[2018] UKUT 164 (TCC)

Reference: FS/2012/0001-5

PENSIONS REGULATOR – Financial support direction – pension scheme of joint venture company insufficiently resourced – jurisdiction – whether Targets connected with or an associate of the employer at the relevant time – yes – whether the legislation can be applied to events all of which occurred before legislation came into force – yes – whether different treatment by Regulator of Targets to co-joint venturer lawful- yes- whether presence of moral hazard necessary – no – whether reasonable to impose financial support direction on the Targets – yes – Pensions Act 2004 ss 43, 100 & 103 – references dismissed

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

GRANADA UK RENTAL & RETAIL LIMITED
GRANADA MEDIA LIMITED
GRANADA GROUP LIMITED
GRANADA LIMITED
ITV plc **Applicants**

- and -

THE PENSIONS REGULATOR **Respondent**

- and -

BOX CLEVER TRUSTEES LIMITED **Interested Party**

TRIBUNAL: MRS JUSTICE ROSE, CHAMBER PRESIDENT
JUDGE TIMOTHY HERRINGTON
MEMBER IAN ABRAMS

Sitting in public at The Rolls Building, Fetter Lane, London EC4A 1NL on 29, 30 and 31 January, and 1, 2, 5, 7, 8 & 9 February 2018

Lord Pannick QC, David Railton QC, Michael Furness QC, Edward Sawyer and James McCreath, instructed by Hogan Lovells International LLP, Solicitors, for the Applicants

Jonathan Hilliard QC, Benjamin Faulkner and Tim Matthewson, instructed by Eversheds Sutherland (International) LLP, Solicitors, for the Interested Party

Nicolas Stallworthy QC, Gabriel Moss QC, Martin Chamberlain QC and James Walmsley, instructed by The Pensions Regulator, for the Respondent

© CROWN COPYRIGHT 2018

DECISION

I. INTRODUCTION AND MATTERS REFERRED

1. This decision concerns references made under s 103 of the Pensions Act 2004 ("PA 2004"). The references relate to a determination made on 21 December 2011 by the Determinations Panel ("DP") of the Respondent. The Pensions Regulator ("the Regulator") contends that five companies from the corporate group of the well-known broadcasting company ITV should be the subject of a Financial Support Direction ("FSD") issued pursuant to s 43 PA 2004 so as to require them to provide financial support to address an estimated deficit of £115 million in the Box Clever Group Pension Scheme ("the Scheme"). The companies which are the subject of the DP's determination are the Applicants in the reference and are referred to in this decision as the "Targets". Box Clever Trustees Limited, the Trustee of the Scheme ("the Trustee"), has been joined to the reference as an interested party.

2. The Regulator's case for an FSD is based on the Targets' involvement in a Joint Venture known as Box Clever (the "Joint Venture" or "Box Clever") which existed between 1999 and 2003. The basic history of the Joint Venture, which is not in dispute, can be summarised as follows:

(1) Box Clever was established in 1999-2000 when the Granada group of companies (now part of the ITV group) agreed to combine its TV rental business with the TV rental business of its competitor, the Thorn group.

(2) Granada and Thorn each sold their respective rental businesses to the newly-created Box Clever group of companies, which was owned 50-50 by Granada and Thorn.

(3) The transaction was agreed in 1999 and completed in June 2000.

(4) The purchase price payable by Box Clever for the rental businesses it acquired was £980 million, of which £600 million was payable to Granada and £380 million was payable to Thorn.

(5) The purchase was funded by Box Clever borrowing £860 million from Westdeutsche Landesbank ("WestLB"); the loan was secured on the Box Clever group's assets. Using the loan monies, (simplifying somewhat) Box Clever paid approximately £530 million to Granada and the rest to Thorn in respect of the purchase price. The balance of the purchase price was left outstanding in the form of loan notes. Neither Granada nor Thorn was liable for the monies lent by WestLB, the borrower being Box Clever.

(6) From June 2000, Box Clever operated the combined rental business.

(7) In October 2001, Box Clever established the Scheme to provide pension benefits for its employees. The Box Clever companies (and not Granada or Thorn) were the employers of the Scheme and were liable to fund it.

(8) Unfortunately, the Box Clever business did not prosper; it fell behind with the repayments to WestLB and ended up deeply insolvent. During September-November 2003, WestLB appointed administrative receivers ("the Administrative Receivers") over the principal Box Clever operating companies.

(9) Thereafter, the Administrative Receivers took over the Box Clever business and sold it. All the proceeds of sale went to WestLB as secured lender.

(10) Neither Granada nor Thorn had anything further to do with the Box Clever business after the Administrative Receivers were appointed in 2003.

(11) According to figures provided by the Trustee, at the time of the Administrative Receiverships, the Scheme had a funding deficit of some £25 million on a gilts-matching basis, which Box Clever was unable to meet due to its insolvency. The reported deficit has since grown to around £115 million.

3. Following the failure of the Joint Venture, the Scheme was closed to new accruals in December 2003 (but not wound up) and discussions and negotiations took place from 2004 onwards between the Trustee and the ITV group as to whether ITV would be prepared for ex-Granada group members of the Scheme to be transferred back into what had been the Granada Pension Scheme (now the ITV Pension Scheme). Similar but less protracted discussions took place with Thorn.

4. These proposals as regards Granada became conditional upon the Trustee withdrawing any request to the Regulator for the issue of an FSD and the Trustee supporting any application that ITV might make to the Regulator for a "clearance statement" under s 42 and s 46 of PA 2004 in respect of the Joint Venture (explained below).

5. Negotiations as to the terms of any such transfer continued intermittently until December 2008, when ITV replaced previous offers with successive, diminishing offers instead to augment ex-Granada members' benefits that had been retained in the ITV Scheme. This was not accepted, and ITV withdrew from negotiations entirely in October 2009.

6. On 17 November 2009 ITV applied (on behalf of itself and many other companies within the ITV group, including all the Targets) for clearance statements under ss 42 and 46 of PA 2004. If granted, such clearance statements would have bound the Regulator to refrain from exercising its powers under ss 38 or 43 of PA 2004. This clearance application by ITV was refused in March 2010. ITV's application for clearance was modelled on an application for clearance that had been made by Granada's partner in the Joint Venture (by then called the Carmelite group) in 2008. That application for clearance had also not resulted in the grant of any clearance statement, but had resulted in a letter of comfort dated 25 February 2009 being issued by the Regulator to Carmelite that it would not pursue an FSD against them. That letter was issued to Carmelite on the basis of a view then held by the Regulator as to the legal effect of the appointment of an administrative receiver on its jurisdiction to issue an

FSD. The Regulator subsequently concluded that that view was incorrect. The Regulator has not pursued the Carmelite group for an FSD.

7. Further to the refusal of the Regulator to grant ITV and its subsidiaries clearance statements in respect of their involvement in the Box Clever Joint Venture, ITV made detailed representations to the Regulator as to why ITV considered that no FSD should be issued.

8. Nevertheless, the Regulator carried out an investigation which in due course led it to seek an FSD against the Targets. Pursuant to s 43(2) of PA 2004 it chose 31 December 2009 as the "relevant time" or "look-back date" with the result that in accordance with the provisions of s 43(9) of PA 2004 and reg 5 of the Pensions Regulator (Financial Support etc) Regulations 2005 (S.I. 2005/2188) as amended by the Pensions Regulator (Miscellaneous Amendment) Regulations 2009 (S.I. 2009/617), reg 2(2), as then in force, any determination to issue an FSD had to be made no later than 31 December 2011.

9. On 30 September 2011 the Regulator issued warning notices to the Targets. Following representations by the Targets the DP made a determination to issue an FSD to the Targets on 21 December 2011.

10. The basis for the DP's conclusion that it was reasonable to issue an FSD to the Targets was summarised by it at [168] of its statement of reasons as follows:

> "… it is our view that it would be reasonable to issue FSDs to the Targets and to require them to secure that financial support is put in place for the Scheme, within six months of the issue of the FSDs. The factors that have weighed most heavily with us are the value of benefits received by the Targets from the Employers and the Targets' relationship with those Employers. Overall it seems to us that this is a case where the Scheme's principal employer, BCT, was set up by the Granada and Thorn groups as part of a transaction that aimed to extract value from the consumer rental businesses of those groups, but leave them able to share in any future profit. A requirement of that transaction was that a pension scheme be set up for transferring employees; no value could have been extracted without this. Valuable financial benefits were received by the Targets, while the structure used to obtain them required BCT to borrow £860m from West LB, left all of BCT's assets charged to secure that borrowing, and left the Scheme with a weak employer as a result. It is also relevant that this borrowing was not secured on any assets of Granada or Thorn group companies, insulating them from financial difficulties of BCT. We do not find misconduct on the part of the Targets, but consider the issue of FSDs to be an appropriate and reasonable response to the events of 1999 to 2003 in relation to BCT and the Scheme."

11. The Regulator and the Trustee contend in these proceedings that the Targets were "connected" with or an "associate" of the employer in relation to the Scheme pursuant to s 43(6) of PA 2004 and that it is reasonable for an FSD to be issued to them, as permitted by s 43(5) of that Act, having regard in particular to the approximately £530 million which Granada received upon the transfer of its rental business to Box Clever in 1999-2000.

12. The Targets contend that there is no jurisdiction to issue an FSD in this case for the following principal reasons:

(1) they deny that they were *"connected"* or *"associated"* at the relevant time of 31 December 2009;

5 (2) the legislation is not retrospective and there is no power to issue an FSD in circumstances where, as in this case, all the facts that fall to be considered in any assessment of reasonableness relate to events which occurred before PA 2004 came into force; and

(3) the difference in treatment between the Targets and Carmelite is
10 discriminatory and that discrimination deprives the Regulator of the jurisdiction it would otherwise have to issue an FSD against Granada.

13. The Targets also contend that if they do not succeed on their challenges to the Regulator's jurisdiction, it would not be reasonable to issue an FSD to them in any event.

15 **II. APPLICABLE LEGISLATION**

The Regulator

14. The Regulator is a statutory body created by s 1 PA 2004. Section 5(1) PA 2004 sets out the statutory objectives prescribed for the Regulator which, so far as relevant, are as follows:

20 "(a) to protect the benefits under occupational pension schemes of, or in respect of, members of such schemes …

(c) to reduce the risk of situations arising which may lead to compensation being payable from the Pension Protection Fund …"

15. These objectives are reinforced by the provisions of s 100 PA 2004 which so far
25 as relevant provide:

"(1) The Regulator must have regard to the matters mentioned in subsection (2) –

(a) when determining whether to exercise a regulatory function … and

(b) when exercising the regulatory function in question.

30 (2) Those matters are –

(a) the interests of the generality of the members of the scheme to which the exercise of the function relates, and

(b) the interests of such persons as appear to the Regulator to be directly affected by the exercise"

16. It is common ground that in addition to the Targets the Trustee will be directly affected by the exercise of the power to issue an FSD by virtue of their office: see on this point *Trustees of the Lehman Brothers Pension Scheme v The Pensions Regulator and others* [2013] 4 All ER 744 at paragraph 69. Thus, while acting in furtherance of its statutory objectives under s 5 PA 2004, the Regulator has in this case had to take into account both (a) the interests of the generality of the members of the Scheme; and (b) the interests of the Targets and of the Trustee.

Financial Support Directions

17. The circumstances in which an FSD may be issued by the Regulator are set out in s 43 PA 2004 which at the time this regulatory action commenced provided as follows:

> "43. (1) This section applies in relation to an occupational pension scheme other than—
>
> (a) a money purchase scheme, or
>
> (b) a prescribed scheme or a scheme of a prescribed description.
>
> (2) The Regulator may issue a financial support direction under this section in relation to such a scheme if the Regulator is of the opinion that the employer in relation to the scheme—
>
> (a) is a service company, or
>
> (b) is insufficiently resourced,
>
> at a time determined by the Regulator which falls within subsection (9) ("the relevant time").
>
> (3) A financial support direction in relation to a scheme is a direction which requires the person or persons to whom it is issued to secure—
>
> (a) that financial support for the scheme is put in place within the period specified in the direction,
>
> (b) that thereafter that financial support or other financial support remains in place while the scheme is in existence, and
>
> (c) that the Regulator is notified in writing of prescribed events in respect of the financial support as soon as reasonably practicable after the event occurs.
>
> (4) A financial support direction in relation to a scheme may be issued to one or more persons.
>
> (5) But the Regulator may issue such a direction to a person only if—
>
> (a) the person is at the relevant time a person falling within subsection (6), and
>
> (b) the Regulator is of the opinion that it is reasonable to impose the requirements of the direction on that person.
>
> (6) A person falls within this subsection if the person is—
>
> (a) the employer in relation to the scheme,

(b) an individual who—

(i) is an associate of an individual who is the employer, but

(ii) is not an associate of that individual by reason only of being employed by him, or

(c) a person, other than an individual, who is connected with or an associate of the employer.

(7) The Regulator, when deciding for the purposes of subsection (5)(b) whether it is reasonable to impose the requirements of a financial support direction on a particular person, must have regard to such matters as the Regulator considers relevant including, where relevant, the following matters—

(a) the relationship which the person has or has had with the employer (including, where the employer is a company within the meaning of subsection (11) of section 435 of the Insolvency Act 1986 (c. 45), whether the person has or has had control of the employer within the meaning of subsection (10) of that section),

(b) in the case of a person falling within subsection (6)(b) or (c), the value of any benefits received directly or indirectly by that person from the employer,

(c) any connection or involvement which the person has or has had with the scheme,

(d) the financial circumstances of the person, and

(e) such other matters as may be prescribed.

(8) A financial support direction must identify all the persons to whom the direction is issued.

(9) A time falls within this subsection if it is a time which falls within a prescribed period which ends with the determination by the Regulator to exercise the power to issue the financial support direction in question.

(10) For the purposes of subsection (3), a scheme is in existence until it is wound up.

(11) No duty to which a person is subject is to be regarded as contravened merely because of any information or opinion contained in a notice given by virtue of subsection (3)(c)."

18. If an FSD is issued, s 45 PA 2004 requires a target to propose financial support for the scheme. Under s 45(2) the arrangements can involve:

(1) all the companies in the employer's group of companies being jointly and severally liable for "the whole or part of the employer's pension liabilities in relation to the scheme";

(2) the holding company of the employer's group being liable for "the whole or part of the employer's pension liabilities in relation to the scheme"; or

(3) any other legally enforceable agreement by which "additional financial resources are provided to the scheme".

19. We are not concerned in these proceedings as to the form or quantum of any financial support to be provided pursuant to s 45 PA 2004 were we to determine that an FSD should be issued to the Targets. That is a matter to be determined later following negotiations between the parties within the framework of s 45 PA 2004 and the other relevant provisions of that Act. However, the Targets have raised a number of arguments in the context of the issue as to whether it is reasonable to issue an FSD in this case which might also be relevant to the question of the quantum of any financial support that may be directed. We deal with those arguments in the context of our consideration of the question of reasonableness.

20. It is common ground that the Scheme is an occupational pension scheme and that the requirements of s 43(1) are met in this case. As mentioned at [8] above, in this case the Regulator determined that the "look back" period would end on 31 December 2009. As a consequence, that date is the "relevant time" for the purpose of establishing whether the requirements of s 43(2) and s 43(6) are met in this case. It is common ground that the requirements of s 43(2) (b) are also met in that the Scheme was "insufficiently resourced" on 31 December 2009.

21. The dispute between the parties as regards the requirements of s 43 is whether any of the Targets were on 31 December 2009 "connected with or an associate of" one of the employers of the Scheme for the purposes of s 43(6)(c) and whether it is reasonable to impose the requirements of an FSD on the Targets, as required by s 43(5)(b), having taken account of the matters set out at s 43(7). In that regard, it should be noted that no matters have been prescribed pursuant to s 43(7)(e).

22. The Targets do not seek to argue that there should be any differentiation between the Targets as to whether the FSD, if made, should apply to some rather than all of the Targets. We therefore proceed on the basis that there is nothing to distinguish between them in terms of their relationship with the employers of the Scheme or in terms of the circumstances which make it either reasonable or unreasonable to issue an FSD against them. Therefore, if we were to direct that an FSD be issued, it would be issued to all of the Targets and if we were to determine that it would not be reasonable to issue an FSD that would be a decision which was applicable to all of the Targets.

23. Section 51 PA 2004 contains provisions which interpret certain of the terms used in sections 43 to 50. In relation to the question whether a person is "connected with or an associate of" an employer for the purposes of s 43(6)(c), s 51(3) so far as relevant provides:

> "(3) For the purposes of those sections—
>
> (a) section 249 of the Insolvency Act 1986 (c. 45) (connected persons) applies as it applies for the purposes of any provision of the first Group of Parts of that Act,

(b) section 435 of that Act (associated persons) applies as it applies for the purposes of that Act, and

(c) …"

24. The relevant definition for the purposes of these references is that of "associated persons" in s 435 of the Insolvency Act 1986. We set out that provision later when considering the Targets' contentions in relation to the requirements of s 43(6)(c).

25. Section 46 of PA 2004 makes provision for the Regulator to issue a clearance statement in response to an application that the conditions set out in s 43(2) or (7) are not met in relation to any particular scheme as follows:

"(1) An application may be made to the Regulator under this section for the issue of a clearance statement within paragraph (a), (b) or (c) of subsection (2) in relation to circumstances described in the application and relating to an occupational pension scheme.

(2) A clearance statement is a statement, made by the Regulator, that in its opinion in the circumstances described in the application–

(a) the employer in relation to the scheme would not be a service company for the purposes of section 43,

(b) the employer in relation to the scheme would not be insufficiently resourced for the purposes of that section, or

(c) it would not be reasonable to impose the requirements of a financial support direction, in relation to the scheme, on the applicant.

(3) Where an application is made under this section, the Regulator–

(a) may request further information from the applicant;

(b) may invite the applicant to amend the application to modify the circumstances described.

(4) Where an application is made under this section, the Regulator must as soon as reasonably practicable–

(a) determine whether to issue the clearance statement, and

(b) where it determines to do so, issue the statement.

(5) A clearance statement issued under this section binds the Regulator in relation to the exercise of the power to issue a financial support direction under section 43 in relation to the scheme to the applicant unless–

(a) the circumstances in relation to which the exercise of the power under that section arises are not the same as the circumstances described in the application, and

(b) the difference in those circumstances is material to the exercise of the power."

26. It is apparent from the terms of this provision that there is nothing to prevent an application for a clearance statement to the effect that it would not be reasonable to impose an FSD in consequence of a transaction that had occurred prior to the coming into force of PA 2004. Clearly, however, there would have been no opportunity before the provision came into force to apply for clearance before such a transaction was effected and make any modifications to meet any concern the Regulator may have had before the transaction was completed.

27. This is the first case that will be the subject of a judicial decision on whether a FSD should be directed. We were referred to the three previous determinations by the DP to issue an FSD, namely *Sea Containers* (2007), *Nortel* (2010) and *Lehman Brothers* (2010). Aside from the fact that all of those determinations were administrative rather than judicial decisions and therefore have no precedent value, all three cases involved global groups which operated on business lines rather than by reference to legal entities and where each group's finances were inextricably linked and operated effectively as one economic entity. The Targets were therefore right to contend that these cases were very different to this case. However, they sought to do so on the basis that they were paradigm examples of the type of situation with which s 43 was intended to deal, in contrast to the present case. We do not accept that these cases are of any assistance in demonstrating as a matter of principle the kind of circumstances in which it will be reasonable to expect that an FSD would be issued or that the circumstances of this case are far removed from the kind of case which section 43 was intended to embrace. As will become apparent later, in our view the question of reasonableness must be carefully considered in each case in the light of all the relevant circumstances and previous decisions are likely to be of limited value. We have therefore not derived any assistance from the application of s 43 in any of the three cases referred to above.

Other provisions of PA 2004

28. Certain provisions in the PA 2004 relating to the PPF are relevant in the context of the Targets' contentions regarding the conduct of the Trustee in delaying triggering an assessment period for the Scheme to be admitted to the Pension Protection Fund until 2014. It is not necessary for us to set out the relevant provisions in full, but we refer to them later where necessary in the context of considering the Targets' contentions on that issue.

Role of the Tribunal

29. Section 96 (3) PA 2004 provides that the determination which is the subject matter of a determination notice (in this case the determination by the DP to issue an FSD to the Targets) may be referred to this Tribunal by any person to whom the determination notice is given (in this case the Targets) and any other person who appears to the Tribunal to be directly affected by the determination. As mentioned

above, the Trustee falls into the latter category and has been joined as an interested party to the references pursuant to the Tribunal's rules of procedure.

30. According to s 103 (3) PA 2004 on such a reference the Tribunal may consider any evidence relating to the subject matter of the reference, whether or not it was available to the Regulator at the material time. Section 103 (4) provides that on a reference, the Tribunal must determine what (if any) is the appropriate action for the Regulator to take in relation to the matter referred to it.

31. In this case, the matter referred is whether an FSD should be issued to the Targets. As this Tribunal made clear in *Re Bonas Group Pension Scheme* [2011] Pens. LR 109 the basis of the Tribunal's jurisdiction is that it considers the matters in dispute *de novo* rather than as an appeal. Warren J said at [37] of that decision:

> "There is nothing in these provisions, or elsewhere in PA 2004, which constrains the Tribunal's approach to its function in the way that an appellate court usually feels itself constrained on an appeal, whether the appeal is by way of review or rehearing… (both of which terms have led to many pages of case reports). Nor is there anything in any other statute which has been brought to my attention or in the Upper Tribunal Rules which does so…".

32. Accordingly, once a reference has been made the Tribunal's function is to provide the final stage in the regulatory process to determine what is the appropriate action for the Regulator to take, having considered all the evidence relating to the subject matter of the reference. In effect, it stands in the shoes of the DP and therefore in this case, must decide whether it is appropriate for the Regulator to issue an FSD. Having made that determination, as provided by s 103 (5) PA 2004, the Tribunal must remit the matter to the Regulator with such directions as it considers appropriate for giving effect to its determination which, by virtue of s 103 (6) may either confirm, vary, or revoke the Regulator's determination or substitute a different determination. Section 103 (7) provides that the Regulator must act in accordance with the determination of, and the directions given by, the Tribunal.

33. It is well established in references of financial services cases in this Tribunal that the burden of proof lies with the Regulator and the standard of proof to be applied is the ordinary standard on the balance of probability, namely whether the alleged events more probably occurred than not.

III. RELEVANT ENTITIES

34. Before turning to the detailed evidence, it is helpful by way of background to outline the principal entities involved in the Joint Venture structure.

35. We attach as an Annex a basic structure chart ("the Chart") showing the corporate structure put in place below the two 50% shareholders in the Joint Venture. We refer in this decision to Granada and Thorn in their capacity as shareholders in the Joint Venture collectively as the "Shareholders".

The joint venture parent companies: Granada and Thorn

36. On the ITV/Granada side, ITV plc and four of its subsidiaries, namely Granada UK Rental and Retail Limited ("Rental & Retail"), Granada Media Limited ("Media"), Granada Group Limited ("GGL") and Granada Limited ("GL") are the five companies to whom the DP issued the determination notice on 21 December 2011 deciding that an FSD should be issued to each of them pursuant to s 43 PA 2004.

37. ITV plc was formed on 2 April 2004 and became the parent company of the Granada group at that time. Before the formation of the Joint Venture, on the Granada side, the ultimate parent company was GL, which in turn owned GGL, which in turn owned Media, which in turn owned Rental & Retail. Below this structure, Rental & Retail owned UK Consumer Electronics Limited ("Consumer Electronics", shown as "UKCE" on the Chart) which (indirectly) owned the company shown as "Telebank" on the Chart (legal name Telebank Television Rentals Limited).

38. Granada reorganised and consolidated its rental businesses within or under Consumer Electronics, transferring relevant staff employed by Rental & Retail prior to the establishment of the Joint Venture. As can be seen from the Chart, as a result of various corporate reorganisations within the Joint Venture ownership of Consumer Electronics was transferred further down the corporate structure.

39. On the Thorn side, the Principal Finance Group of the investment bank Nomura had acquired the Thorn group in June 1998. At the time of the establishment of the Joint Venture, Nomura owned Rental Holding Company Ltd ("RHC"), which in turn owned Thorn Ltd, which in turn owned Thorn UK Ltd (later renamed TUK Holdings Limited and shown on the Chart as "TUK"). TUK owned, inter-alia, Endeva Service Limited (shown as "Endeva" on the Chart).

40. Nomura had undertaken a securitisation of the revenue stream of Thorn's rentals business in June 1999, creating a debt within the business of some £309 million.

41. On 27 March 2002 Nomura transferred RHC and the remaining Thorn group to a private equity firm, Terra Firma, so that Nomura had ceased to be associated with the Joint Venture from that time. At some point after the failure of the Joint Venture, RHC ceased to be associated with Terra Firma. Its parent company became Carmelite Capital Group Limited, which effectively became the other parent to the Joint Venture and is referred to in this decision as "Carmelite".

42. On the Granada side, the principal decision-maker in relation to the establishment and running of the Joint Venture was Charles Allen, the Chief Executive of the Granada Group and on the Thorn side it was Guy Hands, the head of Nomura's Principal Finance Group.

The Box Clever entities

43. At the top of the Joint Venture structure was a newly formed entity which became known as Box Clever Technology Limited (shown on the Chart and referred to in this decision as "BxC Tech") the shares in which were acquired on the establishment of the Joint Venture as to 50% by ITV/Granada and 50% by the former Thorn group, subsequently known as Carmelite. An intermediate holding company became the owner of the companies which operated the rental businesses of Granada and Thorn and which were acquired from Rental & Retail and RHC respectively. That company was Box Clever Finance Limited, an indirect subsidiary of BxC Tech, and is shown on the Chart and referred to in this decision as "BxC Finance".

44. The immediate parent company of BxC Finance became the owner of three companies which operated the rental businesses of Box Clever. That company was Box Clever Holdings Limited and is shown on the Chart and referred to in this decision as "BxC Holdings".

45. As regards the senior management of the Joint Venture, a Shareholders Agreement dated 28 June 2000 entered into between Rental & Retail, RHC and BxC Tech regulated the relationship between the Joint Venture parties. The shares in BxC Tech issued to Rental & Retail were designated as A Shares and those issued to RHC were designated as B Shares. The A Shares carried the right to appoint two persons as A Directors of BxC Tech and the B Shares carried the right to appoint two persons as B Directors of that company.

46. Charles Allen and the Finance Director of Granada, Henry Staunton, were appointed as the A Directors and Guy Hands and a Nomura employee who was also a director of Thorn, Mark Tagliaferri, were appointed as the B Directors. Pursuant to the terms of the Shareholders Agreement, major decisions relating to the Joint Venture could only be taken with the consent of at least one A Director and one B Director. That included, according to the terms of clause 4.3 (k) of the Shareholders Agreement, the "establishment of, or material amendment to, any pension scheme for employees of the [Joint Venture] … except in accordance with rules approved by the A Shareholder and the B Shareholder."

47. Mr Laurence Cooklin, the former Chief Executive of Thorn UK, was appointed as the non-executive chairman of BxC Tech but it was specifically provided that he had no casting vote. Hence the Board would be deadlocked if the A Directors and the B Directors could not agree on a major matter.

48. Mr Roger Mavity, formerly a director of Rental & Retail, was appointed as Group Chief Executive of the Joint Venture and Mr Mike Neal, also a former director of Rental & Retail, as its finance director. Both were also appointed to the Board of BxC Tech. There were two further non-executive directors of BxC Tech, namely Mr Neil Chisman, from the Thorn side and Mr Graham Parrott, the Commercial Director of Granada and a director of Rental & Retail, who was also Chairman of the trustees of the Granada Pension Scheme, from the Granada side.

The employers in relation to the Scheme

49. The Principal Employer under the Scheme is BxC Tech, although it never had any employees and therefore never made any contributions into the Scheme. There were five participating employers, all of which have been in administrative receivership since 5 the last quarter of 2003. They are:

(1) Consumer Electronics which ran the rental businesses' shops and provided administrative services;

(2) Endeva Fulfilment Limited (shown on the Chart as "Fulfilment") which provided logistical staff and management of the movement and collection and 10 installation of the rental products;

(3) Endeva which employed the engineers and carried out equipment repairs;

(4) Telebank which operated a coin operated TV rental business and employed meter collectors and administrative staff; and

(5) TUK which provided cash collection and debt management services.

15 50. Endeva, Fulfilment and Telebank have been referred to collectively in these proceedings as the "Trio" because one of the arguments raised by the Targets that they, the Targets, are not associated with those three companies applies only to those companies but not the other participating employers. In this decision we refer to the Trio, UK Consumer Electronics and TUK collectively as the "Employers".

20 **The pension schemes**

51. Prior to the establishment of the Joint Venture, employees working in the respective rentals businesses of Granada and Thorn would have been members of either the Granada Pension Scheme or the Thorn Pension Fund respectively.

52. The Granada Pension Scheme was an occupational pension scheme which had 25 both a final salary and a money purchase section. Those who were in the final salary section were entitled to a pension at a normal retirement age of 60 calculated on the basis of $1/50^{th}$ of final salary for each year of service. Pensions benefited by an increase each year of an amount equal to the increase in the Retail Price Index, subject to a maximum of 5%. The Trustee of the Granada Pension Scheme was Granada Trust 30 Corporation Limited, whose Chairman at the relevant time was Mr Graham Parrott.

53. The Thorn Pension Fund also had both final salary and money purchase sections. Those who were in the final salary section were entitled to a pension at a normal retirement age of 65 calculated on the basis of $1/60^{th}$ of final salary for each year of service. Pensions benefited by an increase each year of an amount equal to the increase 35 in the Retail Price index, subject to a maximum of 5%. The trustee of the Thorn Pension Fund was Thorn Pensions Trustees Limited, whose Chairman at the relevant time was Mr Robin Charlton.

54. We refer to the Granada Pension Scheme and the Thorn Pension Fund together as the "Legacy Schemes".

55. The Contribution Agreement dated 17 December 1999 ("the Contribution Agreement") which set out the steps to be taken by the parties to establish the Joint Venture made provision (in Schedule 10 of that Agreement) for the establishment of a new stand-alone pension scheme for the Joint Venture. At the time when the Contribution Agreement was concluded, it was envisaged that the new scheme would provide only money purchase benefits and that Granada and Thorn were to agree to the level of employer and employee contributions.

56. There were transitional provisions permitting those who became employees of the Joint Venture to continue to participate in the relevant Legacy Scheme for a period of six months after the establishment of the Joint Venture, after which point their historic liabilities would be transferred to the new scheme and the relevant Legacy Scheme would make a bulk transfer payment to the new scheme.

57. Following detailed discussions about the establishment of the Scheme and its terms, it was ultimately agreed that the Scheme would provide defined benefits based on final salary to those who enjoyed those benefits in the relevant Legacy Scheme. We make findings in further detail as to the arrangements for the establishment of the Scheme and the discussions regarding the proposed bulk transfer payments, which ultimately did not proceed, later in this decision.

58. The Scheme had a single corporate trustee, Box Clever Trustees Limited ("the Trustee") which was incorporated in April 2001. The chairman of the Board of Directors of the Trustee was Mr Alan Herbert, who has remained in that position to the present day. There have been other directors of the Trustee during the period with which we are concerned, including directors nominated by the members of the Scheme and Mr Nicholas Wakelam, a representative of the employers, who was director until 16 October 2017.

59. The Scheme has had a number of advisers during its existence. The actuary was with Mercer's, being first Ms Justine Pegg from 7 June 2001 to August 2003 and then by Mr Akash Rooprai. The legal advisers were Sacker & Partners, represented by Ms Julia Miller until 29 July 2002 and thereafter Ms Pauline Sibbitt. The administrators of the Scheme were Aon.

IV THE EVIDENCE

Factual witnesses

60. Three factual witnesses were called by the Trustee in support of its case for the issue of an FSD against the Targets namely Mr Alan Herbert, Mr Paul Thompson and Mr Nicholas Wakelam.

61. Mr Herbert, as mentioned above, has been the chairman of the board of directors of the Trustee since the establishment of the Scheme. He is a fellow of the Pensions Management Institute and worked as a pensions manager for 37 years. After retiring in 1997, he took on various appointments as an independent pension trustee, before he became chairman of the Board of Directors of the Trustee in June 2001. He was also

Chairman of the Advisory Council of the Occupational Pensions Defence Union for 10 years.

62. Mr Herbert's evidence covered the entire history of the Scheme since its establishment. His evidence therefore covered the decision to establish the Scheme with a defined benefit section, the ultimately inconclusive discussions for the transfer of past service benefits from the Legacy Schemes into the Scheme and the decision to open the scheme for future accruals and to grant Continuous Service Benefits, notwithstanding the failure to agree transfer values from the Legacy Schemes, through the Top-Up Arrangement described in more detail below. His evidence also covered the operation of the scheme after the appointment of the Administrative Receivers over the Joint Venture operating companies, and in particular the decision to close the scheme to further accrual but not to wind it up and the attempts led by Mr Herbert to persuade the Shareholders to support the Scheme after the receivership.

63. Mr Herbert clearly has considerable expertise and experience of pensions matters and has been a dedicated and conscientious chairman of the Trustee doing his very best to promote the interests of the members of the Scheme. His memory of the key events was generally very clear and we found him to be a careful and honest witness doing his best to assist the Tribunal. Bearing in mind the lapse of time since the various events which has inevitably meant that the recollections of the factual witnesses must be treated with some caution, we have primarily relied upon the documentary evidence in making our findings as to the establishment and operation of the Scheme but we have derived some assistance from Mr Herbert's evidence.

64. Mr Thompson was the Company Secretary of the Trustee from 14 November 2003 until 30 June 2017. Mr Thompson is a former Fellow of the Association of Certified and Corporate Accountants, having retired from his Fellowship on 8 December 2014. Mr Thompson has had many years' experience, starting in the 1970s, in the "brown goods" market, a term which includes Hi-Fi equipment, televisions and video players. He joined the Granada Group in 1986 and became financial controller for Rental & Retail, reporting to the finance director, Mr Neal. Mr Thompson's role included responsibility for the financial accounts department, which produced monthly financial statements, comparing actual results against budget and forecast.

65. Upon the formation of the Joint Venture in June 2000, Mr Thompson's employment was transferred to Consumer Electronics. He had the same core responsibilities as before, but his job title was now Financial Services Director with responsibility for the accounting function (excluding management accounting) of the enlarged rental division following the establishment of the Joint Venture, again reporting to Mr Neal who was now the Finance Director of the Joint Venture. Mr Thompson's evidence, which was not challenged in this respect, was that by virtue of his role he was in a position to know about and understand the management decisions which were being taken in relation to the Joint Venture but was not a director of any of the operating companies and was not directly involved in the key Joint Venture structural decisions that were made.

66. Mr Thompson retired from his finance role in July 2002 but remained as Box Clever's pensions manager in relation to the Scheme.

67. Mr Thompson's evidence covered the business model of Granada's rental business before the Joint Venture and what he perceived to be the decline of that business in the face of there being less demand from customers to rent rather than buy brown goods outright. Mr Thompson also gave evidence regarding the extent to which the Shareholders exercised control over the Joint Venture, as well as evidence regarding his role as pensions manager in which capacity he was involved in the negotiation of the announcement of the Top-Up Arrangement.

68. Mr Thompson was also a careful and honest witness doing his best to assist the Tribunal. As was the case with Mr Herbert's evidence, we have treated Mr Thompson's oral evidence with caution bearing in mind the lapse of time since the events in question and we have placed more weight on the relevant contemporaneous documents. We have therefore derived limited assistance from his evidence.

69. Mr Wakelam was a director of the Trustee from the inception of the Scheme in 2001 until 16 October 2017. Mr Wakelam qualified as a Chartered Management Accountant and joined Thorn in 1987, becoming Finance Director of TUK in 1998, reporting to Mr Cooklin who was at that time Chief Executive of TUK. Mr Wakelam remained Finance Director of the former Thorn side of the business following the establishment of the Joint Venture for a short while and then became Finance Director of Endeva, which became the repairs and distribution business of the Joint Venture. He retired in March 2004.

70. Mr Wakelam's evidence covered what he perceived to be the "terminal decline" of the rental business. He also gave evidence as to the degree of control exercised by the Shareholders over the running of the Joint Venture and the Scheme and what he perceived to be the decline of the Joint Venture's business and the problems caused by the level of debt which it bore.

71. We have treated Mr Wakelam's evidence with caution, bearing in mind the lapse of time since the events in question, but because of Mr Wakelam's ongoing role as a director of the Trustee and his involvement in a number of the key decisions relating to the Scheme, we have placed some weight on his evidence in relation to those matters, particularly where that evidence is corroborated by documentary evidence.

72. The Targets did not call any witnesses to give evidence about the events leading up to the creation of the Joint Venture, the transfer of employees to the Joint Venture, the setting up of the Scheme or the operation of both the business of the Joint Venture and the Scheme.

73. Mr Hilliard submitted on behalf of the Trustee that in so far as the Targets sought to challenge any of the factual evidence put forward by the Trustee's witnesses, it was legitimate for adverse inferences to be drawn as a result of the Targets' failure to call any witnesses to support their position. Mr Hilliard relied on *Wisznieski v Central Manchester Health Authority* [1998] PIQR 324 which establishes the proposition that

if there is no credible explanation for a party not calling witness evidence on a particular issue, and evidence is adduced by the other party on the matter in question, adverse inferences may be drawn against the party failing to call a witness: see pages 339 to 340 of the judgment which was approved by the Supreme Court in *Prest v Petrodel Resources Ltd* [2013] 2 AC 415 at [44].

74. Mr Hilliard submits that there were a number of individuals associated with Granada and ITV who might have been called on behalf the Targets, for example Mr Allen, Mr Parrott and Mr Staunton as well as Mr James Tibbitts who still remains a director of Box Clever Technology Limited. Mr Hilliard submits that those individuals could have given evidence in relation to the Targets' control over the Joint Venture, the Targets' control over or in connection with the Scheme, whether the Targets agreed to the Scheme decisions about which they now complain and the Shareholders' knowledge of the risks of the Joint Venture. He submits that adverse inferences can and should be drawn from the Targets' failure to call these witnesses and consequently we should attach increased weight to the evidence of the Trustee's witnesses on these matters.

75. In our view it is not appropriate that we should draw such adverse inferences in this case. As we have indicated, the evidence of the Trustee's factual witnesses has been of limited assistance in the light of the long passage of time since the relevant events in question. We have made our findings primarily by reference to the documentary evidence and the inferences that we have drawn from that documentation. Therefore, whilst the evidence from the Trustee's factual witnesses has to a limited extent been useful in corroborating the inferences we have drawn from the documentary evidence, we have not given it any greater weight because of the absence of any witnesses of fact on behalf of the Targets.

76. Furthermore, as Mr Furness observed, these are regulatory proceedings in which the Regulator has the burden to make out its case and to obtain the necessary evidence for it to be able to do so. In order to assist it in that regard, s 72 PA 2004 gives the Regulator extensive powers to require any person to provide it with documents and information which will assist the Regulator in carrying out its statutory functions. The Regulator could have exercised these powers many years ago by seeking information from the individuals that Mr Hilliard referred to if it was felt that they could provide relevant evidence.

77. We are therefore satisfied the Targets have a credible explanation for why they have chosen not to call any factual witnesses. We cannot regard that decision as being a purely tactical one which should give cause for an adverse inference to be drawn in circumstances where the events in question took place many years ago and, as Mr Furness observed, the inherent fallibility of memory therefore comes into clear relief.

Expert witnesses – corporate finance issues

78. Both the Regulator and the Targets called expert witnesses to provide evidence on corporate finance issues.

79. The Regulator's expert on these issues was Mr Darren Redmayne. He qualified as a chartered accountant within what is now Deloitte's corporate recovery practice in 1998 and then worked for nine years at Close Brothers Corporate Finance Limited, advising on mergers, acquisitions, joint ventures and restructurings. In 2006, he spent six months on secondment to the Regulator, working on the Regulator's approach to the assessment of employer covenant in the context of corporate transactions. In 2008 he founded the UK operations of Lincoln International, providing specialist independent employer covenant advice and corporate finance advice, and as Chief Executive in the UK he had responsibility for, and led client advice in, both employer covenant assignments and wider corporate finance matters. He is now Chief Executive of Lincoln Pensions and a Senior Adviser to Lincoln International LLP where he acts as lead covenant adviser to a number of defined benefit pension schemes of leading UK companies.

80. The Targets' expert on these issues was Mr David Ashton. He is a Fellow of the Institute of Chartered Accountants in England and Wales, having qualified in 1973 with Arthur Andersen and becoming a partner in 1982. He retired from that firm in June 2002. In September 2002 he joined LECG, a consulting firm which was subsequently acquired by FTI Consulting, a global expert services firm specialising in litigation support and valuation where Mr Ashton is now a Senior Managing Director. He has extensive experience in the valuation of shares and businesses in a range of contexts and across different industries, including in shareholder disputes.

81. Mr Redmayne's report covered the following matters:

(1) the nature of the transaction connected with the creation of the Joint Venture (including a comparison between the transaction and an arm's length sale);

(2) the nature and significance of such due diligence and other advice as was carried out or received in connection with the set-up of the Joint Venture;

(3) the nature and significance of the price paid and of any valuation supporting the price paid by the Joint Venture for the businesses purchased;

(4) the risks associated with the Joint Venture (including the risks associated with the debt financing made available by WestLB), and what must have been known when to the participants about these risks;

(5) how the risks affected members of the Scheme;

(6) the reasons for the failure of the Joint Venture; and

(7) the financial, strategic or operational benefits that Granada enjoyed as a result of the creation of the Joint Venture.

