to "engage with reporting agents to see if pragmatic solutions can be found with respect to the challenges they are facing in meeting these requirements". This is welcome news for trustees and scheme administrators as they grapple to deal with many of the other issues the COVID-19 crisis has created for pension arrangements.

#### 2. Financial Considerations

#### Investments

The COVID-19 crisis has led to an almost unprecedented level of market volatility. In response, the Authority has cautioned against making immediate investment decisions "unless absolutely necessary". It

<sup>&</sup>lt;sup>2</sup> EIOPA, Statement on principles to mitigate the impact of Coronavirus/COVID-19 on the occupational pensions sector, issued 15 April 2020.

The Pensions Authority, Press Release issued 24 April 2020.

also recommended that trustees of defined benefit schemes should engage with their advisors to consider the impact of the current market conditions on the funding position of their scheme and any actions that need to be considered.<sup>4</sup>

To date, we have not seen Irish defined benefit schemes suffer the level of investment losses they experienced during the global financial crisis of 2008/2009. Their over-exposure to equities at that time led to scheme assets dropping by up to 30% in many cases. That experience has meant that Irish defined benefit schemes are much less exposed to equities now, which has sheltered them from some of the recent market volatility.

### Government supports and pension contributions

The Irish government has introduced several measures to help ease the financial impact of COVID-19. One such measure is the temporary wage subsidy scheme ("TWSS"). This State funded wage subsidy scheme is due to run for 12 weeks from 26 March 2020. The aim of the TWSS is to help employers retain employees who they may otherwise be forced to lay off.

Employers who have experienced a 25% drop in turnover are eligible to avail of the TWSS. This allows employers to fund a portion of their payroll by a wage subsidy payment, administered by the Irish Revenue Commissioners ("Revenue").

The interaction of the TWSS with pension arrangements has been one of the more complex aspects of the scheme. Revenue have confirmed that employers are not permitted to deduct employee pension

contributions from the wage subsidy portion of employee salaries. Where employers top up the wage subsidy, which they are free to do, pension contributions can be deducted from the top up amount. Many employers have, however, experienced practical difficulties with payroll systems when trying to process pension contributions through payroll where contributions are only being paid on the top up amount.

### 3. Suspension and Reduction of Contributions

In conjunction with pay cuts, many employers seek to temporarily alter pension contribution arrangements. One of the most common issues we have been advising on in recent months relates to the suspension and reduction of pension contributions.

In Ireland, an employer's obligation to pay pension contributions is typically governed by both the employee's terms and conditions of employment and the rules of the relevant pension arrangement.

Any decision to suspend or reduce employer pension contributions without employee agreement may amount to a unilateral variation in the employee's terms and conditions leaving the employer liable to claims for breach of contract. Where the employer operates a trust-based pension scheme, an employer unilaterally ceasing those contributions may breach the scheme rules leaving it liable to be sued by the pension trustees who have a statutory obligation to ensure contributions due under the scheme are paid.

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The Pensions Authority, Press Release issued 27 March 2020.

As a result, this issue needs to be approached carefully so that all stakeholders understand the basis on which any temporary suspension of contributions is pension being implemented. This is best achieved through open dialogue with employees and trustees leading to an agreed and documented basis for the temporary suspension.

Some data is now beginning to emerge on how widespread the temporary suspension of contributions has become. The Irish Association of Pension Funds ("IAPF") recently surveyed Irish trustees and noted that 15% of employers have suggested a temporary suspension of contributions.<sup>5</sup>

Separately, the Authority has recently issued guidance on this topic for trustees and employers. Specifically, it has published a non-exhaustive list of key factors for employers and trustees to consider with their advisors where a contribution suspension is being assessed.<sup>6</sup>

However, as noted earlier, the Authority has not taken any steps to relax statutory requirements, including statutory funding requirements. If employers are already looking to suspend pension contributions, albeit temporarily, it is likely that the Authority will come under increasing pressure relax statutory funding to **EIOPA** requirements, given the announcement in April.

#### Conclusion

Trustees and employers have already had a lot to consider and deal with in the context of COVID-19. However, we may only be beginning to see the fallout from this crisis.

The longer the lockdown goes on, the deeper the economic impact is likely to be.

Even if Irish pension trustees manage the investment side of the crisis better than during the global financial crisis, they may find themselves with employers whose financial position has been significantly weakened. We are already employers in certain sectors who were able maintain pension benefits during the last crisis now look to introduce benefit reductions. Time will tell if trustees and employers will be able to weather this crisis better than the last one, but the early signs in some sectors of the economy indicate that turbulent times lie ahead for pension schemes and their members.

<sup>&</sup>lt;sup>5</sup> IAPF Covid -19 Survey April 2020.

The Pensions Authority, Press Release issued 24 April 2020.

#### Pension and Employee Benefits Insights: France's Response to the COVID-19 Pandemic

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#### **France**



#### Introduction

As part of its efforts to limit the spread of the epidemic, France imposed a nationwide lockdown on March 17, 2020. Emergency legislation was passed by the French government in order to safeguard companies and protect jobs.

Many employers have had to adapt their organization during these difficult times.

Since May 11, 2020 and the gradual lifting of lockdown restrictions, businesses have begun a partial reopening. However, with the virus still circulating, many of the measures that were implemented during lockdown still remain in place.

We take a look at the COVID-19 related employment benefits during and after lockdown.

### 1. "Partial Activity" (Paid/Subsidized Furlough)

To prevent companies from going under and avoid mass unemployment, the French government implemented an extensive "partial activity" scheme. "Partial activity" allows employers to temporarily reduce the workload of employees or to keep them employed while the company is temporarily shut down.

Under this scheme, employees are entitled to 70% of their gross pay per hour not worked (or more if a more favorable collective bargaining agreement applies), i.e. 84% of their net hourly wage.

This allowance is paid by the employer and not subject to social security contributions (it is, however, subject to income tax).

The employer is then fully reimbursed by the State at the rate of 84% of the employee's net remuneration (100% of the compensation paid to the employee) up to a limit of 4.5 times the minimum wage.

As of June 1, 2020, the State's financial relief is expected to be lowered to 85% instead of 100% (to be confirmed).

## 2. Company Health/Death & Disability Insurance Benefits

For employees under the partial activity scheme, the insurance premium normally deducted from the employee's salary is deducted from the partial activity allowance so that the employee can continue to benefit from the group policy coverage.

#### 3. Pension Benefits

The partial activity allowance is exempt from social security contributions.

As a result, it does not generate pension rights.

However, the mandatory pension schemes feature solidarity mechanisms, allowing partial activity periods to be taken into account to a certain extent:

- at the statutory level (basic State pension scheme), 50-day periods compensated under the partial activity scheme are assimilated to one quarter, within the limit of four quarters per year;
- for the mandatory complementary pension scheme, employees are awarded free points for the hours compensated under the partial activity scheme over 60 hours per year.

#### 4. Paid Leave

As part of the emergency measures enacted to deal with the epidemic, employers have been given additional prerogatives to impose, postpone or change the date of different types of paid leaves, within the limit of a certain number of days and subject to a shortened notice period.

For instance, employers were authorized to impose, at their convenience, six days of paid leave (out of a legal annual quota of five weeks), subject to a one-day notice period.

#### 5. Sick Leave

#### Regular sick leave

In case of accident or illness, employees who are unable to work receive daily cash benefits from the French Social Security ("indemnités journalières de Sécurité sociale" or IJSS, literally "Social security daily allowances"), as well as an additional compensation ("indemnités journalières complémentaires" or IJC) from their employer.

While the payment of these benefits is normally subject to compliance with certain conditions (number of hours worked or contribution paid, duration of registration with the French social security, waiting period, seniority), the French government decided to waive these conditions in the context of COVID-19.

### COVID-19 related leave of absence

In addition to the regular sick leave, different new types of specific leave of absence were instituted during lockdown:

- Leave of absence due to isolation (for employees not ill but who are in isolation following a stay in an area affected by the outbreak or contact with an infected person):
- Leave of absence due to childcare (for employees with children under 16, and for employees with children between 16 and 18);
- Leave of absence due to vulnerability (for employees not ill but with a high risk of infection, or living with such a person).

Employees in these situations benefited from similar daily cash benefits from social security and their employer as those on

regular sick leave, without seniority or waiting period conditions.

Moreover, some of the regular sick leave limitations did not apply to these specific leave of absence (no reduction of the employer compensation after a certain amount of time, no taking into account of previously compensated periods...).

Those specific leave of absence were in effect until April 30, 2020.

Since May 1, 2020, only the leave of absence due to isolation remains. On that date, leave due to childcare or vulnerability were converted to partial activity.

#### **ESG Implications of COVID-19**

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#### Canada



Environmental, social and governance (ESG) considerations and criteria have grown in importance in Canada in recent years. There has been increasing acknowledgement that ESG factors can be applied to better understand and predict financial risk and financial opportunity. From a legal perspective, using ESG factors to assess value, rather than promote values, is fully consistent with fiduciary management of pension assets.

How will this growth be affected by the COVID-19 pandemic? Will uncertainty lead fiduciaries to retrench and focus on the usual economic fundamentals or will it expand the recent Canadian momentum to place more reliance on ESG factors by pension funds and other institutional investors?

Some have argued that the transition to a greater appreciation of ESG factors arose because an extended bull market over the past 10 years has permitted

experimentation with ESG. In their view, this may result in some degree of retrenchment to more established financial metrics, thus hindering ESG considerations.

But that does not seem to be the case. There is evidence emerging as a result of the pandemic that investors who take into account ESG factors may be doing better than, or at least not as poorly as, their non-ESG counterparts at least at this stage of the pandemic.1 While it is early days, it appears that risk management techniques and financial strategies that are informed by ESG factors and ESG scenario testing are leading to better results. In my view, the pandemic is more likely to validate the financial objectives behind ESG factor integration and help to dismiss legal and business concerns that ESG factor integration is simply a means for dogooders to impose or promote their values.

losses that have initially resulted from COVID-19, but is also delivering alpha in both passive and active strategies. In the Canadian market, data provided by Fundata shows that more than 83% of responsible investment funds outperformed their average asset class return in Q1. Moreover, 80% of such funds outperformed over the one-year period ending March 31, 2020. The article notes that similar results have been seen in U.S. and other markets.

See Lanz, Dustyn, 'ESG and COVID-19: Four Market Trends', *Investment Executive*, April 20, 2020 <www.investmentexecutive.com/insidetrack\_/dustyn-lanz/esg-and-covid-19-four market-trends>. This article points to evidence that responsible investment funds are outperforming in passive and active strategies. It points to several sources for this, such as Fundata, Morningstar, and MSCI indices. The evidence appears to be that ESG factor integration is not only reducing the depth of

In my view, the pandemic is also likely to shift the emphasis from governance and the environment — the "E" and "G" in ESG investing — to a more urgent and focused approach on social factors — the "S" in ESG. If that happens it could have several implications in the Canadian marketplace.

First, the usual knee-jerk response to financial hardship or recession in Canada has been wage reductions and layoffs. But these appear to be taking a back seat as a mitigation strategy. The financial sector and governments have said they are deeply concerned that layoffs and unemployment may deepen the economic crisis if there is no one to buy the goods or if no goods are being produced or distributed.

Investors and investee entities also appear to be very concerned about reputational risks that affect value. The pandemic is not sector specific. It affects everyone. The business concern is that consumers are likely to remember how companies treated their people and their communities. As a result, social concerns about employee health and safety, fair treatment, childcare considerations. mental health considerations and the welfare of the communities in which companies operate may get a boost because of the pandemic. These types of considerations do appear to be front and center for many corporations as a direct result of the pandemic, and appear to be of interest to investors and lenders assessing how corporations will fare during the pandemic.

Another "social" area of concern to investors and corporations is the supply chain. Are provider agreements, systems and policies in place to continue with business as usual, even if staff are required

to work from home, shopping restrictions are imposed, borders are sealed, or complex supply networks and relationships begin to splinter or disengage? Canadians are now experiencing something I have never experienced in my lifetime shortages of consumer goods, including grocery staples, like flour. Some of this might be attributed to anticipatory hoarding, but other shortages, like face masks, gloves and other medical supplies, have emerged as much more concerning. Back in the 1970s, a famous economist, Fritz Schumacher, wrote a book called "Small is Beautiful" which highlighted the benefits of more localized supply chains which he had been advocating for decades. intelligent fool can make things bigger, more complex ... it takes a touch of genius - and a lot of courage to move in the direction."2 opposite Α possible consequence of the pandemic and the application of ESG factors by lenders and investors may be to ensure corporate oversight at the board level is digging deeper into understanding their own supply chains. It may also stimulate a more human scale on production, with an emphasis on localized supply chains, and improved community relations.

ESG policy development and disclosure might also get a boost from the pandemic. Pension and other institutional investors and creditors will not only want information about a corporation's approach to ESG issues, but will demand it. Just as the urgency of climate change has fostered more and more standardized environmental reporting, the pandemic may broaden the scope and urgency of urgent social factors to be assessed. Production of

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Ernst Freidrich Schumacher, Small is Beautiful (Blond & Briggs, 1973).

an ESG policy may become a standard expectation of investors and lenders in any due diligence process. Those policies will likely be expected to be all business, meaning, they will be short and to the point in demonstrating how ESG factor considerations generate financial growth and mitigate financial risk. I would also predict that investment managers looking for an important market differentiator will begin to take more sophisticated and engaged approaches to ESG analysis.

