

ALLEN & OVERY

Good faith and employee communications

Landmark ruling in IBM UK Holdings Ltd and IBM UK Ltd v Dalglish and others

Key points

Employers undertaking pension scheme benefit change processes need to give careful consideration not only to the detail of member communications, but also to the overall impression they give and to member expectations which could be created by those communications, in light of the High Court's significant new decision in relation to technology giant IBM.

The judgment considers, we believe for the first time, the understanding which a hypothetical reasonable member might take from different types of communication, including a webcast. This is a significant issue: even if statements are technically correct, they may combine or be presented in a way which creates inaccurate impressions or expectations. This may then give rise to a breach of the employer's duty of good faith in exercising its powers under a pension scheme, and/or to a breach of the employer's duty of mutual trust and confidence, which is implied in all employment contracts.

The detailed analysis in this case of different types of member communications and of the weight and meaning which should be attached to them by the Court (in the role of a hypothetical reasonable member) will be critical in designing and testing future communications about benefit change exercises, in terms of both accuracy and overall message.

Pension scheme trustees must satisfy themselves that powers under the scheme rules are being properly exercised (whether or not their consent is required) since, if the exercise is invalid, the terms of the trust will not have been changed. As such, trustees should enquire into the employer's reasons for exercising a power. The extent of those enquiries depends on the circumstances; in some cases an application to Court may be required to determine the position.

The headline issues

The key findings from the judgment are:

- that changes introduced by IBM (including closing defined benefit plans to future accrual and imposing a new restrictive early retirement policy, in an exercise known as ‘Project Waltz’) breached its *Imperial* duty of good faith in the light of reasonable expectations engendered in the members by IBM’s previous conduct; and
- that IBM breached its implied contractual duty of trust and confidence to employees by providing misleading information during the consultation process which preceded the scheme closure. A separate remedy was available for this (in addition to the penalty for statutory breach of duty under the consultation regulations).

The *Imperial* duty of good faith is a shorthand reference to the implied duty between an employer and members/beneficiaries of a pension scheme not to destroy or seriously damage the relationship of trust and confidence between them. It is often discussed in the context of how the employer exercises its powers under the trust deed and rules.

It’s important to note that the pensions changes brought about by IBM would not **in themselves** have given rise to a breach of IBM’s implied duty of good faith.

Many scheme sponsors have undertaken this kind of process as part of managing their defined benefit liabilities. The crucial issue was IBM’s previous conduct and communications to members, in the course of earlier benefit redesign exercises. This had led members to expect that, subject to certain limitations, their pensions were ‘safe’ from further cutbacks. In the context of those reasonable expectations, the actions taken as part of Project Waltz were ones that no reasonable employer could have taken. Instead, IBM needed to reset expectations through communication and consultation, and only make changes which were consistent with maintaining the relationship of trust and confidence with members.

Points to note

The judgment is very substantial (running to 434 pages) so we can only provide an outline summary of the key issues here. Particular points to note include the following:

- In general terms, the meaning of documents and statements must be ascertained in the light of the context in which and the purposes for which they were produced or made. The reasonable expectations which members would have derived from communications must be determined having regard to matters including:
 - the level of understanding of a hypothetical reasonable member, for example in relation to pensions terminology;
 - the method of communication and how it might reasonably have been used by members (for example, a webcast or video is designed primarily to be watched and heard once in real time, not transcribed and analysed or read as a document); and
 - the relative weight which a member might attach to particular types of communication – for example, they were likely to take a single overall message from the webcast.

- IBM’s strong corporate culture, including business guidelines and values which stressed honesty and trust, counted against it in assessing whether IBM had breached its *Imperial* duty. In light of those guidelines and values, it was incumbent on IBM to correct any misperceptions about its intentions in relation to pension changes so that members could make informed decisions.
- Statements and presentations made to the Trustee (rather than directly to members) which were relied on by the Trustee and communicated by the Trustee to members were attributed to IBM in the same way as direct member communications by the company.
- The communications giving rise to members’ reasonable expectations were not simply expressions of intent; they were communications on the basis of which members would take important decisions relating to their careers and retirement. In light of members’ reasonable expectations, IBM could be expected to adopt proposals to meet corporate concerns (global and local) about business costs in ways which, so far as reasonably possible, were consistent with those reasonable expectations.

Comment

The points outlined above are of particular relevance to employers going into a similar process in relation to pension scheme benefit changes. Clearly, employers want to reassure their workforce and present a positive message, but they should avoid ‘spin’ which misrepresents the facts. On the other hand, technical correctness is not enough: employers need to consider what members will understand, as well as what they are actually told; and if there are hard truths to tell, those should be included in communications. Nothing in the *IBM* decision prevents employers from managing pension scheme liabilities in this way, but it’s more important than ever to get the content of all types of communication right.

For more information on the judgment and its relevance to your employee or member communications, contact:



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