82. Mr Ashton's report covered similar ground, although in relation to the valuation issue, he was asked specifically to provide an opinion on whether the amount paid by the Joint Venture for the Granada rental business overvalued it.

83. Mr Redmayne and Mr Ashton produced a joint statement, setting out the matters which were agreed and disagreed between them. This joint statement was followed by a number of supplementary reports dealing with certain of the matters which were not agreed. Amongst the matters which were agreed between experts were:

5 (1) the two underlying businesses had been in decline at the time of the creation of the Joint Venture in June 2000;

(2) the transaction creating the Joint Venture was not at arm's length as between Granada and Thorn on the one hand and the Joint Venture on the other and was a leveraged transaction using debt finance from WestLB;

10 (3) an offer of £450 million received by Granada in 1999 was one contemporaneous indication of the enterprise value of the Granada Rental Business on a stand-alone basis and neither expert was aware of any evidence that the person making the offer had any reason to consider synergies in anticipation of merging the Granada and Thorn Rental Businesses; and

15 (4) it is not possible now to produce a reliable, independent valuation of either the Granada Rental Business or any synergies through valuation methodologies.

84. There were many detailed points of disagreement in the joint statement. Of particular importance, was Mr Redmayne's opinion that an arm's length transaction would have been for considerably less than the £600 million price actually paid for the
20 Granada rental business and would have been significantly below the offer of £450 million for the Granada business on a stand-alone basis received as a result of an arm's length negotiation and the results of the due diligence undertaken. In contrast, Mr Ashton, although unable to support a positive valuation of £600 million, could not say that this figure was wrong, when account is taken of the value that should be attributed
25 to the synergies resulting from the merger of the two businesses.

85. As regards the due diligence undertaken in relation to the transaction, Mr Redmayne's view was that the scope of the due diligence performed was less than was and is typical for an arm's length transaction and was deficient in certain material areas whereas Mr Ashton was of the view that the due diligence performed was not materially
30 less and would have been typical for an arm's-length transaction at the time, with the exception of commercial due diligence, which was not necessary or appropriate in the circumstances of the transaction.

86. As regards the benefits received by the Targets from the establishment of the Joint Venture, Mr Redmayne's opinion was that it was appropriate to compare the price
35 received by the Targets to the value that would probably have been paid in practice by an independent third-party and that the difference should be regarded as a benefit (among others), whereas Mr Ashton approaches the matter from the perspective that there was no benefit where Granada had exchanged its existing asset (its rental business) for another asset (its share in the Joint Venture) for consideration.

40 87. We found both Mr Redmayne and Mr Ashton to be experienced and knowledgeable as regards their respective areas of expertise. Each party sought to question the objectivity of the other side's witness but we reject those criticisms. In our

view, both witnesses were mindful of their duty to the Tribunal and did their best to assist us.

88. As we discuss in more detail later, in assessing the question of reasonableness, and in particular the question of the benefits received by the Targets, we have placed limited reliance on the question of the valuation of the Granada rental business at the time of the transaction establishing the Joint Venture and accordingly we have found Mr Redmayne's evidence, based on his expertise in the corporate finance field, to be more relevant than that of Mr Ashton, whose expertise is predominantly in the field of valuation. Mr Railton submitted that we should treat Mr Redmayne's reliance on his market experience at the time of the Joint Venture transaction with caution, given that he had only been working at Close Brothers for a little over a year then. We reject that criticism; Mr Redmayne clearly has significant experience of corporate finance transactions over a number of years and his later experience would have informed his understanding of market practice at the time the Joint Venture was created. There was no evidence to suggest that market practice had changed to any significant extent from the time that Mr Redmayne commenced his employment with Close Brothers.

Expert witnesses – actuarial issues

89. Both the Trustee and the Targets called expert witnesses to provide evidence on actuarial issues.

90. The Targets' expert on these issues was Mr Ronald Bowie. He qualified as a Fellow of the Faculty of Actuaries in 1980 and has been a partner in the leading firm of Hymans Robertson since 1981 and the Senior Partner since 2002. For the whole of his career Mr Bowie has been actively involved in the provision of actuarial and related advice to companies and trustees in the management of occupational pension schemes. He is currently the immediate past President of the Institute and Faculty of Actuaries.

91. The Trustee's expert on these issues was Mr Nick Salter. He qualified as an actuary with Duncan C Fraser (later Mercer Fraser) and after nearly 11 years at that firm he joined Barnett Waddingham, a leading independent provider of actuarial, administration and pensions consultancy services, as a founding partner in 1989. He is currently Senior Partner of that firm. His work includes acting as Scheme Actuary and general consultant to a large number of significant occupational pension schemes. He is also a past President of the Institute and Faculty of Actuaries.

92. The actuarial evidence was relevant in the context of a number of criticisms by the Targets of the Trustee's conduct in the running of the Scheme after the Administrative Receivers were appointed.

93. In particular, the Targets criticise the decision of the Trustee to agree to what became known as the "Top Up Arrangement", whereby the Scheme would provide not only future service benefits from the date of its creation but also a "top up" consisting of final salary linkage on the past benefits left behind in the Legacy Schemes whereas, following the decision ultimately not to proceed with the bulk transfer arrangements, the rest of a member's pension would come from the Legacy Schemes.

94. The Targets also criticise what they perceive as delay on the Trustee's part in closing the Scheme after the Administrative Receivers were appointed, its decision not to wind up the Scheme because it wanted the Scheme to take advantage of the PPF when it came into existence and thereafter its delay in triggering a PPF assessment period.

95. Accordingly, the principal areas covered by actuarial experts' reports were:

(1) the deficits in the Scheme and their causes;

(2) the decision to adopt the Top-Up Arrangement;

(3) the Trustee's decision to close the Scheme and its timing; and

(4) the conduct of the Trustee in running the Scheme as a closed scheme and the postponement of its winding up.

96. Mr Bowie and Mr Salter produced a joint statement setting out the matters on which they agreed and disagreed.

97. Both experts agreed on the cost of the Top-Up Arrangement at the time it was negotiated in terms of its impact on the deficit in the Scheme and also as to the effects of later salary increases and that there was no requirement for the Scheme Actuary to provide further advice on the Top-Up Arrangement, over and above the advice given.

98. The experts disagreed on whether or not it had been reasonable for the Trustee to rely on the Joint Venture's guidance as to their salary increase policy when costing the Top-Up Arrangement. As regards the running of the Scheme after the Joint Venture entities went into receivership, the experts had some differing views on how the Scheme should have been managed, what events or risks might or might not have been foreseeable in late 2003 and what actuarial advice could or should have been obtained. The experts also differed as to whether it was reasonable from an actuarial perspective to allow the Scheme to have continued as long as it did, Mr Salter believing that it was reasonable and that it was a decision for the Trustee, to be reviewed from time to time while Mr Bowie believed that it was not reasonable given the risks identified.

99. We found both Mr Bowie and Mr Salter to be experienced and knowledgeable as regards their areas of expertise. Both witnesses were mindful of their duty to the Tribunal and did their best to assist us. However, as will become apparent later, we have found their evidence to be of limited value. In those instances where we have relied on the expert evidence, we have, for the reasons that we explain later, generally preferred the evidence of Mr Salter to that of Mr Bowie.

Documentary evidence

100. We received a large amount of documentary evidence, only a small proportion of which we were referred to at the hearing. As we have indicated, our findings of fact have been made primarily by reference to this documentary evidence, including evidence that was before us which we were not taken to.

V. SUMMARY OF THE ISSUES TO BE DETERMINED ON THESE REFERENCES

101. We now set out in further detail the issues which we must resolve in these proceedings. They fall into two categories; in the first category are issues raised by the Targets as to whether there is jurisdiction to issue an FSD in this case (the "Jurisdiction Issues") and in the second category is the application of the reasonableness test set out in s 43(7) PA 2004 (the "Reasonableness Issue").

Jurisdiction Issues

Lack of association

102. The first of the Jurisdiction Issues which we need to determine is whether the requirements of s 43(5) and s 43(6)(c) PA 2004 are satisfied in relation to the Targets, that is to say whether each of the Targets was connected with or an associate of the Employers as at the "look-back" date of 31 December 2009. According to s 51(3)(b) PA 2004, this issue turns on whether the Targets are taken as having control of the Employers within the meaning of s 435(10)(b) of the Insolvency Act 1986 because they were entitled to control the exercise of one third or more of the voting power at any general meeting of the Employers.

103. The issue of the existence of control was argued by Mr Moss QC for the Regulator and Mr Railton QC for the Targets. The Trustee adopted the Regulator's points and Mr Hilliard did not make separate submissions.

Retrospectivity

104. The second of the Jurisdiction Issues is whether the Regulator has jurisdiction to issue an FSD in the circumstances of this case where all the facts regarding the conduct of the Targets that fall to be considered in any assessment of reasonableness relate to events which occurred before s 43 PA 2004 came into force on 6 April 2005. This retrospectivity argument itself has two strands: whether on the proper construction of PA 2004 (bearing in mind if appropriate the presumption against retrospective effect) the Regulator can take into account events that occurred before PA 2004 came into force; and whether Article 1 Protocol 1 of the European Convention on Human Rights ("A1P1") is engaged here and, if it is and if further the legislation is to be interpreted as the Regulator contends, that requires a "special justification" failing which the Tribunal must read down the provisions pursuant to section 3 of the Human Rights Act 1998 so that they do not operate retrospectively.

Discriminatory treatment: the Carmelite point

105. The third of the Jurisdiction Issues relates to the decision of the Regulator not to pursue the other parent to the Joint Venture pursuant to s 43 PA 2004. It arises because the Regulator sent a comfort letter to Carmelite on 25 February 2009 stating that the connection and association of Carmelite ceased before the coming into force of PA 2004 and accordingly it was not able to issue an FSD to Carmelite or any companies in its group.

106. The comfort letter issued to Carmelite was based on what the Regulator now believes was a mistaken view of the law, namely that the appointment of the Administrative Receivers broke the chain of connection between the company at the top of the Joint Venture's corporate group and the Employers. By the time Granada requested a comfort letter, the Regulator had changed its mind and adopted the stance that it has maintained in this Tribunal, namely that the appointment of receivers does not mean that there is any change in the identity of the person who is entitled to exercise control of the voting power attached to the shares held by the company in receivership. The Regulator therefore refused to issue a comfort letter to Granada and has pursued these proceedings. The Targets argue that this difference in treatment is discriminatory and that the treatment of Carmelite deprives the Regulator of the jurisdiction it would otherwise have to issue an FSD against the Targets.

The absence of moral hazard

107. The final Jurisdiction Issue relates to the purposes of s 43 PA 2004. The Targets contend that for s 43 to be engaged, it is necessary to identify behaviour which is in some sense morally hazardous; that is, which engages the rationale of preventing employers or persons associated with them from organising their affairs so as to shift the burden of providing pensions to the PPF, and hence to levy payers. In this case, the Targets contend, a concern about moral hazard could only apply to conduct which occurred at a time when the PPF existed but all the conduct of the Targets which is relied on predated that time. Furthermore, they contend, at the time the Joint Venture was established, the intention was to provide a money purchase scheme which would have been outside the ambit of the regulatory regime. There was no question, therefore of the way in which the parents of the Joint Venture chose to organise their affairs unfairly or unreasonably benefiting them at the expense of pensioners.

108. The challenge to jurisdiction based on retrospectivity, the Carmelite point and the absence of moral hazard were argued by Lord Pannick QC on behalf of the Targets and by Mr Stallworthy QC on behalf of the Regulator. Again, the Trustee did not make separate submissions on these points but supported the submissions of the Regulator.

Reasonableness Issue

109. If the Targets fail on their arguments on jurisdiction, they contend that it is nevertheless unreasonable to impose an FSD on the Targets. By reference to the different factors referred to in s 43(7) PA 2004, the main issues that arise on the Reasonableness Issue are as follows.

The relationship between the Targets and Employers

110. The Regulator argues that the way that the Joint Venture was created and operated shows that there was a very close relationship between the Targets and the Employers from the inception of the Joint Venture until its demise. Further, the Regulator argues that the high leveraging of the business exposed the Joint Venture to considerable risks of failure, and hence a considerable risk that the Scheme would be insufficiently resourced because the business would be unable to service the very high

debt repayments if the business did not prosper as the Joint Venture parents hoped it would.

111. The Targets argue that the setting up of the Joint Venture predates any of the relevant companies becoming Employers and so cannot be part of the relationship between the Targets and the Employers for the purposes of s 43(7) PA 2004. They argue that the Regulator is wrong to say that the Joint Venture was set up in a way which created a risk that the Scheme would be underfunded. They rely on the fact that when the Joint Venture was set up, the intention was to create a defined contribution scheme. They also say that given that there is no basis for any criticism of the way that the Joint Venture was structured or operated, there is nothing about the relationship which points towards it being reasonable to issue an FSD.

The benefit received directly or indirectly by the Targets from the Employers

112. The Regulator argues that the consideration received by Granada from the Joint Venture for the rental business it transferred was very substantially greater than its stand-alone value, whether assessed by reference to its own or its own advisers' assessment of its business's value or assessed by reference to what might have been paid on an arms length transaction. Furthermore, the Regulator contends, the cash received by Granada for its rental business was in and of itself a very great benefit, being an immediate cash realisation of its long-term interest in a declining business.

113. The Regulator contends that these benefits were achieved against a background where the Joint Venture was subjected to increased and particularly significant risks as a result of the maximisation of leverage in the Joint Venture, no due diligence work of any kind having been done on behalf of the Joint Venture, and no commercial due diligence having been undertaken.

114. The Targets dispute that this is the correct way to address the question of benefit. They contend that the Joint Venture was a bona fide transaction undertaken in the belief that it would benefit from synergies and deliver considerable further value in the future to both parents. They contend that such belief was not an idle hope but was supported by the success both businesses had had in acquiring and merging businesses in the past, the structure adopted was a logical one, and the price paid was an appropriate one. They contend that the due diligence which was undertaken was extensive, appropriate in the circumstances, and involved an appropriate consideration of the risks of the transaction. They say there is no warrant for asserting that further due diligence would have changed the course of action. They also argue that even if there was some benefit to Granada, it could not be a benefit "from the employer" as required by s 43(7) because the Employers did not exist at the time the price for the business was agreed and paid.

Connection with the Scheme

115. The Regulator argues that Granada was closely involved in the major decisions setting up the Scheme and in the evolution of the benefits offered by the Scheme, as we describe later. The Targets contend that between the initial decision to approve the creation of the Scheme with a defined benefit section and the appointment of the

Administrative Receivers, there was no evidence of Granada being involved on any informed basis in decisions about the Scheme, in particular regarding the Top Up Arrangement.

Other Factors

116. In addition to the factors described above a number of other issues were identified as follows.

117. The points that the Targets raise in relation to the Jurisdiction Issues are relied on by the Targets as part of their submissions on reasonableness if they fail on the Jurisdiction Issues themselves.

118. The Targets also contend that they had no connection with the Scheme after the appointment of the Administrative Receivers and that the conduct of the Trustee in relation to the operation of the Scheme is a relevant factor. In that regard, they contend:

(1) The Targets ceased to have an economic interest in the Joint Venture after the appointment of the Administrative Receivers and all the liabilities accrued in the Scheme after that date were at the behest of the Administrative Receivers.

(2) There were avoidable delays in closing the Scheme to accrual after the appointment of the Administrative Receivers.

(3) The additional liabilities arising from pay rises after the appointment of the Administrative Receivers could easily have been avoided.

(4) No advice was sought about whether it was advisable to incorporate the Top-Up Arrangement into the rules of the Scheme in December 2003.

(5) Continuing to run the Scheme after 2003 was very risky and was highly likely to result in the large increase in the deficit that has in fact occurred.

(6) It was wrong not to put the Scheme into winding up soon after 2003 so as to take advantage of the anticipated creation of the PPF which has resulted in a large increase in the PPF’s exposure.

(7) There was no justification for not winding up the Scheme after 2003 and not triggering a PPF assessment period after April 2005.

119. Finally, the Targets contend that Granada has already provided a degree of financial support to the Scheme.

120. The issues relating to benefit were argued by Mr Railton QC for the Targets with the remaining points on reasonableness presented by Mr Furness QC for the Targets. For the Regulator, Mr Stallworthy QC argued the points arising from the creation of the Joint Venture and the operation of the business and Mr Hilliard QC argued the points arising from the operation of the Scheme.

V. JURISDICTION: ASSOCIATION OF THE TARGETS WITH THE EMPLOYERS

Introduction

121. As we said at [23] above, s 51 (3) PA 2004 points towards s 435 of the Insolvency Act 1986 for the definition of when one company is associated with another for the purposes of s 43 (6) PA 2004. Section 435 provides so far as relevant:

> "(1) For the purposes of this Act any question whether a person is an associate of another person is to be determined in accordance with the following provisions of this section (any provision that a person is an associate of another person being taken to mean that they are associates of each other).
>
> …
>
> (6) A company is an associate of another company—
>
> > (a) if the same person has control of both, or a person has control of one and persons who are his associates, or he and persons who are his associates, have control of the other, or
> >
> > (b) if a group of two or more persons has control of each company, and the groups either consist of the same persons or could be regarded as consisting of the same persons by treating (in one or more cases) a member of either group as replaced by a person of whom he is an associate.
>
> (7) A company is an associate of another person if that person has control of it or if that person and persons who are his associates together have control of it.
>
> …
>
> (10) For the purposes of this section a person is to be taken as having control of a company if—
>
> > (a) the directors of the company or of another company which has control of it (or any of them) are accustomed to act in accordance with his directions or instructions, or
> >
> > (b) he is entitled to exercise, or control the exercise of, one third or more of the voting power at any general meeting of the company of or another company which has control of it;
>
> and where two or more persons together satisfy either of the above conditions, they are to be taken as having control of the company.
>
> …"

122. It was common ground that the Chart shows the ownership structure of the Joint Venture and the companies comprised in it at the "look-back" date determined by the Regulator pursuant to the provisions of s 43 (9) PA 2004, namely 31 December 2009.

123. It was also common ground that the test of association and control prescribed by s 435 is a technical test to be applied by the application of the statutory provisions properly construed. This means that the question whether a person is "entitled to exercise, or control the exercise" of the relevant voting power is not to be determined by reference to the extent to which the Targets were able to or actually did influence the way any of the companies within the Joint Venture carried on their business. That continued to be the position in respect of all times after the appointment of the Administrative Receivers. In any event, by 31 December 2009, the date at which the association and control issues are to be determined, there was no business left within the Joint Venture to influence.

124. It was also accepted, as we mentioned at [22] above, that there should be no differentiation between the Targets so that if the necessary degree of association and control is established with respect to one of the Targets, then it is accepted that it is established with respect to them all.

125. It was also accepted that in order for the requirements of s 43 (6) to be satisfied, the Targets need only be associated with one of the Employers, as the term "the employer" in s 43 (6) is to be read as "any employer in relation to the scheme": see Regulation 16 of The Pensions Regulator (Financial Support Directions etc) Regulations 2005.

126. Referring to the Chart, it was common ground that:

(1) ITV plc controlled BxC Tech for the purposes of s 435 (10) (b) on 31 December 2009;

(2) BxC Tech, which itself was never in receivership, controlled BxC Holdings at 31 December 2009 and the fact that the latter company was dissolved on 16 March 2010 is of no significance;

(3) There was no relevant relationship of association or control between ITV plc and the company shown as "Elecrent" on the Chart because that company was dissolved on 3 April 2007 and the effect of such dissolution was to terminate any relationship of connection or association between the Targets and Elecrent's subsidiary Consumer Electronics;

(4) The Targets accept that if there had been no appointment of Administrative Receivers to BxC Holdings and its various subsidiaries shown on the Chart then ITV plc would have been an associate (within the meaning of s 435) of BxC Tech by virtue of s 435 (7) because of its right to exercise more than one third of the voting power of that entity. It would also be an associate of each of the Employers because BxC Tech had control of BxC Holdings which in turn had control of each of the Employers, making all of those companies associates of each other through the application in combination of s 435 (6) (a) and (10) (b), with the result that

ITV plc would be an associate of each of the Employers for the purposes of s 43 (6) PA 2004.

127. However, the Targets say that the chain of control was broken as a consequence of the appointment of the Administrative Receivers in September 2003 in a number of ways.

128. First, as far as the Trio are concerned, under the terms of the debenture that was entered into between the Joint Venture companies and WestLB to secure the borrowings from that bank (the "Debenture"), a security agent, initially West LB itself but later JP Morgan (the "Security Agent"), took the legal title of the shares which BxC Holdings held in the Trio. Those shares formed part of the assets of BxC Holdings that were charged to West LB by way of security for the loan facility, with beneficial ownership of those shares remaining with BxC Holdings.

129. The Targets contend that under the proper construction of the terms of the Debenture, BxC Holdings retained the right to exercise control of the voting of the shares in the Trio until a "Declared Default" under the loan facility occurred, at which point voting power transferred to the Security Agent. It was common ground that the appointment of the Administrative Receivers was a "Declared Default" for these purposes. The Targets contend that once voting power had been transferred to the Security Agent, the chain of control for the purposes of s 43(6) PA 2004 was broken. Alternatively, if, according to the terms of the Debenture, notice was required to be given by the Security Agent before it could assume the power to exercise the voting rights, the Targets contend that the requisite notice had been given.

130. Secondly, as far as TUK is concerned, legal ownership of the shares in TUK and its immediate parent (shown as THSP on the Chart) was at no point vested in the Security Agent. However, the Targets contend that following the Declared Default, the Security Agent was entitled to exercise the voting rights provided due notice of its intention to assume the power to do so had been given in accordance with the terms of the Debenture and that such notice had been duly given.

131. Alternatively, the Targets contend that because the Administrative Receivers were appointed to BxC Finance (the legal owner of the shares in THSP), THSP and TUK on September 2003 and as at 31 December 2009 those companies were still in administrative receivership it was the Administrative Receivers and not the registered legal owners of the shares who controlled the exercise of the voting rights for the purposes of s 43 (6) PA 2004. The Targets contend that as a result of the appointment of the Administrative Receivers, in practical and economic terms, the shareholders no longer had any voting power. That was ceded to the Administrative Receivers under the debenture, and the general law, and it was the Administrative Receivers who were entitled to make all decisions as to how the shares were to be voted.

Association of the Targets with the Trio

132. This question is to be determined by reference to the terms of the Debenture, which was dated 28 June 2000 and entered into between BxC Holdings, BxC Finance

and the operating companies within the Joint Venture as Chargors and WestLB as Security Agent, and the proper construction of the relevant terms.

133. Pursuant to the terms of the Debenture each of the Chargors, as a primary obligor and not merely as surety, covenanted to pay or discharge all the liabilities which may become due under the loan facilities granted by WestLB to BxC Finance. As security for these obligations, each of the Chargors charged in favour of the Security Agent (as agent and trustee for the lenders under the loan facilities) all of their assets.

134. As a result of this provision, the shares held by BxC Holdings in BxC Finance and the Trio were subject to a first fixed charge in favour of WestLB as were the shares held by any subsidiaries of those companies including, in relation to TUK, by THSP.

135. The Debenture contained the following relevant defined terms:

(1) "Declared Default" meant "an Event of Default which has resulted in the Senior Agent serving notice under any provision of Clause 24.2 of the Senior Bridge Facility Agreement." The sending of notice by West LB of default on 24 September 2003 amounted to a "Declared Default";

(2) "Group Shares" meant "all shares specified in the Schedule 4 or … when used in relation to a particular Chargor, such of those shares as are specified against its name in Schedule 4 …, together with in each case all other … shares …now or in the future owned by any or (when used in relation to a particular Chargor) that Chargor from time to time". That description covered all of the shares referred to at [134] above;

(3) "Security Shares" meant "all the Group Shares and the Related Rights" and, in the case of each Chargor, meant such of the Group Shares "as are held by it at the relevant time, together all Related Rights in respect thereof". That description also covered all of the shares referred to at [134] above; and

(4) "Related Rights" meant "in relation to the Group Shares … all … rights accruing or offered at any time by way of redemption, bonus, preference, option rights or otherwise to or in respect of any of the Group Shares …".

136. By Clause 4.2 of the Debenture each Chargor mortgaged and charged and agreed to mortgage and charge to the Security Agent all Group Shares which it held either then or in the future by way of a first mortgage. A proviso to the charging provision in Clause 4.2 provided, so far as relevant that:

> "(i) whilst no Declared Default exists, all dividends and other distributions paid or payable (in respect of the Group Shares) may be paid directly to the relevant Chargor free from the security created hereunder…
>
> (ii) whilst no Declared Default exists, the Security Agent shall use all its reasonable endeavours to forward to the relevant Chargor all material notices, correspondence and/or other communication it receives in relation to the Group Shares; and

> (iii) **subject to Clause 10.2, whilst no Declared Default exists, all voting rights attaching to the relevant Group Shares may be exercised by the relevant Chargor or, where the shares have been registered in the name of the Security Agent or its nominee, as the relevant Chargor may direct in writing**, and the Security Agent and any nominee of the Security Agent in whose name such Group Shares are registered shall execute any form of proxy or other document reasonably required in order for the relevant Chargor to do so." [emphasis added]

137. Clause 7.2(b) of the Debenture provided that:

> "(i) Each Chargor is and will … remain the sole beneficial owner of the Security Shares which it purports to charge pursuant to the Security Documents to which it is party and save where the Security Shares have been registered in the name of the Security Agent or its nominee pursuant hereto, it and/or its nominee is and will … remain the absolute legal owner of the Security Shares; … (ii) No Chargor will take any action whereby the rights attaching to the Security Shares are altered or diluted in each case in any way which could reasonably be expected materially and adversely to affect the interests of the Lenders".

138. Clause 8.2 (b) of the Debenture provided that:

> "Each Chargor shall forthwith deposit with the Security Agent...all…share certificates and other documents of title or evidence of ownership in relation to such Group Shares as are owned by it… and shall execute and deliver to the Security Agent all such share transfers and other documents as may be reasonably requested by the Security Agent in order to enable the Security Agent or its nominee to be registered as the owner or otherwise to obtain a legal title to the same and... shall deliver to the Security Agent on the date hereof executed… share transfers for all Group Shares in favour of the Security Agent… and shall procure that all such share transfers are at the request of the Security Agent forthwith registered by the relevant company and that share certificates in the name of the Security Agent…are promptly delivered... to the Security Agent"

139. Clause 10.1 of the Debenture supplements the provisions of Clause 8.2 (b) so far as relevant as follows:

> "Each Chargor hereby authorises the Security Agent…to arrange for the Security Shares to be delivered to any nominee of the Security Agent or to any purchaser or transferee…or registered as the Security Agent may feel appropriate to perfect the security thereover…and each Chargor undertakes from time to time to promptly execute and sign all transfers, contract notes, powers of attorney and other documents…which the Security Agent may reasonably require for perfecting its title to any of the Security Shares…"

140. Clause 10.2 of the Debenture provided that the Security Agent:

> "… may at any time after a Declared Default has occurred or in any other instance where the Security Agent is of the reasonable opinion that it is necessary for the avoidance of an Event of Default or necessary for the

> protection of its material interests … exercise or refrain from exercising (in the name of each Chargor, the registered holder or otherwise and without any further consent or authority from each Chargor and irrespective of any direction given by any Chargor) in respect of the Security Shares any voting rights and any powers or rights under the terms thereof or otherwise which may be exercised by the person or persons in whose name or names the Security Shares are registered or who is the holder thereof … **PROVIDED THAT in the absence of notice from the Security Agent each Chargor may and shall continue to exercise any and all voting rights with respect of the Group Shares subject always to the terms hereof.** No Chargor shall without the previous consent in writing of the Security Agent exercise the voting rights attached to any of the Group Shares in favour of resolutions having the effect of changing the terms of the Group Shares (or any class of them) or any Related Rights or prejudicing the security hereunder or breaching the terms of any Finance Document, in each case, in any way which could reasonably be expected materially and adversely to affect the interests of the Lenders. Each Chargor hereby irrevocably appoints the Security Agent or its nominee as its proxy to exercise all voting rights so long as the shares remain registered in the name of the relevant Chargor and to the extent that the Security Agent is entitled to exercise such voting rights in accordance with the terms of this Debenture." [emphasis added]

141. The effect of Clause 8.2 (b) and Clause 10.1 of the Debenture is that the Security Agent had the option to effect registration of the Security Shares in its name or to leave the registration in the name of the relevant Chargor whilst retaining blank signed transfers and the relevant share certificates which enabled it to perfect its security if it felt it was necessary to do so. As mentioned above, JP Morgan became the Security Agent in place of WestLB and in that capacity it or its nominee became the registered owner of all of the shares held by BxC Holdings in the Trio and continued to hold them after the appointment of the Administrative Receivers. The shares in TUK were not, however, as also mentioned above, registered in the name of the Security Agent or its nominee and continued to be registered in the name of THSP.

142. The legal position as regards the voting rights over the Security Shares before the Declared Default on 24 September 2003 was not in dispute. The starting position is that the registered holder of the shares, that is the legal owner of them, is entitled to exercise the voting rights of shares. This means that if there is a legal mortgage and the shares have been transferred to and registered in the name of the mortgagee then from his position as owner at law of the shares, the ownership carries with it the voting right and it would require a contract to exclude that right: see on this point *Siemens Bros v Burns* [1918] 2 Ch 324 at 331.

143. In practice, therefore, the exercise of voting rights over shares which are the subject of a charge is controlled by contract. In the present case the contract governing the entitlement to exercise voting rights, whether by the Security Agent or the Chargor as the registered holder of the shares, is the Debenture, the relevant provisions being those in Clause 4.2 and Clause 10.2 as set out above. It was common ground that until the Declared Default on 24 September 2003, those provisions in the Debenture overrode the rights that the Security Agent would otherwise have as registered owner of the shares and that entitlement to voting rights remained with BxC Holdings.

144. The first question of construction for us is whether, as submitted by the Targets, reading Clause 4.2 and Clause 10.2 of the Debenture together, the effect of those provisions is that upon the Declared Default, all the voting rights attaching to the shares in the Trio without more vested in the Security Agent to the exclusion of the relevant Chargor.

145. As regards the proper approach to the construction of the Debenture, it is well-established that the context in which the words in the contract are used is important. Where there are rival constructions, the court will adopt a construction which is more consistent with business common sense. The approach was summarised by Lord Hodge at [10] to [12] of the Supreme Court's judgment in *Wood v Capita Insurance Services Limited* [2017] UKSC 24 in the following terms:

> (1) The court's task is to ascertain the objective meaning of the language which the parties have chosen to express their agreement. It has long been accepted that this is not a literalist exercise focused solely on a parsing of the wording of the particular clause but that the court must consider the contract as a whole and, depending on the nature, formality and quality of drafting of the contract, give more or less weight to elements of the wider context in reaching its view as to that objective meaning;
>
> (2) Interpretation is a unitary exercise; where there are rival meanings, the court can give weight to the implications of rival constructions by reaching a view as to which construction is more consistent with business common sense. But, in striking a balance between the indications given by the language and the implications of the competing constructions the court must consider the quality of drafting of the clause and it must also be alive to the possibility that one side may have agreed to something which with hindsight did not serve his interest. Similarly, the court must not lose sight of the possibility that a provision may be a negotiated compromise or that the negotiators were not able to agree more precise terms; and
>
> (3) This unitary exercise involves an iterative process by which each suggested interpretation is checked against the provisions of the contract and its commercial consequences are investigated. Once one has read the language in dispute and the relevant parts of the contract that provide its context, it does not matter whether the more detailed analysis commences with the factual background and the implications of rival constructions or a close examination of the relevant language in the contract, so long as the court balances the indications given by each.

146. Mr Railton's submissions on the construction of the relevant terms of the Debenture can be summarised as follows:

> (1) It is clear from the wording of sub-paragraphs (i) and (ii) of the proviso to Clause 4.2 that those provisions only apply in the pre-default situation;
>
> (2) Likewise, sub-paragraph (iii) to the proviso to Clause 4.2 deals solely with the pre-default situation, both where the shares are registered in the name of the Chargor, and where they are registered in the name of the Security Agent. This sub-paragraph uses the same words "whilst no Declared Default exists" as are

used in sub-paragraphs (i) and (ii) and the words "subject to clause 10.2" at the beginning of the clause are an additional qualification to the operation of the clause and the rights granted by it;

(3) If the words "subject to Clause 10.2" were intended to trump the "whilst no Declared Default exists" condition, there would be no purpose in having that condition and the clause could simply just say "subject to clause 10.2";

(4) The words at the end of sub-paragraph (iii) to the proviso make it clear that whilst no Declared Default exists and where the Group Shares are registered in the name of the Security Agent, as was the case with the shares in the Trio, the voting rights must be exercised by the Security Agent as directed by the relevant Chargor but that right ceases once there is a Declared Default;

(5) Therefore, since the contractual obligation to exercise voting rights in accordance with the Chargor's instructions ceases once there is a Declared Default, the Security Agent, as the registered holder of the shares, is the only person entitled to exercise the voting rights;

(6) Clause 10.2 of the Debenture deals with three situations in which the Security Agent may exercise the voting rights, namely (i) after a Declared Default has occurred, (ii) where it is of the reasonable opinion that it is necessary for the avoidance of an Event of Default or (iii) where it is of the reasonable opinion that it is necessary for the protection of its material interests. The proviso in Clause 10.2 (which we have emphasised when setting out the wording of the Clause at [140] above) only applies in the second and third of these situations; it is not capable of applying so as to give the relevant Chargor a continuing right to exercise the voting rights after a Declared Default in the absence of a notice to the contrary from the Security Agent because the Chargor lost its power to exercise the rights upon the occurrence of that event; and

(7) There is nothing uncommercial about control of voting rights reverting to the Security Agent as registered shareholder on a Declared Default without any further notice and there is every reason for the Security Agent to be able to exercise the voting rights immediately upon the occurrence of a Declared Default which is when the security under the Debenture becomes immediately enforceable.

147. We reject Mr Railton's contention that when the proviso to Clause 4.2 and Clause 10.2 of the Debenture are read together, the effect of those provisions is that the voting rights attaching to the shares in the Trio registered in the name of the Security Agent were exercisable solely by the Security Agent immediately upon the occurrence of a Declared Default without further formality.

148. In full agreement with Mr Moss's submissions on this point, in our view, the proper construction of the relevant provisions of the Debenture is as follows.

149. The proviso to Clause 4.2 of the Debenture is a standard provision to be found in security documents to the effect that even though provision is made for the creation of a first mortgage over the shares which were the subject of the mortgage, which if perfected would result in the mortgagee becoming the legal owner of the shares, then

prior to the declaration of a default, all the economic interest in the shares, including dividend and voting rights should remain with the beneficial owner of the shares, namely the relevant Chargor.

150. Therefore, the starting position is that the proviso to Clause 4.2, when read alone, deals only with the position prior to the declaration of a default. To that limited extent we agree with Mr Railton. Consistent with the usual position, once a security has become enforceable, it is to be expected that dividends and other economic benefits would cease to be received or passed onto the relevant Chargor, without any further action being necessary. The same position would have applied in relation to voting rights but for the addition of the words "subject to Clause 10.2". In our view the effect of the inclusion of these words is that the proviso to Clause 4.2 and the operative provisions of Clause 10.2 must be read together.

151. When read together, it is clear that the words at the beginning of sub-paragraph (iii) of the proviso to Clause 4.2 qualify the rest of the provision in two ways.

152. First, the words concerned create an exception to the general position that prior to the occurrence of a Declared Default the voting rights are exercisable only by the Chargor. This is because Clause 10.2 makes provision for the Chargor to lose its right to exercise the voting rights prior to the occurrence of a Declared Default upon notice to that effect from the Security Agent in two circumstances, that is where in the reasonable opinion of the Security Agent it is necessary for the avoidance of an Event of Default or necessary for the protection of the material interests of the Security Agent.

153. Secondly, the words point the reader to the only provisions in the Debenture which expressly deal with the position as regards the exercise of voting rights in the period after the occurrence of a Declared Default. The starting position in Clause 10.2 is that without any further authority from the Chargor the Security Agent may exercise those voting rights irrespective of any direction given by the relevant Chargor. However, the proviso in Clause 10.2 makes it clear that the exercise of this right is dependent upon the Security Agent having given notice to that effect to the relevant Chargor. In the absence of notice the relevant Chargor "may and shall continue to exercise any and all voting rights....". In our view, the reference to the right to "continue to exercise" can only be a reference to the general right vested in the Chargor that prevailed prior to the occurrence of the Declared Default and which would, but for the opening words of sub-paragraph (iii) to the proviso to Clause 4.2 and the operative provisions of Clause 10.2, cease to have applied leaving the voting rights exercisable by the Security Agent as registered holder. Therefore, the effect of the words "subject to Clause 10.2" in the proviso to Clause 4.2 when read together with the proviso in Clause 10.2 is that the Security Agent may not exercise the voting rights unless it gives the necessary notice that it wishes to do so.

154. We therefore reject Mr Railton's submission that the reference to the right to "continue to exercise" in the proviso to Clause 10.2 of the Debenture is a reference to a right which he submits vested in the Security Agent automatically upon the occurrence of a Declared Default. As we have explained, in our view the effect of the opening words at the beginning of sub-paragraph (iii) of the proviso to Clause 4.2 is to

prevent such a right arising in the first place. The Security Agent will only acquire the right to exercise the voting rights after the occurrence of a Declared Default if it gives the necessary notice under Clause 10.2. The proviso to Clause 10.2 therefore operates as a bridge between the provisions of Clause 4.2 and its proviso and Clause 10.2. The words "in the absence of notice" in Clause 10.2 make it clear that the provisions of Clause 4.2 continue to apply unless and until notice is given pursuant to the latter provision. In other words, as Mr Moss submitted, whoever the registered owner of the shares is, the rights which are continued after the occurrence of a Declared Default are the rights of the relevant Chargor to direct the exercise of the voting rights as provided by Clause 4.2 unless and until notice is given by the Security Agent pursuant to the terms of Clause 10.2.

155. It follows that we also reject Mr Railton's submission to the effect that this analysis would mean that there would be no purpose to having the words "whilst no Declared Default exists" in sub-paragraph (iii) to Clause 4.2. Whilst our analysis would suggest that those words are not strictly necessary, in our view they do add clarity in that they emphasise that the proviso as a whole is only dealing with the position before a Declared Default occurs, consistent with the wording of sub-paragraphs (i) and (ii) of the proviso.

156. In our view our analysis reflects the natural reading of the two provisions, when read together. This analysis also makes commercial sense in that it is consistent with the intention that the Chargor should continue to exercise the voting rights attaching to the shares despite the granting of security over them unless notice to the contrary is given by or on behalf of the mortgagee in accordance with the terms of the Debenture. Furthermore, there is no apparent business sense in there being a difference between whether the shares concerned are charged by way of a legal mortgage or by way of an equitable charge. On Mr Railton's analysis, the position is different because where a legal mortgage had been perfected by the transfer of legal title into the name of the Security Agent, the voting rights would automatically vest in the Security Agent upon the occurrence of a Declared Default, but where there was only an equitable charge because the shares had remained in the legal ownership of the Chargor, it would be necessary for notice to be given under Clause 10.2 before the Security Agent could exercise its voting rights. In our judgment, it makes more commercial sense for the Security Agent to be given the option as to whether it wishes to exercise the voting rights in both circumstances.

157. Furthermore, as Mr Moss submitted, and consistent with standard commercial practice, the lenders sought to enforce their security not through taking possession of the mortgaged property but through the appointment of Administrative Receivers over all the assets of the Chargors. That meant there was no commercial imperative for the Security Agent to assume the voting rights over the Group Shares. As a matter of law, the Administrative Receivers act as agent of the relevant company over whose assets they have been appointed receivers when they deal with those assets. They would nevertheless be able to act in the interests of the lenders when deciding how to exercise those rights in the same way as the Security Agent could have done, were it considered necessary at any point to exercise those rights.

158. Mr Moss also made submissions to the effect that the provisions are consistent with a desire on the part of a Security Agent not to run the risk of being deemed to be a shadow director by virtue of the voting rights becoming vested in it automatically. In the absence of any evidence as to the practice of JP Morgan in this case and whether it did have that concern, we place no weight on those submissions.

159. Therefore, for the reasons set out above, we conclude that the voting rights attaching to the shares held by the Security Agent in the Trio remained under the control of BxC Holdings after the appointment of the Administrative Receivers unless and until a notice was given to BxC Holdings by the Security Agent pursuant to Clause 10.2 of the Debenture.

160. Mr Railton submitted that if we were against him, as we are, on his construction of the relevant provisions of the Debenture nevertheless there had been an effective notice to vest the voting rights in the Security Agent in accordance with Clause 10.2.

161. Mr Railton relies on the demands made by WestLB in its capacity as Facility Agent on the borrower and guarantors under the Senior Facility Agreement as constituting the necessary notice in this regard. Each of these demands was made on 24 September 2003. By way of example, a Guarantor Demand was addressed to BxC Finance on behalf of each guarantor under the loan facilities (which included each of the Chargors under the Debenture). The Guarantor Demand referred to the Senior Facility Agreement and the Debenture, identifying JP Morgan Chase as the Security Agent as successor to WestLB in that capacity. The Guarantor Demand attached a copy of the demand made by WestLB on BxC Finance (the "Borrower Demand") which expressly stated that an Event of Default had occurred. The Borrower Demand referred to Clause 12 of the Debenture going on to say:

> "we hereby notify you that this notice gives rise to a Declared Default, that accordingly the security constituted by the Debenture is enforceable …"

162. The Borrower Demand then reserved various rights of the Security Agent without further notice to exercise its powers to appoint a receiver and the other powers conferred by the Debenture.

