

## Pensions

### A-DAY IS HERE - A LOOK AT SCHEME RULES

From 6 April 2006, the new world of pensions tax simplification is under way. For those schemes that have not looked at their rules with a view to making amendments in light of the new tax changes and provisions of the Pensions Act 2004, some transitional protection will be provided as a result of regulations now in force ("the Modification Regulations"). These aim to protect schemes against having to pay out benefits that are higher than anticipated as a result of the Inland Revenue limits no longer applying (for instance benefits previously limited by the earnings cap – the upper limit of earnings on which benefits and contributions could be based).

*The Modification Regulations apply during the transitional period, which runs until April 2011, or until the first date on which amendments are made to the rules of the scheme.*

During this transitional period, the earnings cap will still apply to both benefits and contributions, employee contributions will continue to be capped at 15% of remuneration, and where benefits are restricted by reference to the existing regime, this restriction will still apply.

Other provisions enable trustees, where the scheme rules would require them to make what would otherwise be an unauthorised payment (for example, the payment of a children's pension to a non-dependent stepchild, etc), to exercise their discretion as to whether or not to make this payment (subject to obtaining any consents specified by the rules).

However, companies cannot choose to disapply only some of the Modification Regulations - either all or none are disapplied. For example, if the trustees wanted the ability to pay the higher tax-free lump sums which are now allowed, the Modification Regulations would need to be disapplied so that they no longer override the scheme rules. That is not the end of the matter, however, as there are certain provisions in the Modification Regulations that the trustees might still wish to take advantage of and so the trustees would need to consider whether the scheme rules should be amended to incorporate equivalent provisions into those rules.

This means that companies and trustees will need to consider carefully whether they wish to amend the rules of their scheme, and take steps to do this as soon as is practicable to avoid having to rely on or be bound by the Modification Regulations.

### THE FUTURE OF PENSION SCHEMES

The news is full of stories of large companies taking steps to close their occupational pension schemes and to make other changes in an attempt to minimise the debts these companies are incurring in respect of such schemes. The BBC, Harrods, Rolls-Royce and Thomas Cook are just some of the companies who have closed their final salary schemes to new members, and British Airways have recently announced proposals to make changes to their final salary scheme, including raising the normal pension age and lowering the rate of accrual of benefits.

Many employers will be thinking along similar lines. They should note, however, that in addition to employment considerations in deciding whether to take such steps, there are new provisions that require companies to consult with employees before making such changes.

The Pensions Act 2004 and associated regulations provide that, from 6 April 2006, employers must consult with employees if they decide to make certain changes to defined benefit (i.e. final salary) schemes, which include closing a scheme to new members, increasing the normal pension age, preventing future accrual of benefits under the scheme, reducing the rate of future accrual of benefit, increasing member contributions, ceasing employer contributions and changing benefits under the scheme to money purchase benefits.

The employer must give written information about the change to employees who are active (or prospective) members of the scheme at least 60 days before the change is due to take place. Consultation must be with representatives of a trade union or elected representatives or, if there are no such representatives, with the members directly.

The regulations apply to employers with at least 150 employees from 6 April 2006, at least 100 employees from 6 April 2007 and 50 or more employees from 6 April 2008.



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Since our November Newsletter there have been a number of important cases that may have an impact on company and business sales. One of these involved a seller being held liable for the fraud of a target company employee involved in the sale even though the seller was not aware of the fraud.

Following completion it was discovered that one of the target's employees (its financial controller) had been fraudulently manipulating the accounts of the target for several years - to such an extent that instead of the target making the anticipated small profit and having net assets of around £25m, the target was making losses and had net liabilities of around £75m! The employee was involved in the negotiations between the seller and the buyer leading up to the sale and in the buyer's due diligence investigation.

The case illustrates that a seller can be liable for statements made by its own employees whether during negotiations or the due diligence investigation. As far as target employees are concerned, a seller is more likely to be held liable for statements by target employees in negotiations than it is for statements made during the due diligence investigation. Even though the seller did not know that the employee had fraudulently misrepresented the target's financial position during the negotiations, the seller had put the employee forward to speak about such matters on its behalf during the negotiations and so, the seller was held liable for the employee's fraud.

