ML Covered - October 2024

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Welcome to the third edition of ML Covered, our monthly round-up of key events that are relevant for those dealing with Management Liability Policies covering D&O, EPL and PTL-type risks.

Director liable for company funds due to failure to keep proper accounting records

In *OmniMax International LLC v Cullen & Ors* [2024], the High Court has indicated that in cases involving alleged breaches of directors' duties, deceit and the use of company funds, the court is prepared to delve into the details of complex financial transactions at a summary judgment stage of the claim.

Background

The case involved a claim by OmniMax International LLC (OmniMax), a North American manufacturer of building products, against three defendants: Simon Cullen (First Defendant), sole director and shareholder of Alumill Limited, Rolmet Limited (together, the Companies) and Aluinox Limited (Second Defendant); and the First Defendant's wife (Third Defendant).

OmniMax alleged that the First Defendant had falsely represented that his aluminium mills could produce 7 million lbs of aluminium, when they only managed to produce 400,000 lbs; and it had paid over $5m in reliance on these misrepresentations. Further, the First Defendant caused the Companies to make large payments to himself and the Second Defendant in breach of his fiduciary duties, with those payments being used to purchase a property (the Property) together with the Third Defendant (the Breach of Duty Claim).

Application for summary judgment

OmniMax applied for summary judgment / to strike out parts of the defence relating to the Breach of Duty Claim. The Defendants opposed the application.

The Judge found that the issues were properly to be considered by way of summary judgment, referring to substantial payments made by the Companies to the First Defendant's personal bank account (the Payments).

It was undisputed that the First Defendant owed a fiduciary duty to the Companies to apply their assets for a proper purpose. The issue was therefore whether the First Defendant had a realistic prospect of proving at trial that the Payments were for a proper purpose in this case.

The First Defendant argued that he was entitled to the Payments, being: (1) repayments of monies directly advanced to the Companies (Direct Payments); and (2) payments representing the assessed value of a customer list transferred to a creditor of Rolmet, and in partial settlement of Rolmet's liabilities to the same creditor (Indirect Payments).

As to the Direct Payments, the Judge found the First Defendant had breached his duty to ensure that proper accounting records were kept, such that the only accounts available for review were the Companies' and the First Defendant's bank statements.

As to the Indirect Payments, the Judge was critical of the "shifting nature" of the First Defendant's narrative, finding that his credibility was undermined by the admitted doctoring of bank statements, self-contradictions and internal inconsistencies.

The Judge granted summary judgment in relation to both the Direct and Indirect Payments, on the basis that: (a) the First Defendant had no real prospect of discharging the burden that would be upon him at trial to establish that he was properly entitled to the sums received under the Director's Loan Account, or that the Indirect Payments were properly made; and (b) there was no other compelling reason why these issues should be disposed of at trial.

Key takeaways

The case serves as a reminder that, when considering an application for summary judgment, the court is willing to undertake a detailed analysis of financial transactions. Further, directors must maintain accurate records to support any payments made, and make sure they use company money for proper purposes only.

To read the case, please click here.

High Court rejects liquidators' wide information request for being unreasonable

In *Webb v Eversholt Rail Limited* [2024], the High Court recently rejected an information request by liquidators, reminding liquidators that such requests must have a reasoned basis.

Background

Eversholt Rail (365) Limited (365Co) and Eversholt Rail Limited (ERL) are both part of the Eversholt UK Rails Group (Group), which owns and maintains railway engines and carriages that are leased to train operating companies. ERL provides asset management and administrative services to companies within the Group.

Following what is described within the judgment as a "funding crisis", 365Co entered creditors' voluntary liquidation.

ERL provided documents to the liquidators in relation to 365Co, but further requests – described by the Court as "far-reaching" – were made by the liquidators to ERL and ERL's solicitors. The liquidators requested "copies of all documents…in its possession custody or control relating to the business, dealing, affairs or property of 365…". The liquidators thought that ERL's solicitors had also provided advice to 365Co.

The liquidators' request for this information ultimately formed the subject of an application to the court, which also included a request for "all documents created for the purpose of carrying out services pursuant to the Services Agreement".

The Application and the Decision

The application was made under s235(2)(a) and s236(3) of the Insolvency Act 1986. These provisions enable liquidators to seek information "concerning the company and its promotion, formation, business, dealings, affairs or property" from both specified persons, but also more broadly, "any person whom the court thinks capable of giving…" that information.

The application was rejected by the Judge for being "fundamentally misconceived". The Judge considered that "the Liquidators' evidence is largely devoted to not explaining or justifying their requirement, but to explaining why documents not yet disclosed by ERL 'evidently exist'…".