As ESG factor integration has matured, governance concerns and increasingly environmental concerns have led to development of more objective performance indicators. The subtlety and subjectivity of social factors will no doubt benefit from a more disciplined review that could be imposed because of the pandemic. Companies that are seen to be proactively engaged in disclosing and developing better "social" performance metrics may be better able to differentiate themselves from the competition during and after the pandemic and gain market share. Consequently, the pandemic may generate more quantifiable targets or more objective analytic approaches.

Finally, the pandemic may shift the perspective that ESG considerations are only relevant to the long-term. Climate change is a good example. The major adverse effects of the carbon that is in our atmosphere right now will not be fully realized for three or more decades into the future, so there is nowhere near the same sense of urgency as the immediate effects imposed by the pandemic. An effect of the

economic immediacy of the pandemic may be to strengthen appreciation of ESG factors as important metrics for the short and medium terms as well as long-term sustainability.

It's early days. However, I think it is more likely than not that the pandemic will not hinder ESG considerations. I think it may accelerate ESG integration in Canada and lead to improvements in ESG disclosure and analysis, particularly as it relates to social factors.

What about "impact investing" that applies ESG factor integration to promote social change or other moral or ethical results?

Viewed in its proper legal perspective, the safest focus for pension and many other institutional investors in Canada is financial. The purpose of pension and similar funds is to provide financial benefits now and over the very long term.<sup>3</sup> In my view, it is that purpose that will continue to expand ESG factor integration, not ethical purposes.

It should also be noted that for other investors and for investee organizations, there are other motivations to embrace ESG factor integration. In Canada. corporations law has required long directors to act in the best interests of the corporation. In 2008, the Supreme Court of Canada made it clear that depending on the circumstances, this may not be as simple as acting in the best interests of shareholders. Directors may, and might have to, consider the interests of other stakeholders including employees. creditors, consumers, government and the environment.4 In some Canadian

Subsection 8500(1) of the Income Tax Act Regulations requires the "primary purpose" of a tax qualified pension plan to provide lifetime retirement income — i.e., a financial purpose.

Existing Canadian securities laws already contain legal requirements for continuous disclosure of material environmental, social and governance

jurisdictions that wider scope has been incorporated explicitly into corporations statutes.<sup>5</sup> And even though the case law and legislation is permissive, it implies a balancing of interests to properly discharge fiduciary responsibility to the "corporation". This, combined with the effects of the pandemic may provide a boost to elevate social considerations in a way that responds to wider stakeholder interests to obviate or lessen risks that corporate decisions or investment decisions are not challenged, or worse, subjected to public divestment campaigns or outright boycotts.

So what effect will the pandemic have on ESG factor integration in Canada? My bet is that it will accelerate the importance of ESG factors in financial analysis. It will also broaden the focus of ESG by giving more airtime to the "S" in ESG. It will result in improved ESG analysis and reporting for short, medium and long terms.

We have slowly crawled out of a wilderness in Canada where many suffered from a mistaken belief that ESG factor integration was simply a means for do-gooders to impose or promote environmental and social benefits regardless of economic effect. The pandemic is likely to validate the financial perspective that ESG analysis brings to the table. That should have fiduciaries running hard to improve and accelerate ESG disclosure standards, as well as the financial metrics and the analytic approaches to ESG considerations.

risks. Refer for example, to lengthy and detailed guidelines published by the Canadian Securities Administrators (CSA), such as CSA Staff Notice 51-333 Environmental Reporting Guidance, dated October 27, 2010 and CSA Staff Notice 51-

<sup>358</sup> Reporting of Climate Change-related Risks, dated August 1, 2019.

See for example, Canada Business Corporations Act, ss. 122(1.1).

# The 'Lucky Country'?: The Australian Economic Response to COVID-19 and Impact on Australian Superannuation Funds



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#### Australia



#### Introduction

Most readers will be familiar with Australia's moniker as the 'The Lucky Country'. However, it may surprise some of you to learn that the term was originally intended as an *insult*.

'The Lucky Country' was the title of a 1964 book by Australian journalist Donald Horne, in which Horne posited that Australia's prosperity was based almost entirely on luck, and that it was a country 'run by second rate people who share its luck'.

In the context of a global pandemic that has devastated families and communities worldwide, luck is a relative term. However, at this too-early-to-tell stage, Australia's response to COVID-19 appears to have been among the most successful in the world, at least from a public health perspective. Right now, Australians *are* feeling lucky, and don't give a damn about Donald Horne.

That said, we are questioning whether our success in containing the spread of the

virus has come at too great an economic cost. Would our luck have held up without, as we Aussies like to say, 'chucking a national sickie'?

Australia's economy miraculously avoided recession during the 2007-8 financial crisis, in large part due to the strength of its banking system and the forced savings generated through its superannuation system. We also avoided the worst of the 1997 Asian crisis and the 'dot com' bubble. However, early indications are that our luck in this regard might be running out.

Once again, Australia's superannuation system has a vital role to play in Australia's economic response to the pandemic and in its economic recovery. This article examines:

- the key reforms to superannuation law that have been introduced in response to the COVID-19 pandemic; and
- some of the unforeseen impacts of the pandemic and the Federal Government's response to it on Australian superannuation funds.

I would like to acknowledge and express my gratitude to my colleague, Samantha Wells, Lawyer, MinterEllison (Sydney) for her significant contributions to this article.

# 1. Early Access to Superannuation for Members Impacted by COVID-19

Under Australian law, superannuation benefits are generally unable to be accessed by a member until the member meets a 'condition of release' — for example:

- reaching age 65;
- ceasing employment after reaching age 60; or
- permanently retiring after reaching 'preservation age' (which ranges from 55 to 60, depending on a person's date of birth).

The law provides for release of benefits in certain limited circumstances prior to a person reaching 'preservation age', such as where a person becomes permanently incapacitated or suffers severe financial hardship. To release benefits on grounds of severe financial hardship, the trustee of the superannuation fund must be satisfied that the member:

- can't meet reasonable and immediate family living expenses; and
- has been receiving relevant government income support payments for a continuous period of 26 weeks.

The payment must be a single gross lump sum of no more than \$10,000 and only one payment is permitted in any 12-month period. The payment is subject to tax.

As part of its economic response to the COVID-19 pandemic, the Australian Government has introduced a new, temporary, condition of release known as the COVID-19 Early Release Scheme,

which can be used by a beneficiary to access up to \$10,000 of their superannuation benefit in each of the 2019-20 and 2020-21 financial years. A beneficiary will be eligible to apply if:

- the beneficiary is unemployed; or
- the beneficiary is eligible to receive certain welfare payments made by the Australian Government; or
- on or after 1 January 2020, the beneficiary is made redundant or their working hours are reduced by 20% or more; or if a sole trader — their business was suspended or there was a reduction in their turnover of 20% or more.

Applications for payment under the COVID-19 Early Release Scheme must be made by 25 September 2020 and payments made under the Scheme will be tax free.

Typically, applications for early release of a superannuation benefit must be made to the trustee of the fund. Before paying a benefit, the trustee is required to conduct certain customer verification checks in accordance with Australian anti-money laundering and counter-terrorism financing (AMF/CTF) laws.

However, the Australian Government has determined that applications for payment under the COVID-19 early release scheme will be assessed by the Australian Taxation Office (ATO), rather than by trustees themselves. The ATO will then notify the trustee and the applicant of its decision, after which point the trustee will be required to pay the approved amount to the beneficiary within five business days.

The Australian Government and the ATO have each confirmed that the Australian Transaction Reports and Analysis Centre (AUSTRAC) — Australia's financial intelligence unit and its AML/CTF regulator

— will not require superannuation funds making payments under the COVID-19 early release scheme to conduct additional customer verification, where the payment is approved by the ATO and processed through the official Australian Government and ATO online portal.

#### Impact and implications

#### (a) Liquidity constraints

As of 30 May 2020, 1.96 million Australians had applied for early release of part of their superannuation benefits under the COVID-10 Superannuation Early Release Scheme, with approximately A\$13.5 billion of payments having been made thus far.

Whilst the amount withdrawn to date amounts to less than 0.5% of the total value of assets invested in the superannuation system, the timing of these withdrawals has coincided with a period during which inflows into superannuation funds have reduced, owing to the fact that a significant number of Australian workers have been stood down from employment or are working reduced hours.

Not surprisingly, the equities market has also fallen in value during this time, which has led to a number of superannuants looking to switch out of equities-based options to more defensive options, such as cash.

This confluence of factors has put liquidity pressure on some superannuation funds — most notably, on certain 'profit to member' industry superannuation funds. This is because industry superannuation funds tend to have a higher asset allocation towards illiquid assets such as

infrastructure and real property assets than 'retail' superannuation funds.

Further, industry superannuation funds tend to be aligned to certain industries. Funds who are aligned with industries that have been hardest hit by the COVID-19 isolation restrictions — such as tourism, hospitality, aviation, retail, building. entertainment and the arts have reportedly experienced triple withdrawal rate of retail superannuation funds and a lower amount of inflows into the fund owing to their higher proportion of members employed in heavily-affected industries.

The Australian Government has, to date, refused to provide a liquidity backstop for industry superannuation funds, on the basis that all superannuation funds have legal obligations to manage liquidity and to stress-test themselves for the possibility of 'hardship' withdrawals.<sup>1</sup>

This has led to a significant amount of work being done in the industry to uplift standards regarding liquidity management and to 'de-risk' portfolios

#### (b) Fraudulent transactions

A COVID-19 Senate inquiry held in early May 2020 heard that the easing of customer verification requirements and the speed in which the Australian Government has urged trustees to pay a benefit approved by the ATO under the COVID-19 early release scheme, has resulted in over 150 fraudulent transactions occurring and upwards of \$150,000 being stolen.

A temporary hold was placed on all applications in May to further investigate these incidents. It was ultimately

published by the Australian Prudential Regulation Authority (APRA).

Per Superannuation Prudential Standard SPS 530 Investment Governance (SPS 530),

determined that the systems break-down which led to the fraud being investigated by the Australian Federal Police did not involve a superannuation fund but, rather, a data breach within an accounting firm.

#### (c) Taxation arbitrage

Any amounts released to beneficiaries under the COVID-19 Early Release Scheme are not subject to tax.

This has led to some superannuants looking to take advantage of the fact that salary-sacrifice contributions to super are generally taxed at up to 15%, whereas ordinary income is taxed at marginal tax rates of up to 45% (plus 2% Medicare Levy).

Specifically, it is possible for a beneficiary to contribute \$10,000 of their pre-taxable income through a salary sacrifice payment made into their superannuation fund before 30 June 2020, while also applying to withdraw the tax free amount of \$10,000 under the COVID-19 early access scheme prior to 30 June 2020. Where the beneficiary has not exceed the legislated on concessional superannuation contributions they can make in a financial year (generally, \$25,000), they will have reduced their tax bill by the difference between the nominal tax rate applied to superannuation contributions (up to 15%) and their marginal personal tax rate (up to 45% plus 2% Medicare Levy) on this amount. Beneficiaries will then be able to repeat the process in July to September of 2020.

#### (d) Family law issues

The speed in which the Australian Government has implemented the COVID-19 early release scheme has created regulatory gaps with respect to family law considerations. Superannuation splitting

laws enable couples to split superannuation payments, payable under a superannuation interest one of them holds, in family law property settlements on relationship breakdown. Superannuation payments may be split by agreement or by court order and a superannuation account may have a flag placed on it which prevents a trustee from making any payment until the flag is lifted.

The regulatory amendments made to implement the COVID-19 early release scheme, do not amend relevant the family law provisions with respect to superannuation splitting between spouses. Accordingly, trustees may be forced to pay the entire amount of any benefit released under this scheme to a beneficiary, without reference to any superannuation splitting agreement or court order that might otherwise mandate that a percentage be paid to a spouse or de facto partner.

## (e) Long term impacts on superannuation balances for vulnerable Australians

The Australian Federal Government has come under significant criticism for permitting Australians to access their superannuation at a time where the value of superannuation investments has fallen by upwards of 10% in some funds as a result of the pandemic.

Industry super funds and various lobby groups have been vocal about the long-term cost to younger members of taking up to A\$20,000 out of their retirement savings, particularly at a time where investment markets are depressed. Industry fund aligned lobby groups have posited that a member aged 25 could see a reduction of over A\$100,000 in their ultimate

superannuation benefit at retirement by withdrawing A\$20,000 today.<sup>2</sup>

Concerns have also been raised about the potential for these reforms to exacerbate structural inequities in the system, as the most vulnerable Australians are more likely to need to fall back on their superannuation as a means of addressing short term cash needs. For example, women on average retire with 47% less in superannuation assets than men, and women on average make up a higher proportion of casual and part-time workers in Australia in industries that have been hardest hit by the pandemic.

### 2. Reduction in Minimum Pension Drawdown Rates

Given that returns on superannuation are concessionally taxed, Australian retirees that choose to draw down their superannuation balance as a pension are subject to minimum withdrawal amounts each year.

The Australian Government has announced that it will allow a temporary 50% reduction in the minimum drawdown for account-based pensions in 2019-20 and 2020-21 to enable retirees to better manage their finances and potentially draw down less of their superannuation balances at a time where asset values are depressed.

