Michaelmas Term

[2018] UKSC 55

On appeal from: [2016] EWCA Civ 1064

JUDGMENT

Barnardo's (Appellant) vBuckinghamshire and others (Respondents)

before

Lady Hale, President

Lord Wilson

Lord Sumption

Lord Hodge

Lord Briggs

JUDGMENT GIVEN ON

7 November 2018

Heard on 11 June 2018

Appellant	Respondents (1-7)
Brian Green QC	Nicolas Stallworthy QC
Emily Campbell	
(Instructed by Eversheds Sutherland (International) LLP)	(Instructed by Stephenson Harwood LLP)

Respondents
and 9th
Andrew Simm
QC
Fraser Cam
(Instructed
Dentons UK
Middle East
(London

Respondents:

Trustees of the Barnardo Staff Pension Scheme –

1. Miles Buckinghamshire

2. Neil Braithwaite
3. Alexis Cleveland
4. Elaine Diver
5. Lesley Lee
6. Hugh Mackintosh
7. Christopher Close (following the retirement of John Bartlett)

Representative Members of the scheme –

8. Janet Forrest
9. Malcolm Dick

LORD HODGE: (with whom Lady Hale, Lord Wilson, Lord Sumption and Lord Briggs agree)

1.
This appeal raises a question of interpretation of a clause in a pension scheme trust deed which defines the phrase "Retail Prices Index" and which allows the trustees of the pension scheme to adopt a "replacement" of the officially published Retail Prices Index ("the RPI").

2.
The background is the recognised need for private pension schemes to provide some form of indexation of pensions to protect the value of members' pensions against price inflation. As discussed below, the question is whether the clause allows the pension scheme trustees to adopt an index of price inflation, such as the Consumer Prices Index ("the CPI"), when the official body responsible for compiling the RPI (now the Office of National Statistics) has not discontinued the RPI, thereby requiring its replacement.

3.
Barnardo's, the well-known charity who is the sponsoring employer, argues that the clause empowers the trustees to adopt another index which they consider a suitable measure of price inflation, whether or not the RPI continues to be published. Barnardo's see the CPI as a more appropriate measure of inflation which will also enable a reduction of the scheme's deficit. Representatives of the members of the scheme, who are concerned that the adoption of the CPI as the index would over time reduce the benefits which they receive from the scheme, argue that the clause does not empower the trustees to depart from the RPI for the purposes of indexation if the RPI continues to be published. The trustees adopt a neutral stance on the question.

The Barnardo Staff Pension Scheme

4.
In 1984 Barnardo's adopted a staff pension scheme which took effect from 1978. In 1991 Barnardo's adopted a new pension scheme which took effect from 1 April 1988 and completely superseded the 1978 scheme. The 1988 rules have subsequently been amended and adopted with effect from 2001, 2004 and 2007. But the relevant provisions of the current rules are in substance the same as those in the 1988 rules, to which counsel referred in their submissions. I therefore set out the relevant provisions from the 1988 rules.

5.

Rule 7 of the scheme gave members a pension of 1/60th of their final pensionable earnings for each complete year of pensionable service. Rule 30 provided for pensions in the course of payment to be increased "by the prescribed rate". Rule 30.1.3 provided:

"For the purpose of this rule 30 'the prescribed rate' means an increase at the rate of the lesser of:-

(a) 5%, and

(b) the percentage rise in the Retail Prices Index (if any) over the year ending on the previous 31 December."

6.
Rule 53, which contains a definition of "Retail Prices Index" lies at the heart of the dispute. An important part of the argument concerns the relationship between the first and second sentences of the definition. In order to assist comprehension I present the definition in a disaggregated manner, adding "(i)" and "(ii)" before each sentence, although the text of the definition is simply an undifferentiated paragraph, and highlighting in italics the critical part of the definition. The rule 53 definition ("the Definition") is as follows:

"'Retail Prices Index' (i) means the General Index of Retail Prices published by the Department of Employment or any replacement adopted by the Trustees without prejudicing Approval.

(ii) Where an amount is to be increased 'in line with the Retail Prices Index' over a period, the increase as a percentage of the original amount will be equal to the percentage increase between the figures in the Retail Prices Index published immediately prior to dates when the period began and ended, with an appropriate restatement of the later figure if the Retail Prices Index has been replaced or re-based during the period."