163. Having referred to the terms of the Borrower Demand, the Guarantor Demand stated:

> "We give you notice that as referred to in the [Borrower] Demand the security created by the Debenture is enforceable and failing payment to us forthwith of all amounts demanded herein, we reserve the right of the Security Agent under the Debenture without further notice to exercise the power to appoint a receiver or receivers over the undertaking, property and assets of each Relevant Guarantor, the power of sale and all other powers conferred on us by law or the Debenture or by any other mortgage, charge or security created by each Relevant Guarantor in the Security Agent's favour."

164. Mr Railton submits that the terms of the Guarantor Demand were sufficient to constitute necessary notice under Clause 10.2 of the Debenture for the following reasons:

(1) It is clear that WestLB is giving notice on behalf of the Security Agent under the Debenture; this is apparent from the use of the language "we reserve the right of the Security Agent under the Debenture" as set out at [163] above and there is nothing in Clause 10.2 of the Debenture that requires direct notice or prevents the use of an agent to give notice;

(2) The role of the Facility Agent in acting on behalf of the Security Agent is also apparent in the last paragraph of the Guarantor Demand where WestLB states that there is no waiver in respect of the rights or remedies of the Security Agent and there is no suggestion that it is not authorised so to act;

(3) Under the terms of the Debenture and the Senior Facility Agreement, the Security Agent is fully entitled to appoint agents and delegate its powers and no formalities are required for the delegation;

(4) The reference in the terms of the Guarantor Demand set out at [163] above to the reservation of the right of the Security Agent to exercise "all other powers conferred on us by law or the Debenture" is sufficiently wide to include the power under Clause 10.2 to give notice. The reference to "us" must be a reference to the Security Agent rather than the Facility Agent because there are no powers conferred on the Facility Agent under the Debenture, the reservation is specifically in respect of the rights of the Security Agent and any recipient of this document would clearly understand that all the Security Agent's powers under the Debenture are being reserved; and

(5) The reference in the terms of the Guarantor Demand set out at [163] above to the right "without further notice" to exercise the relevant powers is in context a reference to the power to vote the shares or refrain from voting them under Clause 10.2 of the Debenture without any further notice so that this is not a reservation of rights to serve notice but a reservation of rights to exercise the power to vote without notice.

165. Once again in full agreement with Mr Moss's submissions, in our view the Guarantor Demand cannot be construed as being a notice by the Security Agent pursuant to Clause 10.2 of the Debenture of its assumption of the right to exercise the voting rights attached to the shares in the Trio for the following reasons.

166. There is no basis for Mr Railton's submission that the Guarantor Demand is made on behalf of the Security Agent. It is quite clearly expressed to be made by WestLB solely in its capacity as Facility Agent under the Senior Facility Agreement. The Guarantor Demand is a carefully drafted legal document. Had WestLB been intending to exercise powers on behalf of the Security Agent as well as its own powers as Facility Agent there is no question that it would have explicitly said so and have represented that it had the necessary authority to do so. We see no merit in Mr Railton's submission that the reader of the document would obviously take the reference to "us" as being a reference to the Security Agent rather than the Facility Agent on the basis that it would be readily apparent to the reader that the Facility Agent had no powers of its own in

relation to the Debenture. The reader would take at face value what is meant by "us" in this context, namely that the Guarantor Demand did not purport to be given on behalf of anyone other than WestLB.

167. In any event, there is no evidence before us on which we could properly make a finding that the Security Agent had authorised WestLB to give notice on its behalf. The best Mr Railton could come up with was that there was no suggestion that it had not been authorised. That is clearly inadequate.

168. Furthermore, even if there was a necessary authority to act on behalf of the Security Agent the language used in the text set out at [163] above is the language of a reservation of rights rather than of their exercise. The language refers to the reservation of the right to appoint a receiver as well as reserving a right to exercise all the other powers given under the Debenture. It was clear that at this stage there had been no actual exercise of the right to appoint a receiver and we see no reason why we should construe the language in relation to the reservation in respect of the other powers any differently.

169. Finally, as it was anticipated that Administrative Receivers were to be appointed later on the same day as the Guarantor Demand was made, it would be expected, as we mentioned above, that it would be the Administrative Receivers who would exercise the voting rights on behalf of the relevant Chargors and it would make no sense at this point to give notice vesting those rights in the Security Agent.

170. As we have rejected the Targets' submissions on both the construction of the Debenture and whether notice by the Security Agent to exercise the voting rights in respect of the shares in the Trio had been given, we conclude that those voting rights remained vested in the relevant Chargor following the appointment of the Administrative Receivers and there is no suggestion that the position changed prior to 31 December 2009.

171. That conclusion is sufficient for us to hold that BxC Holdings controlled the Trio within the meaning of s 435 of the Insolvency Act 1986 and hence was associated with them for the purposes of s 43(6) PA 2004.

Association of the Targets with TUK

172. Since, as we have mentioned at [125] above, association with any one of the Employers is sufficient for the purposes of s 43(6) PA 2004, it is not strictly necessary for us to consider the Targets' arguments as to why TUK was not associated with the Targets at the relevant time. However, since we heard full argument on the issue we will deal with this issue.

173. The Targets relied on two arguments for their contention that TUK was not associated with the Targets at the relevant time. First, they argue that pursuant to the terms of the Debenture the necessary notice had been given by the Security Agent to assume the voting rights pursuant to Clause 10.2 of the Debenture, relying solely on the Guarantor Demand which we have referred to at [161] above. Since we have held that the Guarantor Demand does not constitute notice for the purposes of Clause 10.2 of the

Debenture in the context of our consideration of the position in relation to the Trio, this argument fails here also and we need say no more about it.

174. Secondly, the Targets contend that since the appointment of the Administrative Receivers to BxC Finance and THSP continued as at the relevant date, 31 December 2009, it was the Administrative Receivers rather than any of the relevant corporations in the chain of ownership who are to be treated as controlling the voting rights in TUK for the purposes of s 43(6) PA 2004.

175. Mr Railton submits that if at 31 December 2009 THSP, as the registered owner, was otherwise still entitled to exercise voting power in respect of the shares it held in TUK, or BxC Finance was entitled to do so in respect of the shares it held in THSP, that entitlement was removed by reason of the continuing appointment of the Administrative Receivers in respect of the relevant shares. Mr Railton submits that as a result of the appointment of the Administrative Receivers, in practical and economic terms, the registered shareholders no longer had any voting power. That was ceded to the Administrative Receivers under the Debenture and the general law, and it was the Administrative Receivers who were entitled to make all decisions as to how the relevant shares were to be voted.

176. In support of those submissions Mr Railton relies on the following points:

(1) The Debenture gives the Administrative Receivers very wide powers, including, pursuant to Clause 14.2(b)(i) the power to take immediate possession of, getting in and collecting the Security Assets (which includes the shares in the Chargors) and in Clause 14.2 (b)(xii) to exercise in relation to such assets "all such powers, authorities and things as he would be capable of exercising if he were the absolute beneficial owner of the same and to use the name of such Chargor for all any of such purposes";

(2) Although both under the terms of the Debenture and the general law, the Administrative Receivers were deemed to be the agent of the relevant Chargor when exercising their powers over the relevant Chargor's assets this deemed agency is no ordinary agency but merely a formula for making the company, rather than the mortgagee liable for the acts of the receiver;

(3) Therefore, the situation is in substance the same as the situation where an unlimited or irrevocable proxy or power of attorney is given so that the Administrative Receivers should be treated as having been given such irrevocable proxy or power of attorney because the Chargor in practical terms is completely bypassed and has no say in how the votes are being cast; and

(4) Consequently, the existence of the agency is no answer if, as is the case here, it obliterates any discretion in the actual or deemed principal.

177. In relation to the second of these points, Mr Railton relies on a number of authorities.

178. In *Moss Steamship Co.Ltd v Whinney* [1912] AC 254 ('*Moss Steamship*') Lord Atkinson observed:

> "This appointment of a receiver and manager over the assets and business of a company does not dissolve or annihilate the company, any more than the taking possession by the mortgagee of the fee of land let to tenants annihilates the mortgagor. Both continue to exist; but it entirely supersedes the company in the conduct of its business, deprives it of all power to enter into contracts in relation to that business, or to sell, pledge, or otherwise dispose of the property put into the possession, or under the control of the receiver and manager. Its powers in these respects are entirely in abeyance."

179. In that case the receiver concerned had been appointed by an order of the court, rather than pursuant to a power of appointment on the part of the mortgagee under the terms of a debenture. It was common ground that in those circumstances neither the statutory agency contained in s 44 of the Insolvency Act 1986 (which we refer to later) nor any contractual provision operated so as to make the receiver concerned the agent of the company over whose assets he had been appointed. The position of a court-appointed receiver is more akin to a trustee who contracts and exercises powers in his own name with a right of indemnity against the assets of the company over which he has control. However, Mr Railton contends that the passage from the case referred to above and the approval by Hoffmann J of further dicta from *Moss Steamship* in the *Gomba* case referred to below, are relevant to the consequences of the appointment of any receiver, namely the removal of the powers of the board in relation to any of the assets of the company concerned.

180. In *Gomba Holdings UK Ltd v Homan* [1986] 1 WLR 1301 Hoffmann J (as he then was) said at page 1305 E to G:

> "There are, I think, certain principles which can be deduced from what the parties may be supposed to have contemplated as the commercial purpose of the power to appoint a receiver or manager. The first is that the receiver or manager should have the power to carry on the day-to-day process of realisation and management of the company's property without interference from the board. As Lord Atkinson said in *Moss Steamship Co.Ltd v Whinney* [1912] AC 254, 263, the appointment of a receiver:
>
> > "entirely supersedes the company in the conduct of its business, deprives it of all power to enter into contracts in relation to that business, or to sell, pledge, or otherwise dispose of the property put into the possession, or under the control of the receiver and manager. Its powers in these respects are entirely in abeyance."

181. He then said at page 1307 D:

> "I cannot accept that the Court of Appeal contemplated some kind of diarchy over all the company's assets. This would be contrary to principle and wholly impractical. In my judgment the board has during the currency of the receivership no powers over assets in the possession or control of the receiver."

182. In *Silven Properties Ltd and another v Royal Bank of Scotland plc and others* [2004] 1 WLR 997, a case involving an alleged breach of duty through the sale by receivers of mortgaged properties at an undervalue, the issue raised was whether

receivers who are appointed by a mortgagee to act as agents of the mortgagor owe a duty to the mortgagor to take steps which are calculated to achieve the best price on a sale of the mortgaged property. Lightman J, giving the judgment of the Court of Appeal, said at [26] and [27]:

> "26. The character and incidents of such receivers' agency has been the subject of judicial and extra-judicial consideration. Mr Peter Millett in "The Conveyancing Powers of Receivers After Liquidation" (1977) 41 Conv (NAS) 83, 88 wrote: "the so-called "agency" of the [receivers] is not a true agency, but merely a formula for making the company, rather than the [mortgagee], liable for his acts…" But this agency of the receivers is a real one, even though it has some peculiar incidents… Its reality is reflected in the continuity after the appointment of receivers of the rateable occupation of the mortgage or through the agency of the receivers… and in the absence of personal liability of the receivers for tax in respect of receipts which come to the hands of the receivers as agents…
>
> 27. The peculiar incidents of the agency are significant. In particular: (1) the agency is one where the principal, the mortgagor, has no say in the appointment or identity of the receiver and is not entitled to give any instructions to the receiver or to dismiss the receiver. In the words of Rigby LJ in Gaskell v Gosling [1896] 1 QB 669, 692: "For valuable consideration he has committed the management of his property to an attorney whose appointment he cannot interfere with";….. and (6) the receiver is not managing the mortgagor's property for the benefit of the mortgagor, but the security, the property of the mortgagee, for the benefit of the mortgagee…"

183. Mr Railton submits that these cases show that the appointment of receivers completely deprives those otherwise connected with the relevant Chargor, such as directors and shareholders, of all power over its assets. It follows, he submits, that THSP has no say at all in the exercise of voting power in respect of the shares in TUK.

184. In relation to the third and fourth of these points, Mr Railton relies on the judgment of Lewison J in *Unidare plc v Cohen* [2006] Ch 489. In that case, Unidare was the holder of 100% of the share capital in a company referred to as "Holdings" which in turn was the holder of 80% of the share capital in a company called Kilnoore Limited. The issue was whether a debenture which had been given in favour of Unidare by Kilnoore was valid. That in turn required consideration of whether at the relevant time Unidare had control of Kilnoore within the meaning of s 435 (10) (b) of the Insolvency Act 1986. Holdings sold its interest in Kilnoore to a purchaser, Kozo, on terms which deferred part of the consideration, and in order to secure Kozo's interest, Holdings executed a power of attorney in favour of Kozo, including the power to direct the exercise of voting rights. Holdings also declared that it held the shares on trust for Kozo, which was held to be a bare trust.

185. It was common ground that Unidare was an associate of Holdings, but the question was whether Holdings was associated with Kilnoore through its shareholding. As Lewison J said at [41], the question was not whether Kozo, as the beneficial owner of the shares, was included within the definition contained in s 435 (10) (b) (which it plainly was) but whether Holdings as the registered shareholder was excluded from it.

Lewison J said the answer to that question was not dependent on who is entitled to exercise the voting rights but depended on who was entitled to control their exercise.

186. Having reviewed the authorities, Lewison J said this at [54]:

> "The following is what I derive from these cases. (i) In the vast majority of cases, whether a person is entitled to exercise voting rights is to be determined simply by looking at the register of shareholders and the company's articles of association. (ii) In such cases, it is not permissible to look outside those materials and to enquire whether there are contractual or fiduciary restraints, as between the registered shareholder and others, which inhibit him in exercising those rights. (iii) In general there is no warrant for distinguishing between different degrees of trusteeship. (iv) In such a case control resides in the beneficial owner to the exclusion of the trustee. (v) In the case of a shareholder which is itself a corporation, in determining how its voting rights as shareholders are exercised it is permissible to look outside the register of shareholders and enquire whose voice is heard when its votes are cast."

187. At [57] Lewison J stated that he could not discern any cogent policy reason for concluding that Parliament must have intended that bare trustees would be treated as connected with companies in which they are registered shareholders. He then held at [58] to [59] as follows:

> "58. The phrase I have to construe in section 435 (10) (b) of the 1986 Act is a typically compressed piece of draftsmanship. The verb "entitled" governs both the exercise of voting power and the control of voting power. In looking at control of voting power, the word "entitled" must in my judgment, mean "entitled as between the registered shareholder and the controller of the voting power". Why, then, should the word "entitled" in its application to the exercise of voting power be construed as meaning "as between the registered shareholder and the company"? There is a further slight clue to the meaning of section 435. Unlike sections 736 and 736A of the 1985 Act, which refer to "voting rights", section 435 of the 1986 Act refers to "voting power". The word "rights" naturally directs attention to legal rights, especially since section 736A (2) of the 1985 Act goes on to explain that voting rights means "rights conferred on shareholders in respect of their shares". The word "power", by contrast, gives me some encouragement to look to the economic reality of the case. A registered shareholder who holds a share on a bare trust under which he is required to cast his vote in accordance with the directions of the beneficial owner might be said to have voting rights, but I do not consider that in any real sense he can be said to have voting power. The Court of Appeal, in two cases I have mentioned….. were clearly impressed by the appeal to the common sense and economic reality of the case of a bare trustee. I do not consider that the wording of section 435 compels me to take a different view. In addition Holdings was a corporate shareholder. If I ask whose voice would be heard if, after the declaration of trust, Holdings were to cast the votes attached to the shares registered in its name at a general meeting of the company, the only answer to that question is Kozo's.
>
> 59. I hold, therefore, that following the execution of the declaration of trust Holdings is not to be regarded, for the purposes of section 435 (10) (b) of the

> Insolvency Act 1986, as being entitled to exercise the voting power of those shares. Since such a person is bound to act in accordance with the directions of the beneficial owner, he does not control their voting power either. Thus Holdings was not associated with the company when the debenture was executed."

188. Mr Railton submits that although the relevant Chargor was not a bare trustee of the shares it held in the company lower down the chain, it was in a very closely analogous position following the appointment of the Administrative Receivers. Following that appointment, the registered shareholders not only had no entitlement to control the exercise, but also despite being the registered shareholders, they had no entitlement to exercise the voting power; that power rested with the Administrative Receivers. He submits that just because the Administrative Receivers exercise voting power in the shareholders' name, and as a deemed agent, does not mean that the shareholders have in reality any power at all. Mr Railton submits that the situation is in substance the same as the situation where an unlimited or irrevocable proxy or power of attorney is given, as was the case in *Unidare*. He submits that the "voice to be heard" was that of the Administrative Receivers to the exclusion of the Chargors.

189. We reject all of Mr Railton's submissions on this issue. As Mr Moss correctly submitted, *Unidare* is of no relevance in the circumstances with which we are concerned in this case. *Unidare* merely establishes that where the registered holder of shares is a bare trustee for a person who has the entire beneficial ownership of the shares then, for the purposes of s 435(10) (b) of the Insolvency Act 1986, the beneficial owner is the person who controls the exercise of the voting power attached to the shares, by being able to direct the bare trustee as to how they should be voted. Further, he is also the only person who is entitled to exercise the voting power. In so far as that right to exercise the voting rights is supported by a power of attorney or similar authority given by the registered holder in favour of the beneficial owner, that is simply a question of the mechanics which enable the beneficial owner to exercise the rights that he has. The execution of such a power of attorney does not affect the question of who has the right or power to exercise the votes in question.

190. In this case, THSP was at the relevant time the beneficial owner of the shares in TUK. By analogy with the situation in *Unidare*, it was in the position of Kozo. All that changed upon the appointment of the Administrative Receivers was the question of who had the authority to decide on behalf of the beneficial owner how the shares in question were to be voted. Prior to the appointment of the Administrative Receivers, that decision would be taken by the appropriate persons within THSP who had the authority to make such decisions on the company's behalf. Unless that authority had been delegated the authority would ultimately rest with the directors of the company. Upon the appointment of the Administrative Receivers, the powers of the directors to deal with the assets of THSP, including the shares in TUK ceased. As a result of the application of the general law and the terms of the Debenture all of those powers vested in the Administrative Receivers. Section 44 (1) (a) of the Insolvency Act 1986, provides that the administrative receiver of a company "is deemed to be the company's agent, unless and until the company goes into liquidation" and the Debenture specifically provides that the Receivers shall exercise their powers as agents of the relevant

Chargor. These have the effect that upon their appointment, the Administrative Receivers took the place of the board of directors of THSP and any other person to whom the directors may have delegated their powers. They became the body with the ultimate authority to deal with the company's assets and the rights attached to them, including the right to exercise the voting power over the shares held in TUK on behalf of THSP. There was no change in the beneficial ownership of those shares simply because of the appointment of the Administrative Receivers. There is no basis for treating the voice of the Administrative Receivers as different from the voice of the company any more than one would treat the voice of the board of directors as different from the voice of the company.

191. It follows that in our view none of the cases relied on by Mr Railton as to the nature of the agency relationship between the Administrative Receivers and the relevant Chargor affects the position.

192. For the reasons set out above, we conclude that the Targets controlled the voting rights in the shares in TUK as at the "look-back" date of 31 December 2009 and hence they were associated with TUK for the purposes of s 43(6) PA 2004.

193. We have therefore determined the association issue in favour of the Regulator and the Trustee.

VI. JURISDICTION: RETROSPECTIVITY, DISCRIMINATION, AND ABSENCE OF MORAL HAZARD

Retrospectivity

194. The Targets argue that on its proper construction PA 2004 does not permit the Regulator to found a decision to issue an FSD on events all of which occurred prior to s 43 PA 2004 coming into force. We describe in detail later the narrative of what happened but for present purposes it is enough to say that the Regulator accepts that all the relevant events which it took into account in deciding whether it was reasonable to issue an FSD occurred in the period between 1999 and 2003, well before s 43 PA 2004 came into force on 6 April 2005.

195. The Targets point to a number of provisions which they say show that PA 2004 was not intended to apply in a case such as the present. But they also rely on the presumption against retrospectivity that previous authorities establish is raised against attributing to Parliament an intention to enact legislation which has a retrospective effect.

196. The Regulator contends that the presumption against retrospectivity is not engaged in this case. On its proper construction the jurisdiction in s 43 is founded on the continuing circumstances after the provision has come into force, namely that the target is connected or associated with a service company or to an employer who is insufficiently resourced relative to its pension liabilities at the look-back date. Therefore, the Regulator contends, this is a case where the legislation imposes new obligations in respect of circumstances in existence at the time the legislation came into force without any objectionable retroactivity.

197. If the Targets fail on their point of the construction of s 43 they rely in the alternative on their rights under Article 1 Protocol 1 to the European Convention of Human Rights ("A1P1"). The Targets contend that the effect of s 43 on its property rights requires a special justification and that no such justification can be found here. This means that s 43 must be given a compatible interpretation precluding the issue of an FSD in circumstances where all the relevant events occurred before the provision came into force. The Regulator contends that the interference with property is plainly proportionate to the legitimate aim of the legislation.

The proper construction of s 43 PA 2004

198. We consider first to what extent the question of construction is affected by the presumption against retrospectivity. Section 5.12 of *Bennion on Statutory Interpretation* expresses the principle of retrospectivity in the following terms:

> "(1) It is a principle of legal policy that, except in relation to procedural matters, changes in the law should not take effect retrospectively.
>
> (2) Legislation is retrospective if it alters the legal consequences of things that happened before it came into force."

199. Bennion does, however, refer to the fact that a distinction is sometimes drawn between changes to the law as it has effect in relation to past events and changes to the law that alter existing rights or obligations or other matters but only in the future. He says:

> "The mere fact that legislation is framed by reference to legal relationships or things that happened before the legislation came into force is not generally thought, of itself, to make the legislation retrospective, and certainly not in an objectionable way. A change in the law is not objectionable merely because it takes note that a past event has happened, and bases new legal consequences upon it."

200. This distinction is at the heart of the dispute between the parties on this issue. The Targets contend that s 43 is retrospective and the presumption against retrospectivity is engaged because the Regulator seeks to justify the imposition of a financial sanction through the issue of an FSD, by reference to criticisms that the Regulator makes of specific acts or omissions which occurred in the past, and which are said to make the Targets responsible for the current deficit in the Scheme.

201. The Regulator contends, in reliance on the passage from *Bennion* set out above, and the authorities which it says support that passage, that the rebuttable presumption against retrospectivity is not applicable in this case because s 43 is not retrospective legislation in the relevant sense. Even if it were, the Regulator submits, it would be plain that any retrospectivity was intended and unobjectionable (and reasonable) and the presumption would be rebutted by the social remedial objectives of the legislation.

202. Against that background, we return to the relevant authorities on which the parties rely to support their respective cases on this issue.

203. In *L'Office Cherifien Des Phosphates and anor v Yamashta-Shinnikon Steamship Co Ltd* [1994] AC 486 the House of Lords considered whether s 13A of the Arbitration Act 1950, which was inserted by s 102 of the Courts and Legal Services Act 1990 and came into force on 1 January 1992, applied so as to enable an arbitration claim which had been made in 1985 to be dismissed on the grounds of inordinate and inexcusable delay, where that delay had occurred prior to 1 January 1992. This was therefore an example where the relevant question was whether on a proper construction of the new legislation it could apply to circumstances which were in existence at the time it came into force.

204. Lord Mustill, with whom all the other members of the appellate committee agreed, did not find it helpful to analyse the numerous authorities on retrospective effect, but proceeded directly to the ascertainment of what Parliament intended s 13A to achieve. He applied the following statement by Staughton LJ in Secretary of State for *Social Security v Tunnicliffe* [1991] 2 All E.R. 712, 724:

> "In my judgment the true principle is that Parliament is presumed not to have intended to alter the law applicable to past events and transactions in a manner which is unfair to those concerned in them unless a contrary intention appears. It is not simply a question of classifying an enactment as retrospective or not retrospective. Rather it may well be a matter of degree – the greater the unfairness, the more it is to be expected that Parliament will make it clear if that is intended."

205. Lord Mustill then said this at page 525F of *L'Office Cherifien*:

> "Precisely how the single question of fairness will be answered in respect of a particular statute will depend on the interaction of several factors, each of them capable of varying from case to case. Thus, the degree to which the statute has retrospective effect is not a constant. Nor is the value of the rights which the statute affects, or the extent to which that value is diminished or extinguished by the retrospective effect of the statute. Again, the unfairness of adversely affecting the rights, and hence the degree of unlikelihood that this is what Parliament intended, will vary from case to case. So also will the clarity of the language used by Parliament, and the light shed on it by consideration of the circumstances in which the legislation was enacted. All these factors must be weighed together to provide a direct answer to the question whether the consequences of reading the statute with the suggested degree of retrospectivity are so unfair that the words used by Parliament cannot have been intended to mean what they might appear to say."

206. In this case Lord Mustill considered that the retrospective effect of the statute was limited. He found it "impossible to accept" that Parliament had intended arbitral proceedings that through delay were "already irrevocably stamped with the risk of injustice" to continue after s 13A came into force. He held that the wording was sufficiently clear to persuade him that in the interests of reform Parliament was going to tolerate the "very qualified kind of hardship involved in giving the legislation a partially retrospective effect": see page 529 C to D.

207. It is clear from this analysis that the application of new legislation to existing circumstances does involve a degree of retrospectivity which may create a degree of unfairness or hardship. The court is therefore required to consider whether Parliament had intended legislation to have that effect. But this is not a binary question of whether

the legislation is or is not retrospective and therefore whether the presumption against retrospectivity is or is not engaged. Whether Parliament had that intention depends on the degree of unfairness involved, the greater the unfairness the less likely it is that Parliament intended that result.

5 208. The passage from Staughton LJ's judgment in *Tunnicliffe* was approved by Lord Nicholls of Birkenhead in *Wilson v First County Trust Ltd (No 2)* [2004] 1 AC 816 at [19]. The House of Lords in that case, which concerned the question whether s 3(1) of the Human Rights Act 1998 operated retrospectively, also drew a distinction between a situation where legislation is intended to alter accrued rights and the legal effect of
10 past acts with the situation where legislation alters existing rights and duties only prospectively with effect from the date of commencement: see Lord Rodger of Earlsferry at [188]. At [190] Lord Rodger illustrated the distinction between the two kinds of provision by reference to the judgment of Buckley LJ in *West v Gwynne* [1911] 2 Ch 1. There the issue was whether a statutory provision prohibiting a landlord from
15 demanding payment in consideration of the grant of a licence to assign a lease applied to leases which had been entered into before the statutory provision came into force. Buckley LJ had observed at [11] to [12] of *West v Gwynne*:

> "… Retrospective operation is one matter. Interference with existing rights is another. If an Act provides that as at a past date the law shall be taken to have been that which it
> 20 was not, that Act I understand to be retrospective. That is not this case… there is no like presumption that an Act is not intended to interfere with existing rights. Most Acts of Parliament, in fact, do interfere with existing rights. To construe this section I have simply to read it, and, looking at the Act in which it is contained, to say what is its fair meaning."

25 209. Lord Rodger concluded at [192] of *Wilson*:

> "Since provisions which affect existing rights prospectively are not retroactive, the presumption against retroactivity does not apply. Nor is there any general presumption that legislation does not alter the existing legal situation or existing rights: the very purpose of Acts of Parliament is to alter the existing legal situation and this will often
> 30 involve altering existing rights for the future….
>
> As the sparks fly upward, individuals and businesses run the risk that Parliament may change the law governing their affairs."

210. If the lease in *West v Gwynne* lies at one end of the spectrum of retrospectivity, the legislation considered by the Supreme Court in *Recovery of Medical Costs For*
35 *Asbestos Diseases (Wales) Bill* [2015] AC 1016 ('*Welsh Asbestos*') lies at the other. In that case there was no doubt that the Welsh Assembly had intended that the legislation apply retrospectively to impose on employers of people who suffered from asbestos-related diseases, and on their insurers, a new liability to reimburse the National Health Services for the cost of treating those sufferers. Lord Thomas had this to say regarding
40 the issue of retrospectivity at [103]:

> "Although the charges which can be recovered are only those that are incurred after the coming into force of the Bill and the liability to pay Ministers arises only where a compensation payment is made after the coming into force of the Bill, there is an element

of retrospectivity in the imposition of the machinery of direct liability on employers. The liability imposed, though only in respect of future charges, is retrospective, as it is a new liability owed directly to Welsh Ministers which arises only by reason of negligence or breach of statutory duty which had occurred prior to the coming into force of the Bill. It is not simply an obligation to make future payments to an employee in respect of a recognised head of damages for an established liability, as would be the case if the machinery adopted had been to impose charges directly on the employees and recovery been obtained from employers. In the case of the employers, prior to the Bill, they would have had no such direct liability to Welsh Ministers. Thus the second aim and effect of the Bill has an element of retrospectivity."

211. In that draft legislation, the contrary intention did appear and did rebut the presumption against retrospectivity. The Supreme Court therefore had to consider whether the legislation fell foul of A1P1, as we discuss below.

212. In the light of these authorities we need to consider the following issues:

(1) to what extent the application of s 43 in the present circumstances could be described as retrospective and therefore to what extent there is a presumption against construing it as having that effect?

(2) what other pointers there are in the PA 2004 which indicate that Parliament either did or did not intend to apply s 43 in the circumstances?

213. The Targets' first submission is that there is nothing in PA 2004 which expressly states that s 43 is intended to apply in respect of acts or omissions which occurred before the legislation came into force. Granada arranged their affairs in 1999 to 2000 by entering into a particular transaction by which they disposed of the rental business for which they received a sum of money which they then applied in the course of their business. The Regulator is now seeking to upset those plans as to the sale and the proceeds of sale by imposing a liability that did not exist in 1999 to 2000 and which is based on criticisms of that transaction which they say was responsible for creating risks to the Scheme. To apply s 43 in the way which the Regulator has done would be an unfair retrospective application of that provision.

214. The Targets characterise the liability sought to be imposed on them as a financial sanction, a substantial financial detriment, which even if not imposed by reason of attribution of fault, is being imposed by reason of criticism of the Targets' conduct which is said to have created a relevant risk. That is a new liability that did not exist in 1999 to 2000 when the events which are subject to the Regulator's criticism took place.

215. In our view, s 43 is not retrospective legislation as that term is defined by *Bennion* as stated at [198] above. We agree with the Regulator's characterisation of s 43 as providing a present solution to a present problem; namely an employer being insufficiently resourced relative to its pension liabilities. That current situation may well have arisen because of the way in which the employers and those connected with them had been run historically. It may well be a result of events and transactions that took place some time before PA 2004 came into force. The purpose of the legislation is to create a rescue framework for pension schemes which are in deficit through the medium of imposing new liabilities on those who have had the necessary degree of

association and connection with the relevant scheme at the relevant time. The legislation clearly could not meet those objectives if the Regulator was not able to take into account events which had occurred prior to the legislation coming into force, even if those events had sown the seeds of the problems that exist at the time when the exercise of the powers in the legislation is under consideration.

216. In our view the legislation is a paradigm example of legislation which does alter existing rights and duties but does not do so in a manner which is retroactive. There are new financial obligations imposed by reference to transactions that have been entered into before the legislation came into force but they only operate prospectively and do not alter the legal effect of transactions that have already been entered into. Granada entered into the Joint Venture transaction and received consideration for the sale of the assets that took place pursuant to the transaction. At the time of the transaction, it may well have assumed that there was no prospect of any future liability being incurred in respect of that transaction as a result of a change of legislation in the future. But, as Lord Rodger said at [192] of *Wilson*, individuals and businesses run the risk that Parliament may change the law governing their affairs and, as was the case in *West v Gwynne*, may suffer financial detriment because of the imposition of a new liability.

217. A similar example, which was mentioned at the hearing of these references, would be if Parliament decided to impose new taxes which affected assets held by the taxpayer at the time of the imposition of the new tax. For example, at present an individual taxpayer is entitled to relief from capital gains tax on his principal private residence. If Parliament decided to remove that relief in respect of any disposal of a principal private residence that took place after the legislation came into force, then the taxpayer would suffer financial detriment which would not have occurred had he not acquired the assets concerned prior to the change in the law. There is a change in position for the future but no change to the terms of any transaction that took place prior to the change in legislation.

218. So in this case, s 43 does not upset or interfere with the terms of any of the transactions entered into in relation to the Joint Venture prior to s 43 having come into force. There is no recharacterisation or alteration of any contractual aspect of the Joint Venture transaction or its operation or the past conduct of the Targets.

219. In our view Lord Pannick's reliance on *Welsh Asbestos* is misplaced. Unlike the position in *Welsh Asbestos*, s 43 does not seek to impose a new liability, or augment an existing one, arising out of a past wrong. We do not accept that the issue of an FSD is properly characterised as an imposition of a financial sanction in respect of acts and omissions committed before the legislation came into force. As will become apparent later in this decision, we accept that the transactions that led to the establishment of the Joint Venture were perfectly legitimate business transactions which were not designed to enrich the Targets at the expense of other parties. The Regulator's decision to issue an FSD arose out of its consideration of the circumstances of the Scheme as at the look-back date, a date which is sometime after the legislation has come into force, and whether it would be reasonable to impose an FSD in the light of those circumstances. Seen in that light, we cannot accept Lord Pannick's submission that the imposition of a liability in respect of existing circumstances without the attribution of any

wrongdoing makes the Regulator's action more objectionable. It is not a matter of whether there is fault or criticism or no fault or criticism; rather it is the fact that the test for the issue of an FSD is not necessarily linked to one or more events or transactions but is linked to a state of affairs that exists at a particular time.

220. We therefore conclude that the presumption against retrospective legislation is engaged only lightly, if at all, in this case.

221. We also consider that there are indications in the legislation that Parliament did not intend to impose any cut-off date as regards the matters which the Regulator is entitled to take into account when considering whether to issue an FSD.

222. First, Parliament did address the temporal application of s 43. Section 43(5) limits the power of the Regulator to issue a direction to the situation where the potential target falls within subsection (6) "at the relevant time". The "relevant time" is defined for our purposes in subsections (2) and (9) as the time determined by the Regulator that falls within the prescribed period which ends with the determination by the Regulator to exercise the power to issue the FSD in question. That prescribed period was 24 months. Parliament therefore chose to impose the temporal cut-off date by reference to the existence of the necessary connection or association between the potential target and the employer rather than by reference to when any or all of the factors making it reasonable to issue the FSD occurred.

223. The position is different in the provisions limiting the temporal scope of the Regulator's power to issue a contribution notice under s 38 PA 2004. Section 38(3) provides that the Regulator may issue a contribution notice imposing a liability to pay the specified sum only if the Regulator is of the opinion that the person was a party to an act or a deliberate failure to act which falls within subsection (5) and if the person was an employer or connected or associated with the employer in the relevant period. Section 38 (5)(b) expressly limits the acts or failures to act which can trigger a contribution notice to acts or failures which first occurred on or after 27 April 2004 and which occurred during the period of six years ending with the determination by the Regulator to issue the contribution notice. A similar temporal limit was placed on the power to issue restoration orders under s 52 PA 2004 in respect of a transaction at an undervalue. Again, Parliament expressly limits the application of the power to transactions which were entered into with a person on or after 27 April 2004 and not more than two years before the occurrence of the relevant event as defined: see s 52(2)(b). By contrast Parliament did not include in s 43(7) any temporal limit on the matters which the Regulator is entitled to consider relevant.

224. Indeed, it is difficult to see how such a temporal limit could be applied given the nature of the factors that are included as potentially relevant to the Regulator's assessment of reasonableness. The contribution notice and restoration notice regimes are triggered by specific acts or failures to act or transactions the occurrence of which can be identified as having occurred at a particular time. Section 40(2)(a) provides that the contribution notice must contain a statement of the matters which it is asserted constitute the relevant act or failure to act. The legislation envisages therefore that it will be possible to apply the specific cut-off date provided for in that regime. The FSD

power by contrast is not triggered by a specific event but by the existence of a situation that has arisen in which the employer is a service company or is insufficiently resourced. We do not see how the legislation could properly be applied if there were such a temporal limit in the great majority of cases where the causes of the scheme's weakness can be traced back to myriad different decisions taken by the employer or the trustees of the scheme over many years.

225. In the course of argument Lord Pannick accepted that if the Regulator had identified an act occurring after the legislation came into force as the basis for its issue of an FSD then in order to explain or to address the responsibility for creating the risk that that act posed for the pension scheme, the Regulator can rely on matters that occurred prior to the legislation coming into force, but those earlier matters of themselves could not form the basis for the issue of an FSD. It seems to us that that blurs the very bright line that Lord Pannick sought to draw, namely that if all the acts concerned occurred prior to the legislation coming into force then there was no jurisdiction. On the basis of that concession, if, for example, a deficit in a scheme arose as a result of a whole chain of events which occurred prior to the legislation coming into force and which nobody at the time thought would cause difficulty in the future, but which, because of subsequent events after the legislation came into force have led to the scheme in question being insufficiently resourced, then it would be very difficult to devise a test which would enable the Regulator or the Tribunal to have regard to some circumstances which occurred prior to the legislation coming into force but not others. There is nothing in the legislation that would suggest that a workable solution to this problem can be found. It is even more puzzling to consider how this would apply where the FSD is based on the fact that the employer is a service company – it cannot have been Parliament's intention that only service companies set up after s 43 came into force can be covered. This is a further factor that leads us to the conclusion that Parliament did not intend there to be any difference as far as jurisdiction is concerned between situations where all of the acts concerned occurred before legislation came into force and those where some occurred before and some occurred after that time.

226. Lord Pannick argued that the effect of s 38(5)(b) and s 52(2)(b) is not to limit the temporal scope from what it otherwise would be but rather to extend it so that it could apply to acts, failures, or transactions occurring in the past whereas without those provisions, no act, failure or transaction occurring prior to the PA 2004 coming into force could have been the subject of the exercise of these powers. We do not agree that that is the correct interpretation of those provisions. There is no general principle that absent any indication of temporal scope, powers conferred on public bodies to take action in response to particular events can only be exercised in respect of events which occur after the power is brought into force. We accept Mr Stallworthy's submission that the only coherent reading of s 43 is that the absence of an express temporal limit on the matters to be taken into account when assessing reasonableness under s 43 is that Parliament intended to impose no such limit. As we have previously mentioned, since the contribution notice regime involves an imputation of serious wrongdoing, a feature which is absent from the s 43 regime, we can see why Parliament should have wished to impose a specific temporal limit in relation to the former but not the latter.

227. We must also have regard to the Regulator's statutory objectives. One of these is, as we have observed at [14] above, to reduce the risk of situations arising which may lead to compensation being payable from the PPF. The provisions relating to the PPF came into force at the same time as s 43. As Mr Stallworthy submitted, that objective would be substantially undermined if the PPF were immediately exposed to liabilities in respect of under-funded schemes but because of an inability to rely on events prior to the coming into force of PA 2004 no FSD could be issued. In our view, the legislation should be read so as to regard the powers in s 43 and the support for under resourced schemes available through the PPF as a package of measures which are available in relation to all circumstances concerning the relevant schemes which happen to be in existence after the relevant provisions come into force.

228. The primary element of the FSD regime on which the Targets rely as indicating that an FSD cannot be issued in this case is the power of the Regulator to issue a clearance statement in respect of circumstances described in an application under s 46 of PA 2004. Section 46 enables persons who are potentially the subject of an FSD to seek guidance, to identify the potential consequences of their action, and then decide whether to proceed or not to proceed in the light of the answer they get from the Regulator. That mechanism is a vital part of the machinery that Parliament created under PA 2004. In the case of the Box Clever joint venture, there was no opportunity for the Targets to seek such clearance before entering into the agreements. The Targets contend that if s 43 applies to transactions entered into prior to the coming into force of PA 2004, it puts those who entered into such transactions at a very substantial disadvantage compared to those who entered into transactions once the legislation came into force. It would be surprising, they argue, had Parliament intended the Regulator to base an FSD on transactions already completed, when that would fundamentally frustrate commercial certainty for those who have entered into such transactions.

229. We see the force of Lord Pannick's submission as regards the absence of a clearance regime. Mr Stallworthy's submission that the reason why a clearance regime was considered necessary in the first place was that without such a regime the contribution notice and FSD regimes might inhibit future investment in struggling companies so that there was a need for a procedure which would enable certainty for future business transactions, is not, in our view, a complete answer to the point. However, in our view this potential unfairness is clearly outweighed by the other factors we have described which lead us to conclude that overall the intention of Parliament was that the legislation should apply to circumstances such as those which have occurred in this case – we regard this as "a very qualified kind of hardship involved in giving the legislation a partially retrospective effect" to adopt Lord Mustill's phrase from *L'Office Cherifien*.

230. We can deal with Lord Pannick's submissions as regards moral hazard more briefly. The Targets argue that one of the main reasons why Parliament conferred the power to issue an FSD was to deal with the moral hazard created by the provisions of PA 2004, that is the risk that those managing occupational pension schemes would act irresponsibly secure in the knowledge that the PPF would be available to bailout the scheme if things went wrong. Moral hazard can have no application to events occurring before the coming into effect of the relevant provisions in PA 2004 because at that time

the PPF did not exist. We accept his submission that moral hazard was one of the important purposes of s 43 PA 2004: see the observations of Henderson J in this regard in *Independent Trustee Services v Hope* [2009] EWHC 2810 (Ch) at [55] and [56]. However, as is apparent from the discussion set out above as regards the purposes of the legislation, moral hazard is only one of the purposes and there is nothing in the legislation that suggests it is to be confined to circumstances where those associated with pension schemes act irresponsibly with the intention that the PPF should pick up the increased liabilities that result from such behaviour. As Mr Stallworthy correctly submitted, to confine the application of s 43 in this case on the grounds that there was no suggestion of moral hazard would fail to give due weight to the Regulator's statutory objectives for the reasons we give at [227] above.