#### Impact and implications

These reforms have led to trustees asking themselves difficult questions about how best to implement the reforms. Many pensioners choose to withdraw the minimum amount from their pension each year in order to maximise the concessional

benefits they receive through the superannuation system. However, those decisions have been made on the basis of the normal minimum drawdown amounts, which has now been halved on a temporary basis.

In an ideal world, a superannuation fund trustee might communicate with all of its pensioners and receive updated instructions from them regarding the amount they wish to draw down from their pension. However, the reality is that not all pensioners will provide updated instructions on request, despite a trustee's best efforts to encourage them to do so.

This raises questions regarding what to do with pensioners who have elected to receive the minimum drawdown and do not provide updated instructions. Clearly those past elections were made in the context of the minimums that applied at the time those elections were made. In that context, should past elections to receive 'the minimum' be taken to constitute an election to receive the new minimum? Would the answer to that question differ depending on the way the election form is expressed e.g. if the election form required the member to express the amount they wish to receive in dollar terms (rather than by reference to a percentage of their account balance)?

Unilaterally reducing drawdown amounts to the new minimum will maximise the benefit the pensioner receives from continuing to invest through the concessionally taxed superannuation system. Further, there is merit in this approach because once superannuation is withdrawn from the system, it is generally difficult for a pensioner to recontribute that money.

<a href="https://www.canstar.com.au/superannuation/risks-access-super-early/">https://www.canstar.com.au/superannuation/risks-access-super-early/>.</a>

Nicola Field, 'The long-term cost of taking \$20,000 out of your super fund'

However, it is a difficult thing for trustees to unilaterally reduce the size of pension payments that may be relied upon by elderly Australians to meet their everyday needs, particularly at a time where so much of the country is experiencing financial hardship.

Navigating this issue has required trustees to think very carefully about how they communicate with pensioners and their financial advisers to maximise the opportunity to obtain updated instructions from the pensioner rather than trying to apply a "one size fits all' approach to a large cohort of disengaged pensioners.

#### 3. 'JobKeeper'

Within days of the World Health Organisation declaring COVID-19 to be a global pandemic, the Australian Federal Government unveiled a A\$130 billion wage subsidy referred to as 'JobKeeper', which aimed at keeping 6.5 million Australians — over half the Australian workforce — in jobs. The Federal Government has since revised its estimate of the cost of the scheme and the number of eligible Australians down by about a half due to a reduction in the anticipated economic impact of the pandemic. However, it remains to be seen whether the optimism in these revised estimates will persist as we head into a period of prolonged economic uncertainty.

The JobKeeper supplement is a temporary payment made to eligible businesses affected by the COVID-19 pandemic to support them in retaining full-time, part-time and certain casual employees who have been employed by an employer on a regular and systematic basis for longer than 12 months. The payment is \$1,500 per fortnight for each eligible employee and

must be passed on to each eligible employee in full or used to subsidise their wages, if the employee continues earning more than \$1,500 a fortnight.

In connection with the 'JobKeeper' supplement, the Federal Government has also amended the law to allow employers to stand down employees without complying with the usual obligations under Australian workplace and employment law.

In order to qualify for the JobKeeper supplement and be able to stand down employees as outlined above, an employer must have a reduction in turnover compared to a prior period of:

- (a) 30% or more, if the aggregated turnover for the business is less than \$1 billion (for income tax purposes):
- (b) 50% or more, if the aggregated turnover for the business is more than \$1 billion (for income tax purposes); or
- (c) 15% or more, for registered charities (except education institutions such as universities).

An employer is only able to claim the JobKeeper supplement for eligible employees who were in the employer's employment on 1 March 2020 and continue to be employed while the employer is claiming the JobKeeper supplement. There are several criteria an employee must meet in order to be eligible including being a permanent employee of the employer (or if casual, not a permanent employee of any other employer) and being aged 16 years or over as a 1 March 2020.

The JobKeeper supplement is administered by the ATO and eligible employers need to elect into the scheme through the ATO online portal.

The JobKeeper supplement will be assessed as income for Australian tax

purposes (not capital). The regime operates on a reimbursement basis — the JobKeeper supplement is made to the employing entity, not the employee, and will only be paid to the employer where certain 'wage' (and other) conditions are met. Broadly, the 'wage' conditions require the employer to have paid salary, wages, allowances, commissions or bonuses to the employee for the 'JobKeeper fortnight'.

#### Issues and implications

The JobKeeper supplement program has been of great benefit to Australian businesses in a time of dire economic need. However, it has also presented employers and superannuation trustees with a plethora of legal issues to consider.

Firstly, it is important to consider the interplay between **JobKeeper** Australia's Superannuation Guarantee (SG) regime, under which employers are generally required make SG to contributions of at least 9.5% of an employee's 'ordinary time earnings' in order to avoid liability for a punitive tax known as the Superannuation Guarantee Charge (SCG).

it is not clear whether employers will still be required to pay SG on the JobKeeper supplement where an employee has been stood down. In those circumstances, the payment may be said to not be in respect of ordinary hours worked. Guidance provided by the Australian Treasury seems to suggest that employers will still need to pay SG contributions on the employee's income where they work, but not for any payments paid to the employee where they are not working.

It is also not clear whether employers will be required to pay SG on amounts that are required to be paid to an employee that are over and above their normal salary. Again, the Treasury guidance seems to indicate that employers will have a choice as to whether to pay super on such additional payments. These uncertainties in the application of the SG regime has placed significant additional burden superannuation and trustees their administrators, who each have had to field large volumes of queries about the application of the SG regime to JobKeeper payments.

Secondly, the introduction of JobKeeper has had significant impacts on insurance cover provided by superannuation trustees. In Australia, many superannuation funds purchase group life and salary continuance insurance which they offer to beneficiaries of the fund (and, in fact, provision of insurance is compulsory in respect of a large number of employees who do not choose a fund for themselves and are defaulted into the employer's selected 'MySuper' product).

Group insurance policies are designed so that eligibility for cover may be dependent on the employment status of a beneficiary. It is fair to say that insurance policies have not been drafted with the thought in mind that a person could be employed and earning income but not at work, for example. Depending on the policy wording, cover may cease beneficiaries no longer meet the eligibility criteria, which may not be met during a forced stand down or reduced hours. Additionally, certain benefit types are calculated using average income at the time of disability and may therefore, be reduced where beneficiaries make a claim for disability in these circumstances.

The changing employment status of members during the COVID-19 crisis presents a challenge to trustees, who will

be required to determine whether a beneficiary remains employed or is on a particular type of leave, in order to assess whether that beneficiary remains covered under the terms of the insurance policy. Trustees will also need to assess the impact of any forced stand down or reduction in working hours on the amount of benefits payable, where a valid claim is made during this period. For example, payments made under the JobKeeper supplement may impact the benefit payable under an income protection insurance policy.

Additionally, some group insurance policies are designed so that member eligibility for cover may be dependent on the receipt of SG contributions. A prolonged shut down of businesses will likely impact the SG contributions of many beneficiaries, who are now facing the possibility of income reduction and long-term unemployment. Depending on the policy wording, account balances and any standing election, this may in turn, result in beneficiaries no longer being eligible for cover.

# 4. Changes to Disclosure Obligations for Financial Advisers

Many Australian superannuation funds offer financial advice as an adjunct service beneficiaries of the fund. Superannuation funds can provide beneficiaries with general advice or simple, non-ongoing personal advice on a limited range of superannuation issues. This advice can be charged collectively across the fund's membership and is known as intra-fund advice. Superannuation funds may also offer detailed personal advice through a financial adviser.

The provision of financial advice to retail customers in Australia is highly regulated, and financial advisers have stringent disclosure obligations when providing 'personal advice' to customers. 'Personal advice' is defined under Australian corporations law as advice that is given to a person in circumstance where:

- (a) the provider of the advice has considered one or more of the person's objectives, financial situation and needs (otherwise than for the purposes of compliance with Australian AML/CTF laws); or
- (b) a reasonable person might expect the provider to have considered one or more of those matters.

To facilitate the provision of timely advice to consumers on the COVID-19 early release scheme, the Australian Securities and Investment Commission (ASIC) has issued temporary 'no-action' position superannuation trustees. The purpose of this no-action position is to confirm that, in the circumstances and subject to certain conditions outlined below, ASIC will not take action in relation to personal advice about the COVID-19 early release scheme provided as intra-fund advice on the basis that breaches S 99F of Superannuation Industry (Supervision) Act 1993 (SIS Act).

ASIC's relief and no-action position are temporary and subject to the following conditions:

- clients must be provided with a record of advice (ROA), which meets certain content requirements;
- the advice fee, if any, is capped at \$300;
- the advice provider must establish that the client is entitled to the early release of their superannuation; and

 the client must have approached the advice provider for the advice.

ASIC granted further relief in respect of the provision of financial advice as follows:

### (a) Relief to facilitate advice about the COVID-19 early access scheme

To assist the provision of affordable advice on the COVID-19 early access scheme, ASIC has:

- allowed advice providers to avoid giving a statement of advice (SOA) to customers when providing advice about the COVID-19 early access scheme;
- permitted registered tax agents to give advice to existing clients the COVID-19 early access scheme without needing to hold an AFS licence.

### (b) Relief to extend the timeframe for providing time-critical SOAs

To assist financial advisers meet the demand for time-critical advice during the COVID-19 pandemic, advice providers will now have up to 30 business days (rather than five business days) to give an SOA after time-critical advice is provided.

### (c) Relief to enable an ROA to be given in certain circumstances

Financial advisers will now be able to provide an ROA to existing clients even though:

- the clients' personal circumstances have changed as a result of the COVID-19 pandemic; and
- the client sees an adviser from the same AFS licensee or practice, not their original adviser.

#### Impact and implications

The regulatory initiatives will assist Australians to obtain lower-cost financial advice on a timely basis in response to the economic impacts of the pandemic on their personal financial circumstances. They also provide an opportunity for Australia's embattled financial advice industry to demonstrate its value and repair some of the damage to the industry's reputation that arose from the findings of the recent Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (FSRC).

# 5. Changes to the Formalities of Executing Documents

Under Australian law, generally, an agreement can be in electronic form and executed electronically, where as a deed must be in paper form and signed in wet ink (with limited exceptions being made under the conveyancing laws of certain states).

If a document must be witnessed, then the witness must be physically present during the execution of the document. It remains unsettled whether a witness can electronically sign the document in these circumstances.

In normal circumstances, a company may execute documents under s 127 of the *Corporations Act 2001* (Cth). Whilst a purported s 127 execution carried out electronically may still be valid at common law, many form the view that a s 127 execution requires a physical signature on the document to trigger the benefit of the statutory assumptions relating to due execution.

Due to the difficulties posed by the COVID-19 pandemic, the Australian Government has amended the *Corporations Act* as follows:

- Split execution the officers of a company may sign different/separate physical copies of the document in wetink.
- Modified split execution where one
  officer of the company signs a document
  in wet-ink and then faxes or emails a
  scanned copy of the document to the
  other officer, and that other officer then
  prints and signs that faxed or scanned
  copy in wet-ink.
- 3. **Electronic execution** separate electronic signatures can be applied to electronic versions of the document. In practice, there are a wide variety of means by which officers of a company might sign a document electronically. These include:
  - a. pasting a copy of a signature into a document;
  - signing a PDF on a tablet,
     smartphone or laptop using a stylus or finger;
  - c. cloud-based signature platforms like DocuSign.

Several of the State Governments of Australia have also enacted emergency regulation powers to amend state-based legislation to allow for electronic execution of documents on a temporary basis.

# 6. Other Reforms and Regulatory Announcements

In response to the COVID-19 pandemic, the Australian Government and Australian regulators have made a number of other announcements in response to the pandemic, including:

- ASIC has extended the deadline for unlisted companies to lodge financial reports by one month;
- 2. ASIC will consider applications from listed entities to extend their financial reporting deadlines;
- ASIC will take no action if AGMs are postponed until the end of July, and supports the holding of AGMs using appropriate technology;
- ASIC is proposing to defer the first reporting date to identify portfolio holdings of a superannuation fund by two years to 31 December 2022 (previously 31 December 2020);
- Suspension of consultation, regulatory reports and reviews (such as ASIC report on executive remuneration) and other activities which are non-time critical;
- ASIC has attempted to ensure market resiliency by issuing directions to a number of institutional investors requiring them to conduct a minimum number of trades executed each day;
- APRA has provided a temporary extension of notification period for changes to accountability statements and maps under BEAR;
- an announcement from the Australian Treasurer of a six months' delay to the implementation of the FSRC reforms consulted on in January and February 2020; and
- an announcement from ASIC of a six months' delay to the commencement of the design and distribution obligation or 'DDO' reforms.

#### Conclusion

The response of Parliament and regulators in Australia to the pandemic has given superannuation and pension lawyers plenty to think about and has brought into focus some potential structural weaknesses in the sector, most notably in relation to liquidity.

These developments come at a time when the question of whether superannuation funds were appropriately managing their liquidity was already on the parliamentary agenda, as this was a key area of focus on an enquiry by the House of Representatives Standing Committee on Economics in late 2019 and early 2020.