7.
The Appendix to the Rules of the 1988 rules contains a summary of the rules by which the Commissioners of Inland Revenue ("the CIR") then imposed limits on the benefits which a private pension scheme could confer if it were to obtain the approval to which I refer in para 8 below. The basic limit for a pension of a member who retired at or before the normal retirement date was 1/60th of the final remuneration for each year of service. In several places in the Appendix the text referred to the indexation of benefits "in line with RPI". Thus, for example, in para 6 it was stated that the maximum pension may be increased whilst in payment at 3% per year compound or (if greater) in line with RPI. In para 10 the Appendix defined the phrase in these terms:

"'in line with RPI' over a period means in proportion to increases between figures in the General Index of Retail Prices published by the Department of Employment (or a replacement of that Index not prejudicing Approval), immediately prior to the dates when the period began and ended with appropriate restatement of the later figure if the Index has been replaced or re-based during the period."

8.
The reference to "Approval" in the Rules and in the Appendix was a reference to the discretionary approval of the scheme by the CIR as an exempt approved scheme under Chapter 1 of Part XIV of the Income and Corporation Taxes Act 1988. The definitions of "Tax Approval" in the Rules and of "Approval" in the Appendix were to this effect.

9.

Lewison LJ in the Court of Appeal (para 6) neatly summarised the principal question in the appeal in this way:

"The critical words in the definition of the RPI are 'or any replacement adopted by the Trustees without prejudicing Approval.' Does the definition mean:

(i) the RPI or any index that replaces the RPI and is adopted by the trustees; or

(ii) the RPI or any index that is adopted by the trustees as a replacement for the RPI?"

10.
The first meaning involves a two-stage process by which the RPI is replaced by an official body responsible for its publication and the trustees then adopt the replacement or one of several indices produced as replacements. The second meaning, which Barnardo's advances, involves a single step and would allow the trustees to choose another index as a replacement of the RPI, whether or not the RPI continued to be published.

The decisions of the courts and the appellant's challenge

11.
The trustees of the pension scheme sought a ruling on the meaning of the Definition by a claim under Part 8 of the Civil Procedure Rules. In a judgment ([2015] EWHC 2200 (Ch); [2015] Pens LR 501) Warren J held that, on a proper construction, the Definition did not empower the trustees to adopt an index other than the RPI unless the RPI had been discontinued as an officially published index and replaced. The Court of Appeal by majority (Lewison and McFarlane LJJ, Vos LJ dissenting) dismissed Barnardo's appeal. Barnardo's sought permission to appeal. This court gave permission to appeal on the understanding that there might be clauses in many pension schemes which contained similar wording. But it is not clear whether that is so.

12.
Mr Brian Green QC presented the case on behalf of Barnardo's. I mean no disrespect to his elegant submissions if I summarise them briefly. First, he explained that the scheme had been subject to the CIR's discretionary approval. He referred to the CIR guidance known as IR 12 (1979) which set out the limits on the benefits which the CIR allowed. The arrangement for CIR approval was superseded by the Finance Act 2004 but the requirement for that approval explained the repeated reference in the scheme, including in the definition of RPI in rule 53, to "Approval". Mr Green submitted that the first sentence of the Definition fell to be construed as "RPI or any alternative adopted by the trustees". The phrase, he submitted, contained pointers which supported his interpretation. It was not disputed that the trustees had to exercise discretion in deciding to adopt a replacement. There might be no room for the exercise of discretion if the official body which published the RPI replaced it with another index. Similarly, the requirement that the adopted replacement did not prejudice CIR approval pointed to a circumstance where there was a possibility that the trustees' choice of replacement might not receive CIR approval. That eventuality was very unlikely if the clause operated only when the RPI was replaced by another official index. He also submitted that it was inherently improbable in 1991 that the Government would discontinue the RPI. While recognising that the second sentence of the Definition also referred to "replaced", he submitted that that sentence was of no relevance to a proper understanding of the first sentence as it referred to the phrase, "in line with the Retail Prices Index", which did not appear in the Rules but only in the Appendix. "Replacement" in sentence 1 did not necessarily have the same meaning as "replaced" in sentence 2.