Interference with the Targets' A1P1 rights

231. A1P1 provides as follows:

> "Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No-one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.
>
> The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in the general interest or to secure the payment of taxes or other contributions or payments."

232. A1P1 is given force and effect by the Human Rights Act 1998 (the "1998 Act"). By reason of s 6(1) of the 1998 Act, it is unlawful for the Regulator, as a public authority, "to act in a way which is incompatible with a Convention right." Therefore, if we decide that imposing an FSD in relation to events occurring entirely before s 43 came into force would breach the Targets' A1P1 rights, then it would be unlawful for the Regulator to issue an FSD and we would be obliged, if possible, to construe s 43 as precluding the issue of an FSD in those circumstances.

233. It was common ground that the imposition of an FSD requiring the Targets to provide financial support to the Scheme would affect the Targets' financial resources in a way which engages A1P1. This is because the amount of money that they would have to pay to satisfy the obligation imposed by the FSD is a possession for the purposes of A1P1: see *Axa General Insurance Limited and others v The Lord Advocate and others* [2012] 1 AC 868 (*"Axa"*) at [28].

234. In *Welsh Asbestos* Lord Mance JSC summarised the four stages of the court's review of legislation for compliance with Convention rights: see [45]. The stages for the court to consider are (i) whether there is a legitimate aim which could justify a restriction of the relevant protected right; (ii) whether the measure adopted is rationally connected to that aim; (iii) whether the aim could have been achieved by a less intrusive measure; and (iv) whether, on a fair balance, the benefits of achieving the aim by the measure outweigh the disbenefits resulting from the restriction of the relevant protected right. As to the last stage, Lord Mance noted that the European Court of Human Rights ("ECtHR") has indicated that these stages apply in relation to A1P1 with modifications

which have varied over the years. Having reviewed the case law Lord Mance concluded at [52]:

> "… the approach in Strasbourg to at least the fourth stage involves asking simply whether, weighing all relevant factors, the measure adopted achieves a fair or proportionate balance between the public interest being promoted and the other interests involved. The court will in this context weigh the benefits of the measure in terms of the aim being promoted against the disbenefits to other interests. Significant respect may be due to the legislature's decision, as one aspect of the margin of appreciation, but the hurdle to intervention will not be expressed at the high level of "manifest unreasonableness". In this connection, it is important that, at the fourth stage of the Convention analysis, all relevant interests fall to be weighed and balanced. That means not merely public, but also all relevant private interests. The court may be especially well placed itself to evaluate the latter interests, which may not always have been fully or appropriately taken into account by the primary decision-maker."

235. Lord Mance went on to observe that the ECtHR scrutinises with particular circumspection legislation which confiscates property without compensation or operates retrospectively. In the case of retrospective legislation, "special justification" will be required before the court will accept that a fair balance has been struck. The phrase 'special justification' was drawn from the ECtHR's judgment in *Bäck v Finlan*d (2004) 40 EHRR 1184 at [68].

236. Similar legislation providing that asbestos related pleural plaques are a personal injury and therefore constitute actionable harm was considered by the Supreme Court in *Axa*. Lord Reed described the court's task there as assessing "whether a fair balance has been struck between the demands of the general interest of the community and the requirements of the protection of the individual's fundamental rights" (at [126]).

237. The Targets do not challenge the compliance of the legislation with A1P1 for any reason other than what they contended was its retrospective nature. Lord Pannick also accepted that the first three stages described by Lord Mance in *Welsh Asbestos* are satisfied here – there is a legitimate aim, the measure is rationally connected to the aim and they do not suggest a less intrusive measure. The question therefore is whether a fair balance has been struck. The Targets argue that the Regulator is unable to identify any special justification for retrospective application. Given the unfairness caused to the Targets by the absence of any opportunity to apply for a clearance statement at the time when the terms of the joint venture were being settled and given the absence of any moral hazard, the balance they contend falls against giving s 43 the retrospective effect on which the Regulator relies.

238. We have already concluded at [216] above that s 43 is not truly retroactive or retrospective legislation, but is legislation which can alter prospectively the rights and obligations arising from pre-existing legal relationships. However, had it been necessary to consider the question of special justification in this case we would have accepted the Regulator's submission that the extent to which the provisions operate retrospectively is fair and strikes a reasonable balance between the interests of potential targets, of the members of insufficiently resourced pension schemes who have earned

their full deferred pension by their pensionable service and of the levy payers of the PPF.

239. In this case, the relevant provisions of PA 2004 can be said to be legislation with a social remedial aim, namely to deal with the problems of underfunded pension schemes. If extending the FSD power so that it can be exercised in circumstances where the lack of scheme funds arises from causes stretching back before s 43 came into force were not permissible under A1P1, the legislature would have been faced with two unattractive choices. Either the opportunity for scheme members to benefit from payments from the PPF would have to be delayed for several years so that the underlying reasons for the insufficient resourcing were more likely to post-date s 43 or there would be a substantial period when the PPF would take over the burden of insufficiently resourced schemes but without any assistance from an FSD. Either of those options would have significantly hindered the achievement of the objectives of the legislation. We agree with Mr Stallworthy's submission that Parliament intended there to be a symmetry between the liabilities of the PPF and the FSD regime.

240. Furthermore, there is no automatic imposition of liability if the threshold conditions are satisfied. The legislation confers on a public body a discretionary regulatory power which cannot be exercised except where it is reasonable to do so on the facts of a particular case. The exercise of that power is subject to judicial oversight through an independent tribunal with a full merits jurisdiction. That is a factor that the ECtHR considered relevant in *Bäck v Finland* where the creditor whose debt was extinguished was entitled to and had obtained a thorough and careful assessment of the case and was also entitled to a full review by an appellate court. These proceedings offered him, the Court held, a reasonable opportunity of putting his case to the competent authorities with a view to establishing a fair balance between the conflicting interests at stake: see [64] of *Bäck*.

241. In our view, all of these factors clearly outweigh the features which the Targets rely on as being unfair, namely the lack of a clearance procedure and the moral hazard point. We therefore conclude that any interference with the Targets' A1P1 rights in this case is proportionate and justified.

242. We have therefore rejected the Targets' case on a lack of jurisdiction on grounds of retrospectivity. However, as is apparent from the foregoing discussion, one of the reasons we have done so is because the Targets' arguments on the issue are capable of being considered in the context of the assessment which we must make as to whether it is reasonable in the circumstances of this case to issue an FSD. Therefore, we shall revisit the Targets' arguments in the context of our assessment of reasonableness.

Discrimination: the Carmelite point

The Carmelite point: the facts

243. The Carmelite point has come about in the following way. On 8 December 2008 Clifford Chance LLP acting on behalf of Carmelite applied to the Regulator for two statements. First, they sought a statement that in the Regulator's opinion in the

circumstances described in the application it would not be reasonable to impose any liability on Carmelite under a contribution notice issued under s 38 PA 2004. Secondly, they sought a statement that it would not be reasonable for the Regulator to impose the requirements of an FSD in relation to the Scheme on the applicant. Appendix 2 to the application set out a history of the Scheme and the applicants' association with it. Appendix 4 made the point that all the key events occurred before 27 April 2004 and raised the absence of any "control" within the meaning of the relevant statutory provisions. Carmelite said in the application that although RHC was a 50% shareholder in BxC Tech, RHC ceased to have any "control" as provided for in the Insolvency Act 1986 in relation to the employers in the scheme when the Administrative Receivers were appointed in 2003. This was more than two years previously and hence in the light of the time limits imposed by s 43(9) of the PA 2004, it would not be reasonable to issue an FSD.

244. The Regulator replied to the application on 25 February 2009. The letter ('the comfort letter') recorded the Regulator's view that so far as the contribution notice jurisdiction was concerned, the Regulator accepted that any act or failure to act that may have taken place predated the inception of its powers. As regards the FSD the Regulator said:

> "It is our view that the connection and association of RHC ceased before the inception of our powers and that for timing purposes set out in the legislation with regards to FSDs we would not be able to issue an FSD in relation to RHC or the applicants.
> We have therefore concluded that based on the information contained within the application neither a CN nor an FSD is available to the Regulator.
> We hope that this letter will provide the comfort your client seeks in relation to the events described in the application."

245. A meeting took place between the Regulator and the Trustee on 9 October 2009 at which the Trustee requested that the Regulator explain the rationale behind the comfort letter sent to RHC. The explanation was set out in a letter to the Trustee dated 15 October 2009 ('the rationale letter'). The legal analysis given in the rationale letter was different from the argument that was made to us by the Targets at the hearing and which we have rejected in respect of TUK for the reasons set out above. The rationale letter focused not on the appointment of receivers over the business of the company which held the shares in the Employer company but on the appointment of receivers over the business of the Employer company itself. The Regulator's interpretation was that RHC's "control" of the Employers within the meaning of section 435(10) ceased when the Administrative Receivers were appointed on 24 September 2003 in relation to those Employer companies. The rationale letter referred to *Unidare* as establishing that the use of the word "power" suggested that it was necessary to look at "the economic reality of the case". The Administrative Receivers had in each case taken over the effective management of the Employers and the economic reality was that the shareholders would not have the power to exercise their votes in any meaningful way in relation to the business of the companies. The rationale letter concluded:

> "It should be highlighted that the Regulator is only able to provide a view as to the interpretation of the legislation. The understanding outlined above was based on consideration by internal case teams and reference to counsel, however only the court would be able to give a definitive interpretation of the impact of insolvency on "association"."

246. On 17 November 2009, Hogan Lovells on behalf of ITV submitted an application to the Regulator for statements that it would not be reasonable to issue a contribution notice or an FSD against ITV. The point made in Appendix 4 of the ITV application about the cessation of control in relation to the Employers when Administrative Receivers were appointed was expressed in the same terms and put forward as one reason why it would be unreasonable to issue an FSD. The application also said:

> "ITV plc understands further that RHC and companies in the Carmelite Capital Group also sought clearance from the Pensions Regulator in relation to this matter and that a comfort letter was provided to Clifford Chance LLP in respect of the Scheme. We understand that this comfort letter confirmed that the Pensions Regulator's view is that any act or failure to act pre-dates the inception of the Regulator's powers to issue a Contribution Notice, and that RHC's connection with the Scheme employers ceased before the inception of the Regulator's powers to issue Financial Support Directions."

247. The Trustee was sent a copy of ITV's application and invited to comment on it. Eversheds on behalf of the Trustee wrote to the Regulator on 19 January 2010 responding to that application. The Trustee submitted that clearance should not be given to ITV and that the matter should be put before the DP so that they could consider issuing an FSD against the Targets. They set out at some length their view of the facts supporting the making of an FSD. They also took issue with the control point. The letter said:

> "This 'ceasing to have control' argument was the reason the Regulator gave, in its 25 February 2009 letter to RHC, as the basis for its view that it was not able to issue an FSD. Granada Rental is now seeking to rely on this same argument. However, the Trustee fundamentally disagrees with the Regulator's conclusion, which the Trustee has not previously had the opportunity to comment upon. The Trustee has obtained legal advice from Eversheds LLP and Mr Gabriel Moss QC, a leading insolvency silk, that the appointment of the administrative receivers did not result in the shareholders losing 'control' over the employers. Leading Counsel's opinion is attached as Appendix 2 to this letter.
>
> For the reasons set out in Leading Counsel's opinion, we submit on behalf of the Trustee that Granada Rental and RHC remain connected with and associates of the participating employers, even after the appointment of the administrative receivers."

248. In the conclusion of the letter the Trustee requested not only that an FSD be issued against ITV but that similar action be taken in relation to Carmelite:

> "The 25 February 2009 letter did not constitute a formal clearance, merely a statement of a view being taken on a matter of law. If, in light of the analysis from Mr Gabriel Moss QC, the Regulator is satisfied that the view offered in February 2009 was or could be incorrect, then it is, in our submission, bound to re-open the issue. This point, as to whether the appointment of administrative receivers puts companies beyond the reach of the Regulator, is significant and needs to be resolved by a Determinations Panel."

249. The opinion attached to that letter from Mr Moss dealt with the point that had been explained in the rationale letter rather than the point we have determined. He was asked to advise whether the fact that Administrative Receivers had been appointed over, in our example, TUK meant that THSP as owner of 99% of the shares in TUK no longer controlled TUK because the administrative receivers were now in charge of running TUK's business. The answer to that was clearly no. He did not address the more relevant question namely whether the appointment of the Administrative Receivers over THSP meant that the receivers rather than THSP now controlled the voting power of the 99% shareholding that THSP held in TUK. That is the more difficult question that we have answered in the Regulator's favour.

250. Nevertheless, Mr Moss' opinion was regarded by the Regulator as sufficiently on point to cause them to change their minds. On 11 March 2010, the Regulator wrote to Hogan Lovells attaching the Trustee's response. They said that based on that:

> "… the Pensions Regulator does not feel that it would be appropriate to grant clearance in relation to the Application or to issue a comfort letter in respect of the events and circumstances outlined in the Application."

251. Hogan Lovells responded to this email on 4 June 2010. By this stage the submissions made by Hogan Lovells were divided into jurisdictional issues, including control, and reasonableness issues. As to control, the letter said that ITV agreed that the appointment of an administrative receiver "does not mean that control is lost automatically". But it went on to say that before exercising its powers, the Regulator needed to be satisfied that any target of an FSD was connected or associated in the period of two years prior to the determination to issue an FSD. They then made a point which was not related to the appointment of administrative receivers but to the effect of the Debenture. They attached to the letter an opinion from Richard Hacker QC which dealt with the point arising from Clause 10.2 of the Debenture. They did not in this letter pursue a point about the effect of the administrative receivership of any company in the chain.

252. On 30 July 2010 the Regulator sent a letter to ITV requesting a valuation of ITV's resources for the purposes of the 'insufficiently resourced' test. ITV wrote back on 23 August 2010 objecting to the request arguing that they could not be required to respond to it since it appeared that the Regulator had not yet reached a conclusion on the

jurisdiction point. Again, they relied on the Richard Hacker opinion on the Debenture point rather than on a point about control moving to the Administrative Receivers. The letter, under the heading "Fairness and consistency", said:

> "2.16 The Regulator's current approach to its investigation is not consistent with the principles of fairness or consistency. Box Clever Technology Limited was a joint venture established between Granada and Thorn (and whose shareholdings are presently ultimately owned, respectively, by ITV and Carmelite). We are aware that Carmelite applied for clearance from the Regulator in 2009 and that, by letter dated 25 February 2009, the Regulator issued Carmelite with a comfort letter confirming that it did not have jurisdiction to impose a contribution notice or FSD. On the latter point, the Regulator stated expressly: "It is our view that the connection and association of [Carmelite] ceased before the inception of out powers and that for timing purposes set out in the legislation with regards to FSDs we would not be able to issue an FSD [to Carmelite]".
>
> 2.17 ITV agrees with this conclusion, and has obtained an opinion from Leading Counsel to support that view after careful consideration of the relevant documentation and background facts. The Regulator's approach in this investigation is not consistent with its approach to Carmelite. On the issue of jurisdiction, and whether or not ITV is associated with the Employers, precisely the same circumstances apply to ITV as applied to Carmelite. Having reached the conclusion in 2009 that Carmelite was not associated with the Employers so that the Regulator had no jurisdiction to impose an FSD on them, in order to satisfy the principles of fairness and consistency, the Regulator must either reach the same conclusion for ITV, or must withdraw its comfort to Carmelite and open an investigation into them as well."

253. The 30 July 2010 letter concluded by asking the Regulator to confirm whether it had reached a definitive view on association and therefore jurisdiction and if so to explain what that view was.

254. The Regulator wrote on 27 January 2011 saying that it had now received and considered an opinion provided by Leading Counsel and that the Regulator remained of the view that the threshold for jurisdiction was met. The Regulator declined to disclose the opinion on the grounds of legal privilege. The Regulator then turned to the question of fairness and consistency and the comfort letter issued to Carmelite. It said:

> "The comfort letter set out the Regulator's view of the correct interpretation of the law as at February 2009. However, having considered the various opinions on the question of association, the Regulator's view is now such that we consider that the threshold test is met in these circumstances.

> The principles of fairness and consistency do not require a public authority to be forever bound to a particular interpretation of the law.
>
> The Regulator does not consider that the comfort letter binds it in the consideration of its functions in relation to ITV. As the comfort letter was not issued to ITV, the letter does not provide your client with any expectation of any particular treatment by the Regulator.
>
> The use of powers (or not) in relation to Rental Holding Company Limited is confidential, and we will not discuss the exercise of regulatory functions against that company with your client."

255. By that point, therefore, battle had been joined. On 4 March 2011 Hogan Lovells wrote asking the Regulator to clarify the interpretation of the law which had led the Regulator in February 2009 to issue the comfort letter to Carmelite. The Regulator declined to elaborate saying that the issue of the application of the contents of that letter to ITV did not arise since it was directed to Carmelite alone.

256. The dispute about the disclosure of the Regulator's documents concerning its decisions about Carmelite then ensued. In a letter dated 30 March 2012, the Regulator explained that although it accepted that the legal analysis that had prompted the issue of the comfort letter to Carmelite was wrong, that did not mean that it would have refused to issue a comfort letter even on a correct understanding of the law, given Carmelite's other circumstances. Without prejudice to its primary contention that the position of Carmelite was irrelevant in the proceedings against the Targets, the Regulator pointed out various respects, apparent from publicly available materials, in which Carmelite's position was different from that of ITV.

257. The Regulator also robustly rejected ITV's request for "reassurance" that in the event that the Targets were ultimately ordered to provide financial support, the sum of the support would be "no greater than it would have been had the Regulator in fact proceeded against Carmelite". The Regulator said:

> "Your request asks the Regulator to engage in entirely misconceived mental gymnastics. The Regulator is of the view that the threshold test under section 10(2)(a) of the Pensions Act 2004 is not met in respect of Carmelite entities. The Regulator is also of the view that, if the Regulator had issued a Warning Notice to Carmelite entities, the regulatory procedure would have failed in that respect, because the Determinations Panel would not have determined to issue an FSD in relation to the Scheme to those entities. It necessarily follows from the Regulator's assessment of the merits of the case against Carmelite that, "had the Regulator in fact proceeded against Carmelite", the Regulator considers it overwhelmingly likely that such a procedure against Carmelite would have had no impact at all on the level of financial support from the Targets which the Regulator would have been willing to approve. On that basis, admittedly, we are able to say that "the sum of [the Targets'] financial support will be no greater than it would

> have been had the Regulator in fact proceeded against Carmelite"; but we suspect that in the circumstances this is not the reassurance you seek.
>
> If you are asking the Regulator to ask itself what financial support from the Targets the Regulator would have been willing to approve if the underlying facts had been different, so that if the Regulator had proceeded against Carmelite an FSD would have been issued to Carmelite, and the Regulator had indeed proceeded against Carmelite, that seems to us to be an even more pointless hypothetical exercise. However, we note that one potential option for financial support in those circumstances would have been for all the targets (i.e. both the Targets and the Carmelite entities) to be made jointly and severally liable for the deficit.
>
> The Regulator accepts that if it becomes necessary to seek a section 47 contribution notice in due course, consideration will need to be given to how, if at all, in the specific circumstances of this case, the fact that some entities involved in the Joint Venture have not been issued with an FSD should be taken into account when determining the sum to be specified in the section 47 contribution notice. But now is not the time to engage in such a debate: as was acknowledged at paragraph 24 of the Applicants' skeleton argument for Tuesday's hearing in the Upper Tribunal, the quantum of any support is "a matter to be determined in subsequent proceedings, if not agreed".

258. There was a lengthy response to this letter from Hogan Lovells on 16 May 2012, raising broadly the points that were argued before the Tribunal in the disclosure application referred to at [261] below and before us at the trial. ITV argued in its Reply in October 2012 that the present proceedings represent an unreasonable attempt by the Regulator to single out wealthy targets, at the cost of consistency and procedural fairness.

The Carmelite point: some preliminary comments

259. The discrimination point is put two ways – that it was unfair not to issue a comfort letter to ITV when it was requested or that, having changed its mind as to the law it was unfair to pursue ITV once the Regulator had decided not to pursue Carmelite. The Regulator has made clear that it did revisit the question of whether to pursue Carmelite after it had changed its view of the legal position.

260. None of the parties made any submissions as to the legal effect of the comfort letter issued to Carmelite and nothing in this decision should be taken as saying anything about the legal effect of a letter sent in such terms.

261. In its Statement of Case the Regulator put forward reasons why it had decided not to pursue Carmelite once it had changed its view of the law. The Regulator stated that for the avoidance of doubt, if they are relevant, which the Regulator denies, the circumstances of Carmelite are different as regards the merits of issuing an FSD from

the circumstances of ITV. This prompted the Targets to apply at the case management hearing in September 2013 for an order compelling disclosure by the Regulator of correspondence and information regarding its decision not to impose an FSD on Carmelite. The Regulator was unwilling to share with ITV the details of its investigations into another company. That application was rejected by the Tribunal on the grounds that any inquiry into why the Regulator had not pursued Carmelite was outside the scope of the Tribunal's jurisdiction and that further, the question of whether Carmelite should be pursued was irrelevant to the question whether it was reasonable to impose an FSD on ITV. The Tribunal has not, however, shut the Targets out from arguing that the Regulator has unfairly discriminated against ITV by issuing an FSD against the Targets and not against Carmelite and that this is a factor that points strongly against the FSD being reasonable within the meaning of s 43(7).

262. In the Regulator's opening submissions for the hearing before us, the Regulator relied on publicly available information to show that the Targets were wrong to assert that the position of Carmelite and of ITV were materially indistinguishable. The Regulator identifies the three entities which received a benefit from the consideration paid by the Joint Venture for the RHC business and notes that two of the three now have zero net assets and the third ceased to have any connection with the Joint Venture many years ago.

263. The submissions go on, however, to say that even if the facts relevant to whether to pursue Carmelite were the same as the facts relevant to ITV, that does not affect the Tribunal's task. We address this issue on the basis that the reason why the Regulator issued a comfort letter to Carmelite was its then incorrect construction of section 435 of the Insolvency Act 1986 and that, although it has since changed that view, the Regulator has concluded that it did not wish to retract the comfort letter and pursue Carmelite whether or not Carmelite's position is materially different from that of ITV.

264. The third preliminary comment we wish to make is that the Targets have argued that they are prejudiced by the Regulator's failure to pursue Carmelite because the Regulator seeks to hold them solely liable for the deficit, rather than their being able to share any liability with Carmelite. We agree with what the Regulator said on this point in its letter of 30 March 2012 set out at [257] above. We do not know yet the sum to be set in the FSD or whether, when calculating that sum, some account will be taken of the absence of an FSD for Carmelite. We do not know whether it is possible to reach any conclusion about whether the DP would have determined that Carmelite should be subject to an FSD. ITV's submission in effect is that because Carmelite and the Targets were joint venture partners, it was likely that in the absence of the comfort letter, ITV would have been liable to support only half the Scheme deficit and hence that for reasons of fairness and consistency, the Targets can only be liable for that limited amount now. That seems to us much too simplistic an analysis but it is not possible or desirable to say anything further than that at this stage. These are matters to be taken into account in determining the quantum of any financial support to be given following the issue of an FSD.

The Carmelite point: the decisions in Gallaher and NatWest

265. The primary authority that the Targets rely on is the decision of the Court of Appeal in *Gallaher Group Limited & others v Competition and Markets Authority* [2016] EWCA Civ 719 ('*Gallaher*'). That concerned the aftermath of the decision of the Competition Appeal Tribunal to allow the appeals brought by certain tobacco manufacturers and retailers against the decision taken by the Office of Fair Trading ('OFT') that they had infringed the competition rules in respect of the retail pricing of tobacco. Gallaher was also the subject of investigation by the OFT in respect of the same alleged infringement but entered into an early resolution agreement with the OFT. Under that agreement ('ERA') Gallaher did not contest its involvement in infringing conduct and obtained a substantial discount on the penalty imposed on it as compared to the penalty imposed on those who contested the OFT's allegations. At the time that Gallaher and others in a similar position were negotiating these ERAs, the OFT gave assurances to two other companies ('TMR') that if they entered into an ERA, the OFT would give them the benefit of any successful appeal by other companies without requiring TMR to appeal itself. It was accepted by the Court of Appeal that the giving of this assurance had been a mistake by the relevant official of the OFT conducting the negotiations in the sense that it was made without regard to and was inconsistent with the principles of finality and certainty: see [51].

266. The OFT did not inform any of the others negotiating ERAs about this assurance. Companies which had refused to enter into ERAs and had been subject to substantial penalties did appeal to the Competition Appeal Tribunal and the OFT's infringement decision was quashed as against them on the basis that no infringement of competition law had been established on the evidence. The penalties that had been imposed on the appellants were also quashed. The OFT decided in 2012 to abide by the assurance it had given TMR and paid TMR a sum equivalent to the penalty it had paid. The decision to make this payment to TMR, referred to in the judgment as 'the 2012 Decision', was announced on the OFT website. This prompted Gallaher to ask the OFT to withdraw the infringement decision against it and refund the penalty it had paid. The OFT refused on the grounds that any requirement on the OFT to replicate the effect of the assurance given to TMR would undermine the principles of fairness and legal certainty.

267. Lord Dyson MR, with whom Longmore and Lloyd Jones LJJ agreed, considered first whether the principles of equal treatment and fairness applied to the exchanges between the OFT and TMR. He held that the assurance given to TMR was clear and unambiguous and that it fell within the scope of the equal treatment principle that the OFT was obliged to apply to all parties in the early resolution process: see [33]. The OFT had emphasised in its guidance that it was bound to comply with the principle of equal treatment in all steps leading up to the imposition of a penalty. Moreover, the OFT had stated during the early resolution process that it would pass on to parties who had already reached agreement in principle the benefit of developments in the early resolution process. The Master of the Rolls held that this required the OFT to replicate all substantial aspects of, or relating to, one ERA that could in principle be applied to all and would be valuable to all: [36].

268. He rejected the submission of the OFT that Gallaher was not in a comparable position to TMR because it had not asked for the same assurance. Lord Dyson said:

> "39. In my view, the fact that one party (A) has made a request for more favourable treatment and another party (B) has not done so will rarely amount to a good reason for not treating them as being in a relevantly comparable position for the purposes of equal treatment if they are in fact otherwise in relevantly comparable positions. Take the present case. TMR and the appellants were, as a matter of fact, in relevantly comparable positions. … The fact that TMR (unlike the others) raised the issue of the effect on its position of a successful third party appeal was immaterial to the comparability of their positions."

269. Lord Dyson then turned to the question of objective justification for the difference in treatment as between Gallaher and TMR. The first instance judge Collins J had rejected Gallaher's judicial review application on the grounds that there was an objective justification because the difference resulted from an inadvertent and mistaken failure to take account of highly material matters, namely the principles of finality and certainty. Collins J relied on the decision of Jacob J in *Customs and Excise Commissioners v National Westminster Bank plc* [2003] STC 1072 ('*NatWest*') which we describe below. Collins J described that case as authority for the principle that as a general rule a mistake should not be replicated where public funds are concerned. Lord Dyson held that if Jacob J had laid down a general proposition in *NatWest* as regards mistakes then that was wrong. In an important passage in his judgment, Lord Dyson said, at [53]:

> "… It was accepted that the question whether there was objective justification for the less favourable treatment of the appellants as compared with TMR depended on whether the difference in treatment was fair *in all the circumstances.* Mr Beard [counsel for the OFT] accepted that the fact that a decision by a public authority is mistaken is not a trump card which will always carry the day so as to permit the authority not to replicate the mistake regardless of the circumstances. For the appellants, it was accepted that the question is whether there has been unfairness on the part of the authority having regard to all the circumstances. The fact that there has been a mistake may be an important circumstance. It may be decisive. It all depends."

270. Lord Dyson then distinguished the *NatWest* case from Gallaher's claim. One distinction was that Gallaher "had a strong right to and expectation of equal treatment" because the OFT had expressly committed itself to affording equal treatment to a limited and defined category of parties involved in the ERA negotiations. It was, Lord Dyson held, "relevant that the decision-maker itself recognised and expressly represented to those with whom it dealt that it would apply the principle of equal treatment". Secondly, there was no large administrative system involved in Gallaher's case; there was a small group of individuals within the OFT dealing with the ERA negotiations. Thirdly, there were no complex legal issues facing the OFT comparable to those facing the Commissioners in *NatWest*. The decision whether to give the

assurance to TMR had not been a particularly complex or difficult one. Finally, the Master of the Rolls described the unequal treatment as 'stark and manifest'. The failure at the time by the OFT to inform the other ERA negotiating parties of the assurance that had been given to TMR was particularly unfair and could only be justified on the "unimpressive basis that TMR had asked for the assurances and the other did not". The real question, he said, was whether the decision in 2012 to honour the assurance given to TMR but not treat Gallaher in the same way was justified. He held that this was a plain breach of the principle of equal treatment and was unfair.

271. Turning to the relief to be given, the Master of the Rolls noted that Gallaher had not sought to set aside the OFT's infringement decision as against it. They were seeking instead a payment of a sum equal to the penalties they had paid. This is how the OFT had dealt with TMR and there was no difficulty in adopting the same approach to Gallaher.

272. The *Gallaher* judgment is under appeal to the Supreme Court. The Supreme Court heard argument in the appeal on 13 and 14 March 2018 and judgment is awaited.

273. In *NatWest*, the Court was considering a claim for overpayment of VAT which the Commissioners for Customs & Excise refused in part, arguing that the taxpayer would be unjustly enriched. The taxpayer complained that other taxpayers seeking a refund in similar circumstances had not had to show that they had not been unjustly enriched but their claims had been met without question. Jacob J held first that the Commissioners had been right to conclude that the unjust enrichment defence was applicable in the circumstances and that the Commissioners had therefore been right, as a matter of VAT law, to refuse the refund and keep the VAT. The different treatment of Lombard was the result of different tax offices dealing with claims differently; it was not an unfair plot to single out this taxpayer but just that one tax office was more alert to the unjust enrichment point than others. Jacob J went on to hold that the Tribunal had no jurisdiction to consider the unfairness and equal treatment point. But he considered the substance of the complaint briefly. He said:

> "64. …. Just because a tax gatherer makes a blunder which favours some taxpayers by way of a windfall does not mean that he should perpetuate the blunder in favour of others. A number of wrongs do not necessarily make a right. The interests of the general community are involved – taxpayers collectively have an interest that tax properly due should be collected, and that there should not be repayments to people who are not entitled to them.
>
> 65. The ordinary taxpayer might indeed think that where repayments have not been justified what should really happen is that the tax gatherer should try to recover them. Mr Vajda submitted (on the basis of some provisions, not on a change of circumstances) that there would be difficulties with that here – difficulties which did I not understand and do not matter for present purposes.
>
> 66. The general principle of equality or non-discrimination is, of course, one of the principles of EU law. It requires that "similar

situations shall not be treated differently unless differentiation is objectively justified" …. It appears to me to be entirely within the ambit of objective justification to say that mistakes need not be perpetuated and to take into account the fact that what is involved here is both complex law and a necessarily large administrative system."

The Carmelite point: discussion

274. Even assuming that there was no difference in position between Carmelite and ITV that would justify pursuing one and not the other, we consider that this is a case where (a) the mistake as to the law which prompted the issue of the comfort letter should not be replicated for the benefit of ITV and (b) the Regulator's decision not to withdraw the comfort letter but still to pursue ITV is objectively justified. The *Gallaher* decision establishes that whether a public body can correct a mistake that it has made to the benefit of one entity when it turns to deal with another entity is fact sensitive – as Lord Dyson said "It all depends". We have come to the conclusion that the facts here firmly point in favour of treating the need to correct a mistake as an objective reason for dealing differently with Carmelite and ITV.

275. First, the issue of the comfort letter clearly was based on a mistaken view of the law. In fact, the view of the law expressed there, namely that the appointment of receivers over the business of the Employer company meant that there was a cessation of control was never an argument that ITV thought was strong enough to put forward itself. It did not seek to argue that Mr Moss was wrong in his opinion attached to the Trustee's letter of 10 January 2010. The arguments it put forward in correspondence were based instead on Clause 10.2 of the Debenture. The submissions made to us at the hearing were based both on Clause 10.2 and on the administrative receivership of the shareholder company not of the Employer company itself. This is not a case where ITV was misled by the comfort letter into believing that it was safe from a contribution notice or FSD because it accepted that the Regulator's view of the law was correct. It was a legal mistake made at an early stage of discussions between the Regulator and potential targets.

276. Moreover, the application of the statutory provisions to the structure of the Joint Venture group is a technical and complicated matter, more akin to the legal issue that confronted the Commissioners in *NatWest* than the issue for the OFT in *Gallaher*.

277. Secondly, there was no express indication at any time by the Regulator to ITV that it would take the same decisions as regards ITV as it took against Carmelite. There was no undertaking given by the Regulator that it would give Carmelite and ITV the benefit of the decision that it took as respects the other, in the way that the OFT expressly promised all ERA parties that they would get the benefit of all the negotiations being conducted. The Regulator accepted that it is a general requirement of law that public bodies must treat like cases alike, unless there is an objective justification for the difference in treatment. Consistency is a requirement of the rule of law. To treat like cases differently without an objective justification is arbitrary and therefore disproportionate and unreasonable. The Regulator accepts that such a

principle arises from the common law and from EU law. However, the strength of arguments that will succeed in justifying a difference in treatment must depend on the strength of the expectation of equal treatment that the complainant legitimately has. For example, there is no requirement imposed in the legislation on the Regulator to pursue *every* person who at the relevant time falls within section 43(6). There may be a number of candidates in view from which the Regulator chooses only one or two without needing to devote resources to investigating the other candidates. Given that no candidate can have any expectation that the Regulator will pursue either everyone or no one, the threshold for justifying the Regulator's choice may be very low. We accept that in the present circumstances where ITV and Carmelite were really the only two candidates and inquiries were started against both of them, the Regulator must provide some objective justification for deciding to pursue ITV when it was not pursuing Carmelite. But the threshold for establishing such a justification is lower here than it was in *Gallaher* because ITV has no strong right to or expectation of equal treatment based on anything the Regulator has said. It cannot be the case that more generally a potential target can demand that the Regulator explain why it is not pursuing any other entity that the potential target asserts also falls within section 43(6) in respect of a scheme.

278. Thirdly, we consider that the reference by Jacob J in *NatWest* to the interests of the general community are important here. In *Gallaher* there was scant legitimate public interest in retaining the value of the fines that Gallaher had paid when the infringement decision had been quashed as against all those who challenged it. There could have been little doubt that if Gallaher and the other ERA parties had appealed, the decision would have been quashed as against them too and their penalties refunded. The position was different in *NatWest* where the court held that the taxpayer would be unjustly enriched if the VAT was refunded and that the Exchequer was therefore entitled to retain the money, if the mistake could be corrected. In the present case, if the Regulator is indeed precluded from pursuing ITV because of the comfort letter issued to Carmelite, there will be no one from whom financial support for the insufficiently resourced Scheme can be sought. The whole burden of fulfilling the Scheme members' entitlement will fall on the PPF. We recognise that the PPF is funded by industry levy rather than from the more general public purse, but the public interest is still engaged. We accept the Regulator's submission that it is difficult to see how it could be fair to the levy payers funding the PPF for them to be fixed with an additional liability because of the Regulator's mistake. This is different from the situation in *Gallaher* where it could not be considered unfair for the Exchequer to have to pay a sum equivalent to the penalties when the decision imposing the penalty had been quashed as against all those who had appealed.

279. Fourthly, we do not accept that the Regulator was obliged, once it had realised its mistake, to choose between either pursuing Carmelite as well as ITV or dropping its proceedings against ITV. The Regulator could expect that any attempt to revoke the comfort letter and start an investigation against Carmelite would be strongly resisted. The stream of legal and factual points raised by ITV in lengthy correspondence to which the Regulator needed to respond would have been replicated by having to deal with Carmelite as well. At each stage the proceedings would have been more complicated and expensive. It is not surprising that once the Regulator has focused its limited

resources on one group of financially stable potential targets, it holds back from taking on the challenge of pursuing another.

280. In our judgment, therefore, there was a sufficient objective justification for the difference in treatment between ITV and Carmelite and this element of the Targets' challenge to the Regulator's jurisdiction fails.

The moral hazard point

281. The final point pursued by the Targets as both a jurisdiction point and a point going to reasonableness was that the Regulator has no jurisdiction to issue an FSD because the conduct of the Targets did not generate the moral hazard that the FSD regime is designed to prevent. The Targets say that the practical concern underlying the regime is clear. It does not provide an unrestricted power by which the Regulator can seek ex-post facto to upset the consequences of bona fide commercial transactions, in an unprincipled and uncertain fashion, but seeks to address a particular problem, namely the risk that the existence of the PPF gives rise to morally hazardous behaviour. This is reflected in s 5(1)(c) of PA 2004 which includes as one of the Regulator's statutory objectives the reduction of the risk of situations arising which may lead to compensation being payable from the PPF. It is also apparent from the Report for Grand Committee prepared in October 2004 by Malcolm Wicks, the then Minister of State for Pensions, on what he described as 'the moral hazard clauses of the Pensions Bill' which had been introduced by Government amendment to the Pensions Bill in Commons Committee on 27 April 2004. He described moral hazard as the risk that, because the PPF will compensate scheme members if their employer has become insolvent and the scheme is underfunded:

> "employers will deliberately manipulate their affairs so as to shift their deficits to the PPF, thus increasing the PPF levy costs for responsible employers"

282. Mr Wicks identified the contribution notice and the FSD provisions as the moral hazard clauses. He described the amendments that were planned to the Pensions Bill in response to concerns that had been raised by the clauses that had been introduced.

283. The Targets say that it flows from this that in order for the regime to be engaged, it is necessary to identify behaviour which "is in some sense morally hazardous", that is to say, conduct which involves people organising their affairs so as to shift the burden of providing pensions to the PPF.

284. In the present case the Targets say that there is no question of moral hazard for two reasons. First, the creation of the Joint Venture and the agreement of the terms for the sale of the business to Box Clever occurred at a time before the PPF existed or was even contemplated by the Bill. Secondly, they point out that at the time the Joint Venture was established, the intention was to provide a money purchase, defined contribution, scheme which would have been outside the ambit of the regulatory regime.

285. It is impossible, therefore to identify anything morally hazardous about Granada's conduct or its organising of its affairs and therefore, the Targets submit, there is no basis on which the regime can and should apply.

286. We can dispose of this point shortly. The FSD provisions in the PA 2004 lay down in detail the test which must be satisfied before the Regulator has jurisdiction to issue an FSD. Those do not include any requirement that the conduct of the potential targets was such as to create the moral hazard at which the regime is directed. We do not accept that because the need to avoid moral hazard was part or even the whole of the reason why the FSD regime was devised means that there is some implied additional criterion to be satisfied before an FSD can be issued. There is no basis on which any such requirement can be implied into these detailed provisions.

287. We also reject the submission that the scope of the clearance provisions assists the Targets. They argue that the natural inference from the clearance regime is that Parliament intended the moral hazard powers to apply only in circumstances where companies had the opportunity to apply for clearance for the acts in question so that they could then modify their conduct in the light of the response to an application for clearance. Since the clearance regime did not exist at the time when the arrangements for the Joint Venture were devised, they did not have that opportunity to check that the arrangements did not create the risk of an FSD in the future. We do not agree that it is possible to draw any inference from the clearance regime to override the clear wording of s 43(5) setting only two threshold requirements; that the proposed target falls within subsection (6) and the Regulator is of the opinion that it is reasonable to issue the direction.

Conclusion on the Jurisdiction Issues

288. For the reasons set out above, we have concluded that the Regulator and hence this Tribunal has jurisdiction to direct the issue of an FSD and we now turn to the question of whether it is reasonable to do so in this particular case.

VII. REASONABLENESS: FINDINGS OF FACT

Background to the Joint Venture

The television rental market

289. The Joint Venture was formed against a background of a decline in the market for rented televisions which had been ongoing for many years by the late 1990s. The evidence shows that the turnover of Granada's rental business fell by 19% over two years from 1997 to 1999. Similarly, the turnover of Thorn's rental business fell by 21% over those two years.

290. Granada's strategy in the face of that downturn had been to acquire businesses and benefit from the consequent merger synergies that could be created by eliminating duplicated costs. According to Mr Wakelam's evidence, Thorn had been pursuing a similar strategy in the years preceding the merger. By the late 1990s, renting televisions had become increasingly peripheral to Granada's overall corporate strategy which was

to focus on its media business. At the same time, its strategy of acquisition was reaching its natural end, with Thorn the only significant opportunity left in the market. Unlike the Joint Venture, none of the earlier acquisitions had involved the integration of two equal senior management teams or of two different business models.

291. A report prepared by Price Waterhouse Coopers ("PwC") for the purposes of the proposed Joint Venture in April 2000, known as the "Project Sizzle" report, discloses that Granada and Thorn had different strategies for their rental businesses. Granada's business was focused on profitability, with a heavy investment in rental assets and a focus on encouraging customers to upgrade. Granada also tried to develop non-rental income, for example through retail sales and sought to maintain its rental base through add-on sales. On the other hand, Thorn's rental business was focused on cash generation and had sharply declining levels of capital expenditure and a declining rental base. It had a focus on added value products such as widescreen TVs and Home Movie Centres and on reducing overhead costs. It appears that initially the strategy that was intended to be applied to the Joint Venture was similar to the Granada strategy but that changed in due course to one that was similar to the Thorn strategy.

292. However, aside from the opportunity to merge with Thorn, there were other preliminary discussions regarding a possible sale of the Granada rental business. The evidence shows that Granada was in discussions with a potential purchaser in early 1999. At some stage prior to September 1999 Granada had received an offer of £400 million from Doughty Hanson, and by November 1999 Granada had received an indicative offer of £450 million, which was described in a memorandum to the Board of Granada that month as "the best indicative offer we have received elsewhere."