What this author is most interested in, however, is the role that superannuation funds will play in Australia's economic recovery. Even before the pandemic, Australia was in the position of having historically low interest rates and superannuation funds were subjected to intense regulatory pressure to improve member outcomes (that is, reduce fees and costs and improve investment returns).

There is a tension between seeking to improve returns and liquidity at the same time that is yet to play out, especially given that Australian Governments are already making noises about using the lever of infrastructure investment to stimulate growth and create jobs. Will Australian superannuation funds double down on infrastructure investment as a means to deliver superior investment returns? Or will the current focus on liquidity operate as a handbrake economic to growth Australia? It would seem to this author that the Australian regulators are hoping that industry consolidation will provide the best of both worlds and enable funds to invest larger pools of capital in unlisted

investments without compromising their liquidity position.

#### COVID-19 Measures for the Dutch Pension Sector

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#### The Netherlands

#### Introduction

The coronavirus has created an challenge unprecedented for Dutch employers and employees, and hence for Dutch pension providers. Social partners, interbranch organizations. external supervisory authorities and pension providers are doing everything in their power to enable employers and employees to handle the situation as best as they can. This article provides a short overview of the measures that have been taken.

#### 2. Supervision of Pension **Providers**

As a result of the coronavirus the Dutch Central Bank (DNB), in its role of supervisory authority of the pension providers (pension funds, insurers, and premium pension institutions (PPIs)), has announced the following concessions and adiustments regarding supervisorv measures:

 Pension providers receive three months extra time (until 30 September 2020) to submit their annual report:

- Pension providers can ask for an extension of their monthly and annual reports submission deadline as well as the submission deadline for their recovery plans. This is based on the existing 'Policy Rule discharge financial reporting Pensions Act and Law compulsory affiliation to an occupational pension scheme 2015';
- number of already scheduled investigations will, as yet, not be carried out and the pension providers subject to these scheduled investigations will be notified;
- The priority of supervisory activities will be adjusted. There will, among other things, be increased attention paid to the functioning business continuity of management, cyber risks, and implications of turmoil on the financial markets:
- The frequency of the publication of the yield curve will be increased to be weekly:
- Under certain conditions temporary diversion from the strategic investment policy is allowed. The exceptional market conditions can give reason to

temporarily divert but structural and purposeful increase of the risk profile during a period of recovery is not permitted.

In addition, DNB has announced six measures all pension providers are obliged to take in order to guarantee the continuity of the business operations. Pension providers must actively give further effect to the following:

- The proactive following of developments around the pandemic, preferably using a multidisciplinary team;
- The mapping and analyzing of the potential effects of the pandemic (explicit impact analysis);
- The evaluation of existing business continuity plans (BCP) on their adequacy, taking into account the possible operational effects of the pandemic (among others 30% or more absence of staff);
- The explicit taking into account of the pandemic's scenario in the test strategy of continuity plans;
- The taking into account of changing behavior and preferences of employers, pension- and other beneficiaries and personnel, including the support for a stark increase of internet usage;
- Where external service providers and/or vital suppliers are being used, the ascertaining of whether or not they too have taken adequate measures and are sufficiently prepared for the pandemic (the independence of all outsourcing partners needs to be transparent and the adopted measures sufficient).

# 3. Forbearance Regarding the Payment of Pension Contributions

Pension funds, insurers, and PPIs will, as much as possible, accommodate employers who, as a result of the corona crisis, are facing acute problems in paying their pension contributions. However, the legal rules regarding the period for payment of pension contributions have not (yet) been eased. As a consequence, options for pension providers to grant extensions of pension contribution payments are limited.

The Dutch Pensions Act (Article 26) states that the pension contributions (both those of the employer and of the employee) needs to be paid within two months after the end of the month for which the contribution is set. Where there is a quarterly payment in place, the contribution needs to be settled at the latest within one month after the end of the quarter. And where there is an annual contribution that is estimated at the start of the year, every quarter one fourth of this contribution must be paid. The total annual contribution must be received no later than six months after the end of the calendar year.

A pension fund is subject to reporting requirements when there are contribution arrears, but only when this amounts to 5% of the total annual contributions to have been received by the pension fund. And even then, reporting requirements only happen when the pension fund does not meet the statutory minimum capital requirements and there is a shortfall in coverage. Most pension funds are currently experiencing a shortfall in coverage, therefore any contribution arrears will quickly trigger requirements to report to

beneficiaries (either direct either indirect by reporting to representatives).

Insurers and PPIs must, by virtue of the law, make demonstrable efforts to collect contributions. The underlying rationale is that insurers and PPIs (unlike pension funds) can terminate the implementation of the pension scheme in the case of contribution arrears. It is the case that in these instances the insurer or PPI has to have actively attempted to obtain the contributions (which is at odds with any leniency towards contribution collection) and the participants and employer first has to be informed about the contribution arrears and thus have been given the opportunity to clear any open contribution debt. The insurer or PPI can terminate the scheme only three months after the notification of contribution arrears (and only if by then payment has not been received). However, then the insurer or PPI can do so retroactively up until five months prior to the notification of the contribution arrears.

Forbearance regarding the collection of pension contributions can therefore present a risk to the pension providers and in practice it is used on a very limited basis. In cases where forbearance is being shown, a choice is made for one of the following concessions towards the employers:

- A payment scheme is agreed upon with individual employers who suffer acute financial difficulties and have reported this to the pension fund, insurer, or PPI. A pension fund can only do this, however, if doing so the interests of third parties (for example affiliated employers) are not harmed;
- In certain sectors an extension of the payment period is granted, but then only when these extended payment periods fit within the legal framework;

 A more forbearing approach is taken to the collection of contributions, for example, by postponing handing over the case to a debt collection agency or by neglecting to impose fines or secure the payment of interest.

# 4. Appeal on Reservation of Payment

The Pensions Act allows the employer to include a payment reservation in the pensions agreement and implementing agreement. When this is the case, this extends exclusively to the opportunity to lower or discontinue the employer's contribution if there is "a significant change circumstances". This also covers financial insolvency of the employer in the case of force majeure, which for some employers will certainly be the case right now. Outside of the cases in which an employer can successfully invoke his right to the payment reservation, the employer remains fully liable for the contribution payment. This is only not the case when payment of the contributions by employers would be in breach of the principles of reasonableness and fairness. Generally, it is the case that this is too high of a threshold, especially when the duty to continue to accrue pensions remains with the pension provider.

# 5. Temporary Amendment of the Pension Plan

An employer could decide (with the consent of the works council) to — temporarily — cut back or pause the pension scheme. Of course, the rules for amending the pension scheme are then to be followed and the amendment is only to have consequences for the future pension accrual and future

pension contributions. This therefore does not create a solution for outstanding unpaid pension contributions.

# 6. Temporary Emergency Measure Bridging for Employment Retention (NOW)

In response to the negative financial impact of the coronavirus on employers, in March 2020 the Dutch government decided to issue a temporary emergency measure aimed at retaining employment. This emergency measure, which grants a subsidy as a concession in the labour costs of employers confronted with a revenue decline of at least 20%, has since been extended. Part of the subsidy is a set surcharge (of initially 30% and now 40%) for the additional burden and costs. amongst them the pension contributions. It is very much unclear whether the set surcharge is enough for complete covering of the pension contributions, when with this surcharge other contributions such as the health insurance premium and holiday pay need to be paid as well.

# 7. Taking Over of Pension Contributions by The Dutch Unemployment Benefits Agency

After the bankruptcy of an employer, who have been made employees redundant have the opportunity to, on the grounds of Article 61 and 64 subclause 1 under c of the Unemployment Act (WW), ask the UWV (the Dutch unemployment benefits agency) to take over contribution other still arrears and outstanding dues they have towards the pension provider. The pension provider independently do this. employees can potentially authorize the pension provider to arrange this on their behalf. This is about the still unpaid contributions and fees which the employer by virtue of the employment contract still owed over at most the year directly preceding the dismissal of the employee. However, there must be a monetary disadvantage for the employee for this to be possible. On the basis of jurisprudence it has been decided that — despite the guiding principle for pension funds of 'no contributions, but one will retain rights' even when the employer leaves the pension contributions to the pension fund is still a unpaid, there monetary disadvantage to the employee. Nevertheless, the UWV will have to test whether the employee that knew the employer failed to pay the pension contributions, took adequate and timely action against the employer to make the employer pay their arrears.

#### Conclusion

Netherlands has no specific arrangement for meeting employers who, as a result of the pandemic, have run into financial difficulties paying their pension costs. The statutory rules regarding the meeting of financial pension obligations have not been expanded. The pension providers somewhat try to meet the employers but have limited abilities to do so. The only corona-specific help offered is a surcharge that is a part of the NOWsubsidy, but this does not include a guaranteed coverage of the pension costs. Furthermore, strict rules apply employers hoping to obtain a NOWsubsidy, and this will therefore not be a solution to all employers.

#### **COVID-19 and Pension Funds in Zimbabwe**

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#### **Zimbabwe**



#### Introduction

The impact of COVID-19 (coronavirus) and the measures taken to contain it have been swift and severe. This heightens the need for the pensions industry to understand the possible impacts that the various measures taken by government may have on the funds especially the ability of the funds to meet members' reasonable expectations. There are a whole range of issues that trustees of pension funds, employers and administrators are facing as a result of COVID-19.

Pension assets can take an immediate hit due to high investment exposure in equity and properties and the economic downturn. The resulting monetary policy statement by the Reserve Bank of Zimbabwe on the 27th of March 2020, Statutory Instrument 85 of 2020 permitting businesses to trade in United States dollars (using free funds); Statutory Instrument 96 of 20201 (Deferral of Rent & Mortgage Payments during National Lockdown); Statutory Instrument 91 of 2020 (gazetted on 17<sup>th</sup> April 2020) Pension and Provident **Funds** 

(Amendment) Regulations and **Statutory Instrument 108 of 2020** National Social Security Authority (Pensions and other Benefits Scheme) (Rates of Benefits) (Amendment)<sup>2</sup> published on the 15<sup>th</sup> of May 2020 further enhances uncertainty in an already difficult pensions industry.

#### 1. Advice and Governance

The Insurance and Pensions Commission (IPEC) which regulates the insurance and pensions industry in Zimbabwe has not issued guidelines on how to deal with some of the more immediate issues arising from COVID-19. Meanwhile, the trustees of registered funds who are responsible for directing, controlling and supervising the operations of pension funds<sup>3</sup> are expected to ensure continued compliance with the law and the rules of funds. Trustees are thus obliged keep abreast developments in the legal and socioeconomic environment that are happening in response to the COVID pandemic and their strategies revise and policies appropriately.

Presidential Powers (Temporary Measures) (Deferral of Rent & Mortgage Payments during National Lockdown) Regulations, 2020.

SI 108 2020 National Social Security Authority (Pensions and Other Benefits Scheme) (Rates of Benefits) (Amendment) Notice 2020 (No. 27).

<sup>&</sup>lt;sup>3</sup> SI 180 OF 2017 Pension and Provident Funds (Amendment) Regulations 2017, (No. 24).

In the exercise of their duties during COVID-19 times, trustees are still expected to exercise due care, diligence and reasonable care towards the interests of the funds. In view of the restriction on movement trustees should devise measures that ensure that they continue to exercise adequate oversight over pension in particular making use of funds. information technology to conduct meetings and discuss matters to do with the fund and its administration.

Over the next couple of weeks (and or months) government measures in response to COVID-19 and any directives by the Regulator IPEC are going to have short- and long-term effects on pension funds and trustees should consider specialist advice on all such measures taken.

#### 2. Investments

The preparation and maintenance of the Investment Policy Statement (IPS) is one of the most critical functions for a pension fund as it establishes the formulation of investment strategy that will be adopted by pension funds<sup>4</sup>. Administering a fund in these COVID-19 times requires the formulation on an investment policy to further the objectives and purpose of the fund. This entails the following

- Reviewing investment governance structures to ensure pension funds continue to function and make decisions in light of the government imposed lockdown or restrictions on movements.
- Urgently review any previously agreed investment and risk management decisions due to be implemented in the

- future. This is to ensure they remain appropriate, efficient and do not introduce risks or crystallise losses.
- Review, the Investment **Policy** Statement taking appropriate considerations of COVID-19 on the sustainable long-term performance of a fund's assets. The recent regulations on rental and mortgage deferral have both a short-term and long-term effect on the performance of property investments. These regulations immediately erode the income and liquidity of Pension Funds.

#### 3. Employer Contributions

This is an extremely difficult time for many businesses, with significant uncertainty around trading continuity, staffing, and the longer-term implications for a number of sectors. Funds require payment of contributions from participating employers and these may be delayed or disrupted. The recently gazetted SI 108 of 2020 dealing with the NSSA rates of benefits also has far reaching impacts on funds and benefits thereto. Section 3 of SI108 of 2020 amends the rate of contributions and increases it from 31/2 to 41/2 effective January 2020.

The NSSA amendment has a negative effect on pension fund contributions as employers may be forced to revise downwards the contribution rates to private occupational funds in order to manage expenses associated with providina pension to their employees. This will result in reduced benefits since most Pension funds in Zimbabwe are Defined Contribution Funds where the benefit to be paid at retirement depends on the amount

<sup>&</sup>lt;sup>4</sup> Section 6 E (1) (f) of SI 80 of 2017

that the member accumulates through the periodic contributions made to the fund and return earned from their investment. An increase in the rate of contributions in the compulsory statutory NSSA pension scheme will not necessarily translate in a similar increase of contributions by employers to the private occupational pension funds. Thus employees will have reduced benefits accruing from the funds. However while this may the desired route of employers any such reduction of benefits would ordinarily require the amendment of fund rules. Section 8 of the Pension and Provident Funds Act provides that fund rules can only be amended with the approval of the regulator. Thus any decision taken by employers cannot be effected without approval of amendment of fund rules.