Discussion

The construction of pension schemes

13.
In the trilogy of cases, Rainy Sky SA v Kookmin Bank [2011] 1 WLR 2900, Arnold v Britton[2015] AC 1619 and Wood v Capita Insurance Services Ltd[2017] AC 1173, this court has given guidance on the general approach to the construction of contracts and other instruments, drawing on modern case law of the House of Lords since Prenn v Simmonds[1971] 1 WLR 1381. That guidance, which the parties did not contest in this appeal, does not need to be repeated. In deciding which interpretative tools will best assist in ascertaining the meaning of an instrument, and the weight to be given to each of the relevant interpretative tools, the court must have regard to the nature and circumstances of the particular instrument.

14.
A pension scheme, such as the one in issue on this appeal, has several distinctive characteristics which are relevant to the court's selection of the appropriate interpretative tools. First, it is a formal legal document which has been prepared by skilled and specialist legal draftsmen. Secondly, unlike many commercial contracts, it is not the product of commercial negotiation between parties who may have conflicting interests and who may conclude their agreement under considerable pressure of time, leaving loose ends to be sorted out in future. Thirdly, it is an instrument which is designed to operate in the long term, defining people's rights long after the economic and other circumstances, which existed at the time when it was signed, may have ceased to exist. Fourthly, the scheme confers important rights on parties, the members of the pension scheme, who were not parties to the instrument and who may have joined the scheme many years after it was initiated. Fifthly, members of a pension scheme may not have easy access to expert legal advice or be able readily to ascertain the circumstances which existed when the scheme was established.

15.
Judges have recognised that these characteristics make it appropriate for the court to give weight to textual analysis, by concentrating on the words which the draftsman has chosen to use and by attaching less weight to the background factual matrix than might be appropriate in certain commercial contracts: Spooner v British Telecommunications plc [2000] Pens LR 65, Jonathan Parker J at paras 75-76; BESTrustees v Stuart [2001] Pens LR 283, Neuberger J at para 33; Safeway Ltd v Newton [2018] Pens LR 2, Lord Briggs, giving the judgment of the Court of Appeal, at paras 21-23. In Safeway,Lord Briggs stated (para 22):

"the Deed exists primarily for the benefit of non-parties, that is the employees upon whom pension rights are conferred whether as members or potential members of the Scheme, and upon members of their families (for example in the event of their death). It is therefore a context which is inherently antipathetic to the recognition, by way of departure from plain language, of some common understanding between the principal employer and the trustee, or common dictionary which they may have employed, or even some widespread practice within the pension industry which might illuminate, or give some strained meaning to, the words used."

I agree with that approach. In this context I do not think that the court is assisted by assertions as to whether or not the pensions industry in 1991 could have foreseen or did foresee the criticisms of the suitability of the RPI, which later emerged in the public domain, or then thought that it was or was not likely that the RPI would be superseded.

16.
The emphasis on textual analysis as an interpretative tool does not derogate from the need both to avoid undue technicality and to have regard to the practical consequences of any construction. Such an analysis does not involve literalism but includes a purposive construction when that is appropriate. As Millett J stated in In re Courage Group's Pension Schemes [1987] 1 WLR 495, 505 there are no special rules of construction applicable to a pension scheme but "its provisions should wherever possible be construed to give reasonable and practical effect to the scheme". Instead, the focus on textual analysis operates as a constraint on the contribution which background factual circumstances, which existed at the time when the scheme was entered into but which would not readily be accessible to its members as time passed, can make to the construction of the scheme.

17.
It is nevertheless relevant to the construction of pension schemes that they are drafted to comply with tax rules so as to preserve the considerable benefits which the United Kingdom's tax regime confers on such schemes. They must be construed "against their fiscal backgrounds": National Grid Co plc v Mayes [2001] 1 WLR 864, para 18 per Lord Hoffmann; British Airways Pension Trustees Ltd v British Airways Plc [2002] Pens LR 247, Arden LJ at para 30. In this case, the CIR guidance on approval of schemes, which is contained in the practice note on occupational pension schemes (IR 12 (1979)), forms part of the relevant background. In the footnote to para 6.14 of that guidance, the CIR stated:

"Increases in the cost of living may be measured by the index of retail prices published by the Department of Employment or by any other suitable index agreed for the particular scheme by the Superannuation Funds Office."