The negotiations for a merger of the two businesses

293. Granada had considered combining the two businesses by the middle of 1997 and in the summer of 1998 both companies approached the Office of Fair Trading to discuss a potential merger. At the same time, Lazard Brothers, Granada's financial adviser, advised that an appropriate way to effect the combination was by a leveraged Newco being formed to acquire both businesses, it being envisaged that strong cash flows from the cost savings generated by the merger could be used to support the leverage. In due course Granada could sell or demerge its stake in Newco.

294. An internal paper prepared by Granada in February 1999 was very positive about the prospects for the merged businesses. It noted that stability was needed in the market sector which was under increasing pressure as consumers moved away from renting televisions to buying them. The paper stated that a merger of the businesses would generate a dramatic increase in profit, both through a reduction in shared costs and a big increase in business efficiency.

295. Discussions with Thorn started shortly thereafter. A fax sent by Mr Parrott to Mr Tagliaferri on 16 July 1999, however, recognised that these discussions were taking place against a background where the "rental sector is currently in such serious decline". He noted that whilst both Thorn and Granada had attempted to strengthen their business by introducing new lines, none of these had been successful enough to

come near to compensate for "the endemic decline of their core business". Neither party saw product diversification as a way out of the problem of the serious decline in the core rental market.

296. Therefore, it was clear, as Mr Redmayne, the Regulator's expert, expressed it in his report for this hearing, that the commercial rationale behind the creation of the Joint Venture was to bring together the two largest businesses in the declining UK market for the rental of consumer electronics. They would have the scale to compete more effectively with retailers and benefit from cost synergies through, for example, a rationalisation of stores, service infrastructure, and management and other staff.

297. As mentioned above, Granada appointed Lazard Brothers as its financial adviser and received advice on, among other things, the appropriate price it should receive for its business. Thorn were receiving corresponding advice from Schroders.

298. The first set of valuation materials which were in evidence is a "Project Sizzle" paper prepared by Lazard on 2 March 1999. The aim of the paper was stated to be to provide valuations for the Granada business on a stand-alone basis, for the synergies of bringing the two businesses together (based on information only available for Granada), for Thorn on a stand-alone basis, and for Thorn under Granada's management (not double counting synergies). In summary, the respective valuations were:

(1) For the Granada business on a stand-alone basis, £600 million, the figure that was ultimately adopted as the amount to be paid to Granada in consideration of the transfer of its rental business to the Joint Venture.

(2) For the potential annual costs savings achievable through synergies at some £84.1 million, with a capitalised value of some £550 million.

(3) For Thorn's business in a range between £250 million and £450 million.

(4) For the net present value of the potential improvements that could be made to Thorn's business in a range between £550 million and £650 million.

299. As a result, Lazard considered that the merged business could have a value of between £1.45 billion and £1.85 billion, a sum well in excess of what was ultimately paid by the Joint Venture for the two businesses.

300. In the event, following discussions over the spring and summer of 1999 between the two parties and their respective financial advisers, it was agreed between the two advisers that an appropriate enterprise value for the merged businesses was £1 billion. That figure appears from "Project Sizzle" briefing material prepared by Lazard on 9 September 1999. This agreement followed discussions as to what share of the Joint Venture company each of the parties would have. It was agreed that the combined business would be owned 50:50 between the two parties. This meant that each of them would participate equally in the upside brought about by the synergies, but meant that the owner of the less valuable business would have to make a payment to the owner of the more valuable business to reflect the greater value the latter was contributing. That aspect of the negotiations was described in the Lazard briefing materials as the "share of the cake". The brief referred to the fact that having provisionally agreed that the

enterprise value was in the region of £1 billion, it was important to agree the split of the entity value between the two parties.

301. In that regard, the briefing materials now gave the Granada business a stand-alone valuation of £463 million. At this point in the negotiations, Granada were proposing a "share of the cake" of 65% / 35% in their favour whereas Thorn were proposing 54% to Granada and 46% to themselves. The briefing materials gave figures as to how a "share of the cake" at the midpoint between these two positions would turn out, that is 60% to Granada and 40% to Thorn. On that basis, Granada's share would be £600 million and Thorn's would be £400 million. The brief showed that of that £600 million, £535 million would be paid in cash to Granada by the Joint Venture, with the remaining £65 million representing its equity value in the Joint Venture. The corresponding figures for Thorn would be £335 million and £65 million respectively. A manuscript note on the document highlights the £463 million figure for the stand-alone valuation, contrasting it with the "£ 535 on the previous page."

302. The parties had always contemplated that the cash payments to them for the sale of their respective businesses to the Joint Venture would be financed by a loan to the Joint Venture and that a short time after completion that loan would be securitised. The briefing materials referred to at [301] above showed the Joint Venture having a combined debt capacity of £870 million.

303. A further briefing paper prepared by Lazard for Granada in September 1999 ahead of a meeting with Mr Hands showed Granada's objective as being to create a "50/50 NewCo so that we can both share equally in the upside". This would require a resulting cash adjustment to the amounts that the parties were to receive on the acquisition of the respective businesses by the Joint Venture.

304. In the meantime, discussions had been advanced with WestLB as regards financing for the Joint Venture. The first indication of their involvement that we have is a fax from WestLB to Mr Staunton dated 28 May 1999. The fax requested preliminary due diligence information on a number of key areas, namely an overview of the operations of the TV rental business, the composition of the current rental portfolio and its historic performance, historical financial information and future management projections. As was to be expected, bearing in mind that a securitisation was envisaged, this list of areas for due diligence indicates that WestLB's focus was very much on the cash flow to be achieved from the rental portfolio.

305. On 13 June 1999 Thorn had completed the securitisation of its rental business with another bank, CIBC. The securitisation raised £309 million.

306. An internal WestLB memorandum from Mr Andrew Gardner of WestLB to his colleagues dated 3 November 1999 indicated that by that time WestLB had formed the initial view that Granada's rental business was a good candidate for a securitisation. He said that looking at the plans envisaged for the Joint Venture and the costs savings that the parties expected to generate, the combined business had the potential comfortably to realise debt capacity of £800-£850 million in the medium term. This memorandum described how WestLB had carried out some due diligence on Granada's

business, had met senior management and had a tour of the site and call centre facilities. They had also met the rating agency which reviewed Thorn's recent securitisation. The memo concluded that on the basis of their due diligence and if the cost savings that the management expected were in fact achieved, they were "highly confident" that a securitisation programme could be put in place in a reasonable timeframe.

307. This memorandum indicates that WestLB were alive to the general trend of a long-term decline in the TV rental market, but concluded, on the basis of their due diligence to date and the application of a range of stress factors, that they were confident that the combined businesses could support a securitisation programme in an amount of £850 million. We have no details of any further due diligence that WestLB may have undertaken before it made its decision in December 1999 to finance the Joint Venture. The memorandum also reveals that WestLB had themselves considered purchasing Granada's business as a principal and in so doing, they had considered its enterprise value to be in the region of £450-£500 million.

308. On 10 November 1999 a presentation was given to WestLB by the parties. This indicated that the Joint Venture was seeking to maximise gearing, exploit the synergy benefits and market opportunities and pursue an IPO three years after the merger. The paper referred to the "huge synergy savings" which were envisaged and which motivated the deal.

309. On 16 November 1999 a report by the Granada Group Finance department was made to Granada's Board regarding the negotiations. The report stated that the negotiations with Nomura had established the value of the existing businesses as being £600 million for Granada and £400 million for Thorn. The objective of the deal was to extract that value in cash now and share equally in any additional value created thereafter. The report observed that this valuation was to be compared with the best indicative offer received elsewhere of around £450 million. It was clear that Granada believed that there was additional value to be created through cost savings and benefits from implementation of growth plans and that the value of the equity of the merged entity in three years' time could be around £1.2 billion.

310. The Granada Board resolved on 22 November 1999 to proceed with the merger. By December of that year the negotiations were reaching a conclusion. The "share of the cake" was agreed as to 60% to Granada and 40% to Thorn and it was agreed that each party would own 50% of the shares in the Joint Venture. It was agreed that in order to achieve a commitment from WestLB to provide £860 million of debt to the Joint Venture, the synergy assumptions made in the proposed five-year business plan for the Joint Venture would be supported by a report from AT Kearney and a report on the business model from PwC. AT Kearney had detailed knowledge of Thorn's current rental business as a result of other consultancy work that it conducted for Thorn since its acquisition by Nomura in 1998. We accept that, as it stated in its report, in the course of that work AT Kearney had gained an understanding of the economics of the UK rental business, some of the key issues facing the market, and many of the differences and similarities between the parties in relation to the proposed Joint Venture.

311. AT Kearney provided their report to WestLB on 8 December 1999. In summary, they identified potential synergy savings of around £114 million from the combined cost base of £340 million, representing a 34% saving from the merger of the two businesses. Their view was that those savings could be fully achieved through an 18 month post-merger integration programme incurring a one-off implementation cost of around £89 million primarily for redundancy and property disposal. The categories of cost synergies identified were rationalisation of the overlapping shop networks, reduction of the duplication in central overheads, rationalisation of the distribution and supply networks and harmonisation of business processes, call centre consolidation and harmonisation of debt management processes. The AT Kearney report concluded that Project Sizzle could deliver substantial benefits and "help position the combined company to compete and create value".

312. PwC also prepared a report for WestLB at about the same time, auditing the business model for the Joint Venture. This PwC report dated 17 December 1999 observed that in the very short time available for their work, the scope of PwC's review had been limited and considerably less than would normally be the case in respect of a transaction of this size and nature. PwC's conclusions were tentative, but they did conclude that the merger appeared well researched and planned in detail. PwC identified two assumptions that they considered were critical to the projected cash flow, namely increases in projected average unit rental values and a decrease in the level of total expenditure. They recommended that sensitivity analyses be undertaken by WestLB on those assumptions to determine what effect shortfalls as against those assumptions would have on the business' ability to service its debt facility.

313. Whilst the AT Kearney and PwC reports were prepared for the benefit of WestLB, Thorn commissioned a report from KPMG. This report was limited to advice on the preparation of a balance sheet of the Thorn rental business as at 30 September 1999, a high-level review of that balance sheet and a preparation of a reconciliation to the audited statutory accounts for the year ended 31 March 1999. It appears that KPMG were commissioned to provide a similar report as regards the net assets of Granada's rental business, and although a draft of this report was in evidence we have not seen a final version of the report.

314. Although those KPMG reports would have given some comfort to each Joint Venture partner as to the net assets of their respective businesses, they were not due diligence reports in the conventional sense. It therefore appears that in contrast to WestLB, neither of the Joint Venture parties commissioned any formal due diligence on their respective businesses and certainly none was commissioned on behalf of the Joint Venture itself. Neither did the Joint Venture have the benefit of any advice as to the valuation of the two businesses it was acquiring or its ability to service the debt obligations that it would assume if WestLB agreed to proceed with the financing of the Joint Venture. However, although the Joint Venture had no independent advice in relation to the negotiation of the terms of the Joint Venture, it did have the benefit of some limited warranties and indemnities in respect of the Granada and Thorn rental businesses. These were included in the terms of the Contribution Agreement which was negotiated between Granada and Thorn.

315. It would appear that WestLB were satisfied with the conclusions of the AT Kearney and PwC reports that had been prepared for its benefit. On 17 December 1999 it issued a commitment letter to Granada and Thorn by which, subject to the fulfilment of certain conditions including satisfactory further due diligence, it committed to provide banking facilities to the Joint Venture. This would take the form of, amongst other things, an Interim Bridge Facility of up to £860 million to finance the acquisition by the Joint Venture of the rental businesses of Granada and Thorn and a securitisation programme to finance the ongoing business of the Joint Venture. It was envisaged that the securitisation programme would be implemented so that the Interim Bridge Facility could be repaid out of the proceeds of that programme within twelve months of the establishment of the Joint Venture. Security was to be provided by means of fixed and floating charges over all material members of the Joint Venture group of companies.

316. Obtaining the necessary credit approval within WestLB was not straightforward. This emerges from a judgment of the Düsseldorf District Court of 19 June 2008 relating to a criminal prosecution against Mr Sengera, the Chairman of the Executive Board of WestLB for alleged breach of trust relating to the granting of the loan to the Joint Venture. The judgment states that the central credit management department ("CCM") of WestLB, which scrutinises all significant loan applications, rejected the application on 26 November 1999 on grounds of excessive risk and because it concluded that the anticipated value of the synergies created by the merger of £200 million should not be included in the sum financed – these cost savings were considered to be a typical equity risk that should not be co-financed by the lender. The effect of rejection was that the Executive Board had to provide a special justification if they nevertheless went on to approve the loan, but rejection did not trigger any tighter control mechanisms.

317. Mr Sengera was acquitted by the Düsseldorf District Court but his acquittal was overturned on appeal by the Federal Appeal Court in a judgment given on 13 August 2009 and remitted for a retrial. That judgment makes reference to a survey commissioned by the German Federal Financial Supervisory Authority following the failure of the Joint Venture, which came to the conclusion that the lending to the Joint Venture had been an exceptionally high risk and the commitment was made under time pressure without adequate risk analysis and without the necessary organisational arrangements to monitor the project being in place.

318. We have not relied on these findings in our conclusions on reasonableness, but we observe at this stage that neither party disputed the assertion that CCM had refused the application initially but, as recorded in the judgment of the Düsseldorf court, the Executive Board of WestLB had subsequently approved the transaction on 14 December 1999, which according to the judgment, it was able to do so if a special justification was provided for approval.

The establishment of the Joint Venture

The Contribution Agreement

319. The commitment from WestLB was sufficient for the parties to enter into the necessary legal agreement, the Contribution Agreement, to establish the Joint Venture on 17 December 1999.

320. The parties to the Contribution Agreement were Thorn, Granada, BxC Tech and BxC Finance. The principal terms of the Contribution Agreement can be summarised as follows.

321. First, pursuant to Clause 2.1 of the Contribution Agreement, Thorn and Granada agreed to acquire equal shareholdings in the newly formed parent company of the Joint Venture, that is BxC Tech. Those shareholdings were acquired in exchange for each of Thorn and Granada transferring £5 million of loan notes to BxC Tech issued to them by BxC Tech's subsidiary, BxC Finance.

322. Second, Clause 2.4 of the Contribution Agreement required Thorn and Granada to take the necessary steps to procure that each of the relevant Joint Venture companies drew the maximum sums available to them pursuant to the WestLB facility. Those sums were to be applied as follows:

(1) In paying off the amounts due under Thorn's securitisation.

(2) In paying off the existing indebtedness of the companies carrying on Granada's rental business and which were to be transferred to the Joint Venture, including intra-group indebtedness and external debts.

(3) In paying in cash to Granada $^{53}/_{33}$ of the amount necessary to pay off Thorn's securitisation debt less the amount used to pay off the debts of the companies Granada was contributing to the Joint Venture. The purpose of this appears to have been to compensate Granada in the event that Thorn's proportionate share of the amounts used to pay off the existing debts of the businesses being contributed exceeded the proportion of the total purchase price which it had been agreed Thorn should receive.

(4) Further amounts in cash to each of Granada and Thorn, being a proportion of the borrowings raised from WestLB and not used to pay off the existing indebtedness of the Granada companies and the payment to Granada mentioned at (3) above. The proportions payable were $^{53}/_{86}$ to Granada of the amount available and $^{33}/_{86}$ to Thorn of the amount available.

323. The remainder of the purchase price payable by the Joint Venture was satisfied by the issue of loan notes by BxC Finance to each of Granada and Thorn. The amount issued to each party was calculated in such a way that it took account of the cash adjustment made between Granada and Thorn to recognise the extra value that Granada had contributed to the Joint Venture as opposed to that contributed by Thorn. That factor was also recognised in the formula used for calculating the cash consideration

described at [322 (4)] above. The Contribution Agreement proceeded on the basis that the total value of the businesses transferred was £1 billion of which 60% was attributable to the Granada business, so that with borrowing at £860 million, Granada would be entitled to receive 60% of that sum, namely £516 million, together with an additional payment equal to 10% of the equity value it was effectively transferring to Thorn. That sum was £14 million, being 10% of £140 million, the equity value of the business resulting from the deduction of the £860 million of borrowing from the £1 billion consideration figure.

324. It can be seen from the manner in which the consideration was agreed to be shared, that the higher the value of the combined business, the larger the fraction of the WestLB loan attributable to Granada would have been. This meant that Thorn had an incentive to argue for a lower agreed value for the combined business.

325. Therefore, as appears from Mr Thompson's evidence, the consideration paid by BxC Finance was as follows:

(1) £351,971,619 in cash to Rental & Retail for Granada;

(2) £174,050,300 which was applied to repay Granada's overdraft and other financial debts;

(3) the issue of £73,976,081 in nominal value of loan notes by BxC Finance to Rental & Retail for Granada (of which £5 million were used by way of shareholder's equity contribution to BxC Tech);

(4) £142,792,112 in cash to Thorn;

(5) £184,730,970 which was applied to repay Thorn's debts; and

(6) the issue of £52,476,919 in nominal value of loan notes by BxC Finance to Thorn (of which £5 million were used by way of shareholder's equity contribution to BxC Tech).

326. Accordingly, the value of the consideration to be received by Granada from BxC Finance was £600 million and that received by Thorn was £380 million.

327. Schedule 10 to the Contribution Agreement provided that the Joint Venture should have its own pension scheme. At this stage, the Agreement provided that the Scheme would provide money purchase benefits only. The Schedule envisaged that employees of the Joint Venture would become members of the new Scheme and transfer payments would be made in respect of accrued benefits of those employees in the relevant Legacy Scheme.

328. Completion of the Contribution Agreement was subject to a number of conditions, notably clearance of the transaction by the Office of Fair Trading. Completion was also conditional upon WestLB providing the necessary borrowings on the terms set out in the Term Sheet attached to the commitment letter referred to at [315] above.

329. As also mentioned above, WestLB's commitment was subject to further satisfactory due diligence. In that regard they received a further report from PwC on 19

April 2000. That report, running to some 300 pages, was much more substantial than the December 1999 report. PwC's terms of engagement made it clear that they only assumed responsibility to WestLB for the contents of that report and so expressly stated that they assumed no responsibility to either Thorn or Granada. In their engagement letter dated 25 January 2000, PwC described the work that they were going to undertake as "less than would be normal for this type of engagement". They stated expressly that they had not been asked to review taxation matters or to consider any issues relating to structuring the proposed transaction or issues connected with implementing the merger of the two underlying businesses. It was clear that the assignment was not to include any commercial due diligence, including a review of the market and the business model. The report concentrated on the following areas relating to each of the parties' respective rentals businesses:

(1) Historical results, including the reliability and efficiency of arrangements for management and accounting information;

(2) Balance sheets, including the basis for the valuation of assets and provisions for liabilities;

(3) Cash flows, including analysis of working capital movements and capital expenditure;

(4) Current trading and achievability of management's full-year forecast, together with the soundness and appropriateness of the systems for forecasting;

(5) Future results, cash flows and balance sheets, including comment on significant trends and on the assumptions for projected synergies including shop closure savings, redundancy costs and joint purchasing cost savings; and

(6) An assessment of the main assumptions underlying the forecasts and projections and whether they are realistic but not including any review of projected financing structures and how they may relate to headroom and covenants.

330. The PwC report concluded that the proposed merger had been well researched and planned in detail and that the management were confident that they can implement the changes necessary to meet the projections for cost savings and benefits to result from the merger.

331. PwC recommended various adjustments they considered should be made to the model which had generated the financial estimates, and sensitivities which they considered should be run. These were reductions in assumed growth in non-rental income, a lower assumed mix of more valuable products, a reduction in new installation rates, an increase in the average cost per unit of new rental assets, a reduction in the ceasehire rate and a change in the assumption as to the profile of which assets were re-rented and which were sold. PwC also issued a further report on taxation matters which had been excluded from the scope of their original report.

332. Following this report, WestLB clearly decided to proceed with the maximum amount of the borrowing provided for in their commitment letter. The Secretary of State

confirmed on 19 April 2000 that he would not refer the merger to the Competition Commission.

333. It was envisaged that the entities transferred by Granada and Thorn to the Joint Venture would give security over their assets for the borrowings from WestLB, which would amount to financial assistance in relation to the acquisition of the shares of those entities. It was therefore necessary, pursuant to the Companies Act 1985, that the directors of the relevant companies give statutory declarations to the effect that there were no grounds on which the companies giving the financial assistance would be found to be unable to meet their liabilities as they fell due for a period of 12 months from the date of the financial assistance having been given. The companies' auditors, KPMG, were required pursuant to the provisions of the Companies Act to report to the directors that they were not aware of anything which would indicate that the statutory declarations to be made were unreasonable in all the circumstances. KPMG prepared a lengthy board memorandum for that purpose dated 23 June 2000. The memorandum summarises the work and enquiries which the directors had undertaken in order to satisfy themselves that it was appropriate for the statutory declarations to be given, including the preparation of financial projections in respect of the Joint Venture.

334. KPMG concluded in the memorandum that a considerable amount of detailed work had gone into the preparation of the projections and the sensitivities that related to them. They stated that the original assumptions had been prepared on a prudent basis and that the directors had considered all known significant factors likely to affect the forecasts and the sensitivities. The memorandum therefore concluded that the directors considered that, having made detailed and careful enquiry and given detailed consideration to the Joint Venture's future trading prospects, it was "not inappropriate" for them to make the necessary statutory declarations. KPMG issued the necessary auditors' report.

335. Following the completion of these formalities, the Shareholders Agreement could now be signed, and this duly occurred on 28 June 2000.

The loan facility with WestLB and the Debenture

336. On completion of the Shareholders Agreement, the various financing documents were executed, including the Senior Bridge Facility Agreement. That Agreement, in addition to providing £710 million in senior debt for the purchase of the business, also provided the Joint Venture with £50 million in working capital. A Subordinated Bridge Facility Agreement provided a further £150 million for the purchase. The primary borrower was BxC Finance, with BxC Holdings as guarantor. The sums borrowed were secured by the Debenture, which was entered into on the same date. As mentioned at [133], pursuant to the terms of the Debenture, each of the operating companies in the Joint Venture charged all of their assets as security for the borrowings.

337. The necessary sums were drawn down to meet the obligations under the Contribution Agreement. The working capital facility was also drawn down to the extent of £30 million.

338. The Senior Bridge Facility contained representations from members of the Joint Venture group as to the considered nature and reasonableness of the forecasts and projections which had been provided to PwC for use in its reports.

The Shareholders Agreement

339. A Shareholders Agreement dated 28 June 2000 was entered into so as to regulate the relationship between the Joint Venture parties. We have mentioned at [46] above that major decisions relating to the Joint Venture could only be taken with the consent of at least one of the directors of the Joint Venture representing Granada and one of those representing Thorn. Amongst those major decisions was the establishment of the pension scheme unless the scheme was in accordance with rules approved by the parties to the Joint Venture.

340. Clause 3 of the Shareholders Agreement provided as follows:

> "The parties intend that the Box Clever Group should be self-financing and should obtain additional funds from third parties without recourse to its Shareholders. Subject to any contrary agreement, no shareholder shall be obliged to contribute to the working capital or other financial requirements of the Company, whether by further subscription per shares, by loans, by guarantee or otherwise."

341. This provision is consistent with the terms of the financing arrangements put in place on completion of the Joint Venture. Those arrangements did not make provision for any recourse to the shareholders in the Joint Venture requiring them to repay any of the borrowings.

342. Clause 6 of the Shareholders Agreement provided that all steps should be taken to ensure that 90% of the profits of the Joint Venture available for distribution should be distributed to the shareholders in each year.

343. It is important to put the provisions set out in the Shareholders Agreement into a practical context. The formal process for major decisions relating to the Joint Venture is that those decisions should be taken by the Board of BxC Tech but that in order for the resolution to be valid the board representatives of both Shareholders need to approve it. Therefore, in making those decisions, although the directors concerned have duties under company law to act in the best interests of BxC Tech they do so on the basis that they have the opportunity to take into account their interest as shareholders before casting their vote. As a deadlocked company, the Joint Venture could therefore only operate effectively if both Shareholders were content with the decisions that were being made at the Joint Venture level, both at the level of BxC Tech and also at the subsidiary level, where day-to-day decisions were being made by executive management. Ultimately, therefore the control of the Joint Venture was in the hands of the two Shareholders on equal terms. No significant decisions could be taken unless both were in agreement on the course to be followed.

344. Therefore, in practice, it would have been expected that proposals regarding major decisions would have passed up the chain so that they came to the attention of those who represented the shareholders on the BxC Tech Board, notably Mr Allen and

Mr Staunton for Granada and Mr Hands and Mr Tagliaferri for Thorn. There is little evidence of those decisions being "signed off" in the formal manner envisaged by the Shareholders Agreement. But there is considerable evidence that in practice decisions were agreed informally, particularly any issues raised by the monthly presentations that were made by the Joint Venture's executive management to representatives of the Shareholders as to the current state of the Joint Venture's business. Mr Wakelam's evidence was clear on this point and we accept his evidence that at those meetings representatives of the Shareholders appeared to be those making the decisions. The Targets did not dispute that they were kept informed about matters relating to the Scheme in particular that they could have stepped in to prevent decisions being taken that they were unhappy with even if the management of the Joint Venture and the development of proposals relating to its business was largely left to its executive management. But we accept Mr Wakelam's evidence that the Shareholders' involvement in the Joint Venture's decision making went much further than that, indeed he described the process as quite "autocratic". We believe Mr Wakelam when he said that if Mr Allen and Mr Hands agreed on something that was the end of the matter, and that no major decisions were made without those two individuals being involved.

The establishment of the Scheme

345. As we have previously mentioned at [327] above, Schedule 10 of the Contribution Agreement provided that BxC Tech shall establish a pension scheme on a money purchase basis and that that scheme should be available to all permanent employees of BxC Tech and its subsidiaries. Schedule 10 also provided that the level of employer and employee basic contributions should be payable at such rates as shall be agreed between BxC Tech, Thorn and Granada. The provision therefore envisaged a continuing role for Granada and Thorn in decisions relating to the Scheme, as well as to the Joint Venture itself.

346. Schedule 10 also envisaged that during a transitional period (the "interim participation period") BxC Tech and its subsidiaries would become participating employers in the Legacy Schemes. Employees of the Joint Venture would therefore remain as members of the relevant Legacy Scheme for no longer than six months until the Joint Venture established its own scheme. Schedule 10 envisaged that after the establishment of the Joint Venture scheme, there would be a transfer payment from the Legacy Schemes to the Joint Venture Scheme in respect of those members of the relevant Legacy Scheme who had become employees of the Joint Venture and members of the Joint Venture Scheme and who consented to the transfer of their benefits to the new scheme. The amount of the transfer payment would be equal to the actuarial value of the benefits prospectively and contingently payable to the relevant employees under the relevant Legacy Scheme by reference to their pensionable service up to that time.

347. It was therefore clear from these provisions that as it was intended that the Joint Venture's scheme would be a money purchase scheme, the replacement benefits created in the Joint Venture's scheme created no funding risk to the Joint Venture or the scheme members. It was envisaged at this stage that it would be open to employees not to transfer their existing benefits from the relevant Legacy Scheme. For employees who did not transfer, this would mean that if they became members of the Joint Venture's

scheme then they would receive two pensions when they retired, one from the Joint Venture's scheme based on the value of their benefits accrued in that scheme, and a second pension based on the benefits they had accrued in the relevant Legacy Scheme. Those employees who did consent to transfer their benefits from the Legacy Scheme would receive a single pension from the Joint Venture's scheme in respect of all their service in the Joint Venture and either Granada or Thorn.

348. The interim participation period started in June 2000 when the Joint Venture commenced operations and the relevant Granada and Thorn employees transferred their employment to the Joint Venture. The interim participation period turned out to be much longer than the six months envisaged in the Contribution Agreement, lasting for a period of fifteen months up until 1 October 2001. Mr Cooklin, who as chairman of the Joint Venture liaised with the Shareholders during the period up to the establishment of the Scheme, obtained the approval of the Shareholders to extend the interim participation period. During this period employees of the Joint Venture continued to accrue benefits in the relevant Legacy Scheme.

349. Although the Joint Venture's employees and employers paid contributions to the Legacy Schemes during the interim participation period, if those contributions proved inadequate to meet the full cost of the benefits the Joint Venture employees had accrued, then pursuant to the terms of the Contribution Agreement, Granada and Thorn would each ultimately have to fund the shortfall. It appears that the contributions paid by the Joint Venture to the Granada Scheme during the interim participation period have indeed proved insufficient to cover the true cost of the benefits earned by those employees in the Granada Scheme. This is a funding risk now borne by the ITV Group. The joint statement of the actuaries filed in this case shows that the shortfall was £25 million on a buyout basis four years ago.

350. In January 2001 it was proposed that the Joint Venture establish a defined benefit, rather than a money purchase scheme. The proposals were set out in a paper which was titled "Proposals by Box Clever and its shareholders in respect of pension provision for Box Clever employees". The authors of the paper were Stephanie Monk who was Granada's Human Resources Director, Richard Smelt from Thorn, Kevin Ringrose who was the Human Resources Director of the Box Clever group and two advisers from Mercer. This shows that the proposal was not that of the Joint Venture alone. As envisaged in the Shareholders Agreement, the paper stated that approval by the shareholders in the Joint Venture was one of the items on the timetable for the implementation of the proposals for the Scheme. At the hearing before us, the Targets sought to distance themselves from this being a proposal of the Shareholders rather than one that was proposed by the executive management and approved by the Shareholders. In view of our findings as to the involvement of the Shareholders in major decisions, as described at [343] and [344] above, this is a distinction without a difference. The evidence shows that the Shareholders were clearly closely involved in the proposal to create a defined benefit scheme and that they approved it.

351. The introductory "Background" section of this Proposals paper said:

> "A considerable amount of time and effort has been expended in the development of the proposed new pensions programme and various alternative approaches have been considered.
>
> The suggested design framework is, in our view, the optimal arrangement for boxclever having regard to the dual needs of balancing acceptable emerging costs with the maintenance of appropriate employee relations."

352. We take from this that the "maintenance of appropriate employee relations" was an important factor in the decision to establish a defined benefit rather than a money purchase scheme. The evidence shows that the stance of the Trade Union that represented many of the employees was a key consideration. The parties were keen to keep the Union onside by offering the pension proposal so as to assist with negotiations that would have to take place with the Union on other matters. Therefore, the new proposal was that separate sections were to be established within the Scheme providing mirror image defined benefits for ex-Granada and ex-Thorn members respectively who became members of the Scheme. New employees, that is new hires who were not covered by the transition arrangements, became members of a "Box Clever DC Section" which provided only money purchase benefits.

353. This proposal envisaged that ex-Granada employees would be able to join the mirror DB section for future service without needing to transfer their past service benefits from the Granada Scheme. They could leave those benefits behind in the Legacy Scheme if they so chose. In contrast, former Thorn employees would be required to transfer their past benefits from the Thorn Scheme if they wished to join the mirror DB section. This was because as a result of the establishment of the Joint Venture, Thorn no longer had many active members in its own scheme and if all those employees who had transferred to work for the Joint Venture also transferred their pension benefits to the Joint Venture's scheme then there would be scope to consider winding up the Thorn Scheme.

354. The establishment of the new proposed Scheme was approved in the manner envisaged by the Shareholders Agreement through a resolution of the Board of Directors of BxC Tech passed at a meeting held on 7 March 2001. Present at that meeting were Mr Allen and Mr Staunton, representing Granada, and Mr Hands and Mr Tagliaferri, representing Thorn, alongside the executive directors of the Joint Venture. The meeting first discussed in detail the strategy and costs review agreeing that structural savings would be achieved by reducing radically the number of shops over the coming years with a review conducted every six months. They also agreed to realign central and administration costs to support the new structure of the Joint Venture. Turning to the pension proposals, the resolution records that "in view of the balance of risk and reward it was agreed that the proposal for a mirror DB scheme be accepted on the basis that participants will be required to leave either the Granada or Thorn scheme as appropriate."

355. The Trustee contends that this demonstrates that the Targets intended to transfer away the historic liabilities of the Granada Scheme and to stop further liability for ongoing accrual of defined benefits. The Targets contend that this requirement for a

compulsory transfer of existing benefits was at the insistence of Thorn rather than at their instigation.

356. We accept what the Targets say on this point. But there is no doubt that the effect of the stipulation that all employees would have to agree to transfer their Legacy Scheme benefits in order to obtain a defined benefit pension for their work in the Joint Venture was that if the historic liabilities had been transferred then aside from the possible issue of an FSD, there would have been no continuing obligations on the part of Granada in relation to pensions liabilities in respect of its former employees who became employed by the Joint Venture even in respect of their service whilst employees of Granada. The reference in the BxC Tech resolution to the "balance of risk and reward" suggests that both Shareholders recognised that if the Joint Venture's employees were going to be better rewarded by the establishment of a DB scheme within the Joint Venture rather than a DC scheme then this had to be balanced by a provision that enabled the Shareholders to divest themselves of their historic liabilities relating to the Legacy Schemes in respect of those employees.

357. On the basis of this proposal, an employee who became a member of the Scheme and therefore transferred his accrued benefits from the relevant Legacy Scheme would have a single final pension based upon his final salary with the Joint Venture upon retirement and upon their entire service with both Granada or Thorn, as the case may be, and the Joint Venture combined. We refer to those benefits, as Mr Herbert did in his witness statement, as "Continuous Service Benefits", in contrast to the "split" benefits members would have if they became deferred members of the Legacy Schemes (and would therefore become entitled to a deferred pension based on their final salary with Granada or Thorn, as the case may be, and upon their past service) and then accrued benefits in respect of future service only in the Scheme (and would therefore become entitled to a separate pension based on the final salary with the Joint Venture and their past service with that entity). Continuous Service Benefits were clearly more valuable to members because their eventual final salary with the Joint Venture was "linked" to their service with Granada or Thorn, as the case may be, and not just to their service with the Joint Venture. As was made clear in the transfer pack referred to below, if the employee did not wish to transfer his benefits from the relevant Legacy Scheme, he was only eligible to receive DC benefits in the Box Clever scheme.

358. The Trustee was incorporated on 3 April 2001. Mr Herbert became chairman of the Trustee's Board of Directors on 27 June 2001. On the same date Mr Kevin Ringrose, on behalf of the Joint Venture, wrote to all employees explaining the new pension arrangements. This explanation said that the objective of the new arrangements was to replicate the benefit structures of the Legacy Schemes.

359. In mid-July 2001 employees were sent a "transfer pack" comprising the following documents:

(1) A letter from Mr Mavity explaining that from 1 October 2001 the Joint Venture would have its own pension scheme, and it would no longer be possible to earn benefits in the Legacy Schemes but that identical benefits would be

provided in the new Scheme provided members transferred across their past benefits;

(2) The letter from the relevant Trade Union, welcoming the commitment of the Joint Venture to providing final salary benefits to members at the same level as provided by the Legacy Schemes;

(3) An information pack explaining the structure of the new Scheme, the benefits to be provided, and the decision members had to make, in more detail. The pack applicable to ex-Granada members explained that if they wanted to be able to earn pension benefits for the future on the same basis as they do at the moment, the option to transfer to the new Scheme's DB section allowed them to do so. It emphasised that now was the only time that this could be done;

(4) An explanation of the level of contributions that would be payable, according to whether the member opted to earn DB or DC benefits; and

(5) An election form for members to fill in, indicating their decision either to transfer their past benefits and join the DB sections of the new Scheme, or to become deferred members of the Legacy Schemes, and join the DC section of the new scheme and authorising the Joint Venture to make the appropriate contributions from the member's salary.

360. The vast majority of members elected to transfer to the new Scheme. Those Granada members who opted to transfer received a letter from Aon, the Scheme's administrators saying:

> "I can confirm that we have received your completed option form indicating that you wish to become a member of the Scheme as from 1 October 2001. This means that your Pensionable Service is treated as continuous from the date you first joined the Granada pension scheme; from 1 October 2001 you will continue to pay contributions and earn future pension on exactly the same basis as you would have done had you remained in the Granada pension scheme."

361. It was envisaged that the Scheme would receive a bulk transfer payment which would be large enough to fund the past service liabilities of the members transferring from the Legacy Schemes, plus the cost of providing increases based on salary increases while they worked for the Joint Venture.

362. Mr Herbert accepted in his evidence that there were no promises by the Shareholders that they would stand behind the Scheme and that the message being given to employees was that the Joint Venture was to be a stand-alone business. He accepted that if full transfer values were paid in accordance with the terms of the Contribution Agreement there would be no recourse to the Shareholders. For example, one of the frequently asked questions included in the transfer pack was "What if anything happens to boxclever group in the future?" to which the response given was "The assets of the new scheme will be kept separate from those of boxclever group. Therefore, they are protected if anything happens to the company. Benefits would then be secured for the members according to the scheme's formal documents".

363. As Mr Herbert said in his evidence, at the time of his appointment the assumption was that the transfer values to be paid by the Legacy Schemes would be agreed shortly, and in time for the Scheme to open to accrual on 1 October 2001. However, the negotiations with the Legacy Schemes over the transfer values were far more difficult and protracted than expected, and ultimately no transfer value was agreed and no transfer took place.

364. As the accrual start date of 1 October 2001 approached, the appointed actuary for the Scheme, Ms Justine Peggs of Mercer, was not satisfied with the transfer payments offered by the Legacy Schemes. There was disagreement among the actuaries for the three schemes about how the transfer payment should be calculated. The negotiations were made more difficult by stock market falls in September 2001. Mr Roth, the Joint Venture's actuary, responded in an email of 28 September 2001 to the proposal from Granada that a "market value adjuster" be applied to the transfer value to take account of the market falls. He explained the history of the matter, namely that the transfer value mechanism in the original Schedule 10 to the Contribution Agreement had been devised on the basis that the Scheme would be a defined contribution scheme. It had been agreed that the same mechanism should apply to the defined benefit scheme being introduced but with some adjustments to modify the underlying assumptions. He described the likely effect of the market value adjuster now proposed by Granada as leading to a significant initial deficiency that would have to be made up by higher contributions from Box Clever in the future. This would mean that the transfer value, which Ms Peggs had advised on 17 September 2001 would be sufficient to cover the accrued liabilities based on projected salaries, would be insufficient to cover the liabilities the new scheme would be taking on.

365. The Trustee had to decide what to do from 1 October 2001. Pension contributions were due to be deducted from members' salaries on 26 October 2001, so a firm decision was needed urgently. At its board meeting held on 28 September 2001, the Trustee decided to defer commencement of the Scheme. However, they signed the interim trust deed establishing the Scheme on the understanding that it was left undated and held to Mr Herbert's order by the Scheme's legal adviser, Ms Miller. As Mr Herbert explained in his evidence, the intention was to resolve outstanding issues over the transfers before contributions were due to be paid into the Scheme. Mr Herbert informed Mr Cooklin of this decision and Mr Wakelam reported to Mr Herbert on 1 October 2001 that both Shareholders had been made fully aware of the issue. He said that Mr Cooklin would be meeting Mr Parrott, chairman of the Granada Scheme Trustee and Commercial Director of Granada, on 2 October 2001 to discuss it, a meeting which did not go ahead because of Mr Parrott's illness.

366. On 5 October 2001 Ms Miller sent an email to Mr Neal (Finance Director of the Joint Venture and formerly a Granada director) attaching a draft of a letter to be sent to employees, copying Mr Herbert in. That draft told members that the Scheme was commencing for future service but informed them that arrangements for the transfer of their past service benefits had not yet been completed. For the time being therefore those benefits would remain in the relevant Legacy Scheme. The draft stated that they were working to finalise arrangements and hoped to be able to accept the past service rights shortly.

367. By this time Mr Herbert was concerned that members had been told that they could earn Continuous Service Benefits in the Scheme; that they had signed application and transfer forms in order to do so and had agreed that their new employer could deduct the necessary contributions from their pay and apply them to the Scheme. As far as members were concerned, everything was in place for them to start accruing benefits in the Scheme. Mr Herbert's view was that Ms Miller's draft letter would cause confusion in the membership. On 23 October 2001, following the receipt of legal advice, Mr Herbert took the view that the Scheme be opened, pending agreement of the transfer value, so that future benefits could at least be provided under the Scheme, a course that was agreed to by the other directors of the Trustee.

368. Mr Herbert accepted in his cross examination that rather than defer commencement of the Scheme or commence it only in relation to future service benefits, the Trustee decided to take a third option. That third option was not to inform members of the delay in agreeing the transfer payments, but rather to execute the Interim Trust Deed to establish the scheme on the assumption that the Trustee would be able to resolve the outstanding issues regarding the calculation of the transfer payments. Mr Herbert explained that the Trustee felt able to do this based on the comfort it had from Schedule 10 of the Contribution Agreement which contained provisions for calculating the past service transfer from the Legacy Schemes. Mr Herbert understood that if the transfer payments could not be agreed (and there was no obligation on either the Joint Venture or the Trustee to accept a transfer payment) then the liability for the past service benefits would have to stay with the Legacy Schemes. Accordingly, Mr Cooklin was asked to authorise the dating and release of the Interim Trust Deed. He did so on 29 October 2001, the effect being that the Scheme was established with effect from 1 October 2001.

369. There was no evidence that members had been told about the delay in agreeing the transfer payments and hence the transfer of their benefits. Indeed, a letter that Aon sent on 10 October 2001 to those who had become members of the Scheme informed them that their pensionable service was to be treated as continuous from the date they first joined the relevant Legacy Scheme. It did not indicate that this was still conditional upon the transfer payments being completed. Furthermore, there is an email from Mr Craig Murphy, one of the employee representative directors of the Trustee, dated 22 November 2002 in which Mr Murphy states that over a year after the Scheme opened and when the transfer of Legacy Scheme benefits had still not been agreed, very few, if any, members appreciated the fact that the transfers had not taken place.