Thus employers have a contractual and statutory duty (NSSA) to pay contributions and a failure to pay result in penalties against employers. Employers through difficult challenges are likely to prioritise contributions to the compulsory NSSA pensions system as opposed to the contributions to pension funds. COVID-19 pandemic and subsequently the lockdown have affected and disrupted the employer-employee relationship resultantly contributions to pension funds might be delayed or disrupted and resultantly lead to increased contribution arrears. Trustees of funds have a duty to act in the interests of funds at any given time and this includes ensuring that members do not lose benefits as a result of changes in the operating environment

# 4. Pension Fund Administration

COVID-19 is placing huge additional pressures on the administration of pension schemes. With many fundamentals of business operations changing in a dramatic and unpredictable way, forecasting will be difficult. SI 91 of 2020 (Pension and Provident Funds) Regulations 2020 amends Statutory Instrument 80 of 2017 (Pension and Provident Funds) Regulations 2017. The 2020 regulations have the effect of introducing new provisions in the administration of pension funds particularly the conduct of business by fund administrators. While the new regulations may have come during the pandemic mischief behind the regulations cannot be faulted. The regulations effectively deal with governance and regulation of fund administrators. As fund administrators are responsible for managing funds their regulation is critical to ensure proper fund administration. Trustees of funds have to ensure that the fund administrators they engage comply with section 6 and 7 of the Pension and Provident Fund Regulations 2020 to avoid any sanctions from IPEC. Trustees and administrators should also ensure they focus their activities on the key risks to pension savers:

- benefits need to be paid timeously
- processing of bereavement services
- employers need to continue contributing.

Trustees should have appropriate monitoring and contingency plans in place and be alive to risks pension funds are facing. The trustees of all pension funds should work closely with their service providers, administrators, employers and

# PENSION LAWYER

IPEC to ensure that their pension funds continue to be administered on a timely basis. The effects of COVID-19 will continue for years and funds need to continue to be alive to the challenges that lie ahead.

# Retirement Funds and COVID-19: Options for Payment of Contributions in South Africa



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**South Africa** 

#### Introduction

When employers or employees financially distressed there are a number of options that may be considered in the South African pension environment in respect of contributions to pension funds ("funds"). I have not set down all the options, just those that seem to have been more prevalently considered to date. In what follows you will see a reference to fund rules, which are the constitution of a fund. What a fund can and cannot do is set out in its rules, which are required in terms of the Pension Funds Act ("the Act"), to be approved by the regulatory authority which is the Financial Sector Conduct Authority ("FSCA").

#### Liability for contributions

Contributions to funds are dealt with in section 13A of the Act which requires an employer to pay any contributions which, in terms of the rules of the fund, must be deducted from the employee's remuneration, and any contribution for which the employer is liable in terms of the fund's rules. Fund contributions must be paid by no later than seven days after the

end of the month for which the contributions are due.

It is important to note that non-compliance with this section by any person, including employers and directors, is a criminal offence that could give rise to a fine (up to R10 million) and/or imprisonment on conviction. Every director of a company 'who is regularly involved in the management of the company's overall financial affairs' will be personally liable for the company's payment of contributions and compliance with section 13A.

Thus, careful consideration needs to be given to altering the payment of fund contributions to avoid criminal liability or contravention of the Act.

The FSCA has stated that it will take action against funds that allow employers to suspend or reduce contributions where the fund's rules do not permit it.

Note: any contributions that have been actually deducted by an employer from remuneration must be paid over to the fund. If not paid the member is effectively being defrauded, which is a criminal offence.

### Employment terms and conditions

The relationship between a fund and its members is separate to the relationship between employers and their employees. Each relationship is governed by different rules and relevant laws. When deciding on what options to choose as regards the suspension or reduction of contributions it is important not just to deal with the fund issues but also to check the employment terms and conditions that exist between the employers and its employees regarding employee benefits. This may also include checking relevant collective bargaining agreements. Changing contributions could amount to a change to terms and conditions and may require engagement within bargaining structures or even agreement from the employees themselves. In additions, it is important to note that employers owe employees a duty of good faith, which gives rise, among other things, to requirements to communicate or consult with employees.

Terms and conditions of employment may include the provision of employer-owned insured risk benefits (e.g. employer owned disability policies). As those are not fund benefits they are not the responsibility of fund trustees, nor can the premiums for these therefore be funded by a fund. Employers should consider an alternative means of funding these policies, or discuss an alternative arrangement with insurers.

#### Continuing as is

The most desirable option, from simply a retirement funding point of view, is to continue to make contributions to the fund at the same rate as previously. I have not dealt with this option as nothing needs to be

done in this situation, except perhaps communication to allay members' fears.

## Paying risk premiums and fund costs

It is also desirable, especially during the pandemic, that insured risk benefit premiums for fund benefits and fund expenses are paid. The FSCA have also stated as much. If an employer cannot fund these costs, then the fund can consider amending the fund rules to allow for these costs and premiums to be paid from the members' retirement savings or from the assets of a fund (if the rules do not already allow for this). However, it may be that this is not an option, depending on the level of of employers financial distress employees and as a result insured risk benefits may fall away, if not paid.

## The meaning of the words "suspension" and "reduction"

When the words "suspension" or "reduction" are used in the context of COVID-19 and contributions to funds, they mean different things to different people. The way that I have used the words in this article is:

**Suspension** – means a total suspension of all contributions to the fund for a period. No contributions are made to the fund, not even for fund costs or insured risk premiums.

**Reduction** – means that some contributions are being paid to the fund, at whatever level is agreed by the fund board for an agreed period, but that level of contribution is less than the contributions that were previously contributed to the fund.

#### 1. Options to Consider

#### **Options include:**

Option 1: suspend contributions to the fund altogether for a period

Option 2: make reduced contributions to the fund for a period

Option 3: reduce pensionable salary for a period (which has the effect of reducing contributions).

# Option 1: suspend contributions to the fund altogether for a period

This option assumes that the employer no longer pays any contributions whatsoever to the fund. Thus, there will be no allocation to retirement funding during the period of suspension. This may mean that:

- (a) Insured risk benefit premiums and fund expenses are no longer paid; or
- (b) That risk benefits and fund expenses (and anything else required to be deducted

Contributions	Continue as is	Suspension	Reduction
Risk premiums paid from contributions	Yes	No	Maybe
Fund costs paid from contributions	Yes	No	Maybe
Retirement funding from contributions	Yes	No	Maybe

from contributions) are paid for from an alternative source by the fund, for example by reduction of members' retirement savings or fund assets.

(a) Insured risk benefit premiums and fund expenses are no longer funded from contributions

If insured risk premiums are not paid then the cover for the insured risk benefits, such as the insured portion of death and disability benefits (and any other risk benefits), as provided by the fund, will fall away.

It is common for employer-owned risk policies (for example disability policies) to be funded from the contributions made to the fund. In this situation, the fund is a conduit for payment of those premiums. If contributions are suspended, and thus the premiums for employer-owned risk policy are not made through the fund, the cover for those employer-owned risk policies will cease. Boards need to ensure that employers are aware of this if contributions are suspended.

Fund expenses such as administration fees, consultants fees, board expenses, etc may be also be paid through deductions from contributions. If contributions are ceased, the payment for these will have to still to be paid and, because they are expenses which generally it is the fund's responsibility to pay, the expenses may need to be funded from members' retirement savings or fund assets. If the fund rules do not enable this then they will need to be amended.

This bring us to (b): that risk benefits and fund expenses are paid for from an alternative source by the fund, for example from members' retirement savings or from fund assets

Many fund rules already allow (particularly in the absence from service rules) for the option of risk benefit premiums payable by the fund and fund costs and expenses (for example administration and consulting fees) to be paid from members' retirement savings or fund assets where there are no contributions being made to the fund.

A question arises as to whether, notwithstanding the rules (which may not contravene the law) this would constitute a contravention of section 37A of the Act, which prohibits the reduction of a benefit or a right to a benefit. I do not believe so, either with respect to risk premiums or fund costs.

The reason for this is that a member's individual account is determined in terms of the formula in section 14B of the Act as MC+EC-X+IC+OC. That is, in summary, member's contributions (MC) employer's contributions (EC) minus reasonable expenses as the board determines (X) plus commencing or conversion amounts (IC) plus other amounts lawfully permitted, credited to or debited from the individual account (OC). Thus, the calculation already allows for expenses and permissible debits. (Defined benefit categories have similar allowance.)

Section 37D of the Act, which sets out certain permissible deductions from members' retirement savings does not prohibit deductions which are not listed as permissible; rather, it simply permits the specific deductions (OC in the above formula) and in any event does not prohibit the so-called deductions in question. Thus, section 37D is irrelevant to the question.

As stated above, funding risk benefit premiums payable by the fund and fund costs from members' retirement savings or fund assets may only be implemented if the rules allow for it.

Although fund rules may allow for the reduction or suspension of contributions in individual member cases (for example absence from service rules), it is my view that if reduction or suspension of contributions is sought (related to COVID-

19) that this may be better achieved by way of a general rule amendment.

# Multi-employer funds (called "umbrella funds" in South Africa) with special rules:

Umbrella funds (funds that have multiple, unrelated employers participating in the fund) generally speaking have general rules (those rules which apply to all employers) and special rules (those rules that apply only to a particular employer participating in the umbrella fund). In my view, it is sufficient to amend the general rules to provide adequately for the suspension or reduction of contributions. The FSCA has a different view and has sought to require that the special rules also be amended (in addition to general rules).

### "Repayment" of suspended contributions

Some rules specifically provide that any contributions that are suspended must be paid over after a specified period (set out in the rules or agreed between the board and the fund) after the suspension. Funds should be careful with this type of rule and should retain enough flexibility to respond to the employer's and employees' financial position.

## Option 2: make reduced contributions to the fund

In this option, reduced ongoing contributions are made to the fund (member, employer, either or both) for a period.

Usually the level of the reduced contributions that is chosen is chosen specifically in order to be able to continue the funding of insured risk benefits and fund expenses. But for this option, what is stated under Option 1 applies similarly.

# Option 3: changes to pensionable salary

This option would involve reducing how much is contributed to the fund by:

- Reducing remuneration and thus pensionable salary;
- Reducing what makes up pensionable salary so that more remuneration is left out of the definition;
- Reducing the percentage of pensionable salary that is contributed to the fund.

Theoretically speaking, anything between zero per cent and 100 per cent of pensionable salary could be what is required to be contributed to the fund for a period agreed between the employer and the fund, thus allowing for the suspension of contributions or the payment of a much lower contribution to the fund. The much lower contribution to the fund could be set at a rate whereby overall contributions still for certain deductions contributions like risk benefits premiums and fund expenses (please see the discussion relating to this above in option 1). If the pensionable salary is reduced to zero then the rules should provide that fund costs and insured fund risk benefit premiums payable by the fund be deducted from the retirement savings of members or fund assets.

Most rules will allow the employer to change pensionable salary on notice to the fund.

## What has the FSCA said in Communications?

Amongst other COVID-19 related documents, the FSCA has issued Communication 11 of 2020 (Retirement Funds) on the 26th of March 2020 which is headed COVID-19: section 13A of the Act

and financially distressed employers and employees — submission of urgent rule amendments. The FSCA's Communication applies to pension and provident funds (as defined in the Income Tax Act). I have not set out the contents of that whole Communication in this article, but the points below should be noted as relevant to that Communication.

- Funds need a formal request from the employer as regards the suspension or reduction of contributions. Retain the request by the employer;
- The fund and the employer would need to agree the date from which the rules will be applied. It is preferable that this is set down in writing. This is an important decision to be made by the fund (where the rules allow for a decision or discretion to be applied) and the fund must ensure the decision is recorded in a resolution:
- The fund must engage with the employer. Retain correspondence and other evidence around the fund's engagement with the employer; and
- It is important that, where possible, premiums for risk benefits continue to be paid. Thus, the FSCA has stated that funds "must attempt to ensure that full risk benefit premiums continue to be paid in full in respect of the affected employees/members in order to ensure that the fund risk benefits will continue to be provided".

#### **Administration requirements**

The FSCA require that funds keep a proper record of affected members of the fund, which they will be required to produce upon request by the FSCA.

In my view, funds should note this to their administrators and request these reports so that they can see them for themselves.

#### **Communication requirements**

The FSCA requires funds to inform affected members of the employer's request to reduce or suspend contributions and of the attendant proposed rule amendments within 30 days of receipt of the request or a decision. Thirty days from the request and 30 days from the decision by the fund may be two different dates, thus, in my view, to be safe it is probably better to apply the earlier date when counting down your 30 days.

Note: as the employer also has a duty to communicate with its employees, communication to members/employees requires co-ordination between the fund and the employer. This includes any option forms that may be provided to members with regard to contribution options.