As far as the due diligence investigation is concerned, a target employee is more likely to be regarded as acting in the course of his employment when dealing with due diligence queries - and so acting on behalf of the target rather than on behalf of the seller.



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*Sellers will need to think very carefully about including target employees in its deal team on transactions, especially when those employees may take part in the negotiations.*

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## PREFERENCE SHARES - DEBT OR EQUITY?

Recent changes to accounting standards have changed the accounting treatment of preference shares and other equity-type instruments. These changes mean that preference shares and preferred ordinary shares (which we will refer to as preference shares in this article), which were previously treated as equity, may now be categorised as debt for accounting purposes.

The rights attached to preference shares can differ widely, although a typical preference share has a dividend which is payable automatically (if the company has enough distributable reserves) and which is redeemable on a specified date or dates or at the option of the holders. Such shares will now be treated as debt for accounting purposes. Preference shares can now only be classed as equity if they are not redeemable on a specified date or dates or at the option of the holders and where dividends are at the discretion of the company.

The treatment of preference shares as debt means that a company's balance sheet will be weakened. Possible effects can include a reduction in net asset value,

which could result in a weakening of the company's credit rating and so lead to demands from third parties for guarantees of the company's obligations, or breach of financial covenants in banking documents and the consequential triggering of events of default.

If a company wishes to avoid its preference shares being treated as debt, it will need to amend its articles of association to say that the company has discretion as to the making of dividends and, in the case of redeemable shares, to provide that redemption only arises at the option of the company. Other changes may be necessary depending on the precise share rights. Any changes will obviously require the consent of the holders of the preference shares.

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*This can create uncertainty for holders of preference shares as to whether dividend payments will be made or whether the shares will ever be redeemed. In practice, this may not be an issue if the holder controls the board of the company and is, therefore, able to make sure that dividends are approved and paid and the shares are redeemed.*

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However where the holders are not able to control the board this can radically alter the nature of the share from the holders' point of view. In this case the holders may want to consider what "leverage" they will have if, for example, dividends are not approved and paid. This will very much depend on the particular circumstances of the company, the holders of the preference shares and the other shareholders. It could include entering into a shareholders' agreement or making amendments to an existing shareholders' agreement. Whatever is agreed, the company will want to ensure that such agreement does not jeopardise the treatment of the preference shares as equity.



# Trusts

## THE TRUST CHANGES IN THE BUDGET - DO THEY AFFECT YOU?

Most senior executives can't help but have noticed the considerable amount of publicity given in the Budget on 22 March to the proposed inheritance tax changes to trusts - old and new. Many of you will have filed these on the back burner as not affecting you personally - after all the Government has stated that they only affect 1% of us. You have many other things to worry about in running a modern business and keeping up with all that paperwork.

You might be lucky and need do nothing - but there again, the exact opposite could be the case.

What if you die? All right, you have made a will - everything is left to your wife, if she survives you by 30 days. As your assets pass to your wife, no inheritance tax on your death and your wife might well have time to pass assets to the children free of tax. Nothing to worry about surely!

Ah well....it depends. If you leave everything to your wife absolutely, then no inheritance tax on your death. She can do what she likes with your assets. You might be happy about that.....

You might, however, be part of the growing band of people who have married more than once and, whilst wanting to ensure that your present wife is fully provided for on your death, you want to ensure that the bulk of your assets pass to the children of your first marriage. Wills have often been drawn up such that your present wife would receive a "life interest" in your estate when you die, but it would otherwise pass to your children when she dies. Perfectly sensible planning with no inheritance payable until your present wife dies and the assets pass to your children. But no longer! You would now have an inheritance tax charge on your death at 40% of the value of your assets in excess of the nil rate band (at present £285,000). A nasty surprise indeed!