370. The key terms of the Interim Trust Deed (which was in fact never replaced with a Definitive Trust Deed) can be summarised as follows:

(1) BxC Tech was the Principal Employer (although, as mentioned before, the actual employers were operating subsidiaries within the Joint Venture).

(2) Clause 7 (A) required the Trustee to give effect to the "Explanatory Literature" as far as is practicable. "Explanatory Literature" was defined as "Any literature setting out the principal provisions of the Scheme … that is issued to Members and prospective Members in a form and manner agreed by the Principal Employer and the Trustees". Copies of the initial Explanatory Literature were

annexed to the deed and the definition went on to say that any decision of the Trustee as to the interpretation of the Explanatory Literature was final. The material annexed to the deed included the explanatory leaflets issued to members in July 2001 as part of the transfer packs.

(3) Clause 11 provided that BxC Tech, subject to advice from the Scheme Actuary, would decide the contribution rates that the Employers would pay to the Trustee. However, as we have seen, pursuant to Schedule 10 of the Contribution Agreement the contribution rates also needed to be approved by the Shareholders.

(4) Clause 20 set out how the deed could be altered by BxC Tech, with the consent of the Trustee. Clause 20 (C) provided that alterations or modifications could be made if notice in writing was given in a form agreed by the Trustee and the Principal Employer to members in the form of a notice. Once again, pursuant to the terms of the Contribution Agreement, alterations would require the consent of the Shareholders through their representatives on the BxC Tech Board.

(5) Clause 32 set out when the Scheme could be wound up, namely when BxC Tech stopped making contributions, having given 12 weeks' notice to the Trustee, unless the Trustee decided to continue the Scheme as a closed scheme. As it happened, BxC Tech never made any contributions, as members were employed only by its subsidiary companies, meaning that Clause 32 could not take effect.

The decline of the Box Clever business and the securitisation of the WestLB debt

371. As Mr Redmayne recorded in his expert report for the hearing before us, the business strategy of the Joint Venture had not been clearly defined at the time that the transaction was completed. The paper put to the Granada Board in November 1999 appeared to assume that the Joint Venture would employ the strategy of the Granada Rental Business, which was to invest heavily in rental assets and encourage customers to upgrade; to focus on the development of non-rental income, for example through retail sales, and to maintain the rental base through add-on sales. In contrast, the strategy of the Thorn Rental Business was focused on cash generation in recognition of a declining rental base, with reductions in overhead costs and sharply declining levels of capital expenditure, concentrating on added value products, such as widescreen TVs and home movie centres.

372. PwC's report of December 1999 had referred to the need for management to consider how to merge the two strategies in practice, but the April 2000 report stated that the strategy of the Joint Venture would be to move the Granada business towards the Thorn strategy. The financial projections and consequently the basis on which WestLB agreed to provide the financing appear to have been based on the Joint Venture moving towards the Thorn strategy.

373. The monthly shareholder review prepared by the Joint Venture's management on 7 March 2001 recognised that the "endemic shortcomings of rental" dictated a strategy of "managed decline". The paper sought shareholder approval for a number of strategic recommendations. The goal was to sell or manage down the rental book. The paper also recommended that all shops should be closed within four years.

374. In June 2001, in the context of a group reorganisation which involved the giving of financial assistance by certain members of the Joint Venture group in the context of the acquisition of their shares, a Board Memorandum was prepared in order to satisfy the directors of the relevant group companies that the necessary statutory declarations to the effect that the companies concerned could pay their debts as they fell due within the next 12 months could be given. In the memorandum's conclusion relating to budgeting it was stated:

> "… The directors acknowledge that market conditions and fundamental strategy have changed significantly since the preparation of the Sizzle model. The decline in the rental market has accelerated and Box Clever has not achieved an improvement in market share. The directors have now accepted that this is unlikely in the longer term and that the market for rental TV products is in terminal decline."

375. This change of strategy is confirmed by a shareholder review paper prepared in September 2002 where the Joint Venture's strategy is described as maximising "cash returns from a declining business" on the assumption that "new business will not be actively pursued".

376. Mr Redmayne draws the following conclusions from this evidence, which we accept:

(1) In the course of a relatively short time before the creation of the Joint Venture, the initial strategy changed from one of implementing the strategy of the Granada rental business to implementing the strategy of the Thorn rental business;

(2) The WestLB facilities were based on the adoption of the Thorn rental business model;

(3) The strategy of the Joint Venture was not developed fully before completion of the transaction; and

(4) Within one year of the transaction, the strategy shifted to one of closing the entire store network and running the business for cash in a managed decline.

377. The Joint Venture's accounts for the year ended 30 September 2001 became available at the end of July 2002. These accounts showed that the underlying business made profits of £12 million, but there was interest to pay of £88.6 million. Accordingly, the business made a substantial loss. However, net debt had been reduced from £943 million to £898 million and it appeared that cash flows were sufficient to meet costs. The securitisation of the Joint Venture's debt took longer than planned but was completed in June 2002. The proceeds of the securitisation were used to repay most of the existing indebtedness to WestLB.

378. However, Mr Herbert explained that from September 2002 he began to consider whether the Joint Venture's shareholders would support the Joint Venture and the Scheme in the event of insolvency. Mr Herbert had accepted that it was unlikely that the Trustee would be able to continue to rely on capital backing from the Joint Venture. On 6 September 2002 Mr Herbert wrote formally to Mr Mavity saying that the board

of the Trustee "having considered various economic scenarios" had asked him to seek clarification about the shape of the Joint Venture and its future over the next 10 years. He asked Mr Mavity to discuss the matter with representatives of the Shareholders and ascertain the extent to which they would be prepared to support the Scheme. Following a meeting with Mr Cooklin, Mr Mavity and Mr Neal on 28 November 2002 it was apparent to Mr Herbert that the clarification as regards to the shape of the company which he had been seeking would not be forthcoming and it was made clear that financial support would not be forthcoming from the Shareholders in the event of the Scheme being discontinued with insufficient assets to secure the members' accrued benefits. Mr Herbert also had concerns about the strength of the financial covenant of the Joint Venture because of the way that it was financially structured.

379. In its operations review of July 2002, the Joint Venture's management stated that there was limited scope for significant improvement of the business for various reasons including the "inevitability of historic trends and inability of the business over many years to influence market decline". During the year ending September 2002, the number of shops was reduced to 180 from its high point of 900 as at 30 September 2000 and staff numbers were substantially reduced. Although it was able to meet its interest payments, the accounts of the Joint Venture for the year ended 30 September 2002 recorded a drop in revenues of over 20% in the year. The business was seriously affected by redundancy and property closure costs, goodwill of £391 million was written off, and accordingly a net loss of £466 million was made.

380. In January 2003, it became evident that one of the covenants in the Joint Venture's mezzanine borrowing facility, which was to be tested for the first time as at 31 December 2002, would be breached.

Further developments concerning the Scheme

381. After the establishment of the Scheme in October 2001, discussions continued between the Trustee, led by Mr Herbert, and representatives of the Legacy Schemes in an attempt to try to agree the transfer values of those members who had elected to join the Scheme. This would enable the implementation of the bulk transfer by which the Scheme would take over the responsibility for providing pensions to members in respect of not only their future service within the Joint Venture but also of their employment in Granada or Thorn, including Continuous Service Benefits.

382. The negotiations were protracted and ultimately unsuccessful. Problems had occurred in sourcing complete data about the employees from the Legacy Schemes and this took a long time to provide. Although by June 2002 Mr Herbert believed that the transfer values were substantially agreed, further delays were caused by Thorn and Granada's request that a formal transfer agreement be drawn up before the transfer payments could be made. During this time the Scheme's first actuarial valuation report was being prepared, a report which was necessarily closely related to the transfer value negotiations. Calculations were produced of the Scheme's discontinuance position upon acceptance of the bulk transfers as at 24 June 2002. This showed a very large buyout deficit which caused Mr Herbert considerable concern.

383. Therefore, in early September 2002, by which time the markets had deteriorated significantly, the Trustee's Board decided not to accept the transfers. Mr Herbert explained that the reasons for that decision were primarily:

(1) The substantial initial deficit that would arise upon a transfer;

5 (2) An awareness that, in accepting the transfers, the Trustee would be accepting very large liabilities and assets relative to the Joint Venture's size, thereby putting the future funding of the Scheme in considerable risk; and

(3) The Trustee's view that the Joint Venture's financial covenant was not particularly strong, in the light of indications that there would be no support from 10 the Shareholders.

384. No criticism is made of the decision of the Trustee not to accept the transfer value offered. Indeed, it is accepted that if the transfers had taken place, the deficit in the Scheme would be considerably greater than it is currently. Likewise, no criticism is made of Granada for the failure to agree on the transfer value in respect of the Granada 15 Scheme.

The Top Up Arrangement

385. Once it became clear in Autumn 2002 that agreement on the transfer values that was necessary to implement the bulk transfer from the Legacy Schemes was not going to be forthcoming, the Trustee explored other ways in which the Continuous Service 20 Benefits of the members of the Scheme could be provided. The Joint Venture took the view that Continuous Service Benefits should be provided if at all possible, so that, in essence, members would receive the same total pension that they would have received had the transfers gone ahead, a position that the Trustee agreed with. It was clear that this point was also of considerable importance to the Trade Union and that keeping the 25 support of the Union was important to the Joint Venture.

386. On 3 September 2002 Mr Herbert sent an email to Mr Mavity setting out in outline what became the Top Up Arrangement. In essence, under such an arrangement:

(1) Members would become deferred members of their Legacy Schemes and final pensionable pay under those Schemes would be calculated as if they had 30 ceased service on 30 September 2001;

(2) Members would be provided with benefits from the Box Clever Scheme in respect of their service with the Joint Venture, based on final pensionable pay at the date of leaving the service of the Joint Venture;

(3) The Box Clever Scheme would also provide members with "Top Up" 35 benefits, in effect reintroducing the final salary link to members' accrued benefits in the Legacy Schemes. This would make up any difference between the pension they received under the Legacy Schemes and in respect of service with the Joint Venture from the Scheme, and the pension they would have received had the Legacy Schemes maintained a final salary linked to Joint Venture pay; and

40 (4) In relation to pensions which had started to be paid in the Box Clever Scheme, on the assumption that the transfer payments would be made, the Box

Clever Scheme would be regarded as having been the paying agent for the relevant Legacy Scheme and reimbursed accordingly.

387. In explaining to us why he thought that the Top Up Arrangement was a good idea in principle, Mr Herbert said that whilst the arrangement might involve taking on an immediate deficit, the immediate deficit was much smaller than if the Trustee had accepted the bulk transfers. Although the cost of the arrangement would be sensitive to the actual salary increases granted, he had been told that salary increases would be strictly controlled and would be not much higher than the increase in inflation. Further, he said that the liabilities of the Scheme would be no more sensitive to actual salary increases under the Top Up Arrangement than if the Scheme had accepted the bulk transfers.

388. It was clear that Mr Herbert assumed that Mr Mavity would seek the views of the Shareholders on this proposal. He said in his email that "We will… need to ask you to agree with the two shareholders that the exercise is carried out in a spirit of co-operation as over the past 15 months extreme positions have been taken up by the respective parties and their advisers which has involved a lot of time and expense."

389. It was calculated, on a rough basis, that the immediate cost to the Scheme of the arrangement might be in the region of £5 million. The Joint Venture reached the view that the Top Up Arrangement was the best way to proceed at a meeting in London on 28 November 2002, which was attended by Mr Mavity, Mr Cooklin and Mr Neal. In advance of this meeting, Mr Herbert had written a letter to Mr Mavity on 18 November 2002. It is clear, again, from the terms of that letter that Mr Herbert envisaged that Mr Mavity would seek the views of the Shareholders on the proposed arrangement under which the Box Clever Scheme will "pick up any shortfall to meet the promise of receiving a pension based on total service with both companies". In closing that letter, Mr Herbert said that within the financial constraints that Box Clever has to operate, it is not in a position to offer the financial comfort that the Trustee needs to offer that security. If the Shareholders were not prepared to offer additional support then the Trustee would need to proceed on the basis of the arrangement described, given that the security of members' benefits was paramount.

390. The proposals were then considered in some detail; on 19 December 2002 Ms Pegg sent Mr Herbert a lengthy draft letter on issues arising from the arrangement, updated on 23 December 2002. Mr Herbert prepared a paper, dated 8 January 2003, which was considered by the Trustee's Board on 14 January 2003. This paper set out the basis of the arrangement as agreed with the Joint Venture, which was to put members who had requested that their past service benefits be transferred to the Scheme in the same position as if the transfer values had been accepted by the Trustee. Mr Neal confirmed at that meeting that when the next Scheme valuation was done as at 30 September 2002 the costs of the Top Up Arrangement would be incorporated into the employers' contribution rate.

391. The minutes of the Trustee's board meeting held on 14 January 2003 record Mr Herbert reporting that "both Granada and Thorn" had agreed in principle to the request from the Joint Venture with regard to treatment of past service benefits "within the legacy schemes (the Granada Pension Scheme and the Thorn Pension Fund)". Mr

Herbert confirmed in his oral evidence to us that his understanding was that the Shareholders did support the Top Up Arrangement on the basis of the discussions and other communications that he had had on the issue.

392. On 31 January 2003 Mr Herbert had a telephone conference with Mr Parrott and Ms Annette Scott, the Granada pensions manager. They emphasised that they wanted to move ahead with the implementation of the Top Up Arrangement and had some comments on the draft communication to members. They also asked that the trustee of the Granada Scheme enter into formal agreement with the Trustee to record the arrangements.

393. The arrangements were formally agreed by the trustee of the Granada Scheme on 6 March 2003 and a letter to members was sent out. That letter explained that the Trustee and the Joint Venture had concluded that members' past service pension would not be adequately funded if the transfer went ahead. It also explained that the Top Up Arrangement would be put into effect instead. A further joint communication from the Trustee and the trustee of the Granada Scheme in April 2003 explained the Top Up Arrangement in detail. Mr Herbert explained that the Trustee regarded that communication as being a binding change under the Scheme effected pursuant to Clause 20 (C) of the Interim Trust Deed.

394. The Scheme started paying benefits out to members on the basis of the Top Up Arrangement with effect from 1 May 2003.

Events leading up to the receivership of the Joint Venture

395. It was clear by May 2003 that the burden of debt repayments and the interest payable on the Joint Venture's debts was having an adverse effect on cash flows. On 20 May 2003 Mr Mavity sent a message to all Box Clever employees in response to recent negative press coverage. Mr Mavity stated that whilst very good profits were generated, the Joint Venture had very high borrowings and that discussions were taking place with the banks with a view to reshaping the borrowings.

396. On 26 June 2003 WestLB and BxC Finance agreed a suspension agreement to allow time for a new business plan to be prepared and for additional capital to be provided. This agreement was extended to 15 September 2003.

397. On 15 August 2003, Mr Herbert was informed by the Scheme's actuary, Mr Rooprai, that there had been some large salary increases and decreases in the number of active members. It transpired that, although the generality of increases were in line with previous assumptions, some exceptional salary increases had been granted in excess of the assumed 0.4% per annum above inflation in 2001 and/or 2002.

398. On 20 August 2003 Mr Herbert met with Mr Mavity who told him that the business plan had been received positively by the banks, and the final outcome was awaited. Mr Mavity said later that the revised business plan made provision for funding the Scheme deficit.

399. On 5 September 2003 Mr Rooprai provided a draft actuarial valuation report as at 30 September 2002. This disclosed an ongoing deficit of £8.3 million, which was higher than expected. Mr Herbert noted that the increased deficit was partly due to some exceptional salary increases. It appears that the average increase in salaries over two reviews had been 9%, compared with the 5.4% that had been assumed.

400. As we have seen, on 24 September 2003 WestLB gave notice of default under its facilities with BxC Finance. This amounted to a Declared Default under the Debenture and Administrative Receivers from PwC were appointed over all of the assets of BxC Finance, the Trio, THSP, TUK and UKCE. Telebank followed into receivership on 20 November 2003 as did BxC Holdings on 21 December 2004. BxC Tech, the ultimate holding company of the Joint Venture, was never in receivership.

The operation of the Scheme in the aftermath of the receivership

401. The directors of the Trustee met on 29 September 2003. One of the Administrative Receivers, Mr Lomas, and Mr Tooke, PwC's pensions specialist, attended that meeting. They confirmed that they would continue to make contributions to the Scheme at present levels but they would not be making up any funding deficit. In the light of that, it was agreed that Mr Herbert should write to the Shareholders requesting that they either make good the funding deficit or accept a return transfer of members and their liabilities to the Legacy Schemes. It is apparent that at this time Mr Herbert was alive to the concern that since the Scheme was underfunded, the further contributions paid by the Administrative Receivers might just go towards pensioner members and would not benefit active members on whose behalf those contributions were being paid. This would be the result of the priority in which assets were applied in the event the Scheme wound up. Mr Herbert was also aware that under the power of amendment in the Interim Trust Deed, the power to close the Scheme to future accrual rested with the Principal Employer, BxC Tech, subject to the Trustee's consent.

402. At the meeting the Trustee resolved to change its investment strategy to 100% gilts and index-linked stocks.

403. Mr Herbert wrote to Mr Hands and Mr Allen on 3 October 2003 requesting assistance to resolve the situation in which the Scheme found itself due to the appointment of the Administrative Receivers. He suggested that either the Legacy Schemes take back responsibility by providing pension benefits for those who had previously been members of that Scheme and that a transfer value could be paid back to them, or Granada and Thorn make good the shortfall in respect of their former employees by making a cash contribution into the Box Clever Scheme.

404. A further meeting of the Trustee's board was scheduled for 16 October 2003. In advance of that meeting Mr Rooprai confirmed the very approximate funding position as at 30 September 2003 on an ongoing basis. This showed an ongoing total deficit of £8.5 million. At the meeting, which was also attended by the Administrative Receivers for the discussion relevant to them, the Trustee noted that it was for BxC Tech, as

Principal Employer, to decide whether to close the DB sections of the Scheme for future accrual but that it would have no objection in principle to such a decision being taken. Mr Herbert is recorded as having reported that the PPF proposed by the Government may have retrospective effect from June 2003 or that schemes which close now but do not commence winding up until after the Regulations are laid may still be covered. He said "The PPF may be of assistance to the Scheme and should be considered in all discussions regarding wind-up".

405. Mr Herbert wrote to members on 28 October 2003, explaining the impact of the appointment of the Administrative Receivers and telling them that the Scheme's latest Actuarial Valuation Report on the Box Clever scheme as at 30 September 2002 showed that if the Box Clever scheme continued on an ongoing basis, there was a deficit of £8.5m equivalent to a funding level of 48%. He also told them that both the Trustee and the Receivers had written to the Shareholders requesting support for the Scheme.

406. On or around 4 November 2003, the Receivers granted pay rises of 3% to all Endeva staff and 2% to the remaining staff with effect from 1 October 2003. At the same time, exceptional salary increases in excess of those amounts were granted to 16 employees. The Administrative Receivers said that these increases were necessary and appropriate in the context of the receivership and of the new roles that certain senior members of staff were asked to assume as a result of other senior level dismissals. Mr Herbert accepted in cross examination that the pay rise could have been made non-pensionable, but at the time he regarded this as a matter of remuneration policy for the Administrative Receivers who at the time were trying to keep the business running as long as possible in order to facilitate a sale.

407. On 21 November 2003 Mr Lomas, one of the Administrative Receivers, wrote to Mr Cooklin, with a copy to Mr Herbert, stating that he was extremely concerned that contributions continued to be paid into the Scheme with a very real prospect that little or no additional benefit will accrue to the active members who were all employees of the companies for which the Administrative Receivers were responsible. As a result, Mr Lomas requested that BxC Tech give consideration to closing or winding up the Scheme.

408. The directors of the Trustee met again on 16 December 2003. It was agreed at that meeting that the Trustee would agree to the closure of the Scheme to new accruals with effect from 31 December 2003. The deed amending the Scheme to that effect was executed by BxC Tech and the Trustee on 23 December 2003. Mr Herbert wrote to the members of the Scheme on 23 December 2003 explaining what had happened. At the same time, the opportunity was taken formally to incorporate the Top Up Arrangement into the rules of the Scheme.

409. According to the Actuarial Valuation Report as at 31 December 2003 (prepared in May 2004), the Scheme had a deficit on an ongoing basis of £24.8 million of which £16.7 million was attributable to ex-Granada members. Significant factors in this increase included the larger than expected salary increases and the fact that lower investment returns may be expected following the switch into gilts.

The operation of the Scheme after 2003 to the present day

410. The question as to whether to wind up the Scheme was first considered by the Trustee in October 2003. Mr Herbert's unchallenged evidence, which we accept, was that the Trustee gave frequent consideration to the issue of whether to wind up the Scheme in the years that followed.

411. Mr Herbert explained the main reasons why the Trustee decided not to wind up the Scheme as follows:

(1) Keeping the Scheme going allowed negotiations to take place with Granada and Thorn and the Legacy Schemes about providing assistance to the Scheme whereas if the Scheme had completed its winding up by buying out benefits, it would have been impossible for members to transfer their benefits back to the Legacy Schemes. As we mention below, negotiations continued up until October 2009;

(2) Running the Scheme on as a closed scheme ensured that the members could benefit in the event that the Regulator decided to issue an FSD, following the relevant statutory powers coming into effect in April 2005. Mr Herbert considered that the possibility of an FSD (which he first raised with the Regulator in July 2005) increased the prospects of a negotiated outcome; and

(3) The Trustee wished to ensure that the Scheme was eligible for entry into the PPF. In October 2003, the Trustee was aware that the relevant statutory provisions for the creation of the PPF, which ultimately were contained in PA 2004, were at that time under consideration.

412. Mr Herbert accepted in his cross-examination that the Trustee was aware that, by running on the Scheme, it faced a number of risks to the funding of the Scheme, for example:

(1) the impact of interest on the deficit and expenditure of the Scheme's assets on administrative expenses;

(2) the fact the pensions would have to be paid in full, depleting the remaining asset coverage for other members; and

(3) financial and demographic risks, such as interest rates and longevity assumptions moving against the Trustee.

413. Mr Herbert was also aware that the Scheme's funding position became progressively worse whilst the Scheme ran on. However, Mr Herbert explained that the Trustee was prepared to take the risks involved in running on the Scheme, on the basis that the Trustee was seeking to obtain either support from the Shareholders or the issuing of an FSD by the Regulator. He did, however, accept that at the end of the day, if neither of those options worked out, the Scheme could look to the PPF to give support to the Scheme. He accepted that the strategy of running on the Scheme would have been extremely risky if the PPF had not been available as a backstop.

414. Discussions took place with the Shareholders over a number of years about the possibility of the Legacy Schemes receiving back their former employees as members.

The Trustee's objective, pursued with persistence under Mr Herbert's leadership, was for the benefits which it had been envisaged the Scheme provide to be secured by either of the two options put forward by the Trustee to the Shareholders, as described at [403] above.

5 415. Some progress was made and at a meeting of the Board of Directors of the Trustee on 29 September 2004, Mr Herbert was able to report that ITV might be willing to take back the ex-Granada members into the ITV Scheme, provided that the cost did not exceed £10 million.

416. An "in principle" proposal from ITV in March 2005 indicated that although ITV
10 emphasised that it had no legal obligation to fund any of the Scheme's deficit, it offered to seek the agreement of the trustee of the ITV Scheme to accept a transfer back of ex-Granada members provided there was a transfer payment from the Scheme to the ITV Scheme of at least £10 million. This was on the basis that members' salaries as at 30 September 2001, indexed from that date, would be used and the ITV Scheme would
15 provide pensionable service from 30 September 2001 until 31 December 2003.

417. The Trustee sought to improve the offer because they realised that the result of calculating pensions by reference to salary as at 30 September 2001, was that benefits would in a number of cases be below the benefits provided by the PPF. The Trustee's objective was to secure Scheme members' benefits fully. The Trustee also continued to
20 place pressure on the Administrative Receivers to contribute towards a deficit.

418. Negotiations with ITV proceeded slowly until a revised offer was received from ITV on 8 November 2007. The basis of this offer, which was in respect of benefits built up in the Scheme up to 23 September 2003, was that ITV would facilitate a transfer back for ex-Granada members into the ITV Scheme, with benefits being offered of
25 105% of those that would be paid if the Scheme went into the PPF. This offer was conditional upon the Scheme paying a transfer amount of at least £9.5 million to the ITV Scheme. The Trustee decided to accept this offer in principle, subject to certain clarifications, and requested that ITV consider extending the offer to include pensionable service after 23 September 2003.

30 419. On 16 April 2008 ITV made a revised offer to the effect that pensioners (but not deferred members) would be able to transfer all their benefits from the Scheme to the ITV Scheme in respect of service both before and after 23 September 2003. All pensioners would receive a full pension equal to that which they were receiving under the Scheme. However, before that offer could be accepted, ITV revised it and indicated
35 on 16 December 2008 that it would no longer support a transfer back of ex-Granada members into the ITV Scheme. Instead it was now examining the possibility of an augmentation to the benefits of deferred members of the Scheme in the ITV Scheme that would cost it no more than £7.5 million. On 29 January 2009, ITV's advisers indicated that in the light of the economic climate it was now reducing the value of the
40 revised offer. On 12 March 2009 ITV indicated that it would offer no more than £2.5 million for benefit augmentations. The Trustee accepted the revised offer in principle and negotiations progressed about the details of the settlement. But before these

negotiations were concluded, ITV notified the Trustee on 7 October 2009 that ITV was no longer able to maintain any offer and that it was withdrawing the existing offer.

420. The Trustee had first made a request to the Regulator in a letter dated 15 July 2005 that the Regulator consider issuing an FSD to BxC Tech and its associated companies to put in place financial arrangements to support the Scheme's pension liabilities. Following that request, the Regulator began to investigate the possibility of the issue of an FSD. However, it was not until 30 July 2010, following the Targets' unsuccessful clearance application, that the Regulator said that it was now considering whether or not to issue an FSD to the Targets. A Warning Notice was served on 30 September 2011, confirming that the "look-back date" was 31 December 2009. At that date the Scheme's assets were £14.4 million and buyout liabilities were £76.5 million, so that there was a deficit of £62.1 million of which about £41.2 million related to the former Granada employees.

421. Following the issue of the DP's determination on 21 December 2011 and the reference of that determination to this Tribunal by the Targets, progress has been slow in bringing the matter to a hearing, largely due to protracted litigation regarding the proper scope of the pleadings. That litigation has resulted in two interlocutory hearings in this Tribunal. The Tribunal's first interlocutory decision was set aside by the Court of Appeal which remitted the application to which it related for a rehearing. These decisions and the Court of Appeal's judgment can be found at [2014] UKUT 0175 (TCC) and [2016] UKUT 0192 (TCC) and [2015] 4 All ER 919 respectively. The ultimate result of this litigation was to dismiss the Targets' application to strike out parts of the Trustee's and Regulator's pleadings. That application had been made on the basis that it was not open to the Tribunal in this case to consider certain contentions made by the Trustee and the Regulator in their pleadings because they had not been made either in the original Warning Notice or the Determination Notice that resulted from the proceedings before the DP.

422. The Scheme is now in a PPF assessment period. This was triggered when one of the employers, UKCE, was put into liquidation (at the instigation of the Trustee) on 10 November 2014. This liquidation caused the whole of the Scheme to start a PPF assessment period which may result in the Scheme entering the PPF. During the assessment period, an assessment is made as to the assets in the Scheme and whether they are sufficient to pay a pension to members of at least PPF compensation levels. This assessment is being delayed pending the outcome of these proceedings.

VIII. REASONABLENESS: DISCUSSION

Introduction

423. To recap, provided the other conditions in s 43 PA 2004 are satisfied, s 43 (5) (b) permits the Regulator to issue an FSD to a person if it is of the opinion that it is reasonable to impose the requirements of the direction on that person.

424. Section 43 (7) requires the Regulator, when deciding whether it is reasonable to impose the requirements of an FSD on a particular person, to have regard "to such

matters as the Regulator considers relevant". In that respect, s 43 (7) requires the Regulator to have regard, where relevant, to the following specific matters:

> (a) the relationship which the person has or has had with the employer (including, where the employer is a company within the meaning of subsection (11) of section 435 of the Insolvency Act 1986 (c. 45), whether the person has or has had control of the employer within the meaning of subsection (10) of that section),
>
> (b) in the case of a person falling within subsection (6)(b) or (c), the value of any benefits received directly or indirectly by that person from the employer,
>
> (c) any connection or involvement which the person has or has had with the scheme,
>
> (d) the financial circumstances of the person, and
>
> (e) such other matters as may be prescribed.

425. It is clear from the provisions of s 43 that the specific matters referred to above are non-exhaustive of the matters that the Regulator must take into account when assessing reasonableness. It is clear that all relevant factors in the circumstances of the case must be considered. Likewise, in our view, the absence of any circumstances falling within the scope of those specific matters does not preclude the issue of an FSD if, taking into account all other circumstances, it is reasonable to do so. Nor, in our view, is it the case that each of the specific matters should necessarily be given equal weight. We accept, as the Regulator submitted, that the jurisdiction in s 43 is primarily founded on there being a present or past relationship between the potential targets of an FSD and the scheme and the nature of that relationship making it reasonable for the potential target to provide financial support to the scheme. It is therefore apparent that the closer the relationship is or has been the more likely it will be that it will be reasonable to issue an FSD, whereas if the relationship in practice was more distant, or ceased to exist a long time before the issue of an FSD was being considered, then it is less likely that the issue of an FSD would be reasonable, even if the potential target has received benefits directly or indirectly from the employer.

426. Therefore, the fact that a target has not received any substantial benefit directly or indirectly from an employer is not a bar to the issue of an FSD if, taking into account the nature of the relationship between the potential target and the employer or the scheme, it is otherwise considered reasonable for an FSD to be issued in circumstances where the scheme is insufficiently resourced, particularly where those circumstances have arisen as a result of the breaking of the connection between the potential target and the employer or the scheme.

427. However, if the potential target has in fact received substantial benefits from the employer in circumstances where there is or has been a close relationship between the potential target and the scheme or its employer, it is more likely that it will be reasonable to issue an FSD where the employer is insufficiently resourced.

428. As we have previously indicated, in making the reasonableness assessment, the Regulator needs to be guided by its statutory objectives. In this case, the relevant objective is to protect the benefits of members under occupational pension schemes and to reduce the risk of situations arising which may lead to compensation being payable from the PPF. The effect of s 100(2) PA 2004, as set out at [15] above, is that in considering whether to issue an FSD in support of its statutory objectives, the Regulator must take into account the interests of the potential targets, as persons directly affected by the exercise of the power. Therefore, when considering the various factors, the Regulator must consider whether the inevitable interference with the potential targets' property rights that will occur by the issue of the FSD is justified in all the circumstances.

429. As we have indicated at [32] above, we must determine the matter afresh. It is not simply a question of us considering whether the Regulator's determination was one that was open to the Regulator to make. We now stand in the shoes of the Regulator and our function is to determine what is the appropriate action for the Regulator to take. We must therefore assess the question of reasonableness by application of the provisions of s 43, taking into account the Regulator's statutory objectives and the provisions of s 100 PA 2004. However, in contrast to the position of the Regulator, whose decision-making body, the DP, is an administrative decision maker, we make our decision acting judicially. It is well-established that in cases of this kind, where the court or tribunal is asked to decide whether a particular course of action is reasonable, it is necessary to undertake a multifactorial assessment and arrive at a value judgment. This means that we should treat all the relevant circumstances as facts which have to be balanced together to reach an assessment or evaluation in relation to this particular case, using our expertise as a specialist tribunal.

430. Furthermore, in making our assessment, we should give the legislation a purposive interpretation, having regard to the policy objective of the legislation, which, as we have stated at [215] above, is to create a rescue framework for pension schemes which are in deficit through the medium of imposing new liabilities on those who have had the necessary degree of association and connection with the relevant scheme at the relevant time. We should therefore consider whether the legislation was intended to embrace the circumstances pertaining to this case as being circumstances in which it is reasonable to issue an FSD. Therefore, we should not interpret the provisions restrictively and should give terms such as "relationship" "involvement" and "benefit" a wide meaning.

431. It is also the case, as we have previously mentioned, that s 43 PA 2004, in contrast to the contribution notice regime created by s 38 PA 2004, is not a fault based regime. The jurisdiction under s 43 is not established by reference to specific acts or omissions having occurred but by reference to the circumstances prevailing at the time the decision is taken to issue the FSD.

432. We understand that for the Targets the imposition of a substantial liability under an FSD certainly feels very much like a punishment for some culpable conduct in the past. Although Lord Pannick, in his submissions on the question of retrospectivity, appeared to accept that the jurisdiction was not fault based, he submitted that the

Regulator was seeking to impose a liability based on criticisms of the Joint Venture Transaction which the Regulator says was responsible for creating risks to the Scheme.

433. In our view, it is not necessary to find well-founded criticisms of the manner in which a particular transaction was structured or implemented, or the way that a business was operated before the jurisdiction can be exercised. As will become apparent, we do not seek to attribute any blame to the Targets as regards the manner in which the Joint Venture was structured or implemented but there is an important distinction between blame and responsibility. Even if all the decisions made by the Targets were taken for good commercial reasons at the time and, without the benefit of hindsight, were perfectly reasonable decisions to take, in our view the key question is whether the structure left the Joint Venture vulnerable to adverse movements in the market so that Granada should bear some responsibility for the risks which eventuated for the Employers and the Scheme. The fact that this is a matter of responsibility rather than blame is also relevant to the extent to which hindsight is a legitimate factor in our consideration.

434. Allied to the question of fault is the existence or otherwise of moral hazard. The Targets contend that the regime does not provide an unrestricted power by which the Regulator can seek ex-post facto to upset the consequences of bona fide commercial transactions, but seeks to address a particular problem, namely the risk that the existence of the PPF gives rise to morally hazardous behaviour. The Targets submit that as the setting up of the Joint Venture and the establishment of the Scheme predate the creation of the PPF the Shareholders could not possibly have had in mind that the risk of the Scheme failing would fall on the PPF. They submit that none of the conduct or commercial structures which are being scrutinised in these proceedings involved any benefits being extracted or any risks being taken on at the expense of the PPF or the Scheme.

435. We accept that had there been any evidence that in choosing to structure the Joint Venture in the manner in which they did the Shareholders relied on the existence of the PPF to justify insulating themselves from any possible liabilities arising out of the establishment of the Scheme were the Joint Venture to fail then that would be a highly relevant factor pointing strongly in favour of the issue of an FSD. We have found no evidence to that effect. However, it follows what we have said about the nature of the FSD regime and its foundation being the present and past relationship between the potential target and the employer and the relevant scheme that the absence of any such motivation is not a material factor militating against the issue of an FSD. We therefore regard the absence of moral hazard in this case as a neutral factor in our consideration.

436. However, the Targets relied on a number of additional factors which they contended were relevant to the assessment of reasonableness and which were factors tending against the issue of an FSD. These are the factors set out at [117] to [119] above.

437. We did not take the Regulator and the Trustee to disagree that the points that the Targets raise in relation to the Jurisdiction Issues and in relation to their lack of connection to the Scheme after the appointment of the Administrative Receivers were relevant factors that we should take into account in our assessment of reasonableness.

In relation to the criticisms the Targets make of the Trustee's conduct and the Targets' contention that Granada has already provided a degree of financial support to the Scheme during the interim participation period described at [346] above, the Regulator contends that these matters are irrelevant to the assessment as to whether it is reasonable to issue an FSD but are questions which (if relevant) should be addressed in relation to the negotiation of the form and quantum of financial support to be provided within the framework laid down by s 45 (2) PA 2004.

438. We accept the Targets' submissions that there is no justification in trying to draw a strict line between those matters which go to the assessment of reasonableness in the context of s 43 PA 2004 and those matters which are purely questions of quantum to be negotiated between the Targets and the Regulator. We accept that if the conduct of other parties who have had responsibility for the operation of a scheme or dealings with it has contributed to the scheme being insufficiently resourced or if the potential targets have already provided a degree of support to the scheme then these are factors that should be taken into account in the overall assessment of whether in those circumstances it is reasonable to expect the potential targets to provide any support at all. Accordingly, we consider whether in the circumstances of this case these additional factors should, when taken together with our conclusions on the other relevant factors, lead us to conclude that no FSD should be issued but, beyond that, we will make no findings as to the form or quantum of any financial support that should be provided.

439. We can dispense with two of the specific factors set out in s 43 (7) PA 2004 briefly. First, no matters have been prescribed pursuant to s 43 (7) (e). Secondly, we do not consider the financial circumstances of the Targets to be relevant in this case. It was common ground that the Targets have the funds to comply with any direction that is imposed. However, we do not consider that the fact that they do have substantial funds points in favour of issuing an FSD. In a case where potential targets are sufficiently resourced, financial circumstances should be regarded as a neutral factor and accordingly we say no more about that factor.

440. Against that background, we now turn to consider the factors relating to reasonableness which are relevant in this case.

The relationship which the Targets have or have had with the Employers

441. As we have previously found, each of the Targets has control of each of the Employers within the meaning of s 435 Insolvency Act 1986 and that therefore the condition set out in s 43 (6) (c) is satisfied in this case. As we observed at [123] above, the test of association and control prescribed by s 435 is a technical test applied by construction of the statutory provisions but it is one of the tests that has to be met before there is jurisdiction to issue an FSD. The necessary connection is not established by reference to the extent to which any control is actually exercised in practice. In our view, s 43 (7) (a) in contrast requires an examination of how close the connection between the potential targets and the employers was in practice. Jurisdiction is conferred by s 43 (6) (c) when the potential target is a company not only when the potential target controls the employer but also when it is associated or connected with it. Thus, the jurisdiction threshold would be satisfied if the potential target and the

employer were associated by being controlled by the same company without the need for the potential target to be the controller of the employer.

442. Section 43 (7) (a) makes specific reference to the situation where the potential target has control of the employer which suggests to us that Parliament intended that it would be more likely to be reasonable to issue an FSD against a target if the link between the target and the employer is that the target controls the employer rather than that they are merely members of the same corporate group controlled by another person.

443. However, we consider that Parliament intended in relation to companies who are related through the shareholding structure that there should be an examination that goes beyond merely the shareholder relationship and calls for an examination more generally of the relationship between the potential targets and the employers. Therefore, in this case, it is necessary for us to examine the relationship between the Targets and the Joint Venture, both in the manner in which the Joint Venture was structured and financed initially and also the extent to which the Shareholders influenced the running of the Joint Venture's business thereafter, taking into account that any influence that the Shareholders had over the running of the business was in practice eliminated following the appointment of the Administrative Receivers.

444. From the findings of fact that we have made, we have therefore identified the following points that in our view we should consider in assessing the relationship between the Targets and the Joint Venture:

(1) In relation to the establishment and structure of the Joint Venture and its financing arrangements:

(a) the acquisition of the existing rental businesses of the Shareholders was effected in such a manner so as to ensure that the Shareholders received a predetermined amount of cash negotiated between themselves, funded pursuant to borrowing arrangements entered into between the Joint Venture and WestLB which were negotiated by the Shareholders and which were secured by charges over the assets of the operating companies within the Joint Venture;

(b) the extent of the due diligence as to the debt that the Joint Venture would be able to sustain;

(c) the retention of an ongoing interest in the Joint Venture which enabled the Shareholders to receive any potential upside in the event that the Joint Venture was successful but did not require them to support the Joint Venture financially; and

(d) the fact that at the time of the Joint Venture transaction there were no employers in existence, in the sense that no pension scheme had been established so that at the time of the transaction, there was no relationship with an employer.

(2) The individuals appointed to manage the Joint Venture;

(3) The terms of the financing arrangements;

(4) In relation to the extent of involvement of the Targets in the ongoing business decisions of the Joint Venture when it was established:

(a) the matters reserved in the Shareholders Agreement as needing prior approval by the BxC Tech Board including approval by the directors nominated by the Shareholders;

(b) the extent to which the Shareholders were "hands-on" in relation to the management of the Joint Venture;

(c) the commitment made by the Shareholders that the Joint Venture would freeze the monthly charges for existing customers on their existing contracts as required by the Office of Fair Trading in the context of the application for clearance for the merger;

(d) the extent to which the Shareholders decided or approved the Joint Venture's strategy; and

(e) the extent to which the Shareholders had an active role in arranging the ongoing finance for the Joint Venture, and in particular the securitisation in June 2002;

(5) The reasons why the Joint Venture failed;

(6) The fact that the Targets made no promises to support the Joint Venture financially; and

(7) The fact that the Shareholders had no actual control over the Joint Venture since the Administrative Receivers were appointed in 2003.

The establishment and structure of the Joint Venture

445. The key point to emphasise is that the relationship between the Shareholders and the Joint Venture was one that was created by the Shareholders without any independent assessment on behalf of the Joint Venture itself being made as to whether the structure that was created was in the best interests of the Joint Venture as opposed to the interests of the Shareholders. During the negotiation of the transaction, it was repeatedly characterised by the Shareholders as a "merger", a term which was used in the press release issued on 17 December 1999 announcing the transaction. As we have outlined at [319] to [321] above, it was the Contribution Agreement, the terms of which was negotiated between Granada and Thorn, which established how much the Joint Venture would pay for the acquisition of the respective rental businesses and how much cash would be paid to the respective parties. The amounts to be paid were calculated by reference to the amount of the loans that were to be made by WestLB to the Joint Venture and the Contribution Agreement obliged the Shareholders to procure that the Joint Venture drew down the required amounts under the borrowing facilities. It is therefore clear that the Shareholders not only decided what the level of borrowing should be but how it should be utilised. The consent of the relevant entities within the Joint Venture to the arrangements were therefore a matter of formality, with the relevant directors implementing arrangements that had previously been agreed between the Shareholders.