#### Accessing retirement benefits as a form of relieving COVID-19 related financial distress of employers and employees

Retirement fund benefits in South Africa (depending on the retirement vehicle) will generally only permit access to benefit on specific events, such as termination of employment, death, disability retirement. Thus, unless there is such an event members of retirement funds may not access their benefit. For example, if the member is "laid-off" that is, he or she is still employment but not receivina remuneration, such a member is not entitled to access his retirement benefits.

Thus there have been numerous calls to Government to consider different ways of accessing retirement benefits in different retirement vehicles as well as to alleviate taxation on benefits. Most of the mechanisms that have been proposed to allow access to benefits would require legislative amendment. At this stage (and at time of writing this article) Government has not responded formally to the proposals and legislation has not been amended.

As regards ways that retirement savings may be accessed that are already permitted in legislation, these are very limited. They currently include:

- fund loans to employers (which must always be in the best interests of the fund) up to 5% of fund assets (and up to 10% on application to the FSCA); and
- any positive balances in an employer surplus account (in the fund) being used to fund an employer contribution holiday or in limited circumstances (and subject to onerous conditions) being used to avoid retrenchments.

The Act does not permit a fund to make a loan to a member who is financially distressed. The only type of loan permitted to be made to a member is for housing purposes (e.g. to finance a house). Nor is it permissible, in terms of the Income tax Act, for a partial distribution of an accrued benefit to be made to a member from an occupational fund on grounds of the financial distress of a member.

We await further information from Government as regards access to retirement benefits and other COVID-19 relief proposals as they relate to retirement funds, but this is a highly emotional and complex subject and South Africa's circumstances are different to many other countries.

# Sustainable Investing of U.S. Retirement Assets

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#### Introduction

Increasingly, the globe across considerations of sustainability have become an important topic for retirement funds and risk management. Countries diverge considerably in their regulatory boards approaches when plan committees use sustainability factors to make investment-related decisions regarding retirement assets. The United States (U.S.) regulatory approach has long caused fiduciaries, especially fiduciaries for private-sector plans, to be wary of incorporating sustainability considerations into their decision-making. In June 2020, the Department of Labor (DOL) proposed a regulation that is likely to further chill fiduciaries from following the international trend of increasing the attention they pay to sustainability factors.1

# 1. U.S. Retirement Fund Categories

In order to understand the regulatory implications for sustainability consideration,

it is necessary to differentiate among four categories of U.S. retirement funds. The first category is public plans, which hold \$8.8 trillion.<sup>2</sup> Private-sector DC plans hold \$6.8 trillion. Private-sector DB plans hold \$3.4 trillion. Individual Retirement Accounts (IRAs) hold the largest proportion of assets at \$11.0 trillion.

#### 2. U.S. Regulation

It is easiest to describe the fiduciary regulation of decision making in IRAs typically there isn't any relevant regulation. Individual account holders have decisionmaking power over their account assets. A few constraints on available investments exist (for example an account holder cannot purchase the home she lives in and hold it as an asset within an IRA). As a general matter though, an account holder may invest in sustainable investments, even if those investments are not designed to maximize the financial return for a given level of risk. The situation becomes slightly more complex if the account holder appoints a fiduciary with discretionary asset

Company Institutes' fourth quarter report. https://www.ici.org/research/stats/retirement/ret\_ 19\_q4. In addition, \$2.3 trillion is held in annuity reserves.

Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 39113 (proposed June 30, 2020) (to be codified at 29 CFR Part 2550).

All asset amounts are approximate, as of December 31, 2019, and are from the Investment

management authority or receives advice from a fiduciary investment adviser. Even in those situations, though, it is possible for an IRA account holder committed to sustainability to ensure that is part of the decision-making process.

All retirement plans sponsored by privatesector employers are governed by the Employee Retirement Income Security Act of 1974 (ERISA). ERISA imposes the fiduciary duties of loyalty, prudence, and diversification. Courts frequently have looked to traditional trust law to define those duties. Decisions to invest DB plan assets are fiduciary decisions.3 In most U.S. DC plans, the members either explicitly select their individual investments from a menu of options or if they fail to do so then their assets are invested in a diversified fund (default funds). It now is well established that the selection of menu options and default funds are fiduciary decisions.

Prior to the June 2020 proposed regulations, guidance on the consideration of non-financial criteria when making investment decisions for DB plans primarily was found in Department of Labor (DOL) advisory opinions, information letters, and interpretative bulletins; there are few court decisions that directly address the question. Early guidance permitted limited use of some non-financial criteria such as

preferences for union-based investments.<sup>4</sup> Between 1994 and 2018, the DOL issued four bulletins on the use of non-financial criteria in retirement plans. The underlying question in each was the extent to which taking such factors into account can be reconciled with ERISA's fiduciary obligation of loyalty.

Each bulletin used slightly different language, and at least purports to clarify or rescind prior guidance.5 Although the bulletins may have varied in their signaling, the guidance consistently has allowed ERISA fiduciaries to consider non-financial factors when evaluating the risk and return profile of investments only so long as the fiduciary's goal is to maximize the economic interests of plan participants and beneficiaries. Until 2018, the guidance consistently permitted fiduciaries to take into account non-financial benefits to third parties as a "tiebreaker" if two investments have identical risk and return profiles. Guidance provided in 2018 signaled a more hostile attitude to non-financial considerations, stating, among other language: "Fiduciaries must not too readily treat ESG [Environmental, Social, & Governancel factors as economically relevant to the particular investment choices at issue when making a decision." Two prominent U.S. law scholars have argued that even using non-financial

For simplicity this article only discusses investment decisions. Similar legal principles apply to shareholder engagement including proxy voting. "unduly discouraged fiduciaries from considering ETI[]... factors."); DOL Interp. Bull 08-1, 73 Fed. Reg. 61,734, 61,735 (2008) (superseding the 1994 guidance and advising fiduciaries they should consider ETI factors only "in very limited circumstances"); DOL Interp. Bull. 94-91, 59 Fed. Reg. 32,606, 32,606 (1994) (stating that a fiduciary may consider economic benefits to third parties as part of its investment decision-making process).

DOL Info. Ltr. From Robert Doyle to James S. Ray, Wash. Serv. Bureau No. DLO0135 (July 8, 1988).

DOL FAB 2018–01, at 2 (reminding that "[f]iduciaries must not too readily treat ESG factors as economically relevant."); DOL Interp. Bull 15-01, 80 Fed. Reg. 65,135, 65,136 (2015) (revoking the 2008 guidance, which it said

considerations as a tiebreaker violates traditional trust law.<sup>6</sup> In 2019, President Trump required the DOL to investigate whether trends in retirement plan investments' damaged the U.S. coal, oil, and natural gas industries, signaling a potential increase in hostility to private-sector pension plans taking into account sustainability factors.

The regulation proposed in June 2020 reiterates the DOL's commitment to the maximization of plan participants' beneficiaries' financial interests. indicates that this time the Department really means it. The preamble discusses the general trend to increased use of ESGoriented investments and states that "ESG investing raises heightened under ERISA." The proposed regulation requires that fiduciaries make investment decisions "based solely on pecuniary factors that have a material effect on the return and risk of an investment..." The proposed regulation's explanation of pecuniary factors explicitly refers to ESG factors saying: "[ESG], ... are pecuniary factors only if they present economic risks or opportunities that qualified investment professionals would treat as material economic considerations under generally accepted investment theories." It adds an additional burden on fiduciaries considering ESG and similar factors, even when they are financially material, to compare the investments with other alternative investments. If ESG investments are economically equivalent, the regulation calls for the fiduciary to document why it selected a particular equivalent investment based on "the purposes of the plan,

diversification of investments, and the interests of plan participants and beneficiaries in receiving benefits from the plan."<sup>7</sup>

The June 2020 proposed regulation also addresses the selection of ESG-oriented investments for investment menus in participant-directed DC plans, such as 401(k) plans. An ESG-oriented investment is not permitted to be any part of a plan's safe harbor default fund (a QDIA). **Fiduciaries** may add **ESG-oriented** investments to a plan's menu of investment options, but must use only "objective riskcriteria" return when choosing monitoring the investment options, and application of the decision criteria must be documented.

ERISA does not apply to public sector retirement plans. Instead, each state develops its own regulation governing plans and the federal government separately regulates federal plans. All have some version of fiduciary obligation. When questions occur about the scope of fiduciary duty, courts typically look to the interpretations applied to ERISA plans for quidance.

#### 3. Data on the Use of Sustainability Criteria

Estimates vary widely on the number of private sector DB and DC plans that incorporate ESG factors into their investment decision making. A 2018 report by the Government Accountability Office (the GAO) gathered data on DC plans from a number of surveys. The two reports

Schanzenbach, M. & R. Sitkoff, 'Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee,' (2020) 72 Stan. L. Rev. 381-453.

Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 39,113, 39,115, 39,127 (proposed June 20, 2020) (to be codified at 29 CFR Part 2550).

covered 600 and 1900 DC plans and estimated respectively that about 2% and 8% offer an ESG investment option that in some way may prioritize non-financial goals.

In order to estimate consideration of ESG factors by DB plans, the GAO interviewed asset managers. According to those asset managers few private-sector DB plans incorporate ESG factors at all. Those interviews as well as interviews directly with public plans indicated that public DB plans were more likely to look to ESG factors when making investment management decisions.

At a general level, the GAO data aligns with Callan's 2019 ESG survey. That had a small number of responses (89 participants of which 36% had under \$500 million in assets). According to that survey the proportion of public funds that incorporate ESG criteria has increased significantly since 2013 to 49%. The report did not separately break-out data for private-sector DB plans. However, looking at all DB plans, 35% used ESG factors. Clearly, that average means that private-sector plan usage is significantly less than 35%. The DC plan data's sample size of 11 plans limits the reliability of that sample. As a signal of the low levels of engagement by private-sector plans in sustainability, the Bloomberg LP Retirement Plans are the plans sponsored by for-profit employers that have signed the United **Nations Principles** for Responsible Investments. Michael Bloomberg, the founder of Bloomberg LP, has been active on environmental issues in many ways including as Chair of the Task Force on Climate-related Financial Disclosures.

One of the reasons cited by asset managers interviewed by the GAO to explain the low levels of incorporation of ESG factors in investment decision-making by retirement plans was regulatory uncertainty. Some of the asset managers believed the changes in the various DOL bulletins were substantive enough to raise concerns about the scope of fiduciary duties and the future reliability of the guidance. It is understandable, given the frequency of litigation in private-sector retirement plans, that plan fiduciaries might be reluctant to venture into uncertain investment territory, particularly as first or early movers.

The proposed regulation, if finalized, will increase the reliability of the guidance, but not in a way that is likely to encourage fiduciaries to increase their consideration of ESG-oriented investing until there is more clarity on the materiality of ESG factors and agreement on their use in a strict risk-return analysis.

# 4. Examples of the Use of Sustainability Criteria

This article has frequently referred to sustainability criteria rather than ESG or non-financial factors because the article is derived from а presentation sustainability scheduled for 2020 joint conference of IPEBLA and the Pension Lawyers Association of South Africa. The scheduled panelists discussed among ourselves the definition of sustainability, how it is different from ESG, and whether the legal principles differ based on the type of non-financial factor being considered. My personal view is that investors have long considered governance factors, significant research finds those factors linked with risk and performance, and the factors are reasonably well defined. In terms of definition, social factors writ large are at the opposite end of the scale. That is not to say they are unimportant. My particular interest is in environmental factors so the following two examples focus on how plans have operationalized their consideration of those factors.

First, the consideration of ESG factors by public-sector funds has not been without controversy. The California **Public** Employees' Retirement System (CalPERS), the largest public-sector fund in the U.S., has engaged in a variety of ESG activities when investing. In 2018, the fund's board president lost her seat on the board after plan members elected a board candidate who ran on an anti-ESG platform. On the social front, CalPERS decision to divest from tobacco companies reportedly resulted in forfeiting \$3 billion in returns. Critics pointed out that as of March 31, 2017 four of the nine worst performing funds in which it invested were private equity ESG funds. CalPERS responded that those funds held \$600 million of CalPERS \$26.4 billion private-equity investments.

On the other hand, climate change protestors at a CalPERS board meeting in early 2020 demanded divestment of fossil fuel companies. CalPERS has an investment policy statement acknowledging the physical and transition risks of climate change on its investment portfolio. In response to the "die-in" by protestors, CalPERS explained it prefers a strategy of engagement and advocacy with portfolio companies on the issue instead of divestment.

The controversy about CalPERS ESG investing activities has not discouraged all U.S. public plans from developing and executing sustainability strategies. By 2018, the New York State Common Retirement Fund (NYSCF), the third largest in the U.S. had increased its commitment to

address climate risk. One of the "problems" in incorporating ESG factors identified by some public- and private-sector plans is the significant percentage of assets they hold in relatively low-fee index funds. Rather than view passive funds and investing with a concern for climate risk as mutually exclusive, the NYSCF increased its investment in a low-carbon index. The state's Comptroller explained its general approach as one that includes ESG factors as part of its decision making. That contrasts with the use of a screen of the type the CalPERS protestors sought.

#### Conclusion

Unlike a number of other countries, U.S. retirement plans have been slow to incorporate sustainability factors in their investment-related decisions. Investors and investment managers frequently cite the lack of comparable information as a barrier to expanding the criteria they use to evaluate opportunities. U.S. plans, however, have access to the same, admittedly imperfect, information that is used in the rest of the world.