Further, blanket statements provided by the liquidators did not assist the court in weighing in balance the liquidators' "apparent need to see, in this case, pretty much everything…" that was held by ERL and its solicitors relating to 365Co, against any asserted inconvenience to or oppression of ERL. As the liquidators' evidence did not explain why the documentation was reasonably required, the Judge did not need to consider any alleged inconvenience or oppression on the part of ERL.

As above, a request for information and documents was also made to ERL's solicitors. The Judge noted that ERL and 365Co were "sister" companies (as opposed to a parent and subsidiary relationship) and no evidence had been provided of legal advice obtained by ERL being habitually disseminated to 365Co. The fact 365Co might have been the subject of that advice was insufficient to give rise to joint interest privilege.

As with the requests to ERL, the application was so wide and unsupported by evidence it was bound to fail.

Key takeaway

Webb v Eversholt Rail Limited serves as a helpful reminder that any request for documents by liquidators must explain why the information or documentation is reasonably required. Where a party's application is based upon the fact that the documents are simply available, that party can expect their application to fail. D&Os should carefully consider what documents and information they are required to provide to liquidators in such circumstances. With the increasing number of corporate insolvencies we expect to see more of these types of contested applications.

To read the case, please click here.

The new duty to prevent sexual harassment: what does this mean for employers?

A new proactive duty on employers to take reasonable steps to prevent sexual harassment will come into force on 26 October via The Worker Protection (Amendment of Equality Act) Act 2023 (the Act). The Act adds a new section 40A to the Equality Act 2010, introducing a positive obligation on employers to take 'reasonable steps' to prevent sexual harassment by their employees in the course of their employment.

What is the current position?

Currently, employers are vicariously liable for sexual harassment committed by their staff in the course of employment unless they show that they took 'all reasonable steps' to prevent the harassment from occurring. Tribunals are often reluctant to accept that employers have satisfied the 'all reasonable steps' defence. The new Act introduces a positive obligation, obliging employers to put reasonable steps in place to prevent sexual harassment of employees from arising in the first place.

Does the duty extend to third parties?

A duty to prevent sexual harassment by third parties was removed from the Bill in October 2023, so employers are not presently liable for harassment by third parties. However, the Equality and Human Rights Commission's (ECHR's) guidance on the new duty includes a duty to prevent sexual harassment by third parties such as customers, clients and friends and family of colleagues. Further, Labour's Plan to Make Work Pay (part of its manifesto on Employment Law reform) pledges to ensure that workplaces are free from harassment, including by third parties (read more about Labour’s Plan to Make Work Pay in our previous edition of ML covered). It therefore remains to be seen whether further secondary legislation will re-introduce the third-party duty.

Practical steps for compliance

Employers will need to show that they have reasonable steps in place to prevent sexual harassment. Whether or not an employer has taken reasonable steps is an objective test and will depend on the facts and circumstances of each situation. However, there are a number of general steps that companies may wish to take in preparation for the new duty:

1. Carrying out enhanced training and risk assessments on sexual harassment;
2. Updating and reviewing the company's current policy on sexual harassment or creating a standalone policy on the topic;
3. Creating an independent reporting line for incidents of sexual harassment;
4. Keeping a thorough record of steps taken to prevent sexual harassment, which is regularly reviewed; and
5. Circulating anonymous surveys to better understand the protection required from staff.

Consequences of non-compliance

If the employment tribunal is satisfied that the preventative duty has been breached, it may order the employer to pay additional compensation to the worker (a 'compensation uplift’) of up to 25% of an award of compensation. The EHRC can also take enforcement action against employers in breach of the new duty.

Right to a predictable working pattern is not so predictable…

The right for individuals to request a more predictable working pattern was due to come into force in September 2024 through The Workers (Predictable Terms and Conditions) Act 2023 (the Act). However, a spokesperson for the Department of Business and Trade has reportedly confirmed that its enactment will not go ahead. Instead, provisions aiming to bring security to atypical workers are likely to be reflected in the forthcoming Employment Rights Bill and Labour's Plan to Make Work Pay: Delivering a New Deal for Working People (Labour's New Deal) programme to avoid overlap and confusion (read more about the Employment Rights Bill and Labour's New Deal in previous editions of ML covered).

Matthew Taylor’s 2017 review of modern working practices and the gig economy originally suggested the introduction of such a policy, noting that it would support many workers who currently experience ‘one-sided flexibility’. A right for workers to request a more predictable contract was subsequently proposed in the Conservative Party's 2019 manifesto and the Act received Royal Assent in September 2023.

The Act had sought to address the imbalance of power between some employers and atypical workers and end the 'guessing game' of putting these workers' lives on hold to make themselves available for shifts that may never actually come. It would have allowed workers on atypical contracts - including those on zero hours contracts and fixed-term contracts of less than a year’s duration - to apply (up to twice a year) for a more predictable working pattern. Employers would have needed to respond to such requests within one month and would have only been able to reject the application under one or more of the statutory grounds, which included 'the burden of additional costs', a 'detrimental impact on other aspects of the employer’s business' and 'insufficiency of work during the periods the worker proposes to work'.