446. Therefore, how much cash was paid to each of the Shareholders was determined as a result of an assessment by the Shareholders as to how much debt could be raised and how the amount raised was to be allocated between the parties, as agreed between them. This agreement was concluded following each of the Shareholders obtaining financial advice as to what their respective businesses were worth followed by a negotiation between them. Again, there was no independent assessment by the Joint Venture as to the amount it was being asked to pay for the respective businesses.

447. Consequently, both experts readily accepted that the transaction creating the Joint Venture was not at arm's length. We do however, accept the Targets' submission that the price arrived at was arrived at following an arm's length negotiation between the Shareholders.

448. We also accept that the sale of the respective rental businesses was a bona fide commercial transaction and that a combination of the businesses was recognised by all concerned at the time as being a logical and obvious step for both of them, should the Office of Fair Trading permit it.

449. We also accept that a joint venture was a logical structure to the transaction. Granada did not see the rental businesses as being part of its core business, and as it was looking to exit the market eventually it did not wish to buy Thorn, neither was there any suggestion that Thorn wished to acquire Granada.

450. The Targets chose to structure the transaction in a way that maximised the cash that could be realised on its completion, with both parties participating equally in any future upside which, not unreasonably, was expected to be realised as a result of the considerable synergies to be created as a result of the transaction. However, that cash consideration could only be realised through the borrowings which the Shareholders determined that the Joint Venture should raise and which would be secured by charges over its own assets without the Shareholders themselves giving any guarantees or other security.

451. Again, we make no criticism of that choice, but clearly that choice gave rise to greater risks of failure if the Joint Venture was unable to generate sufficient cash flow to service its debt obligations in a business environment where the parties recognised that the rental market for brown goods was in "continuing serious and endemic decline".

452. Mr Redmayne identified a number of risks which were inherent in the transaction and which he said would have been clear to the Shareholders at the time. The risks identified included:

(1) Turnaround risk, that is the risk that historic declines will continue despite the Project Sizzle Model predicting turnover growth.

(2) Market risk, that is the risk that the decline in the core rental market might accelerate.

(3) Business model risk, that is the risks associated with the implementation of a combined strategy which would result in changing the management and sales

practices of a material portion of the new organisation because there had been two distinctly different historical strategies (one focused on profitability and the other on cash generation).

(4) Cost synergy risk, that is the risk that benefits anticipated from the merger would not materialise, or would materialise to a lesser extent than assumed by the Project Sizzle Model.

(5) Debt financing risk resulting from the fact that the merged business would need to be refinanced after one year of operation and once the securitisation structure was in place, the Joint Venture would be required to make capital repayments which increased if the rental asset base declined.

453. Mr Ashton did not dispute the existence of these risks, or that they would have been known to the Shareholders at the time of the transaction. We accept the existence of these risks, and that they would have been known to the Joint Venture parties. They therefore undertook the transaction in full knowledge that these risks existed. We accept that these risks were managed to a degree as a result of the material generated through the due diligence process and we make no criticism of the Shareholders having decided to proceed with the transaction notwithstanding their awareness of these risks. However, as it was the Shareholders who decided the level of risk that they would ask the Joint Venture to bear, and there was no independent assessment of those risks on its behalf, it is clear that there is a high degree of responsibility on the part of the Shareholders for what ultimately transpired, namely that many of these risks came to pass and the Joint Venture failed. We do not seek, however, to attribute blame to the Shareholders; to do so would be to exercise a degree of hindsight and we accept that at the time of the transaction the Shareholders hoped and expected that the Joint Venture would be a success.

454. However, there were other alternatives that could have been chosen to structure the Joint Venture. As the Regulator submitted, the Shareholders could have treated the businesses which they transferred as capital contributions to the Joint Venture, in return for shareholdings relative to the negotiated valuations of their respective businesses. That would have given them a significant equity investment through which they had the opportunity to make a return over a longer term through the payment of dividends were the business to have been profitable. Alternatively, they could have taken the equal shareholdings which they did, addressing the different valuations negotiated for their respective businesses through a balancing or equalisation payment. However, the Shareholders chose to maximise the amount of cash paid out upfront, with the prospects of further returns being dependent upon the future success of the Joint Venture, but without any recourse to the Shareholders should that not be the case. They chose not to wait and see for a period how the Joint Venture fared and how its strategy was working against a background of a long-term decline in the rental business for brown goods before gearing the business and extracting cash.

455. We have mentioned the fact that the Joint Venture had no independent advice on the Joint Venture and none of the due diligence reports prepared before the transaction were addressed to it. In terms of the financing commitments, the due diligence that was

carried out was designed to give comfort to WestLB as to whether the Joint Venture could support the level of debt that the Shareholders were seeking to raise.

456. There was undoubtedly some consideration given to the impact of the level of debt envisaged in the reports produced by the various consultants (AT Kearney, PwC and KPMG) so that the forecasts of EBIT and free cash flow contained in those reports did generally contain allowance for the cost of servicing the debt. However, it appears that the forecasts produced generally reflect the numbers that the Shareholders gave to the consultants in question and were not the product of a business plan specifically prepared for the Joint Venture which had been subjected to any degree of risk assessment. It appears that there was no provision for amortisation to cover repayment of the debt, presumably on the basis that it was anticipated that a disposal of the business would occur at some stage in the future. We have also referred at [312] above to PwC's recommendation that a sensitivity analysis be undertaken by WestLB on the assumptions to determine what effect shortfalls as against those assumptions would have on the business' ability to service its debt facility but we have seen no evidence that any such analysis took place.

457. The experts differed as to whether it would have been market practice at the time for the Joint Venture to have obtained independent advice or commissioned its own due diligence, particularly as to its ability to service its debt. Mr Redmayne said that he thought it was common practice at the time, whereas Mr Ashton thought that it was not. We make no finding on that or criticise the Shareholders for not having ensured that the Joint Venture did obtain independent advice. However, the absence of independent advice meant that the Joint Venture was entirely reliant upon whatever due diligence the Shareholders themselves had undertaken, which is a significant factor in reinforcing our conclusion that the Joint Venture was a creature of the Shareholders and that the terms of the transaction and how it was structured was under their sole control.

458. The Targets say that it is important to note that the relationship between the Joint Venture and the Employers only came into existence once the transaction had been completed and once the Scheme had been established. Therefore, they say that there was no relationship for the purposes of s 43 (7) (a) at the time of the transaction and therefore the points made about the features of the transaction are irrelevant to our assessment of reasonableness.

459. We reject that submission; the relationship that was subsequently created through the establishment of the Scheme was derived from the establishment of the Joint Venture and the decision to create a defined benefit scheme was made within the framework of the Shareholder Agreement which contemplated that such a decision should require the approval of the Shareholders and was clearly made within the structure and financing arrangements of the Joint Venture which had been created. We accept, as Mr Furness submitted, that it would be wrong to simply apply a "but for" test, that is to say the Scheme would not have been inadequately resourced but for the entering into of the Joint Venture, but we do say that the responsibility of the Shareholders for the creation of the Joint Venture with the features that it had, in the context of which a decision was made to establish a defined benefit occupational

pension scheme, is a highly relevant and important factor in our assessment of reasonableness.

The individuals appointed to manage the Joint Venture

460. As we have recorded at [47] and [48] above, the executive management of the Joint Venture was in the hands of Mr Roger Mavity as Group Chief Executive of the Joint Venture and Mr Mike Neal, as finance director. Both of these individuals had been directors of Rental & Retail. In terms of the key non-executives, Mr Graham Parrott was the Commercial Director of Granada and Mr Laurence Cooklin, the non-executive chairman of the Joint Venture had formerly been Chief Executive of Thorn UK. Mr Mavity and Mr Neal also became the sole directors of each Employer. These appointments are further indications of the closeness of the relationship between the Shareholders, and Granada in particular, and the Joint Venture and there were no independent non-executive directors who may have operated as a challenge to the decisions made by the executive management. Again, we make no criticism of that structure which was one that the Shareholders were perfectly entitled to adopt but the structure of the Joint Venture's senior management would in practice have meant that there was a close relationship between the Joint Venture and its Shareholders.

The terms of the financing arrangements

461. As we have previously indicated, the terms of the financing arrangements for the acquisition of the Shareholders' rental businesses by the Joint Venture were negotiated between the Shareholders and WestLB before the Joint Venture's board was operational. This is reflected in the fact that the commitment letter given by WestLB on 17 December 1999 was addressed to Granada and Thorn. It therefore follows that all of the terms of the financing, and in particular the interest rates payable, the financial covenants to be observed and the security to be granted over all of the Joint Venture's assets, were those judged by Granada and Thorn to be appropriate and agreed with WestLB. Likewise, Granada and Thorn committed the Joint Venture to a refinancing of the acquisition facilities through a securitisation programme within one year of the drawdown of the facilities. Further, Clause 2.4 of the Contribution Agreement required Thorn and Granada to ensure that each of the relevant Joint Venture companies drew the maximum sums available to them pursuant to the WestLB facility. The Joint Venture did not have the option, once it came into existence, of reducing its initial level of borrowing.

The extent of the involvement of the Targets in the ongoing business decisions of the Joint Venture

462. We have described in broad outline at [339] to [344] above the structure of the Shareholders Agreement and the manner in which the approvals that were necessary according to its terms operated in practice.

463. The Targets seek to characterise the relationship between the Shareholders and the Joint Venture as regards the running of the Joint Venture's business as one where they did no more than take a natural and responsible interest in their shareholding. They

contend that the executive management of the Joint Venture took the decisions, but they first consulted the Shareholders. They contend that one of the ways in which that consultation took place was at the monthly shareholder review meetings.

464. In our view that characterisation is not supported either by the terms of the Shareholders Agreement in relation to matters which are covered by that agreement, or the manner in which significant decisions relating to the Joint Venture were taken in practice.

465. There is a long list of specific matters in Clause 4.3 of the Shareholders Agreement which require the consent of both the A Directors and the B Directors. As we have previously indicated, the giving of such consent is in practice the approval of the Shareholders to what is being proposed because the A Directors and the B Directors are appointed by the respective Shareholders and will take into account the interests of those Shareholders when making their decisions on behalf of the Joint Venture. In practice, if a proposal is not one that either of the Shareholders is in favour of, then it would not happen.

466. The list of matters specified in Clause 4.3 of the Shareholders Agreement includes the creation of new banking facilities or renewal of existing banking facilities of more than £5 million, the declaration or payment of any dividend or distribution, the entry into any material contract or arrangement outside the ordinary course of business and the adoption of the annual operating and capital budgets of the Joint Venture and the annual update of its business plan. The Shareholders Agreement defines "Business Plan" as meaning the rolling business plan as amended and updated annually "by the parties in accordance with this Agreement". Therefore, the Shareholders Agreement clearly envisages that the Business Plan for the Joint Venture is essentially under the full control of the Shareholders.

467. A further illustration of the degree of control and influence that the Shareholders exerted over the Joint Venture is that in their press release issued on 17 December 1999 announcing the proposed merger, they stated that they had committed the Joint Venture to freeze in perpetuity all monthly charges for existing customers on their existing contracts which is clearly a significant factor in the context of the Joint Venture's ongoing business. We understand that decision was as a result of a requirement of the Office of Fair Trading made in the context of the Shareholders' application for clearance of the transaction.

468. There is evidence of decisions made by the BxC Tech Board being referred to the Shareholders for approval. For example, the minutes of its meeting held on 14 September 2000 record that the meeting "agreed in principle" to a proposal from Mr Neal to appoint particular IT consultants to integrate Granada's IT platform systems on to the Thorn platform. The minutes state that Mr Tagliaferri, one of the Thorn representatives on the Board, and Mr Tibbitts, one of the Granada representatives, "would now seek approval from shareholders as quickly as possible." As we have said before, in practice this meant seeking approval from Mr Allen of Granada and Mr Hands of Thorn. The minute also recorded that the Joint Venture would seek further approval for any additional expenditure beyond the preparation phase of the project.

These minutes also give insight into the manner in which the Shareholders influenced the business planning exercise. The minutes record that "the JV partners were looking for an agreed base plan against which to manage the business, with the objective of maximising shareholder value."

5 469. An example of how the Shareholders were briefed on strategic and management proposals so that their input could be obtained is to be found in a memorandum sent by Mr Mavity to Mr Allen on 27 September 2000. In this memorandum, Mr Mavity outlines the proposed commercial strategy. As an example of how the Shareholders continued to influence the way the Joint Venture was managed, the memorandum refers
10 to how Mr Hands was recommending a management restructuring which Mr Mavity said he would like to discuss with Mr Allen.

470. An illustration of the manner in which the Shareholders were involved in decisions regarding shop closures is to be found in a hand-written memorandum dated 13 December 2000 from Mr Tibbitts to Mr Staunton recording the way in which
15 shareholder approval was being sought for those closures. The memorandum states that clearance for another 135 shops to be closed is being sought urgently and ends "Do you agree please Henry?".

471. It is clear that the Shareholders were closely involved in relation to the securitisation, which as we have found, was agreed to by the Shareholders as the means
20 to refinance the borrowings incurred by the Joint Venture upon its formation. As we mention below, both Mr Redmayne and Mr Ashton identify the terms of the securitisation as being a contributory cause of the failure of the Joint Venture. In particular, Mr Redmayne notes the covenants in the securitisation documentation which required mandatory repayments of capital in the event of operational underperformance
25 (over and above interest in scheduled repayments) with the result that there could be more pressure on the Joint Venture's performance which in turn may lead to difficulties in servicing its debt.

472. A memorandum from Mr Staunton to Mr Allen dated 16 May 2002, prior to the securitisation having been completed, stated that Mr Staunton had had a meeting with
30 Mr Mavity who had explained that there were some problems with regard to the securitisation revolving around the poor performance of Endeva which was causing a "hole in the cash flows about 2 ½ years out". The memorandum went on to say that an impasse had developed between Nomura and WestLB and that "we will need to become more involved in the situation over the course of the next 14 days.".

35 473. We were referred by the Trustee to a number of other examples of where in practice the Shareholders exercised control over the operation of the Joint Venture as follows:

(1) When, after completion of the merger, the first budget presented by the Joint Venture's management to the Shareholders was described by Mr Allen in a
40 handwritten note on the November 2000 monthly report as "just unacceptable", the January 2001 monthly report records that the Joint Venture's management

had become "focused on a major re-thinking of the business, linked to a zero-base cost reduction programme, following the recent meeting with the shareholders".

(2) The minutes of a meeting of the BxC Tech Board held on 7 March 2001 record proposals for structural savings through among other things a radical reduction in the number of shops over a four-year period and that "the shareholders agreed that the proposals should be implemented."

(3) As an example of the Shareholders' control in relation to remuneration matters, a paper dated 2 February 2001 set out proposals for a Long Term Incentive Plan, setting out recommendations "for consideration by the Shareholders as to the most appropriate LT IP arrangements for box clever in the light of the strategy and structure agreed in October." The memorandum concluded by saying "we trust that the proposals are acceptable to the Shareholders."

(4) A further example in relation to remuneration matters is recorded in the minutes of the operations review held with the Shareholders on 22 May 2001 where it is stated that both Shareholders had agreed to a proposed pay freeze to the end of September 2001, to be followed by an increase in the 3.5 – 4.0% range.

(5) A file note of a meeting held on 27 May 2003 regarding refinancing proposals records that both Shareholder representatives at that meeting "would be prepared to accept the terms".

(6) The Shareholders also became involved in more mundane matters. An email of 11 February 2003 records that an offer to landlords about rentalisation of property improvements "needs shareholder backing".

474. This clear evidence of the Shareholders being very much "hands-on" in the manner in which they participated in the Joint Venture's decision-making processes is supported by Mr Wakelam's evidence. Mr Wakelam himself used the same phrase to describe the relationship between the Shareholders and the Joint Venture.

475. Although it was put to Mr Wakelam that the true position was that decisions relating to the management of the Joint Venture were taken by the executive management team after consultation with the Shareholders rather than the executive management team making recommendations which the Shareholders would approve, Mr Wakelam was quite clear that the latter represented the true position. Although the events took place many years ago, Mr Wakelam was present at many of the monthly shareholder review meetings or operational review meetings attended by representatives of the Shareholders and his evidence was, particularly in relation to financial matters such as budgets, that it was the Shareholders who made the ultimate decision. We therefore accept his evidence as being reliable on this point as it is consistent with what we have seen from the documentary evidence. We also accept Mr Wakelam's evidence that it was very rare that any minutes would be taken of actions agreed at review meetings, but if it was reported that a particular proposal had been signed off then that was accepted without further formality and matters proceeded on the basis that Shareholder approval had been given.

476. Mr Wakelam's evidence was that he had not seen the Shareholders Agreement itself, but his evidence was that the kinds of decisions for which Shareholder approval was given included those in relation to business strategy, pay rises and bonus and incentive plans, staff numbers and redundancies, integration of the IT systems, shop closures, other ways to reduce costs, how Endeva was to recharge the rest of the Joint Venture for its services, and financing. All this is consistent with the Shareholders Agreement itself as well as the documentary evidence we have referred to above.

477. We accept Mr Wakelam's evidence that in terms of individuals who made the decisions, as far as Granada was concerned it was Mr Allen, Mr Staunton and Mr Tibbitts, although Mr Tibbitts was himself generally acting on the instructions of the others. This is consistent with the decision making on the IT issue referred to at [468] above when Mr Tibbitts was present at the relevant meeting but had to seek approval, presumably from either Mr Staunton or Mr Allen. We accept, as Mr Wakelam said, that Mr Mavity and Mr Neal viewed Mr Allen and Mr Staunton as their "bosses" from Granada, rather than simply fellow directors on the BxC Tech board who had equal say with the other directors. This is reflected in the distribution list of the monthly management reports (such as the September 2001 report) where Mr Allen, Mr Staunton, Mr Parrott and Mr Tibbitts are listed under "Granada" whereas Mr Cooklin, Mr Mavity and Mr Neal were listed under "box clever". The circumstances are consistent with our observations at [344] above that the formal terms of the Shareholders Agreement were applied in a practical manner and individuals such as Mr Allen and Mr Staunton would take the necessary decisions wearing different hats, either as board members of the Joint Venture or as representatives of Granada, as was necessary or appropriate.

478. We therefore conclude that the Shareholders exercised close control in practice over the operations of the Joint Venture and all major decisions relating to its business during the life of the Joint Venture prior to the appointment of the Administrative Receivers.

The reasons why the Joint Venture failed

479. Mr Ashton stated that the Joint Venture failed because it was not generating adequate cash flows to service and repay its debts when due. In his view the principal causes of the failure were:

(1) the unexpected pace of the decline in the rental market;

(2) the unintended consequences of closing shops to an extent that went beyond rationalisation, in response to that decline;

(3) Endeva's losses and the failure to develop business to supplement and/or replace the declining TV rental business;

(4) the unintended consequences of the securitisation; and

(5) in the light of the above (and in particular the unexpected pace of the decline in the rental market), the high leverage of the Joint Venture and the resulting burden which the debt placed on it.

480. Mr Redmayne gave one reason. Similar to Mr Ashton's overall assessment, he stated that the Joint Venture was unable to meet the terms of its financing in September 2003. In his opinion, a lower level of debt could have provided the Joint Venture with increased financial flexibility, and therefore time, to reshape the business and adapt to 5 the challenges of the declining rental marketplace.

481. We accept Mr Ashton's assessment and the reasons he gave for it, which are supported by the evidence. We also accept Mr Redmayne's analysis that a lower level of debt would have given the Joint Venture more time to adapt to the rapid decline in the market. It is consistent with our observation that the Shareholders could have chosen 10 to commence the Joint Venture with a lower level of debt and extract less debt from the outset to enable them to wait and see how the business developed.

482. We do not suggest that the impact of Endeva's losses and the impact of closing shops were matters under the control of the Shareholders as opposed to a reflection of management decisions taken by the Joint Venture itself, but we do say that those matters 15 would have had less of an impact if the Joint Venture had been less highly leveraged. The initial financing of the acquisition, with the commitment to refinance the borrowings through a securitisation, were, as we have found, the result of decisions made by the Shareholders. Those decisions were made against a background of a long-term decline in the rental market as the Shareholders were fully aware. It is therefore 20 plain that the failure of the Joint Venture was a direct result of the structure adopted by the Shareholders and they therefore must bear the responsibility for it, even if, as we previously said, we make no criticism of the choice they adopted. They were fully aware of the risks and they decided to accept them. This is therefore another clear factor demonstrating a close relationship between the Shareholders and the Joint Venture.

25 *Lack of Shareholder financial support for the Joint Venture*

483. The picture that emerges from the findings as to the nature of the relationship between the Shareholders and the Joint Venture is one that is no different in substance to the usual relationship that would be expected between a parent company and its subsidiaries or Head Office and the separate divisions of a large enterprise. However, 30 this relationship was different in one significant respect. This was that the Joint Venture was expected to stand on its own feet financially and could not expect any financial support from its Shareholders, whether in the form of loans or guarantees or other security to support its borrowings. As we have seen, the Shareholders Agreement made it quite clear that if additional funding or security was required by the Joint Venture it 35 had to be obtained from third parties without recourse to the Shareholders.

484. This is in contrast to the position in the *Sea Containers* case referred to at [27] above where the insufficiently resourced employer was a service company within a group where it had always been the intention of the target company to stand behind the pension liabilities of the employer and it had done so for many years. The situation in 40 this case is also and in contrast to the position in *Lehman Brothers* where the ultimate parent company in the group had given guarantees in respect of the scheme. Those circumstances were very strong factors in favour of the imposition of an FSD in those cases which would in essence ensure that the financial support that had always been

contemplated would be given was continued. Had the Shareholders undertaken to support the Joint Venture then that would clearly be a strong pointer in favour of the issue of an FSD but that is not the position in this case.

The effect of the appointment of the Administrative Receivers

5 485. The Targets contend that if (as we have found to be the case) the necessary connection or association is established to found jurisdiction pursuant to s 43(6) PA 2004 it will have been on the most technical basis. It is accepted by all parties that after the start of the administrative receiverships, the Administrative Receivers were in practical control of the Joint Venture's operating companies, including the Employers 10 and the Targets have not had any actual control or influence over the Employers at any time after September 2003. The Targets' commercial connection with the company ceased over 6 years before the look-back period began.

486. The Targets submit that to impose regulatory action on the basis of such a technical form of connection or association is inconsistent with the substantive 15 importance which the regime attaches to a target's actual influence over the employer. They submit that the connection/association gateway is one designed to reflect the fact that control over an employer's affairs is likely to be central to any justification for regulatory action.

487. Therefore, the Targets submit, imposing an FSD when the period for doing so is 20 being extended far beyond the date at which the Targets ceased to have any commercial connection with the employers would be unfair because:

(1) companies in the position of the Targets in this case will not know when, if at all, their connection or association with the employers has been broken, as that is in the hands of the Administrative Receivers; and

25 (2) companies in this position may not know that they need to, and may not be able to, break the link of connection and association themselves, and hence trigger the start of the look-back period.

488. We do not think that this is a strong point in favour of the Targets for the following 30 reasons.

489. As explained by Briggs J (as he then was) in *Re Nortel* [2011] Bus L.R. 454 at [31] in a passage which was endorsed by the Court of Appeal and the Supreme Court in that case:

> "Although the list of potentially relevant considerations is not exclusive, the 35 emphasis of three out of the four of them is upon the relationship of the target with the employer (where the target is not the employer itself) and with the relevant scheme, both at the issue date and previously. The focus may therefore be upon an ongoing relationship which is expected to continue, or upon a purely historic relationship which has ended."

490. This passage indicates that the historic relationship can be as important as any ongoing relationship. Insofar as the Targets had responsibility for the manner in which the Joint Venture was structured and operated, the die was cast at the outset of the transaction and, subject to the point about the operation of the Scheme which we consider below, the Receivers did nothing to alter the structure or the consequences that flowed from it. Their role was simply to realise as many of the assets as possible for the benefit of the secured creditors. It is what happened during the period when the Joint Venture was under the Shareholders' control where the focus on the relationship issue should be in this case rather than what happened afterwards.

491. In our view, as we have found that the level of control and influence was very strong in practice during the historic relationship period, this outweighs the fact that at the time the look-back period began, the Targets only had control in the technical sense.

Conclusion on the relationship issue

492. In summary, the circumstances relating to this issue point very strongly in favour of the issue of an FSD to the Targets. We have discounted the fact that practical control ceased some years before the look-back date. As far as the other factor in favour of the Targets is concerned, namely the fact that it was never contemplated that the Targets would support the Joint Venture financially, in our view although actual or expected financial support in the past from the Targets to the Joint Venture would be a strong factor in favour of the issue of an FSD, we do not think its absence in this case weakens the case for the issue of an FSD based upon the relationship issue.

493. In reality, the Joint Venture was a continuation of the prior participation of each Shareholder in its respective business through a vehicle which they created and structured according to what they perceived as being in their own interests. Because of the measure of control that the Shareholders exercised in relation to the formation of the Joint Venture and its subsequent operation, it could not be said that the Shareholders had established a freestanding business or that the situation could be compared to where the company had disposed of the business it no longer wished to have an interest in to a third party and where it would be expected that the purchaser would have a free hand in how it structured and operated the business and therefore should ultimately be responsible for its ultimate success or failure.

494. In choosing to adopt the structure they did, and again we make no criticism of that commercial decision, the Shareholders extracted considerable cash from the business with no risk of recourse to their assets. They retained an ongoing interest in the merged business with the possibility of further value being generated if the business was successful, but without having to bear any responsibility if the business, whose strategy they continued to determine, subsequently failed. Putting it starkly, they had all the power to be expected of a parent over its subsidiary but with none of the obligations to support that subsidiary which are the norm when financial difficulties arise.

The value of any benefits received directly or indirectly by the Targets from the Employers

495. As we have observed at [430] above, we should give the legislation a purposive interpretation, having regard to its policy objectives and we should not interpret the provisions restrictively. Therefore, in considering whether in this case the Targets have received benefits directly or indirectly from the Employers and what is the "value" of those benefits, we should not construe s 43(7)(c) restrictively.

496. In that regard, the Targets submit that any benefits deriving from the creation of the Joint Venture cannot be benefits "received directly or indirectly… from the employer" because at the time of the creation of the Joint Venture, there was no relevant occupational pension scheme in existence, and one was not even contemplated at that time. Therefore, there could be no "employer" for the purpose of s 43 (7) (c). For the reasons we gave at [459] above, in relation to our consideration of s 43 (7) (c), we reject that submission. In our view, the legislation is sufficiently wide in its terms to cover a situation where the benefits concerned have been obtained prior to the making of the decision to establish the relevant scheme, and therefore create the relevant relationship for the purposes of the legislation. What is required is a holistic assessment of the entirety of the relationship.

497. Neither in our view is it necessary to establish a particular monetary value for any particular benefit. Clearly, if a specific cash benefit received by a target can be established, then it will be easier to identify the nature of the benefit received, but that is not to say that there has not been the receipt of other benefits in respect of which it is difficult to establish a precise monetary value.

498. From the findings of fact that we have made, we have therefore identified the following points that in our view we should consider in assessing the value of the benefits received by the Targets from the establishment of the Joint Venture:

(1) the calculation of the price paid by the Joint Venture;

(2) the fact that the cash consideration could be realised because the Joint Venture entities, including the Employers, charged their assets as security for the loans obtained from WestLB which were used to pay the purchase price;

(3) the lack of any recourse to the shareholders in the event that the business failed; and

(4) whether there was any evidence that the Targets were motivated by the desire to shift their liability for the pensions of the transferred employees out of the Legacy Schemes into the Scheme established by the Joint Venture.

The price paid by the Joint Venture for the acquisition of the Granada and Thorn rental businesses

499. Central to this question is whether it can be said that the Joint Venture overpaid for the acquisition of Granada's rental business. Bearing in mind what we have said about the lack of an independent price assessment by the Joint Venture itself, were it to be shown, assisted by the experts' evidence, that the price paid by the Joint Venture clearly overvalued the business, then in our view there would have been a substantial benefit received indirectly from the Employers, in that the values of their respective businesses would have been considerably less as a result of the acquisition at an overvalue, and the value of such benefit would be the difference between the price paid and what is likely to have been paid had the transaction been on an arms length basis.

500. In resolving this issue, we accept that the burden is on the Regulator and the Trustee to demonstrate that the £600 million paid by the Joint Venture overvalued the Granada rental business.

501. The Targets accept that in circumstances where Granada and the Joint Venture were not arm's length parties no presumption can be relied on that the price represents the market value simply because it was the agreed price. This is accepted by the experts in their Joint Statement. However, the Targets submit, against a background which involved two separate arm's length transactions, between the Shareholders themselves and between the Joint Venture and WestLB, the inherent probability must be that it represented a figure within the reasonable range of values for the business because:

(1) The price was in part the result of an agreement between Lazard and Schroders as to what the appropriate value of the combined businesses was. There is nothing to indicate that this agreement between Lazard and Schroders was other than it appeared to be, namely a true reflection of their respective opinions as to value.

(2) The implication of the report prepared for Granada's board in November 1999 is that by that time the advice which Lazard was giving to Granada and on the basis of which Granada was acting was that its rental business was worth £600 million.

(3) WestLB would only have been prepared to lend some proportion of the value they perceived to be in the Joint Venture and the amount lent was well above the price paid or payable by the Joint Venture to Granada for its business.

502. Neither expert was able to say with any degree of certainty so far after the transaction was effected what would have been an appropriate valuation for the business at the time. The experts agreed in their joint statement that "it is not possible now to produce a reliable independent valuation of either the Granada Rental Business or any synergies through valuation methodologies."

503. Nevertheless, Mr Ashton stated in his report, that so far as it is possible to form a view on the basis of the evidence available, he did not consider that the amount payable or paid overvalued the Granada Rental Business. In his opinion, the appropriate standard of valuation to adopt to answer the question was "Synergistic Value", that is by consideration of the value of the business in the hands of the Joint Venture, on the

premise that the Joint Venture has the benefit of 100% of the synergies from combining the Granada and Thorn businesses.

504. Mr Ashton's opinion was that to determine what the value of the asset the Joint Venture received was, it is essential to include the value of those synergies. His opinion was that a third-party purchaser in the position of the Joint Venture would also have had to pay Granada an element of the value of those synergies.

505. Mr Ashton concluded that there was no "proper basis on which the figure of £600 million, which formed the basis of the deal, can be discounted as reasonable."

506. Mr Redmayne took a different approach. He focused on the observation recorded in the minutes of the Granada Board's meeting of 16 November 2009 that the best indicative offer received from a third party had been around £450 million. Mr Redmayne regarded that as "the most robust external market value bid in the evidence available". However, he went on to say that the "final transaction value might be lower and, in the absence of a competitive situation, would be unlikely to be higher as typically indicative offers are pitched at a level sufficiently high to elicit engagement and interest from a potential seller to consider a sale transaction." Mr Redmayne was also of the view that an independent third-party purchaser would have paid nothing material for the prospective synergies not yet delivered in a declining business. Mr Redmayne also observed that due diligence would have revealed matters, including the decline in the market, which would have caused any third-party bid to be reduced. Mr Ashton does not accept that the due diligence process would necessarily have led to any reduction in the price paid, and it may indeed have resulted in an increase.

507. The price was not negotiated between the Joint Venture and Granada on an arms length basis, so there is some force in what Mr Redmayne says as to the likelihood that if there had been a third-party negotiation, a third party, who may have carried out further due diligence than that which was actually done in this particular case, may well have paid less than £600 million for the Granada rental business. However, we cannot say, so long after the event, in circumstances where both experts agree that it is impossible now to do a proper valuation of the business, that a price of £600 million is so obviously unreasonably high that it cannot reflect a proper valuation of the Granada rental business at the time. We therefore have not concluded that the price of £600 million paid overvalued Granada's rental business at the time.

508. However, we do not conclude from this that the fact that the Targets may have paid an appropriate price for the business is a positive factor tending against the issue of an FSD. All we have concluded at this stage is that the Targets did not obtain any benefit from the Joint Venture having acquired the Granada rental business at an overvalue.

The payment of cash consideration to Granada upon the acquisition by the Joint Venture

509. Mr Redmayne identified amongst the benefits which he says in his report the Targets achieved through the creation of the Joint Venture the following:

(1) An immediate cash realisation of its interest in a declining business.

(2) Access to potential upside in the event that the Joint Venture generated distributable funds or was listed in the future, with protection from any downside given the non-recourse structure of the Joint Venture.

(3) The proceeds of the transaction helped Granada reduce its net debt and improve its financial position.

510. The Targets' response to these points is:

(1) If Company A pays Company B a sum of money for an asset, Company B cannot be said to have benefited as a result if the sum paid for the asset is equal to the value of the asset. Where Company B divests itself of an asset for value it is wrong to regard it as having "benefited".

(2) The fact that Granada realised cash immediately cannot be said to be a benefit where the cash realised did not exceed the value of the business at the time it was transferred.

(3) No potential upside was ever realised.

(4) Protection from any downside cannot be a "benefit" received but was simply a consequence of the fact that the business was transferred to a separate legal entity; not agreeing to guarantee any of the liabilities of the Joint Venture cannot be described as a "benefit" when there was no legal obligation to do so.

(5) There was no evidence indicating that Granada was able to reduce its debt as a result of the receipt of the cash consideration.

511. We accept that all of the matters identified by Mr Redmayne are properly characterised as valuable benefits received by the Targets directly or indirectly from the Employers for the purposes of s 43 (7)(c) PA 2004 for the following reasons.

512. As we have previously mentioned, the Targets chose to structure the Joint Venture transaction in the way that they did. By procuring that the Joint Venture subsidiaries, including the Employers, charged all of their assets the Targets were able to extract cash from the business. If the Joint Venture entities had had a free choice and had chosen not to finance the acquisition in the way that they did, then the Targets would have had to adopt a different structure, such as a share for share exchange which would have enabled the Targets to have realised value through the payment of dividends on their equity interest over a longer timeframe. There could be no doubt that the receipt of dividends would be regarded as a benefit of value received directly or indirectly from employers. We therefore see no reason why a structure which delivers value upfront should be regarded as being intrinsically different. The decision made by the Joint Venture, made at the behest of the Shareholders to charge their assets to support the borrowings made to fund the acquisition must therefore be regarded as a valuable benefit, even if no specific monetary value can be placed upon it.

513. Likewise, having the potential upside of further returns in the future if the Joint Venture was successful, either through dividends or other distributions or an exit through a flotation or further sale without any risk to the cash already having been extracted, must be regarded as a real and valuable benefit. In essence, Granada had obtained a free option on any future upside of the business, leaving the Joint Venture to bear the consequences should the Joint Venture not be successful. We do not think that it makes any difference that these potential benefits were not in fact realised.

514. The receipt of a benefit by the realisation of cash which could be used to pay off immediate borrowings, which indeed was required to be disbursed in that manner according to the terms of the Contribution Agreement, self-evidently is a benefit of value, even if a specific monetary amount cannot be put on it. The repayment thereby improved Granada's balance sheet, as a result of the structure of the transaction that was adopted.

Lack of recourse to Shareholders

515. We have nothing to add to what we have said in relation to this matter at [484] above. We do not think that this can be treated as a "stand-alone" benefit, but its presence as a feature of the Joint Venture transaction enhances the value of the benefit that we have found the Targets received as a result of the way the Joint Venture was structured.

Motivation to shift pensions liabilities

516. The evidence from the Contribution Agreement shows that the Shareholders did not intend that there should be a defined benefits scheme for employees of the Joint Venture and the Contribution Agreement envisaged that historic liabilities in respect of pensions benefits could remain with the Legacy Schemes.

517. However, as we have found, the opportunity to join the defined benefit section of the Scheme when it was established was only open to those employees of the Joint Venture who elected to transfer their existing DB benefits from the Legacy Schemes. The result of this stipulation would clearly have worked in the Targets' favour had the historic liabilities been transferred, but of course they never were. Moreover, we accept that it was Thorn's insistence that members transfer their benefits out of the Legacy Schemes to the Scheme which prevailed over Granada's preference which resulted in the stipulation that there could be no DB benefits within the Scheme unless the historic liabilities were transferred. Therefore, had the transfer of historic liabilities taken place, then undoubtedly Granada would have benefited. In the absence of the transfers having taken place and in light of the fact that Granada agreed to an interim participation period and indemnified the Employers against pensions liabilities incurred in the interim participation period, which is a clear indicator that there was no general desire to shift the historic liabilities, we conclude that we should place little weight on this factor in our assessment.

Conclusion on the benefit issue

518. In summary, the points that we have made regarding the benefits which arose out of the payment of the cash consideration and the structure of the Joint Venture transaction, reinforce the conclusions we have come to on the relationship issue, to which they are closely linked. We find that the other factors that we have considered in relation to the benefit issue are broadly neutral.

The connection and involvement of the Targets with the Scheme

519. From the findings of fact that we have made, we have identified the following points that in our view we should consider in assessing the relationship between the Targets and the Scheme:

(1) The decision to establish the Scheme as a defined benefit scheme, including the reasons why that decision was taken and the responsibility for making that decision.

(2) The decision by the Shareholders that they would not guarantee or financially support the Scheme having taken the view that it had to be supported by the Joint Venture as a self-standing business. Therefore, the Trustee had been aware since the inception of the Scheme that it could rely only on the covenant of the Joint Venture and not on any expectation that Granada or Thorn would make good any deficiency in the Scheme.

(3) The decision to offer employees who transferred into the Scheme Continuous Service Benefits.

(4) The decision to inform members that they would have Continuous Service Benefits on what the Targets describe as a "fingers crossed" basis, that is before an agreement had been reached on the transfer payments that would fund the payment of those benefits.

(5) The decision not to accept the bulk transfer of the rights of the transferred employees accrued in the Legacy Schemes.

(6) The decision to amend the Scheme so as to include the Top Up Arrangement.

(7) The effect of the pay rises approved by the Administrative Receivers after September 2003.

(8) The decision to delay closing the Scheme to new accruals because of the ongoing negotiations with the Shareholders for financial support for the Scheme.

(9) The decision not to wind up the Scheme shortly after the Administrative Receivers were appointed or at any time thereafter.

The establishment of the Scheme

520. As we have found at [343] and [344] above, the Shareholders were involved in approving all major decisions regarding the Joint Venture and its operation, albeit sometimes informally. As we have found at [350] above, the Shareholders were clearly closely involved in the proposal to create a defined benefit scheme rather than the

defined contribution scheme envisaged in the Contribution Agreement and they approved it.

521. As we found at [352] above the maintenance of good employee relations was an important factor in the decision to establish a defined benefit rather than a money purchase scheme. Granada therefore clearly recognised that good employee relations was an important factor in the success of the Joint Venture as a whole, and therefore it was in their own interests, as well as those of the Joint Venture itself, to take account of this factor when approving the proposal for the Scheme.

522. The proposal recorded that the actuaries for each of the Legacy Schemes and the proposed new Scheme had agreed that the basis for the transfer payments from the Legacy Schemes would not lead to a significant initial surplus nor deficiency and that pension costs would in fact reduce in future years. Clearly that factor influenced Granada's decision to approve the establishment of a defined benefit scheme. Nevertheless, the decision to create a defined benefit scheme did create a funding risk to the Employers, and consequently a risk to pension benefits that former Granada members would in future earn in the Scheme. Furthermore, Granada made a conscious decision to approve the establishment of the Scheme as a defined benefit scheme against the background of the Employers being part of a highly leveraged Joint Venture, with the inherent risks of such a structure. Without the support of the Shareholders the Employers' covenant was therefore undoubtedly relatively weak.

523. It is clear from our findings at [354] above that Granada was aware of the "balance of risk and reward" inherent in the decision to establish a defined benefit scheme, and although the initiative to require employees to transfer their benefits from the relevant Legacy Scheme if they wished to have DB benefits in the Scheme came from Thorn, Granada agreed to it. As we observe at [356] above, the arrangements had the advantage of potentially enabling the Shareholders to divest themselves of their historic liabilities relating to the Legacy Schemes in respect of the employees who transferred to the Joint Venture.

524. We therefore find that Granada was closely involved in the decision to establish the Scheme and it did so in full knowledge and acceptance of the risks and rewards that may result. The establishment of a defined benefit Scheme therefore became an integral feature of the Joint Venture that the Shareholders created. We therefore place no weight on the Targets' contentions that at the outset of the Joint Venture there was no intention to create a defined benefit scheme.

No guarantee of financial support from the Shareholders

525. There was no suggestion when a defined benefit scheme was being proposed that the Shareholders would stand behind the Scheme. Indeed, a letter from the Joint Venture to employees on 27 June 2001 refer to the establishment of the scheme as being "a major milestone in box clever and Endeva becoming stand-alone businesses." Mr Herbert accepted in his cross examination that this reflected his understanding of the position.

526. Clearly, had any such promises been made then that would have been a significant factor supporting the issue of an FSD, as it had been in the *Sea Containers* and *Lehman Brothers* cases which we have previously referred to. We do not, however, see the factor as being one which in the circumstances of this case weakens the case for the issue of an FSD.

The decision to give Continuous Service Benefits on a "fingers crossed" basis

527. The Targets relied on what turned out to be the detrimental effect on the solvency of the Scheme of the decision that was made to open the Scheme with effect from 1 October 2001 on the basis that it would provide Continuous Service Benefits notwithstanding that the transfer payments had not been agreed at that time. The Targets regard that decision as being one that was taken by the Joint Venture and the Trustee together.