It appears therefore that the CIR, in giving discretionary approval to a scheme, would not have objected to a scheme which empowered its trustees to substitute an appropriate index for the RPI. This is relevant background as it means that there was no CIR constraint which might influence the construction of the words in dispute. This contrasts with the National Grid case in which the fiscal background was directly relevant to the interpretation of a phrase in the scheme. The tax regime did not allow an employer to be paid part of a surplus of scheme funds, which had already received tax exemptions when payments were made into the scheme. But the tax regime did not prohibit the release of a debt due by the employer to the scheme which had not had those tax advantages. This assisted the House of Lords to construe narrowly a provision in the scheme which prohibited the making of scheme moneys payable to the employers. In the present case, as Lewison LJ stated at para 32 of his judgment, the draftsman of the scheme did not track the wording of the Revenue guidance in the Definition but chose different language. The scheme could have empowered the trustees to select an index as an alternative to the RPI. The question is whether it did so.

18.
Finally, a focus on textual analysis in the context of the deed containing the scheme must not prevent the court from being alive to the possibility that the draftsman has made a mistake in the use of language or grammar which can be corrected by construction, as occurred in Chartbrook Ltd v Persimmon Homes Ltd [2009] AC 1101, where the court can clearly identify both the mistake and the nature of the correction.

The construction of the Definition

19.
I am persuaded that the judge and the majority of the Court of Appeal were right to conclude that the correct interpretation of the first sentence of the Definition is the first of the options to which Lewison

LJ referred and which I have repeated in para 9 above, namely, that “the RPI” means “the RPI or any index that replaces the RPI and is adopted by the trustees”. I reach this view for the following eight reasons.

20.
First, the draftsman has chosen to use the word “replacement” which does not naturally suggest the selection of an alternative to an option which remains available. It is, nonetheless, capable of bearing that meaning and one must look to the context for guidance.

21.
Secondly, the word order and grammatical construction of the phrase “a replacement adopted by the trustees” suggest that the RPI must first be replaced and that the trustees adopt the replacement. The word order suggests a sequence of events rather than the single event of an index being adopted by the trustees as a replacement.

22.
Thirdly, the existence of a discretion on the part of the trustees and the requirement that the adoption should not prejudice the CIR’s approval do not militate against this view. In paras 15-20 of his judgment Lewison LJ usefully sets out the history of official cost of living indices in the United Kingdom which he derived from a report, “UK Consumer Price Statistics: A Review”, by Mr Paul Johnson, the Director of the Institute for Fiscal Studies, which was prepared for the UK Statistics Authority in 2015. There is no benefit in repeating that account in this judgment. It suffices to say that there were several additional official price indices in 1991 when the 1988 rules were prepared, namely the state pensioner indices introduced in 1969, the Tax and Prices Index introduced in 1979 and the Rossi Index, which was introduced in 1981 and was used to uprate income-related state benefits. In 1981 the UK started to issue index-linked gilts, using the RPI. A cautious draftsman may well have chosen to provide for the eventuality of the RPI being replaced by more than one official index. As a result the trustees would be required to exercise discretion in the selection of the appropriate replacement and the CIR themselves would have an interest in making sure that the chosen index was suitable when considering whether to approve the scheme.

23.
Fourthly, it is trite both that a provision in a pension scheme or other formal document should be considered in the context of the document as a whole and that one would in principle expect words and phrases to be used consistently in a carefully drafted document, absent a reason for giving them different meanings. In the second sentence of the Definition the draftsman has defined the phrase “in line with the Retail Prices Index”. That sentence speaks of the RPI having been “replaced or re-based”. The re-basing of the RPI involves the resetting of the starting point for measuring changes in prices to 100. The authority responsible for publication of the RPI has re-based the index from time to time. It is not suggested that anyone other than the official body responsible for the index could re-base it. Other things being equal, I would expect that the draftsman of the phrase “replaced or re-based” envisaged the same official body either replacing or re-basing the index. This is supported by the definition of the same phrase (albeit referring to “RPI” rather than “Retail Prices Index”) in the Appendix, which I have set out in para 7 above. It is clear that the definition in the Appendix is referring to the replacement or re-basing of the RPI by an official body responsible for the production of that index. In the late 1980s the Central Statistical Office (“CSO”) took responsibility for the RPI and the CSO became part of the Office for National Statistics in 1996. Consistency within the scheme as a whole, and indeed within the Definition itself would suggest that it is that official body and not the trustees who are to effect the replacement in the first sentence of the Definition.

