Insolvent business transfers and the interaction of EC law and local jurisdictional law on liability for accrued pension rights

We consider pension protection for employees on the insolvency of their employer in light of two recent ECJ cases concerning German companies. The cases highlight the importance EC law attaches to pension protection for pre-transfer service in an insolvency, which the UK sought to address through establishing the Pension Protection Fund (PPF) and Germany likewise through the "PSV".

Readers will be aware of the "pension exemption" to the automatic transfer of employment rights on business sales, where employees find their employment transferring under TUPE to a new employer, with the terms and conditions of their pre-transfer employment protected. The EC Acquired Rights Directive (ARD) carved out from employment protection any rights which transferring employees may have to old age or pension benefits under occupational pension schemes (although case law has established that certain early retirement or redundancy rights do transfer, but that is the subject of a different article) "*unless Member States provide otherwise*".

The UK chose to keep the carve-out for pensions, with the Pensions Act 2004 providing certain protection for transferring employees with occupational pension scheme rights by requiring transferee employers to provide a minimum level of *future* pension provision for such transferee employees. By contrast, the broad position in Germany for pension arrangements, including past service, is that they transfer as part of the employment relationship to the new owner who, in principle, must continue the arrangements. Amendments and replacements to the pension arrangements are only possible within certain parameters.

How the protections on TUPE transfers play into the insolvency arena is interesting and there has recently been discussion on the scope of the wording of an article of the ARD which reflects the wording of article 8 of the EC Insolvency Directive (ID). In essence, article 8 of the ID provides that EU member states must take "*necessary measures*" to protect the accrued rights under occupational pension schemes of TUPE transferred employees and former employees at the date of the employer's insolvency. In the UK, the government established the PPF with this in mind.

The ECJ recently considered the question of pension protection in corporate insolvencies for member states. In two cases involving German insolvency proceedings, the ECJ considered whether or not members of private German occupational pension schemes should enjoy pension benefits based on pre-insolvency service, or whether the protection of pension rights should relate to post-transfer service only.

In the cases under consideration, the employers had fallen into insolvency and the business activities, and relevant employees' contracts of employment, had transferred to new operations. In one of the cases, the German occupational pension guarantee association, the PSV, informed the individual in

question that he had not acquired any definitive right to pension benefits and would consequently not receive any benefit from PSV if there were to occur an event that would theoretically allow him to claim benefits from PSV. The employee was unhappy with this and sought full pension rights from his transferee employer, based on full prospective service to retirement and not just post-transfer service.

In the second case under consideration, the employee in question had started to draw his pension, which was based on post-insolvency service only. He claimed that his transferee employer should be ordered to pay him a higher occupational retirement pension which took account of periods of service carried out before the opening of insolvency proceedings.

The transferee employers argued in both cases that, according to automatic transfer principles in Germany, their liability was limited to the portion of pension derived from service falling after the start of the insolvencies. (This is as for the UK, where the law protects pension rights related to post-transfer service.)

The ECJ ruled that the restriction under German law for protection of rights arising from post-transfer service is compatible with the ARD and the ID, provided that the interests of the employees were protected at a level equivalent to that required under the ID. That appears to suggest that member states must offer protection through other means, such as the PPF or PSV, where local law does not protect pre-insolvency accrued pension rights.

The ECJ noted that the ARD allows member states to adopt their own measures for the protection of employment on automatic transfer (so EC law does not require strict harmonisation across the member states). Member states are free to provide that, even where transferee employers are subrogated to rights and obligations arising from the employment relationship existing at the time of the transfer (although this is not the case in the UK or in Germany), they are liable only for employees' rights derived from periods of employment after insolvency proceedings. However, the qualification to this is that, for the portion of benefit for which the transferee is not liable (here benefits derived from pre-insolvency service), member states must adopt measures to protect employees which are equivalent to the level of protection required under the ID.

The ECJ followed its recent decision in the case of *Bauer*, emphasising that the minimum protection required under the ID means that affected employees must receive at least half of the pension benefits deriving from the accrued pension rights under a private occupational pension scheme. Similarly, the ECJ considered that minimum protection does not permit a "manifestly disproportionate" reduction of an employee's occupational retirement benefits affecting the ability of the person concerned to meet his needs or reducing his standard of living to below the poverty threshold.

As for applicability in local law, the ECJ emphasised that the ID is capable of having direct effect and can be relied upon in proceedings against a body governed by private law, designated by the member state concerned as the body that guaranteed occupational pensions against the risk of insolvency of employers. However, the body in question must be one which is treated as equivalent to the state (the PPF in the UK, a creature of statute and reporting to a government department, satisfies this).

What is the significance of this for the post-Brexit landscape? If the UK wishes to maintain "frictionless" economic and, even where possible, political relations with the other EU member states after Brexit, it seems to us that the UK will have to do so in light of the parameters of EC law, as developed in part by the ECJ since the inception of the EU. Perhaps there is a tenuous link between future trading and political relations and pension protection in insolvency; however, our view is that there will be at least an expectation that the UK adheres to recognised principles of trade and employee relations and upholds freedoms and protections espoused by its fellow European states.

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