528. Mr Herbert explained in his evidence that the Trustee felt able to agree to this course of action based on the comfort it had from Schedule 10 to the Contribution Agreement which contained provisions for calculating the past service transfers from the Legacy Schemes. As matters transpired, as we have found, the Trustee eventually decided not to accept the transfers for the reasons set out at [383] above.

529. The Targets contend that this is a decision that "stored up trouble" for the future. A commitment by the Trustee to provide Continuous Service Benefits meant that if the transfers could not be agreed, the liability for the past service benefits would have to stay with the Legacy Schemes. The effect of the decision was that members could accrue future service benefits within the Scheme but left "up in the air" the question what would happen to past service benefits. Mr Herbert accepted in cross examination that that was the effect of the decision, but he justified the approach on the basis that the Joint Venture planned clearly to honour in the interim before the transfer payments could be agreed the arrangements that had been previously outlined to employees in the July 2001 communications.

530. The Targets pointed out that members were not informed of the true position, namely that the Continuous Service Benefits were being provided notwithstanding the fact that the transfer payments had not been agreed and paid to the Scheme. Mr Herbert explained that he decided not to follow Ms Miller's advice and not to send the letter she had drafted notifying the members of the lack of the transfer payment on the basis that it would cause confusion and uncertainty. The Targets' response to that point is that the earlier communications had made it clear that benefits were conditional on a transfer actually taking place so that in fact no unqualified promise had been made to employees.

531. As we have found, it was clear that the provision of defined benefits was a matter of considerable importance to the employees, including the provision of Continuous Service Benefits. Mr Herbert had to make a judgment as to whether any doubt should be raised as to that expectation and so, in good faith, he decided to ensure that the members' reasonable expectations were satisfied and that informing them at that stage that there were still difficulties with the transfer payments, may have created

unnecessary concerns. In addition, at that stage, all parties believed that the bulk transfer would be agreed and it was clear that both Shareholders wanted the transfer payments to go ahead with the effect that the historic liabilities of the Legacy Schemes in relation to the employees of the Joint Venture would be transferred. It was clearly therefore in everybody's interests on the basis of the information available to them at that stage that the transfer payments proceeded.

532. In any event, although there is no evidence of any formal approval on the part of the Shareholders to the opening of the Scheme on the basis that Continuous Service Benefits would be provided, it is clear that representatives of the Shareholders were fully involved in the discussions that led up to the opening of the Scheme and in our view it must be inferred that at the very least they knew that it was to be opened on that basis. We see no reason why they should have not agreed to that decision being taken, bearing in mind that it was clear that they wished the transfer payments to be made. A further example of the Shareholders' involvement is an email that Mr Herbert sent to a number of Box Clever executives, including Mr Neal, on 30 September 2001, shortly before the decision was taken to open the Scheme where Mr Herbert refers to Mr Cooklin having agreed to discuss " the Granada problem" (that is the outstanding issues regarding the transfer) with his "Granada colleagues" and that Mr Cooklin would propose that a meeting was set up with the "key players of both Box Clever and Granada with their advisers to resolve the outstanding issues at the earliest opportunity this week". This is consistent with our earlier findings that the Shareholders were involved in approving all key decisions made in relation to the Joint Venture.

533. Furthermore, the Shareholders participated through their representatives on the BxC Tech Board in the decision to execute the Interim Trust Deed.

534. We therefore have concluded that although this decision to open the Scheme on a Continuous Service Benefits basis before the transfers took effect was a risk and may have led to further decisions which increased the current deficit in the Scheme, they were decisions that were taken with the full knowledge and approval of the Targets, they were decisions that were reasonable at the time and which potentially benefited the Targets by smoothing employee relations, making it more likely that the Joint Venture would move forward successfully. We do not therefore place any material weight on this factor as pointing against the issue of an FSD.

The Top Up Arrangement

535. The Targets contend that the rejection of the transfer payments left the Trustee and the Joint Venture's executive management in a very difficult position, given what the members had been told in October 2001 and the "fingers crossed" basis on which the Scheme had been administered. They argue that the Top Up Arrangements have increased the deficit suffered by the Scheme. They submit that they should not be regarded as responsible in any way for the additional problems encountered by the Scheme arising from the Top Up Arrangement for the following reasons:

(1) It was a matter of choice for the Joint Venture's executive management and the Trustee as to whether to introduce the Top Up Arrangement there being no legal obligation for it to do so.

(2) The Top Up Arrangement was an unusually onerous benefit structure which imposed a significant funding risk on the Scheme. Careful legal and actuarial advice should have been taken so that different options could be considered. For example, it would have been possible to proceed with the "future service only" DB scheme, or offer backdated membership of the DC section. Nevertheless, the Trustee and the Joint Venture's management adopted the assumption that the Top Up Arrangement needed to be introduced.

(3) The Joint Venture's management and the Trustee chose to introduce the arrangement knowing that the Shareholders would not provide financial support to the Scheme and believing that the Joint Venture could not offer a strong financial covenant without obtaining adequate costings or other appropriate advice. The Trustee took the Joint Venture's actuary's advice that the proposal was estimated to cost £5 million, which was not given on a discontinuance basis and no advice was taken on the impact of the arrangement if the Scheme entered winding up. The Trustee did not give any thought to the longer-term possibility of higher salary increases, and simply proceeded on the basis that the Joint Venture's salary increase policy would not change.

536. In our view, it would have been very difficult for the Scheme not to have granted Continuous Service Benefits given the fact that the Explanatory Literature stated that such benefits would be available if a member transferred his or her past service to the Scheme. Members had been told that they could transfer their benefits if they elected to do so, without any suggestion that the transfer of legacy benefits might not be possible. We accept Mr Herbert's evidence that it was important to ensure good employee relations and good relations with the Trade Union that the benefits would be identical to those in the Granada Scheme. In that regard, it was an important feature that members were told that the link to final salary would remain and in October 2001 Aon had told members that their pensionable service was being treated as continuous. We accept that the Trustee found itself in a difficult position following the decision not to proceed with the transfer payments but they made a reasonable judgment in conjunction with the executive management of the Joint Venture.

537. Neither do we accept that the Trustee should have taken any more advice than it did as to the course of action that it should adopt. The £5 million estimate given by the Scheme's actuary as to the cost of the arrangement was agreed by Mr Bowie and Mr Salter, the actuarial experts who gave evidence in these proceedings, as being a reasonable estimate for the cost of the Top Up arrangement in 2002 and early 2003, based on the assumed salary increase assumption of 0.4% per annum above inflation. The experts also agreed that the actual salary increases granted in 2001 and 2002 did not materially affect that estimate. On the basis of what the experts said in their respective reports, estimated discontinuance costs would not have made a material difference to the estimate.

538. In cross examination, Mr Bowie, the Targets' expert, ultimately accepted that the question whether further costings and advice were required was simply a matter of what the Trustee's duties were in the particular circumstances, and there was no mandatory requirement in this respect. There is no suggestion that the Trustee was in breach of its fiduciary duties in any respect.

539. As regards the question as to whether the estimate should have taken into account actual salary increases, Mr Salter's view was that it was sufficient for the Trustee to rely upon the assumed salary increases, given that levels of pay were within the control of the Joint Venture. In the light of Mr Bowie's acceptance that this was a relevant factor, we accept Mr Salter's evidence on this point. The Targets' observation that the Top Up Arrangement made the liabilities of the Scheme highly sensitive to salary increases must be read in the context of the fact that pay rises had a gearing effect on benefits by the salary link to the past service benefits left behind in the Legacy Schemes, with the result that a large part of the Scheme's present deficit is attributable to this final salary link.

540. In the light of the real difficulties that the Joint Venture would have faced had it not agreed to proceed with the Top Up Arrangement we agree with the Trustee's assessment that the estimated cost was modest. The experts also agreed that the £5 million cost was considerably less than the immediate deficit of £16 million that would have arisen upon acceptance of the bulk transfer, that the sensitivity of cost to actual salary increases granted was no worse, in absolute terms, under the Top Up Arrangement than if the bulk transfer had been accepted and if the bulk transfer had been accepted the Scheme would have been exposed to much greater risk because of the size of the assets and liabilities taken on.

541. It is also clear that the Trustee gave conscientious attention to the detail of the Top Up Arrangement and how it would work. Ms Peggs, the Scheme Actuary, attended the relevant Trustee Board meetings and provided detailed written advice as to the costs. The Scheme's legal adviser also raised the question of cost at the board meeting held on 14 January 2003.

542. In any event, in our view the evidence shows that the Shareholders were fully aware of the Top Up Arrangement and approved it, albeit informally. In this respect, we rely on the findings we made at [343] and [344] as to the general manner in which the Shareholders were involved in major decisions concerning the Joint Venture as well as our detailed findings at [462] to [473] as to the degree of influence and control that the Shareholders exerted over the Joint Venture. Although, as the Targets submitted, there were fewer references in the Shareholder review documents to matters concerning pensions, there is clear evidence that in fact the Shareholders were involved in the decisions relating to pensions matters following the establishment of the Scheme. This was to be expected, bearing in mind the importance of pensions matters to the Joint Venture generally.

543. More specifically in relation to the Top Up Arrangement, Mr Wakelam's evidence on this was clear. As we have previously stated, we accept his evidence that important decisions would not have proceeded without the Shareholders' approval. In

relation to the Top Up Arrangement, Mr Wakelam's evidence, which we also accept, was that Messrs Mavity, Neal, and Cooklin, in their capacity as directors of BxC Tech would not have agreed to such a decision without Shareholder approval. Thus, when, as we found at [389] above, the Joint Venture approved the Top Up Arrangement at the meeting held in London on 28 November 2002, in our view this would have followed the Shareholders having approved that course of action. This is supported by Mr Herbert's letter of 18 November 2002 to Mr Mavity, also referred to at [389] above, where Mr Herbert clearly envisaged that Mr Mavity would seek the views of the Shareholders on the proposed arrangement, and Mr Herbert confirmed his understanding to that effect in his oral evidence which we accept.

544. Furthermore, Mr Parrott and Ms Scott, were both involved in the drafting of communications regarding the Arrangement. The Targets submit that Mr Parrott was acting in his capacity as chairman of the Granada Scheme. However, he was also Granada's Commercial Director, and clearly if in that capacity he had any misgivings about the Arrangement that would have become apparent. Mr Herbert's letter of 18 November 2002, makes it clear that he expected that Mr Parrott would be involved wearing his Shareholder hat in considering the Top Up Arrangement.

545. Finally, when the Top Up Arrangement was formally incorporated into the Interim Trust Deed by the execution of a supplemental deed on 23 December 2003, it had previously been approved at the meeting of the BxC Tech Board held on 22 December 2003 which was attended by Mr Parrott and Mr Tibbitts (as alternate to Mr Allen), as representatives of Granada, pursuant to the terms of the Shareholders Agreement.

546. In view of these findings, we have come to the same conclusion as we came to as regards the decision to open the Scheme on the basis of Continuous Service Benefits. Once it became clear that the transfers from the Legacy Schemes were not going ahead, the Top Up Arrangements was a reasonable course for the parties to adopt. The Top Up Arrangement was adopted with the full knowledge and approval of the Targets, it was a decision that was reasonable at the time and again it potentially benefited the Targets by smoothing employee relations, making it more likely that the Joint Venture would move forward successfully. We do not accept that the existence of the Top Up Arrangements is a factor which materially points away from the appropriateness of issuing an FSD against the Targets.

The decision to delay closing the Scheme to new accruals

547. The appointment of the Administrative Receivers on 24 September 2003 clearly changed the nature of the relationship between the Shareholders and the Scheme, as it did with the Joint Venture. All of the activities of the operating companies of the Joint Venture were being undertaken now for the benefit of the secured creditors regardless of the interests of the Box Clever group or the Shareholders. Therefore, as the Targets observed, they ceased to have any influence over the running of the operating companies or any decisions taken in that regard that may have had an effect on the liabilities arising in the Scheme.

548. Therefore, as a result of employees' continuing pensionable service and, as we shall see, receiving pay rises, liabilities continued to accrue in the Scheme after 24 September 2003. It was the Administrative Receivers who had the power to determine whether those additional liabilities continued because it was their choice as to whether to continue the employment of the employees and grant pay rises. The additional liabilities which accrued from 24 September 2003 to 31 December 2003, when the Scheme was closed to new accruals, have been calculated by the Scheme's actuary as being 15% of the Scheme's total liabilities, or 20% of the deficit. The effect of these factors combined has been to increase the deficit as at 8 January 2016 by £15 million.

549. The Targets accordingly say that they cannot reasonably be regarded as being responsible for funding any Scheme liabilities accrued on or after 24 September 2003. Furthermore, the Targets criticise the Trustee for not taking the initiative in ensuring that the accrual of benefits under the Scheme ceased promptly after the Administrative Receivers were appointed. They contend that the Trustee and its advisers should have recognised that it was imperative that the accrual of benefits under the Scheme should cease promptly, bearing in mind that it was likely that any contributions paid into the Scheme would be insufficient to cover the true cost of accruing liabilities on a discontinuance basis which would mean that the solvency deficit would worsen. The Trustee is also criticised for not being alert to the fact that if the Receivers granted pay rises (the usual salary review date being first October each year) these problems would be exacerbated, particularly if the pay rises were large given the gearing effect of the Top Up Arrangement.

550. The Targets contend that closing the Scheme to accrual required an amendment to the Scheme, which could only be effected by the "joint action" of BxC Tech, as Principal Employer, and the Trustee. They contend that only the Trustee had a fiduciary duty to act in the members' interest, and it ought to have recognised that it was imperative to take action quickly to prevent the harm to members outlined above. They contend that the Trustee should have brought these considerations home to BxC Tech and pressed for the Scheme to be closed as quickly as possible, but it failed to do so.

551. We reject these criticisms of the Trustee for the following reasons.

552. First, the Targets misrepresent the position regarding responsibility for taking the decision to close the Scheme. Under the Interim Trust Deed, this was a decision that had to be taken by the Principal Employer, namely BxC Tech, acting with the consent of the Trustee. That clearly suggests that responsibility for taking the initiative rested primarily with BxC Tech. That was a decision it could take notwithstanding the appointment of the Administrative Receivers because BxC Tech was never in receivership. The Trustee, rightly in our view, took the position that it had no objection to closing the Scheme should BxC Tech decide to do so. The evidence from the minutes of a Board meeting of BxC Tech held on 7 October 2003, attended by the Shareholders' representatives, indicates that initially BxC Tech wished that contributions be continued to be paid into the Scheme and the possibility of the banks being asked to inject money into the Scheme instead should be looked into. BxC Tech was reminded on 19 November 2003 that the decision to close the Scheme was one for BxC Tech, in

response to an indication from BxC Tech that it would be supportive of any decisions made by the Administrative Receivers and the Trustee.

553. Secondly, in our view the Trustee cannot be criticised for any delay that is perceived to have arisen in not agreeing to the Scheme being closed earlier. As mentioned above, BxC Tech wished that the Scheme remain open whilst the question of whether there would be any support from the banks was explored. It was not unreasonable of the Trustee to take the course it did on 3 October 2003 of writing to Mr Hands and Mr Allen to see if Shareholder support would be forthcoming as described at [403] above. The fact that the Shareholders had previously indicated that they would not provide financial support to the Scheme did not mean that it was not reasonable for the Trustee to explore the position again in the light of the appointment of the Administrative Receivers and, as we have seen, in fact Granada did engage in negotiations that could have led to the Scheme being given financial support. When, as described at [407] above, on 21 November 2003 the Administrative Receivers requested that BxC Tech give consideration to closing or winding up the Scheme (and it is notable that the letter was addressed to BxC Tech) the Trustee, who was copied on the correspondence, responded promptly.

554. Thirdly, the grant of the large pay rises by the Receivers was a business judgment that they had to make in the context of needing to retain key staff and thereby give the business the best prospects of surviving. Whilst Mr Herbert accepted that it might have been possible to prevent such pay rises being pensionable, in the absence of a decision to close the Scheme, that could only be achieved by seeking agreement from individual members to enter into non-pensionability agreements, which was impracticable in the circumstances. Neither, as the Trustee submitted, was it the Trustee's role to intervene in the contractual relationship between employers and employees and they were not consulted by the Administrative Receivers about them.

555. We accept that if the evidence demonstrated that a very large part of a Scheme's deficit could be attributed to the conduct of a scheme's trustee or employers which occurred after the potential targets had ceased to have any effective control over the employer's business then that would be a strong factor against the issue of an FSD. However, in this case only a part of the current deficit in the Scheme can be attributed to events which took place between the appointment of the Administrative Receivers and the time when the Scheme was closed to new accruals. In those circumstances, the question of what account should be taken of the increase in the deficit attributable to this period should be left to be determined as a part of the process for determining the level of financial support to be provided, in the event that an FSD is directed to be issued. We therefore place only limited weight on this factor in our assessment.

The decision not to wind up the Scheme

556. The observations that we made at [547] above regarding the lack of influence of the Targets over the running of the Joint Venture's business after the appointment of the Administrative Receivers are equally applicable in relation to this issue. The Targets contend that they cannot reasonably be made responsible for funding any of the Scheme liabilities accrued after that appointment and, which in relation to this issue, they

contend have arisen as a result of the Trustee's decision not to have triggered a winding up of the Scheme many years ago.

557. In particular, the Targets point out:

(1) The Scheme's buyout deficit has grown very substantially as a result of the Scheme having continued since 2003 and the security of members' benefits as well as the position of the PPF have also been prejudiced.

(2) The decision to continue the Scheme was made by the Trustee for strategic reasons, namely to give members access to PPF compensation and therefore brings the present case within the Regulator's moral hazard powers.

(3) The reasons offered by the Trustee for continuing the Scheme are inadequate. The desire to continue negotiations with the Shareholders and to bring the Scheme within the scope of the moral hazard provisions of the legislation were not precluded by commencing the winding up of the Scheme. The desire to bring the Scheme within the scope of the PPF could at most only justify continuing the Scheme until 6 April 2005.

(4) The desire to bring the Scheme within the scope of the PPF was not a legitimate reason to continue the Scheme. *Independent Trustee Services v Hope* [2010] EWHC 2810 (Ch) ("*Hope*") is authority for the proposition that availability of PPF compensation is a legally impermissible consideration for the trustee of an occupational pension scheme to take into account when making decisions about the future of a scheme.

(5) One of the purposes of the moral hazard legislation was to prevent the decisions of those involved in running pension schemes from being distorted by the potential availability of PPF compensation and such distortion has occurred in the present case, because had it not been for the existence of the PPF, the Scheme would have been wound up shortly after 2003 when the deficit was much smaller.

558. It is important to keep the effect of running the Scheme on after 31 December 2003 in perspective. The Joint Statement of the actuarial experts shows that the cost of funding members' benefits in full would have been £19 million less as at 8 January 2016 (out of a total deficit as at that date of £95 million) if the Scheme had been wound up on 31 December 2003. The comments we made at [555] above are therefore equally applicable in relation to this issue, and even when these effects are taken together with the effects of not closing the Scheme to future accruals before 31 December 2003, in our view the total amounts concerned are not so substantial that we should conclude that this issue amounts to a strong factor against the issue of an FSD. For that reason, we have not found it necessary to deal with the detailed factual and actuarial evidence on this issue.

559. Furthermore, we do not accept that the fact that the Scheme was not wound up earlier indicates that the Targets should not bear responsibility for the insufficient funding of the Scheme deficit for the following reasons. First, in our view, the objectives that the Trustee was seeking to achieve through further negotiations with the Shareholders may have been frustrated had the Scheme commenced winding up. The

Trustee was seeking to obtain agreement that the members of the Scheme be transferred back into the Legacy Schemes but, as the Trustee submitted, s 135 PA 2004 provides that such a transfer would be void after the PPF assessment period commenced unless validated pursuant to s 136 by the PPF, and there could be no certainty that such a transfer would be validated. Those negotiations went on over a long period of time, but they appeared to be bearing fruit through the various stages through which they went, such that in our view it was reasonable for the Trustee to allow them to take their course. Mr Herbert accepted that the strategy of negotiation carried risks for the Scheme if they were ultimately unsuccessful, but the Trustee successfully persuaded ITV to make a series of offers up until November 2007. From December 2007 until October 2009, the Trustee accepted (in principle) a series of decreasing offers from ITV. In our view, it was reasonable to continue to run the Scheme on in circumstances where it might reasonably have been thought that a final settlement was imminent. Once ITV withdrew all further offers in October 2009, the prospect of FSD proceedings had become realistic, and it was not unreasonable for the Trustee to have believed that that process might have led to further settlement offers, or if it had not, that the regulatory process might result in the issue of an FSD. As regards the prospect of the issue of an FSD, although the issue of an FSD is not precluded in respect of a Scheme for which the PPF has assumed responsibility, s 47 (5) PA 2004 precludes the issue of a contribution notice where the terms of any financial support have not been agreed following the issue of an FSD in respect of a scheme for which the PPF has assumed responsibility.

560. Secondly, we do not accept that the Trustee's reliance on the PPF as a backstop if negotiations failed, or if there was no prospect of an issue of an FSD, was impermissible in the circumstances.

561. It is helpful at this point to refer to the conditions for the entry of a scheme into the PPF, by reference to the relevant parts of the summary in that respect contained at [42] to [46] of *Hope* as follows:

> "42. The key provision is section 127, which imposes three principal conditions for entry of a scheme into the PPF:
>
> (a) the scheme must be an "eligible scheme";
>
> (b) the sponsoring employer must have suffered a "qualifying insolvency event"; and
>
> (c) the value of the scheme's assets, immediately before the qualifying insolvency event occurs, must be less than the amount of its protected liabilities (i.e. the amount it would cost to secure benefits at the PPF level).
>
> 43. If those three conditions are satisfied, the Board must then "assume responsibility" for the scheme. The consequences (see section 161) are that:

> (a) the assets and liabilities of the scheme are automatically transferred to the Board;
>
> (b) the trustees of the scheme are discharged from their obligations; and
>
> (c) the Board becomes liable to pay "pension compensation" (i.e. benefits at the PPF level) to members of the scheme.
>
> 44. The qualifying insolvency event marks the beginning of an "assessment period" (section 132) which is the period during which the funding level of the scheme is assessed to determine whether the Board must assume responsibility for it. This is achieved by means of a valuation under section 143. If the valuation discloses sufficient assets to meet the protected liabilities, the scheme does not go into the PPF but must be wound up by the trustees: section 154. If the assets are insufficient, the Board assumes responsibility by giving a "transfer notice" to the trustees which triggers the consequences set out in section 161: see section 160.
>
> 45. Whether or not a scheme is "eligible" is governed by section 126 and the Pension Protection Fund (Entry Rules) Regulations 2005, SI 2005/590. In essence, all occupational pension schemes (other than those which provide exclusively money purchase benefits) are eligible unless:
>
> (a) they went into winding up before 6 April 2005; or
>
> (b) they are in one of the various categories of scheme excluded by regulation 2 of the Entry Rules Regulations.
>
> …
>
> 46. A "qualifying insolvency event" occurs in relation to an employer if it is the first "insolvency event" to occur in relation to that employer after 6 April 2005: see section 127(3). The definition of "insolvency event" is broad (section 121) and covers bankruptcy and individual voluntary arrangements in relation to individuals and compulsory or voluntary liquidation (other than a members' voluntary liquidation), company voluntary arrangements, administration orders and the appointment of administrative receivers for companies."

562. In this case, the Scheme has been accepted as being an "eligible" scheme. The appointment of the Administrative Receivers in respect of the Employers was an "insolvency event" but it was not a "qualifying insolvency event" because it did not occur after 6 April 2005. The "qualifying insolvency event" in this case was when one of the Employers, UKCE, was put into liquidation (at the instigation of the Trustee) on 10 November 2014.

563. In summary, the prescribed level of PPF benefits (set out in Schedule 7 to PA 2004) provides by way of compensation to pensioners already receiving a pension

100% of their basic scheme entitlement. Deferred members are not entitled to compensation until they reach normal pension age when they will be entitled to receive 90% of their basic scheme entitlement, subject to a cap of a prescribed amount.

564. In *Hope*, the sponsoring employer of the Scheme was insolvent and the trustee was proposing:

(1) to use the assets of the scheme to buy out the benefits of higher earning employees (who would otherwise have been subject to a cap on the level of their pensions pursuant to the provisions governing the operation of the PPF) and that part of the benefits of certain other members that the PPF does not provide by way of compensation; and

(2) to take advantage of the compensation available to the other members of the Scheme through the PPF by winding up the scheme and placing it in the PPF without its assets. The proposal was therefore intended to exploit the availability of PPF compensation by intentionally minimising the scheme assets which would otherwise vest in the PPF and using assets that could and should have been put towards providing PPF compensation to instead providing those benefits that exceeded PPF compensation limits.

565. Henderson J observed at [115] of his judgment that these proposals sought to subvert the legislative policy that lay behind the establishment of the PPF. He concluded at [154] that if the proposal before him was lawful, schemes which sought to take advantage of the PPF would rapidly proliferate, citing the parallel of the tax avoidance industry. He therefore found that taking the availability of PPF compensation into account in the circumstances before him would be impermissible.

566. However, Henderson J did explain that in some cases it would be permissible for trustees to take into account the availability of PPF compensation in their decision-making. He said this at [106]:

> "Mr Giffin QC [counsel for the PPF]…prefaced his oral submissions on the point, however, by stressing that his argument was not that it can never be appropriate for trustees to have regard to the existence of the PPF. He accepted, for example, that it might be perfectly proper for trustees to have regard to the PPF in deciding whether, or when, to bring about a qualifying insolvency event, as part of the planning for an orderly running down of an under-funded scheme. Similarly, it would plainly be relevant for trustees to consider whether an action they were otherwise minded to take might render the scheme ineligible for entry into the PPF… Mr Giffin submitted, and I would agree, that there is no single all-purpose answer to the question whether the PPF is a relevant consideration for trustees to take into account. It all depends on the context and purpose of the particular power which the trustees are proposing to exercise, and the particular way in which they wish to take the PPF into account."

567. At [119], having held that taking into account the availability of compensation under the PPF would be unlawful in the circumstances of the case before him, he went on to say:

> "Further than that I would not, at present, go, bearing in mind that the existence of the PPF is in certain contexts a legitimate matter for trustees to take into account, and the dangers of invoking public policy in relation to a situation which is not before the court. I would, however, say that if my conclusion in the present case is soundly based, I would expect a similar approach to be adopted in any instance where trustees seek to take advantage of the existence of the PPF as a justification for acting in a way which would otherwise be improper."

568. It is quite clear to us, therefore, that Henderson J was not seeking to lay down any general principle as to when it was legitimate for a trustee to take into account the availability of the PPF. The question has to be considered on a case-by-case basis. We accept the Trustee's submissions that the circumstances in this case are quite different, and rather than having the objective of ensuring that the PPF would be available to provide compensation, its primary aim was to avoid that event occurring through its negotiations with the Shareholders or, if those failed, the regulatory process leading to the issue of an FSD. The fact that the Trustee knew that the PPF would be available were neither of those objectives realised, does not in our view make the Trustee's strategy impermissible in the way that it was found to be in *Hope.* We accept that the Trustee was not seeking to justify by reference to the PPF a course of conduct that would otherwise have been improper. It was seeking to preserve the possibility of continuing negotiations with the Targets and to preserve the possibility of an FSD (and ultimately a contribution notice) if a compromise could not be reached, fully aware of the risks if either of those outcomes was not achieved.

569. Furthermore, Henderson J expressly accepted at [106] of Hope, that having regard to the PPF in deciding whether to bring about a qualifying insolvency event and taking into account whether an action would render a scheme ineligible for the PPF was perfectly reasonable. We also accept the Trustee's submission that its actions were perfectly consistent with the PPF's statutory purpose of providing a safety-net for underfunded schemes. There is nothing in s 126 PA 2004 which suggests that taking the conditions for the scheme to be aN "eligible scheme" into account would be contrary to the policy of the legislation.

570. There is no suggestion in this case that either the Regulator, whose objectives include protection of the PPF, or the PPF itself has any objection to the way in which the Trustee has acted. The PPF has delayed the completion of the assessment period pending the resolution of these proceedings.

571. Therefore, in those circumstances, we do not think that the postponement of a decision on whether to wind up the Scheme (which decision, as we have accepted, was kept under constant review) significantly shifts responsibility for the deficit from the Targets to the Trustee. The question of what account should be taken as regards the increase in the deficit attributable to this period should be left to be determined as a part of the process for determining the level of financial support to be provided, in the event that an FSD is directed to be issued.

Other factors relating to reasonableness

The interim participation period

572. We found at [349] above that the shortfall in the sufficiency of the contributions paid by the Joint Venture to the Granada Scheme during the interim participation period provided for under the Contribution Agreement to meet the true cost of the benefits earned by the participating employees during that period amounted to some £25 million.

573. The Targets submit that the shortfall amounts to financial support to the Scheme, which otherwise would have had to bear these costs. They submit that this contribution, which was not made to the Scheme directly, but to the benefits of the Joint Venture's employees while they were working for the Joint Venture, should be recognised and put into the scales on reasonableness, and should be compared with the likely amount of deficit which the Targets could be ordered to pay if an FSD were issued.

574. Put in this way, the argument is clearly one that can only be relevant to the question of quantum, were an FSD to be issued. In any event, the burden of a deficit in the Granada Scheme cannot be equated to financial support to the Scheme. We therefore place no weight on this factor in our assessment.

The Carmelite point and other issues relating to Thorn

575. In dealing with the Carmelite point in the context of jurisdiction, we concluded that there was sufficient objective justification for the difference in treatment between ITV and Carmelite. In those circumstances, it cannot be said that it would be unreasonable to issue an FSD to the Targets in the absence of an FSD being issued to Carmelite.

576. However, as we observed at [264] above, the question as to whether it would be reasonable to pursue the Targets for the whole of the deficit in the Scheme is a matter to be considered in the context of the discussions on quantum which will take place if an FSD is issued. We have therefore not placed any weight on this factor in deciding whether it is reasonable to issue an FSD.

577. In our view, the same reasoning applies in relation to the position of TUK. The Targets submit that it would not be reasonable to impose liability on them in respect of pension liabilities of that entity. TUK is a Thorn entity, and its pension liabilities relate exclusively to ex-Thorn employees. Granada has received no benefit from this company because none of the purchase price payable by the Joint Venture was attributable to that entity, and it received no dividends from the Joint Venture or from its employees. Again, we conclude that this is a matter to be considered in the context of the discussions to be held regarding quantum, and we have not placed any weight on this factor in deciding whether to issue an FSD.

The technical nature of the connection between the Targets and the Employers

578. We have dealt with this issue fully in our discussion of the relationship between the Targets and the Employers, and in particular our findings that the historic

relationship was a strong factor that was not diminished by the fact that Granada's effective influence over the business of the joint Venture ended with the appointment of the Administrative Receivers: see in particular [483] to [489] above.

Retrospectivity and moral hazard

579. As we have observed at [433] above, we have regarded the key question to be addressed in our assessment of reasonableness as being whether the structure created by the Shareholders left the Joint Venture vulnerable to adverse movements in the market so that Granada should bear some responsibility for the risks which eventuated for the Employers and the Scheme, notwithstanding the absence of any blame to be attributed to the Targets in that regard. As a consequence, we concluded at [435] that the absence of moral hazard should be regarded as a neutral factor in our consideration of reasonableness.

580. However, we accept that because, as we have found, the legislation is capable of imposing new financial obligations by reference to transactions that have been entered into before the legislation came into force, the question as to whether taking account of all the circumstances it is reasonable to direct such an imposition is a highly relevant factor to be taken into account in our assessment of reasonableness. As we observed at [16] above, account must be taken of the interests of the Targets as well as those of the members of the Scheme and the Trustee.

581. As we observed at [207] above, the application of new legislation to existing circumstances does involve a degree of retrospectivity which may create a degree of unfairness or hardship. We should consider whether in the circumstances of this case that degree of unfairness or hardship is so significant that we should conclude that it would not be reasonable to direct the issue of an FSD to the Targets.

582. As Lord Pannick powerfully submitted, Granada arranged their affairs in 1999 to 2000 by entering into a particular transaction by which they disposed of the rental business for which they received a sum of money which they then applied in the course of their business. The Regulator is now seeking to upset those plans as to the sale and the proceeds of sale by imposing a liability that did not exist in 1999 to 2000. Although Lord Pannick had submitted that the basis of the Regulator's case for the issue of an FSD is based on criticisms of the transaction, we seek to make no criticism of the choice that the Targets made in how they wished to structure the transaction.

583. As we have found, the transaction did create risks for which the Targets are responsible because of the manner in which the Joint Venture was structured. At the time of the transaction, however, there was no basis on which the Targets could have foreseen that many years later they may be called upon to support the liabilities of the Scheme and the whole basis of the structure that the Shareholders created was that both the Joint Venture and the Scheme were to be non-recourse to the Shareholders.

584. Furthermore, as we have observed at [228] above, there was no opportunity for the Targets to seek clearance as to the transactions and thereby identify the potential consequences and decide whether or not to proceed in the light of the answers they

received from the Regulator. There is clearly a disadvantage to those who entered into transactions prior to the coming into force of PA 2004 relative to those who entered into transactions once the legislation came into force. However, we decided at [229] above, that the degree of hardship created was a very qualified kind of hardship.

5 585. We therefore conclude that the fact that the Targets could not have known at the time of the transaction that further liabilities were liable to be imposed as a result of it and that they had no opportunity to seek clearance in relation to the transaction are significant factors tending against the issue of an FSD in this case.

Conclusion on the Reasonableness Issue

10 586. We can summarise our conclusions on the various factors that we have taken into account in our assessment of the Reasonableness Issue as follows:

(1) The circumstances relating to the relationship which the Targets had with the Employers point very strongly in favour of the issue of an FSD: see [492] to [494] above. By their choice of structure for the Joint Venture, the Shareholders
15 extracted considerable cash from the business with no risk of recourse to their assets. They retained an ongoing interest in the merged business with the possibility of further value being generated if the business was successful, but without having to bear any responsibility if the business, whose strategy they continued to determine, subsequently failed.

20 (2) These findings are reinforced by our conclusions on the benefits issue: see [518] above.

(3) The Targets had a strong connection and involvement with the Scheme up to the point at which the Administrative Receivers were appointed, a factor which is not diminished significantly by the fact that the practical connection with the
25 Scheme ceased once the Administrative Receivers were appointed or by the actions that the Trustee took after that time.

(4) We place some weight on the other factors identified by the Targets, the most significant being the issue of retrospectivity.

587. The Targets' case is, as they say, straightforward. The Joint Venture was a bona
30 fide transaction undertaken in the belief that the new venture would benefit from synergies and deliver considerable further value in the future to the Shareholders. That belief was not an idle hope but was supported by the considerable success both Shareholders had had in acquiring declining businesses in the past. The structure adopted was a logical one, and the price paid was an appropriate one. The due diligence
35 which was undertaken by the Shareholders for their own benefit was considerable, appropriate in the circumstances, and involved appropriate consideration of the risks of the transaction. The Tribunal must guard against being illegitimately influenced by hindsight. Questions of judgment of risk must be assessed by reference to what was actually known at the time. Furthermore, at the time of the transaction the Targets had
40 no reason to believe that further liabilities would be imposed and there was no basis on which they could have obtained clearance for the transaction.

588. As we have said, we do not take issue with the commercial merits of the transaction or the manner in which it was structured. However, taking those factors together which we say point strongly in favour of the issue of an FSD, our conclusion is that the key issue of responsibility for the risks to the Scheme that the Shareholders agreed to create as a defined benefit scheme because it was in both the Joint Venture's and their own interests to do so, and the substantial benefits received, all through a structure that the Shareholders created and which meant that the Scheme had a weak employer's covenant, clearly outweigh on the facts of this case the strong points that the Targets make on retrospectivity.

589. We therefore conclude that it is reasonable in this case for the Regulator to issue an FSD to the Targets.

IX . CONCLUSION AND DIRECTIONS

590. We have had the benefit of excellent written and oral submissions from no fewer than seven leading counsel, supported by their juniors. The fact that we have not referred to all of the submissions that they have made does not mean that they have not all been carefully considered and appreciated. We are grateful to all counsel, and their legal teams, for their assistance.

591. The references are dismissed. Our decision is unanimous.

592. Section 43(3)(a) PA 2004 requires an FSD to specify the period within which financial support for the Scheme is to be put in place. We heard no submissions on the period that should be specified and accordingly we propose to specify a period of 6 months, the same period as was specified by the DP in its determination. Accordingly, in accordance with the relevant provisions of s 103 PA 2004:

(1) We determine that the appropriate action for the Regulator to take in relation to the matters referred to us on these references is to issue an FSD to each of the Targets such direction to specify that financial support for the Scheme is put in place within six months of its issue;

(2) We therefore confirm the Regulator's determination to that effect; and

(3) We remit the references to the Regulator with a direction that effect be given to our determination.

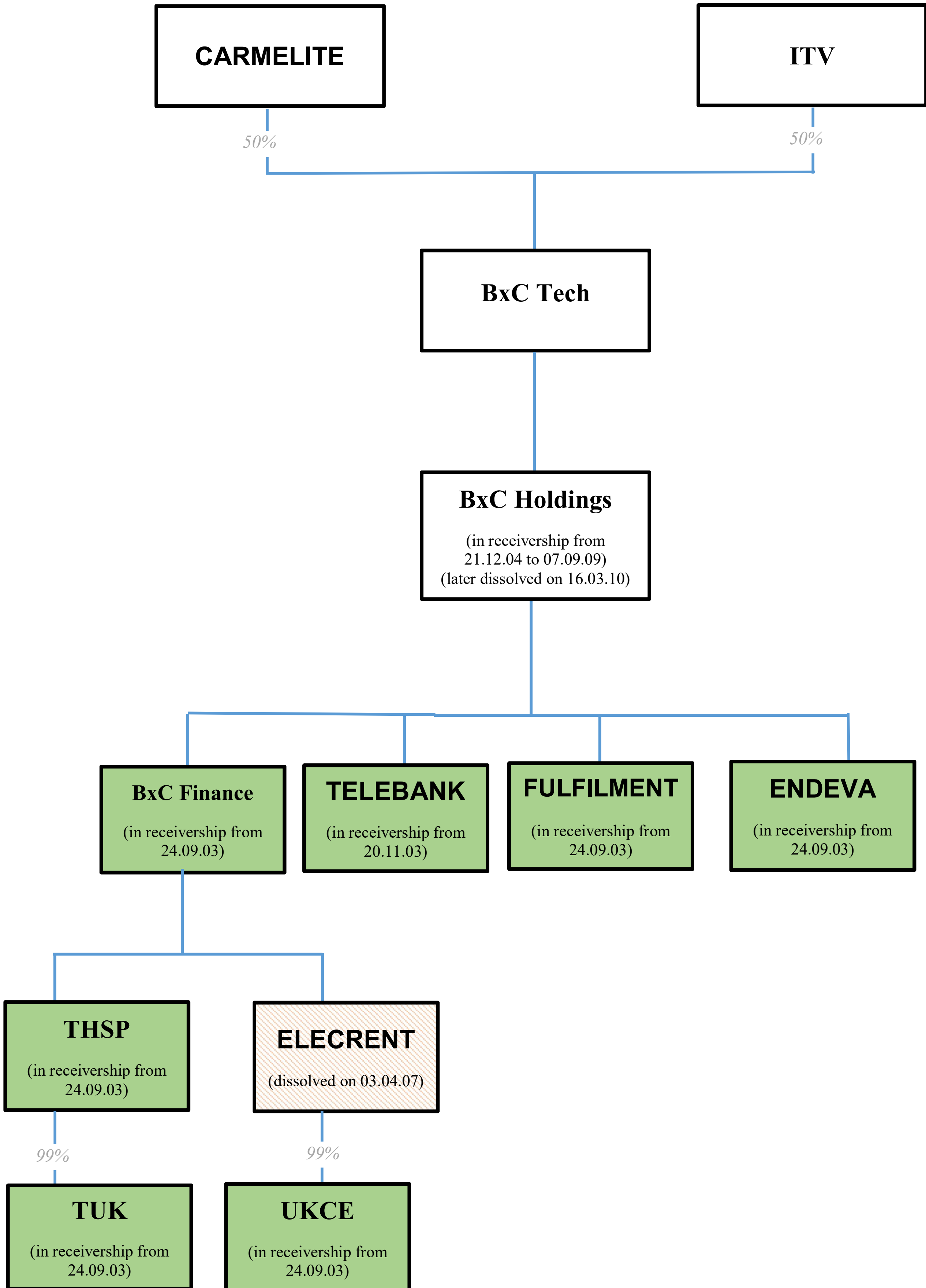
Post Script

After we had sent a draft of this judgment to the parties and received back their comments, the Supreme Court handed down its ruling in *Gallaher Group Ltd v Competition and Markets Authority* [2018] UKSC 25. The Supreme Court allowed the CMA's appeal against the decision of the Court of Appeal discussed at paragraphs 265 onwards above. Since we had in any event decided to distinguish the present case from the facts of *Gallaher* that Supreme Court ruling cannot affect our decision.

MRS JUSTICE ROSE **JUDGE TIMOTHY HERRINGTON**

UPPER TRIBUNAL JUDGES

5 **RELEASE DATE: 18 May 2018**


CARMELITE
ITV
50%
50%
BxC Tech
BxC Holdings
(in receivership from 21.12.04 to 07.09.09)
(later dissolved on 16.03.10)
BxC Finance
(in receivership from 24.09.03)
TELEBANK
(in receivership from 20.11.03)
FULFILMENT
(in receivership from 24.09.03)
ENDEVA
(in receivership from 24.09.03)
THSP
(in receivership from 24.09.03)
ELECRENT
(dissolved on 03.04.07)
99%
99%
TUK
(in receivership from 24.09.03)
UKCE
(in receivership from 24.09.03)