It remains to be seen what the current Government's exact proposals will be on predictable working patterns. However, Labour's New Deal seeks to ensure security and predictability for workers, by banning 'exploitative' zero hours contracts and ensuring that everyone has the right to have a contract that reflects the number of hours they regularly work.

TPO upholds complaint against employer for failing to pay member contributions into plan

The Pensions Ombudsman (TPO) has upheld a complaint against Ash Contracts Ltd (AC) for failing to pay member contributions that were deducted from an employee's salary into their pension plan. The Claimant commenced employment with AC in October 2021. Soon after AC started deducting pension contributions from the Claimant's salary. However, the Claimant was only enrolled into the pension plan (the Scheme) from 1 November 2022. Between November 2021 and 19 December 2022, AC failed to pay contributions to the Scheme. The Claimant discovered AC's underpayment after contacting AC's accountant to enquire where his contributions were going because he had not received such information from AC. The Claimant eventually left AC's employment on 19 December 2022.

Unsurprisingly, TPO upheld the Claimant's complaint and concluded that AC had failed to contribute £4,464.57 into the Scheme on behalf of the Claimant. TPO determined that AC's failure to pay the monies into the Scheme amounted to unjust enrichment and ordered AC to repay the Claimant.

In addition to returning the missing contributions AC was also ordered to (i) pay the Claimant £1,000 for the distress and inconvenience caused; (ii) calculate whether the late payment of contributions had resulted in fewer units being purchased had the contributions been made on time (i.e. any investment loss); and (iii) pay any reasonable administration fees charged by the administrators.

The facts of this complaint were unusual in the sense that an employer has clearly failed to allocate an employee's contributions to the Scheme. AC also failed to engage with TPO which likely also reflects the eagerness for it to award £1,000 for serious distress and inconvenience caused. However, it is also a reminder of the exposure to any employer when it comes to ensuring that it is properly administering a pension scheme and the relevance of PTL to any employer.

To read the decision in full please click here.

Mr G (CAS-110116-G1N5) – Pension transfer complaint dismissed as proper due diligence carried out

The Pensions Ombudsman (TPO) has rejected Mr G's complaint against a trustee and administrator concluding that there was no maladministration. TPO found that due diligence checks were conducted appropriately and even if the updated guidance had been followed, it was likely that Mr G would have proceeded with the transfer regardless.

In February 2013, the Pensions Regulator (TPR) launched a campaign to raise awareness of pension liberation schemes. As part of this initiative, TPR distributed materials such as the Scorpion Leaflet to help members identify potential scams. Mr G, a deferred member of the Asda Group Pension Scheme (the Scheme), a defined benefit arrangement administered by the Asda Pensions Team (the Administrator) managed by Asda Group Pension Scheme Trustees Ltd (the Trustee), was approached in 2014 by a pension adviser recommending a transfer to the Global Pensions Administration Ltd Plan (the Global Plan). After authorising Bailfort & Associates, a Gibraltar-based regulated adviser, along with Aspinal Chase Ltd, an unregulated adviser, to request his cash equivalent transfer value (CETV), Mr G received a CETV of £32,692.88. He was also provided with the Scorpion Leaflet and warnings for him to be cautious if he was transferring due to a website promotion, cold call or advert encouraging him to transfer to access a cash payment or loan. The transfer was completed in September 2014, with Mr G later directed to invest in the Optimus Retirement Benefit Scheme, which was ultimately determined to be fraudulent.

Mr G lodged a complaint asserting that the Trustee and Administrator had failed to follow TPR's guidance before processing the transfer. He argued that they did not conduct sufficient due diligence and overlooked critical warning signs, such as the receiving scheme being newly registered and the involvement of unregulated advisers. The Trustee and Administrator argued that they had performed the necessary due diligence and complied with statutory requirements. They argued that Mr G was not obligated to seek advice from a regulated financial adviser at the time and that there were no warning signs of a fraud. In response to Mr G's concerns, they clarified that:

1. The Global Plan had been registered as a qualifying recognised overseas pension scheme (QROPS) for over a year prior to the transfer.
2. There were no signs that Mr G sought early access to his pension or felt pressured to complete the transfer.
3. They were unaware of any unsolicited approaches to Mr G.
4. As the transfer was to a QROPS, there was no need to verify Mr G's employment status.

Given their due diligence findings, the Trustee and Administrator maintained there was no need to contact Mr G for further information. They argued that even if additional inquiries had been conducted, it is unlikely that any warning signs would have been identified that would change Mr G's decisions.