24.
Mr Green submitted that the court in construing the first sentence of the Definition should not attach any significant weight to the second sentence because it was defining an expression used only in the Appendix and it duplicated the definition in the Appendix in any event. I do not agree. Clause 3 of the Deed containing the rules of the scheme stated that “the Scheme will be governed by the Rules (including the Appendix) contained in this deed”, thereby clarifying that the Appendix was to be seen as part of the rules. Further, rule 32, which prohibited the payment of benefits in excess of the CIR limits, referred to the Appendix as containing a summary of those limits. The rules and the Appendix are intimately related. While it is true that there was no need to include the second sentence of the Definition because of the definition of the same term in para 10 of the Appendix, its inclusion cannot be viewed as a mistake. The second sentence forms part of the Definition and cannot be airbrushed out of it simply because there has been duplication. Thus in construing the scheme as a whole the court must have regard to the use of the words “replacement” and “replaced or re-based” in the same definitional rule and also the use of the latter words in the parallel definition in para 10 of the Appendix.

25.
Fifthly, I do not derive any assistance from the CIR guidance in IR 12, because (as I have discussed in para 17 above) the draftsman has not chosen to use wording similar to that guidance in the Definition. If there were any inconsistency between the terms of IR 12 on the one hand and the rules and Appendix of the Scheme on the other, the latter must prevail. It may be that the draftsman thought that IR 12 was addressing the initial choice of index when a scheme was first established rather than an alteration of an index during the currency of the scheme. But whether or not that is a correct inference, it cannot be doubted that he or she chose to use language in both the Definition and the Appendix which differed from IR 12.

26.
Sixthly, I do not derive any real assistance from the superseded 1978 scheme, in which the term “Index” was defined in the introductory interpretation clause as:

“the Government’s Index of Retail Prices or any other official cost of living index published by authority in place of or in substitution for that Index.”

This definition can provide little assistance because the 1988 rules involved a wholesale re-drafting of the earlier rules in which the draftsman may or may not have had regard to the wording of the earlier rules, with the result that there is no basis for assuming that the draftsman’s use of different words points to an intention to achieve a different meaning. In any event, I agree with Lewison LJ in para 23 of his judgment that the nature of a pension scheme, which may have members who have no knowledge of the prior rules, makes it unprofitable to delve into the archaeology of the rules in this case.

27.
Seventhly, a provision which provided for the circumstance of the official replacement of a cost of living index does not lack a rational purpose. The United Kingdom Government had changed its official index in 1946 and again in 1956 and, as I have said, had published additional indices by 1991 when the 1988 rules were drafted. Whether or not it was likely that the Government might dispense with and replace the RPI, a cautious draftsman of a long-term contract or trust such as the scheme might well provide for such an eventuality. Commercial common sense therefore does not point against the interpretation to which a primarily textual analysis of the words points. While, since 1991,

the RPI has fallen from favour as an appropriate measure of the cost of living, it is not appropriate to use hindsight of such post-execution events to assess whether a provision makes good commercial sense.

28.
Eighthly, while the requirement of indexation by reference to the RPI imposes obligations on Barnardo's and contributes to the pension deficit at a time when many see the CPI as a more reliable index for the cost of living, the court must construe the scheme without any preconceptions as to whether a construction should favour the sponsoring employer or the members: British Airways Pension Trustees (above), Arden LJ at para 31. The sponsoring employer's gain may be the members' loss and vice versa.

29.
Finally, I must address an argument which Vos LJ favoured and which contributed to the reasoning in his dissent. That argument is that the provision would be inconveniently inflexible if the trustees were not able to switch to another index in the eventuality that the RPI ceased to be a suitable index for measuring the cost of living for pensioners but was not abolished because it was retained in existence for other purposes. The proviso to rule 46 of the scheme prevents Barnardo's from altering the scheme to the prejudice of any pension or annuity then payable under the scheme or any benefit already secured. Thus, it was argued, common sense required the trustees to be vested with a power to change the index if the RPI ceased properly to reflect inflation in the cost of living. But, while it may have been desirable to have that flexibility, the draftsman appears to have put his or her faith in the suitability of the officially-produced index and not to have foreseen the circumstances in which the RPI ceased to be seen as an appropriate index for the cost of living. Only by relying on hindsight can weight be given to this consideration; and that is not legitimate.

30.
For these reasons, which are essentially the same as those which Lewison LJ gave in his impressive judgment, the appeal must fail. As a result, it is not necessary to address the cross-appeal on the subsisting rights provisions contained in sections 67 and 67A-67I of the Pensions Act 1995.

Conclusion

31.
I would dismiss the appeal.