U.S. regulatory action has long seemed to discourage private-sector retirement plans from joining other types of investors in expanding their consideration sustainability risk. The regulatory guidance on the ways in which fiduciaries may fulfil their obligations while considering other than traditional financial factors was neither detailed nor stable. Investment managers report that relatively few DB plans ask that sustainability criteria be used. Surveys indicate that a limited percentage of DC plans offer members an opportunity to choose a targeted ESG fund. New guidance, issued in the form of a proposed regulation, appears intended to chill ESGoriented investing based on the DOL's view that such investments often focus at least in part on social goals and, thus, are incompatible with a strict risk-return analysis.

Some public sector retirement funds have been more aggressive than private plans in incorporating sustainability concerns in some way. The use of screens resulting in divestiture have particularly been controversial. CalPERS has seen strong criticism of past divestment decisions. Yet, climate activists call for divestiture of fossil fuel companies. One open question is why some public sector funds have committed to consideration of sustainability factors when the fiduciary standards for those plans tend to parallel the standards for private-sector plans. Possible explanations include the differences in the basis for claims (state law as compared to ERISA) and the public nature of public plans investment portfolios as compared to the less transparent private plan investments.

# A Comparison of the Regulation of Death Benefits in Occupational Pension Arrangements in South Africa, Germany and France

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#### 1. South Africa

# Occupational pension landscape

In terms of the legislation in South Africa, there is no compulsion on an employer to establish a pension or provident fund or participate in such a fund. However, once the employer decides to participate in such a fund, then in terms of the tax and other legislation, it is obligatory for such a fund to provide death benefits as one of its core benefits.

Private pension and provident funds as well as those of para-statals such as Telkom and Eskom are currently regulated under the Pension Funds Act 24 of 1956 (the "Act"). This Act also regulates retirement annuity and preservation funds. Since 1976, the payment and distribution of lump

sum death benefits is regulated by section 37C of the Act. However, we also have several government institutions that have separate Acts of Parliament that regulate the provision of pension benefits for their employees. An example of this would be the Government Employees Pension Fund, which covers State employees such as teachers, policemen, nurses, etc. Whilst the State pension funds do not have the exact wording of section 37C, the principles underlying the distribution of benefits in these funds are very similar to section 37C of the Act. Therefore, in South Africa, whether you belong to a private or government-type fund, upon your death, you will be subject to a similar type of legislation.

The employer, in addition to the benefits in the fund or as an alternative, may also provide death benefit cover for its

This paper was to be presented at the Annual Pension Lawyers Conference in Cape Town on

<sup>19</sup> March 2020. However, the conference was cancelled due to the COVID-19 Pandemic.

employees under a self-standing group life insurance policy issued by a long-term insurer. Such policies are regulated under insurance law and the benefits are normally payable to the nominated beneficiaries of the employee.

# Object of the death benefit legislation

Section 37C of the Act removes the member's freedom of testation in respect of death benefits as the benefit is not paid according to the member's nomination or to the estate, where it can be distributed in terms of his/her will. Instead, the benefit must be distributed by the Trustees of the Funds taking into account the needs of all the dependants of the deceased with a strong focus on the financial dependency of such dependants.

The courts, the Pension Funds Adjudicator, and the recently established Financial Services Tribunal, in a series of rulings have consistently held that the section represents a form of social policy, which is to be implemented by the Boards of Management or Trustees of Funds. The aim of this policy, broadly stated, is to ensure that persons who were dependent on the deceased are not left without financial support or become destitute, thereby reducing the liability of the State. This social protection policy, even though paternalistic, is necessary in a developing economy and ensures an equitable distribution of resources.

The current policy objective is clear, but its limited application or reach can be questioned. That is, if this is such an important State policy to be implemented for the social good of the country, then why is it limited to retirement funds only? Put differently, why are other group employment benefits, such as proceeds of

group insurance policies, not subject to such a policy? Whilst accepting that retirement fund contributions enjoy tax concessions and the implementation of the social policy is what the State expects in return, it does raise the question why this policy is only applied to retirement funds and not extended to other financial products?

## Broad definition of a "dependant"

In line with the social policy, it follows that we have a very broad definition of a dependant. It not only covers persons whom the deceased had a legal duty to maintain, but also non-legal dependants and so called future dependants. Non-legal dependants cover a range of persons including life permanent partners, financially independent adult children and de facto dependants (persons that the deceased had no duty in law to maintain but who he/she nevertheless in fact maintained such persons). Future dependants, refer to a person, in respect of whom the member, as at date of death, had no duty in law to maintain but would have become legally liable to maintain, had the member notionally been alive as at the date a decision is made by the fund. It potentially covers parents or engaged couples or parties intending to marry etc.

#### Onerous duty on funds

In light of the broad definition of a dependant, who is required to find all of these persons? The tracing of dependants in a retirement fund, unlike in an insurance policy context (which by and large allows for payment to the nominated beneficiaries) is an arduous responsibility. Whilst there is no problem for the insurer to find and locate the nominated beneficiaries of an

insurance policy, however, in a pension fund context, there is a very onerous duty on the boards of funds to trace and locate dependants of the deceased. This requires funds to conduct in-depth investigations to find the circle of beneficiaries.

Our courts and the Adjudicator have consistently held that there is no duty on a dependant to come forward and prove that he/she is a dependant. Rather, the duty is squarely on the Board of the Fund to take all the reasonable steps to locate the dependants. The law recognizes this difficult task and hence funds have been given a 12-month period to trace dependants. When dealing with multispouse households, more time may be required to complete the investigation. Whilst other types of products/institutions providing death benefits, for example, funeral policies, can pay the benefit shortly after the death of the member, the onerous duties placed on funds means that they cannot pay shortly after the death of a member.

#### "Equitable distribution"

When distributing the benefit, the law requires the fund to effect an equitable distribution. The legislature does not define this concept nor does it specify what factors the board may or should consider in effecting an equitable distribution. However, the Adjudicator and the courts have consistently held that in exercising an equitable distribution, the Board needs to consider a wide range of factors. The most important of these factors relate to financial dependency and financial need on the part of the beneficiaries. This places a heavy burden on the funds as they are required to obtain financial data of each beneficiary and then analyse that data to determine a reasonable allocation. This entire process

is time-consuming and often leads to unhappiness and bitterness among the surviving beneficiaries.

#### Mode of payment

Regarding minors' benefits, the law grants a discretion to the Board to pay to the guardian/caregiver directly or to fund Beneficiary Fund (a special established to administer death benefits for beneficiaries) or to a Trust in certain circumstances. Another difficult decision funds must make is when to deprive the guardian or caregiver of the right, to administer the benefits on behalf of the minor. The fund is required to consider a number of factors largely based on the premise that financial competency of the guardian leads to monies being utilized in the best interest of minors.

However, one may have guardians, who are very well qualified and experienced in finances, but does that mean they will use the monies in the best interests of the minor children? Moreover, if one examines the various rulings from the Adjudicator, it is clear that this discretion is extremely difficult to exercise and does pose an enormous administrative burden on the board, and even if the discretion is legally correctly exercised, can still lead to the monies not being utilized in the minor's best interest. We currently have the anomalous scenario, where a member on retirement in a pension fund, retirement annuity fund, pension preservation fund (and provident fund with effect from 1 March 2021), cannot take his/her entire benefit in cash, unless it is below a minimum threshold, but the Act permits the entire lump sum death benefit of a minor to be paid to the guardian.

Having regard to the move towards annuitization, it does beg the question as to whether the time has come for the legislation to ensure that all minor death lump sum benefits ought to be paid to a beneficiary fund or a trust arrangement or some other form of instalment basis payment from the fund. This would also be in line with the broader pension reform principles currently advanced and must be in the best interests of minor children.

#### Dispute resolution

If a beneficiary is unhappy with a decision of a private fund, in terms of our law, he/she may either bring a complaint before the Adjudicator (or the Public Protector for State Funds), or bring an action in a civil court. The beneficiary is not obliged to lodge the claim in either of the forums. Where the beneficiary choses to lodge a complaint with the Adjudicator/Public Protector, unlike going to a civil court, it is a free service and does not necessarily require an attorney. The process is meant to be informal and speedy. Where a party is unhappy with the decision of the Adjudicator, he/she can also lodge a review application with the recently established Financial Services Tribunal, which is also a free service and there is no need for legal representation.

In death benefit distributions, there is a potential for a multiplicity of persons to complain. That is, if a person is not considered a dependant, he/she may be aggrieved and can lodge a complaint. If a person is regarded as a dependant but receives a nil benefit, he/she can lodge a complaint. Finally, if that same person receives a portion of the benefit, he/she can still be unhappy as to why others have

received a benefit or why he/she is not entitled to the entire benefit. Therefore, in most death benefit distributions, there is potential for somebody to be aggrieved by the decision. The other problem faced by funds, is that where they have made payment, and the beneficiary subsequently successfully challenges the decision, and the Adjudicator or a court orders the fund to re-distribute the benefit, then the fund may not have adequate resources to give effect to such a payment.

#### Retirement reform

Over the years, there have been ad-hoc changes to the section and never a complete review. From the various discussion papers issued by National Treasury, there is a leaning towards the principle that death benefits should be in the form of income payments. The papers also recognize that the current difficulties facing boards in the distribution and payment process should be removed. However, in light of all the recent changes in the pension landscape, there is now a need for an overhaul of the entire section rather than effecting ad-hoc changes.

#### **Germany**<sup>2</sup>

## Occupational pension landscape

According to the German Occupational Pension Act (*Betriebsrentengesetz, BetrAVG*), there is no statutory compulsion on employers to provide employer-financed occupational pension commitments to their employees.<sup>3</sup> Nor does the statutory law

The German part of this article is based on an article by Marco Maurer that was published in the Labor Law Magazine, Issue No. 01, March 26, 2020, p 17.

<sup>&</sup>lt;sup>3</sup> However, pursuant to Sec. 1a BetrAVG, German employers may be obliged to establish employeefinanced occupational pension arrangements on a deferred compensation basis: Upon the

oblige employers to provide any death benefits in pension schemes thev establish.4 However, the **BetrAVG** recognizes the death of a beneficiary as a qualifying pensionable event and, in practice, many pension schemes in Germany actually provide benefits for surviving dependants in such event.

Different to the situation in South Africa, occupational pension commitments in Germany do not necessarily require the involvement of a pension fund. According to the BetrAVG, employers can either commit themselves to pay direct occupational pension benefits or opt for an indirect way of financing pensions by involving an external pension carrier for this pension fund. purpose, such as а Occupational pensions may also be provided by means of a so-called direct insurance, i.e., the employer enters into a life insurance contract to the benefit of the employee (and its dependants) contributes to this life insurance by paying insurance premiums. Providing occupational pensions in an indirect way does, however, not exempt the employer from being ultimately liable for the fulfillment of the occupational pension obligations (i.e., no "pay and forget"). Apart from one exceptional case — following a recent legislative amendment, the BetrAVG now provides for pure defined contribution schemes on the basis of collective bargaining agreements — the employer always guarantees a minimum benefits amount to the employees and, succession, their surviving dependants.

employee's request, a part of the employee's future salary is to be converted into an occupational pension entitlement. The pension entitlement is also subsidized by the employer, if

# Definition of death benefits and surviving dependants

The statutory law neither specifies the type of benefits that legally qualify as "death benefits", nor does it provide a definition of the term "surviving dependant" (*Hinterbliebener*).

Thus, there is leeway for the employer to define the type of death benefits to be provided to eligible surviving dependants, e.g. annuity payments and/or a one-off payment. To that end, pension schemes often determine death benefit amounts as a certain percentage of the defined old-age benefit amount. However, not every benefit that is triggered by the event of a beneficiary's death does qualify as a death benefit in the sense of the BetrAVG. According to case law of the German Federal **Employment** Court (Bundesarbeitsgericht, death BAG), benefits have to serve the purpose of providing maintenance to the surviving dependants. This precondition is, in particular, not met where benefits merely aim to support dependants during the special situation of the beneficiary's death (e.g., by compensating incurred funeral costs or providing a short-term support).

In the absence of a legal definition of a "surviving dependant", case law developed a broad interpretation for this term: Any person whose provision with maintenance an employee typically has an interest in (typisiertes Versorgungsinteresse) may be considered a surviving dependant by the employer. Besides spouses and children, this interpretation could in particular include

and in the amount, the employer saves social security payments due to the salary conversion.

Such an obligation may exist pursuant to applicable collective bargaining agreements or other collective agreements.

unmarried life partners, same-sex partners, parents, siblings and/or grand-children. The employer is generally free to define the scope of eligible persons among this group of surviving dependants. The decision on who is to be considered an eligible surviving dependant may even be transferred to the employee.

#### Distribution of death benefits

The employer has leeway to define the preconditions of eligibility correspondingly, to limit its own financial risk in connection with the distribution of death benefits. The provisions pension schemes occupational are. however, subject to mandatory including but not limited to the principles of equal treatment pursuant to the German Act on Equal Treatment (Allgemeines Gleichbehandlungsgesetz, AGG). BAG is continuously developing defining the limits to a permissible contractual design of death provisions. The following examples of most recent case law developments on two typical clauses in occupational pension schemes, which both limit a spouse's eligibility for death benefits, may provide a better sense of the legal situation.