*So you are part of Gordon Brown's 1% - whether you realised it or not! No prize - just a nasty tax charge. The answer could be simple - dig out your old will (is it appropriate anyhow?) and have a chat with us to see if it needs reviewing.*

The story is still unfolding and we won't know "the ending" until the Finance Act receives Royal Assent, usually in late July.



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### But a few other points

The legislation as drafted suggested that if, like most executives, you had a life policy written in trust for your wife/children, you could also be caught by the above. The Government have relented on that point but only for policies in force on 22 March 2006. What if the cover is increased? Many will offer cover of 2, 3 or 4 times salary - if your salary increases, so does the cover. Will this be caught?

*Owners of family businesses/agricultural land may qualify for business property or agricultural property relief on their deaths. So there will still be no tax? OK - as far as it goes but remember that not all such property qualifies and the rate of relief is not always 100%.*

Did you create an accumulation and maintenance settlement pre 22 March 2006, giving your children/grandchildren an interest in your business - normally at age 25? Now the trust will have to be changed so that they become absolutely entitled at age 18 or the trust will face an inheritance tax charge.

Are some of the shares in the company you work for held by such a trust? If the beneficiaries become entitled at age 18 will this affect the company?

So what should you do now? Answer - don't rush into things as changes could take place before Royal Assent, but at the very least take your will out of the cupboard, dust it down and have a chat so you can act as soon as we know what the changes will be.

# Share Options and Pensions

## TRANSFERRING SHARES FROM EMPLOYEES' SHARE SCHEMES INTO PENSION SCHEMES

From 6 April 2006 (the so called "A-Day"), employees who exercise options under a Save-As-You-Earn Share Option Scheme (also often known as a Savings-Related Share Option Scheme) or a Share Incentive Plan may transfer the shares into any registered pension scheme (essentially schemes which were previously approved schemes) by way of contributions to that scheme. In doing so, they may benefit from additional income tax relief.

*Income tax relief is given on the market value of the shares which are transferred into the pension scheme at the date of transfer. The value of the shares will be grossed up at the basic rate of income tax and higher rate taxpayers can also claim further relief.*

The shares must be transferred within 90 days of the exercise of an SAYE option or the release of SIP shares from the trust in which they are held.

Pension scheme rules will need to be checked to see if they permit such a transfer of shares and the pension scheme administrator should be consulted in order to obtain any relevant consents and to ensure the necessary administrative procedures are in place to enable shares to be transferred within the time limit.

There is no relief from capital gains tax when shares from a SIP or an SAYE Scheme are transferred into a pension scheme and so this will need to be considered. However, depending on the circumstances, there may be no capital gains tax charge or it may fall within an employees annual capital gains tax exemption (currently £8,800).

# Tax and Corporate

HAPPY ANNIVERSARY. LET'S BREAK UP!

It is ten years since the Hanson Group demerged its tobacco, chemicals and building materials businesses. There is still a common misconception that demergers are really only appropriate to large PLCs. However, a demerger can benefit a modestly-sized company or group of companies where:

- Greater value would be created by strategic or operational separation of distinct businesses;
- There is high-risk business whose exposure is not ring-fenced from the other assets of the company or group;
- There is a possibility that one of the businesses or a subsidiary will be sold;
- One of its businesses has particular financing requirements;
- There is a disagreement between key shareholders; or
- There are assets, like land or securities investments, that are prejudicing the availability of reliefs from capital gains tax.

With careful planning at an early stage, it is often possible to structure a demerger so that there are no or minimal tax charges and that there is full compliance with company law.

Rollits has worked recently with several companies and their advisers on successful demergers. If you or one of your clients might be interested in a demerger or other company reconstruction please contact Nasim Sharf [Nasim.sharf@rollits.com](mailto:Nasim.sharf@rollits.com); DD: 01482 337336, Tom Farrington [tom.farrington@rollits.com](mailto:tom.farrington@rollits.com); DD: 01482 337301 or your usual Rollits' contact.