TPO dismissed Mr G's complaint, agreeing that the Trustee and Administrator had fulfilled their obligations based on the regulatory guidance available at the time. TPO noted that Mr G's transfer request was made shortly after the 2014 fraud action pack was published. Whilst the Trustees argued that the request was too soon to comply with the updated guidance, TPO disagreed, stating that the due diligence checks were completed within the one-month grace period following the guidance's release. There was no evidence to suggest that the process extended beyond the grace period. TPO acknowledged that Mr G had received multiple warnings about potential scams and confirmed his understanding of the risks by signing the transfer documents. TPO concluded that even with adherence to the 2014 guidance, it was likely Mr G would have proceeded with the transfer regardless.

This is a helpful reminder of the obligations on trustees (and administrators) relevant to a PTL policy for trustees when it comes to due diligence on pension transfers.

To read the decision, please click here.

TPR cracking down on schemes failing to deliver value

The Pension Regulator's (TPR's) latest Compliance and Enforcement Bulletin reveals that Defined Contribution (DC) schemes have been fined £33,750 in total following the introduction of TPR's detailed value for members (dVFM) assessments last year. These assessments require trustees to assess whether they deliver value to members. TPR's focus on value for money is consistent with the government's Pensions Review with its focus on tackling waste in the pensions system and delivering better outcomes for future pensioners.

Between January and June 2024, TPR used its powers 10 times in relation to dVFM assessments, issuing 7 penalties totalling £19,250 and 3 improvement notices. During the pilot exercise between November 2023 and January 2024, TPR issued penalties of £14,500 for dVFM breaches. The dVFM assessments are also leading some schemes to wind up. Around 17% of the schemes TPR engaged with concluded their schemes did not offer good value and opted to wind up. TPR has noted that if this percentage applied across the 1,323 DC schemes caught by dVFM regulations, over 200 schemes would be opting to wind up following assessment.

TPR's Bulletin also reveals the regulator fined two pension schemes for failures relating to annual climate change reports, with GKN Group Pension Scheme and The Prudential Staff Pension Scheme fined £8,000 and £5,000 respectively. TPR confirms it is increasing its focus on investment governance and warns that "trustees should expect to be challenged on whether their climate reporting disclosures are the product of strategic decision making aimed at protecting savers from the financial risks of climate change, both now and in the future".

TPR also continued to use its automatic enrolment powers having issued the following between January and June 2024:

- 30,688 Compliance Notices compared to 29,489 in the previous period
- 18,589 Unpaid Contribution Notices compared to 17,451 in the previous period
- 20,677 Fixed Penalty Notices compared to 19,538 in the previous period
- 7,682 Escalating Penalty Notices compared to 8,400 in the previous period

The above shows trustees of DC schemes are under increased pressure to ensure schemes are delivering value for money alongside other compliance measures, particularly with the government also looking to address waste as part of its focus on the pensions industry and is yet further evidence of the increased regulatory burden in the pensions area.

DB funding code takes effect

TPR has confirmed that trustees of defined benefit (DB) schemes whose actuarial valuations dates fall after 22 September 2024 should now refer to the new DB funding code (which is due to come into force in late November 2024). The Regulations require trustees to:

- Determine a funding and investment strategy, setting out how they intend the scheme to provide benefits over the long term; and
- Record the funding and investment strategy in a statement of strategy.

Trustees are required to submit their statement of strategy "*as soon as reasonably practicable*" after preparing their funding and investment strategy. TPR is due to launch a digital platform to accompany the new code in spring 2025 and has confirmed that it "*will not regard trustees or scheme managers as being in breach of the regulations if a delay in the launch of its digital system next year results in there being a gap between preparation of the funding and investment strategy and submission of the statement of strategy*". Despite this, TPR has warned trustees against delaying valuations simply because they must wait to submit them on the new platform.

TPR issues compliance and enforcement policy for pensions dashboard

On 5 September 2024, the Pensions Regulator (TPR) introduced its compliance and enforcement policy for pensions dashboards, emphasising the obligations for all relevant schemes to connect by 31 October 2026. The Department for Work and Pensions has set a phased timetable, with the first connection date on 30 April 2025. "Connect by" dates depend on pension scheme size and type and the number of members as at year end 2023/2024.

TPR's policy highlights the importance of immediate action from trustees and scheme managers to ensure compliance. Key requirements include preparing for connection, improving data quality and maintaining comprehensive audit trails.

As connection dates approach, TPR plans to engage with schemes this autumn to evaluate their readiness and data management processes. The TPR emphasises the need for accurate and reliable data and sets out best practices for addressing data-related risks. Trustees are also reminded to report any data breaches to TPR promptly. For any DC or DB trust-based schemes operated by an employer they need to pay regard to the obligations imposed by the pension dashboard and ensure they meet connection deadlines – this will be something PTL insurers will want to consider asking impacted schemes about at renewal.

RPC's blog on this can be read here.