#### Late marriage clauses

Occupational pension schemes often define the maximum age an employee may have at the time of his or her wedding as a precondition for the spouse's eligibility for death benefits. The main intention of this so-called *late marriage clause* is to exclude spouses from death benefits if there is a reasonable suspicion that the primary purpose of the marriage was to provide the partner with such benefits.

Due to inconsistent case law in the recent years, there is considerable legal uncertainty regarding the permissibility of late marriage clauses. In 2015, the BAG had to rule on a clause that excluded spouses from death benefits if the employee had been older than 60 years of age at the beginning of the marriage. In this decision, the BAG held that late marriage clauses generally violated the prohibition of old-age discrimination pursuant to the AGG and were, therefore, invalid. Subsequently, the Court of Justice of the European Union (CJEU) decided that the underlying EU directive. which permits age-related differentiations for old-age and disability benefits, also applied to late marriage clauses, provided that these clauses were based on an occupational pension scheme. In consideration of the CJEU's decision, the BAG modified its case law. It now considers the age-related differentiation in a late marriage clause justified if (i) the death benefit amount is determined on the basis of the amount of the company pension scheme's old-age benefit, and (ii) the maximum age specified in the late marriage clause is appropriate and necessary according to the AGG provisions. In the opinion of the BAG, the latter requirement is regularly met if the maximum age corresponds with the structural principles of company pension law, in particular with the age limit for the eligibility for old-age benefits as defined in the underlying occupational pension scheme.

These new principles developed by the *BAG* can form a profound legal basis for including late marriage clauses in future occupational pension schemes. However, further case law is still required to clarify the details of the aforementioned principles.

#### Age gap clauses

There is more consolidated case law with regard to another typical clause in

occupational pension schemes: Spouses are often excluded from death benefits if he or she is a certain number of years younger than the employee. Such so-called age gap clauses mainly serve the employer's legitimate interest in manageable and calculable pension liabilities by excluding marriages from death benefit eligibility which bear a significant risk that a surviving spouse might outlive a former employee by many years. According to recent case law of the BAG, this legitimate interest of the employer generally justifies the age-related differentiation associated with such age gap clauses: Based on the fact that in more than 80 percent of all marriages the age gap of the spouses actually amounts to less than seven years, the BAG considers it permissible to completely exclude from death benefits spouses who are at least 15 years younger than the employee. In another case, the court considered it permissible to reduce the death benefit entitlements of spouses with an age gap of ten or more years on a pro rata basis. However, the court has yet to decide whether a ten-year age gap would also justify a complete exclusion.

Both examples show that there are legal possibilities for employers to define the scope of death benefits in occupational pension schemes and, correspondingly, control the financial risks associated with such commitments. However, it is evident that provisions on the distribution of death benefits always have to consider the current developments in case law in order to be as legally secure as possible.

#### Works council codetermination rights

In the context of the distribution of death benefits, employers in Germany always have to consider that co-determination rights of a competent works council (Betriebsrat) may exist. The employer's general decision whether to establish an occupational pension scheme is not subject to works council's co-determination rights. Also, the employer may define the financial budget of a pension scheme without involving a works council. However, the question how to distribute a defined pension budget among the eligible beneficiaries and their survivors is subject to the competent works council's codetermination. As а result. pension schemes are often implemented by way of a works agreement (Betriebsvereinbarung) between employer and works council.

#### Law enforcement principles

Different to the situation in South Africa, there is no special duty on German employers or external pension carriers to identify, trace and locate any surviving dependants who are eligible for death benefits. According to the general German civil law enforcement principles, it is the burden of each surviving dependant to assert his or her death benefit entitlements and to take any further legal action, if necessary.

However, following the event of a beneficiary's death, the employer and/or any pension carrier involved is obliged by statutory law to provide comprehensive information upon the surviving dependants' request on any accrued death benefit entitlements. Further, the employer or involved pension carriers may be held liable for any culpable non-fulfillment or delayed fulfillment of surviving dependants' death benefit claims. Such liability may, in particular, result in additional damage claims and/or interest on arrears of the surviving dependants.

#### **France**

In France, as in South Africa and Germany, there is no general obligation for employers to set up death benefits for employees. It is nevertheless a widespread practice among employers as a result of collective bargaining agreements, since employers and union representatives regularly enter into negotiations on this subject.

However, unlike their counterparts, French employers are less involved in the distribution of death benefits, as this matter mainly concerns insurance companies: death benefits are mostly provided within the framework of group insurance, where the employer is merely the policyholder.

# The death benefit set up for employees

An employee may be covered by a "prévoyance loured" contract, which includes temporary disability benefits (salary during the sick days), permanent disability benefits and also death benefits.

According to the French law, the setting up of this kind of contract is not mandatory for employers but most collective bargaining agreements implement such benefits (including death benefits) and have the following key features:

For employees with an executive or equivalent status, the November 17, 2017 national collective agreement compels the employer to pay a contribution equivalent to 1,50% of the first wage bracket ("tranche A", from €0 to €3428 in 2020), financed exclusively by the employer. At least 50% of the contribution must cover the risk of death. The remainder is used to cover other risks like temporary or permanent disability. The contribution has to

finance a contract taken out with an insurance company. This national collective agreement applies to a large proportion of employees in France.

 Concurrently, industry-wide agreements often require the employer to put in place coverage for employees against temporary/permanent disability and death, and define the content of the coverage and to which extent the employer will have to fund these benefits. The bargaining agreement often specifies the type of death benefits and may provide a definition of the beneficiaries.

In these contracts, the death benefits could refer to:

- a lump sum (or an annuity) granted to a beneficiary in the event of the employee's death;
- and/or annuity payments:
  - for the employee's children, to either, finance their studies or support them if they have a disability at a determined date,
  - o and/or, for the employee's spouse.

For "prévoyance loured" contracts, the operator is always an insurance company.

Alongside "prévoyance loured" schemes, employers may set up "employee supplementary pension plans" (a defined contribution or defined benefits retirement pension plan). These kind of contracts are relatively rare and usually set up only in large companies.

For employee supplementary pension plans, the operator is an insurance company or an investment management fund. Death benefits (in the narrower sense) are provided only when the supplementary pension plan is taken out

with an insurance company. Indeed, if the supplementary pension plan is subscribed through an investment management fund, the plan is closed upon the death of the employee (who dies before retirement) and the death benefits become part of the estate of the deceased.

In supplementary pension plans managed by an insurance company, the death benefits could refer to:

- a lump sum (or an annuity) granted to a beneficiary if the employee dies before retirement:
- a specific entitlement granted to a beneficiary if the employee dies after retirement, an educational annuity payments, and/or a reversionary pension (survivor's pension for the spouse). The inclusion of these types of death benefits is possible but not mandatory (additional option in the contract).

#### Death benefits distribution

In both cases ("prévoyance loured" or employee supplementary pension plans), the employer is never responsible for the distribution of death benefits. The insurance company is the sole debtor liable for the distribution of the benefits.

The employer has only two prerogatives:

- to take out an insurance contract (it is an obligation if the collective bargaining agreement so provides);
- to pay a certain amount of contributions to finance the contract.

The employer is not required to distribute the death benefits. Furthermore, if the employer were to directly distribute a lump sum to the employee's relatives, it would be considered a "salary", i.e., it would be subject to tax and social contributions. It is why French employers take out insurance contract to cover this risk, especially since there are incentives applied to the contribution.

Consequently, any difficulties related to the enforcement of the contract are borne and settled by the insurance company.

## A very broad definition of the beneficiary

In "prévoyance loured" contracts and "employee supplementary pension plans" taken out with an insurance company, the rules to define the beneficiary are very common regardless of the insurance company:

- the death benefits are excluded from the devolution (division of the estate);
- the employee chooses the beneficiary.
   The employer has no discretion in this respect.
- To choose the beneficiary, insurance contracts offer two possibilities:
  - The employee nominating a beneficiary (a nominee);
  - o If no nomination is completed, a standard nomination clause applies. The contract drafted by the insurance provides company а standard nomination clause. When the employer takes out the contract for the employees, he or she may request to amend the clause provided by default (for example, to include permanent life partners in the nomination standard clause). However, it is very rare in practice.

The nomination form allows the employee to choose one or several persons as beneficiary(ies) (freedom of choice of the

employee). The beneficiary(ies) could be a permanent life partner, financially independent adult children, a fiancé(e), parents, brothers, sisters, a friend, another family member, a lover, a charity, etc.

The standard nomination clause determines a rank for beneficiaries, in the following order: spouse; children; grandparents; etc. The standard nomination clause provides for the designation of contingent beneficiaries if the primary beneficiary died.

# The insurance company must respect the employee's choice

Regardless of whether or not there is a material need for support for a dependant, the insurer must respect the employee's choice and there is thus a primacy of the employee's choice.

The only reservations are:

- illegal nominations in favor of the physician or nurse who provided care during the illness of the insured person whose death occurred, or in favor of guardians or trustees,
- fraudulent (excessive) financial investment in an insurance contract for the sole purpose of disinheriting the heirs. In any case, this is a rather rare situation in group contracts taken out via the employer.

The employee can therefore extensively exercise his/her free will, which is well-preserved (for instance, the courts have held that the beneficiary may be a partner in an adulterous relationship).

The distribution of the death benefits does not have to be equitable. It only needs be in accordance with the choice of the insured person (here, the employee).

## Current challenges facing insurance companies

Although the rules for the determination of the beneficiaries appear clear-cut, the distribution of the death benefits by insurance companies does not always go uncontested, and the handling of funds is not devoid of difficulties.

Those issues relate to the respect of the employee's choice (identification of the "right" beneficiary) and to the unclaimed insurance policies.

#### Respect for the nomination

The current challenges insurance companies face arise when the employee chooses an unexpected beneficiary. For example, he or she chooses a new life partner. The choice of the new stepmother or stepfather could cause bitterness among the employee's children.

However, there is no precondition of eligibility for death benefits, -except in the specific case of the reversionary pension in supplementary pension plans, which is necessarily granted to a spouse or exspouse and distributed according to the duration of the marriage, so the insurance company merely needs to comply with the employee's choice.

In practice, when an employee completes a nomination form (especially if it happens shortly before his/her death), it is therefore necessary to ensure the validity of the signature on the nomination form or to check that the employee is sound of mind (no insanity/mental disorder/diminished capacity, no vitiated or lack of consent, for example due to mental illness or duress).

In order to ensure that the nomination was completed by the employee, insurance companies must scrutinize the nomination form with care and check for the consistency and similarity of the signature.

If the company is aware of a health condition likely to alter the employee's consent, it must take the necessary precautions (for example, request a medical assessment before the courts).

Disputes often arise *after* the insurance company has paid the death benefits to the beneficiary. If necessary, the judge can request a handwriting analysis, or order the production of any other document to ascertain the will of the beneficiary and the absence of vitiated consent.

If members of the family successfully challenge the distribution:

- the fraudulent beneficiary must return the funds to the true beneficiary,
- failing which, the insurance company has to pay twice if it is proven that it did not take the necessary precautions (e.g., benefits paid while the nomination form was manifestly incomplete).

The insurance company must therefore be cautious when distributing the death benefits and be able to demonstrate its good faith in the event of a subsequent dispute.

## Duty to trace the beneficiaries for insurance companies

The aim of the "Eckert Law" of June 13, 2014 (n° 2014-617), pertaining to dormant bank assets and unclaimed life insurance policies (including supplementary pensions plans), was to mobilize operators, especially insurance companies, to search for beneficiaries who might have forgotten or who might not be aware of their nomination in a policy or even of the existence of such a policy.

Pursuant to this Act, operators must inquire about the possible death of their entire insured portfolio at least once a year by consulting the death records from the National Directory for the Identification of Physical Persons (RNIPP). Indeed, sometimes, the insurance company is not informed about the death of the insured person.

Once a death related to an unclaimed policy is detected, the insurance company has to instigate a certain number of measures to trace and locate the beneficiary (attempt to contact the notary; obtain a full copy of the death certificate; request help from the tax authorities).

As an incentive for insurance companies to seek the beneficiaries, the death benefits are subject to annual revaluation from the date of the insured person's death until receipt of the documents necessary for the payment of the benefits, or until the transfer of the funds to the *Caisse des Dépôts* (French public sector financial institution).

If, despite the efforts of the insurance company, the beneficiary cannot be identified, the death benefits will be transferred to the *Caisse des Dépôts*.

Insurance companies who fail to comply with their obligation to track and inform the beneficiaries are liable for severe penalties, in the form of a heavy fine from administrative authorities, with interest for late payment.

For instance, in a 2014 decision (ACPR decision 2013-03 of April 7, 2014), the Sanctions Committee of the French Prudential Supervision and Resolution Authority handed down a reprimand as well as a fine of €10 million to a company (publicly named in the decision) for its shortcomings and delays in upholding those rules.

# PENSION LAWYER

In another decision (ACPR decision 2014-01 of December 19, 2014), another company (also publicly named) received a reprimand and a €50 million fine for excluding 99,5 % of its portfolio when consulting the RNIPP, failing to notify the beneficiaries and holding onto amounts that should have been paid out to them.

Thus, the task is less arduous than the determination and tracing of dependants (like in South Africa), but there is nonetheless a duty and a responsibility (sanctioned by the law).

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