## Employment

OUTSOURCING -  
A MORE LEVEL PLAYING FIELD UNDER TUPE

The new Transfer of Undertakings (Protection of Employment) Regulations 2006 ("TUPE") came into force on 6 April and introduced some significant changes which the majority of contractors will be grateful for. Certainly, those tendering for contracts gain more clarity and protection.

Often, much anguish was caused by having to make an often uncertain assessment as to whether TUPE applied at all. A new definition of a relevant transfer will mean that most service provision changes will be clearly caught by TUPE and it is to be hoped that there will therefore be more general acceptance on the issue of liability for the employees engaged in the activity to be transferred.

*Also, there is a new obligation placed on any outgoing contractor to provide the new service provider with information about the employees it will inherit. This includes details of the names, ages, length of service, contracts of employment and disciplinary and grievance records of the transferring employees. Any failure to provide this information can give rise to a complaint by the new contractor and a minimum award in its favour of £500 in respect of each transferring employee.*

There remains an obligation on both transferor and transferee to consult with trade union representatives or elected workforce representatives regarding the fact of the transfer and any measures either party proposes taking in connection with it. An unfortunate consequence of previous TUPE Regulations was that any liability arising out of a failure to inform and consult passed to the transferee so that in many changes of service provision the outgoing contractor had little incentive to comply with its obligations. There is now a mechanism whereby a Tribunal can determine who is most to blame for any failure to inform and consult and apportion any award in favour of the employees accordingly.

Unfortunately, any increased flexibility does not extend to changes in terms and conditions. On the face of the new TUPE Regulations there is increased scope for the transferee to change terms and conditions. The reality is that this will be severely limited by the requirement that any change must be ones which "entail changes in the workforce". A desire to harmonise terms with an existing workforce is not such a permissible change.

Also, experience has taught us to expect the unexpected in this area of law. The old TUPE proved to be fertile ground for employment lawyers and the situation is unlikely to be any different with the new Regulations.

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# Food Group

## WHAT'S IN A NAME?

European law is not often something to get the pulse racing. But when in 1992 the European Commission adopted Council Regulation (EEC) No. 2081/92 (on the protection of geographical indications and designations of origin for agricultural products and foodstuffs) and Regulation No 2082/92 (certificates of specific character) it lit a fuse to a very large tinderbox.

According to Defra's 'Protecting Food Names' guidance on the regulations, the legislation provided "a simpler system for the protection of food names on a geographical or traditional recipe basis." In reality the system aimed at protecting registered food or drink against imitation throughout the European Union proved anything but simple.

There are three main designations in EU legislation:-

- **A PDO (PROTECTED DESIGNATION OF ORIGIN)**  
for products produced, processed and prepared in the geographical area;
- **A PGI (PROTECTED GEOGRAPHICAL INDICATION)**  
for products with at least one geographical link to production, processing or preparation; and
- **A TSG (TRADITIONAL SPECIALITY GUARANTEED)**  
which is not linked to a geographical area but highlights the traditional character of the food.



In each case there must be quality, reputational or traditional characteristics.

Examples of successful PDOs and PGIs in the UK include many regional cheeses (e.g. Stilton), Jersey Royal potatoes, Scotch beef, Welsh lamb, Newcastle brown ale and Cornish clotted cream. However, some applications have been contentious, most recently the PGI sought by the Melton Mowbray Pork Pie Association, which is being considered by the European Commission but has been referred to the European Court of Justice. The PGI would restrict production of Melton Mowbray pork pies to a defined geographical area, albeit one which stretches from Nottingham to Northampton.

On 20 March 2006 The Agriculture Council in Brussels adopted two new regulations (Council Regulation (EC) No. 509/2006 and 510/2006) to clarify and streamline the rules on geographical indications and designations, whilst implementing the findings of a recent WTO panel. The 1992 Regulations have now been repealed. We look forward to seeing how much better the new legislation proves to be.

Julian Wild - our Food  
Group Director



*Julian Wild, our Food Group Director, previously worked on the Melton Mowbray pork pie case and has considerable knowledge of PGIs.*

## PAPERLESS SHARE TRANSFERS?

The Institute of Chartered Secretaries and Administrators (ICSA) has launched a consultation on proposals for the introduction of mandatory electronic share transfers.

The proposals involve:-

- The replacement of share certificates with share statements;
- The provision of a shareholder reference number for each shareholding held;
- Share certificates cease to be legal evidence of ownership;
- Every time shares are sold, or new shares are bought, the registrar would issue the shareholder with a new statement showing his current holding, even if all shares have been sold.

It is proposed that the new system would be mandatory for all shares issued in the UK and which are admitted to the Official List, AIM, OFEX and ShareMark, with voluntary application to private companies.

The proposals would allow shareholders to keep their name on the register of members and so maintain a direct relationship with companies (including the ability to attend and vote at shareholders' meetings, the direct receipt of annual reports, dividends and other company information, and the receipt of any shareholder privileges).

The consultation ends on 30 June 2006. If the proposals gain the necessary support, ICSA intends to work to resolve outstanding issues and develop a detailed implementation plan. Timing of the implementation will depend on progress of the Company Law Reform Bill currently going through Parliament and any subsequent regulations that will be required to facilitate the process. On current projections it is unlikely that full implementation could be achieved before 2008.

# Commercial

## OFT CLAMPS DOWN ON UNLAWFUL PENALTY CHARGES

The Office of Fair Trading ("OFT") has given banks until the end of May to agree to reduce their default charges for overdue credit card payments. Failure to reduce charges may result in the OFT taking legal action over what it claims are unfair penalties for consumers. The OFT expects all credit card issuers to reduce their default charges in line with a guidance note issued last month. Where a card issuer wishes to impose default charges greater than £12 the OFT has said that it will take the view that the charge is unfair and is open to challenge in the courts unless there are exceptional circumstances justifying the increased charge.

## BUYING AND SELLING DATABASES - INFORMATION COMMISSIONER RELEASES GUIDANCE

The Information Commissioner's Office ("ICO") has released guidance advising businesses on how to comply with the Data Protection Act 1998 ("the Act") when buying and selling databases containing customers' confidential information.

On issuing the guidance, a representative from the ICO said: "The guidance is intended for use when a database is sold, for example, when a business is insolvent, closing down or being sold. In these circumstances the Act does not prevent the sale of a database containing the details of individual customers, providing certain requirements are met."

The requirements include the following:

The individuals on the database must have been told at the time their information was collected what the information would be used for.

*When the database is sold, the seller must make sure that the buyer understands that the information can only be used for the purposes for which it was collected. If the buyer wants to use the personal information for a new purpose, it will have to get consent for this from the individuals concerned.*

The buyer should make sure that all the affected individuals are told about the sale of their information. This should be done as soon as practicable, giving the new owner's contact details and confirming that the information obtained will only be used for the same purposes as before.

The buyer can only use the database for unsolicited marketing if the individuals referred to in it have agreed to receive such marketing, or receipt of such marketing is likely to be within their reasonable expectations. Where this is the case the buyer can only market products and services similar to those that have been advertised through the database before.

The buyer should also establish whether the individuals would only expect to receive marketing via a particular medium, for example by post. Particular care should be taken when using the telephone or email to ensure that the special rules governing electronic marketing are complied with.

The Act requires that any personal information held should be adequate, relevant and not excessive, and that it should not be kept for longer than is necessary. The new owner of a database should decide how much of the information they need to keep. Any unnecessary personal information should be deleted. Personal information should not be held simply on the basis that it might become useful one day.

The ICO's guidance shows that any business which intends to sell or buy a database should take advice before proceeding, so that it can ensure that it obtains appropriate warranties and written assurances from the other party.

### INFORMATION

**If you have any queries on any articles  
in this newsletter or other corporate or  
commercial matters generally please contact:**

**Keith Benton or Tom Farrington on (01482) 323239**

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It is for general guidance only. It provides useful information in a concise form.

Action should not be taken without obtaining specific advice.

We hope you have found this newsletter useful. If, however, you do not wish

to receive further mailings from us, please write to

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