

Trustee Focus

Newsletter for pension trustees

Legislation in force

The last six months has seen the advent of A-day, but it must not be forgotten that parts of the Pensions Act 2004 have also come into force during this time. Here we highlight some areas that trustees should have considered.

Internal Controls Regime

From 6 April 2006, occupational pension schemes had to comply with new internal controls requirements under the Pensions Act 2004, which promote good trustee governance. The draft code of practice published by the Pensions Regulator provides trustees with guidance on their duty to establish and operate adequate internal controls. These controls must be sufficient to ensure that the scheme is administered and managed in accordance with the scheme rules and the relevant legislation. The draft code provides practical guidelines on developing a risk management framework, helping trustees to focus on the key risks to their schemes. The Pensions Regulator can impose penalties for non-compliance.

Internal Dispute Procedure

Under Section 273 Pensions Act 2004, there was a proposal to introduce a new simplified one-stage internal dispute procedure on 6 April 2006. However, following comments received as a result of consultation, the Department for Work and Pensions now believes that the proposed change would not have the desired effect of simplifying procedures or introducing greater flexibility. Consequently it has decided not to bring in the new legislation.

Life Assurance Only Schemes

The Department for Work and Pensions recently confirmed that Section 255 of the Pensions Act 2004 prohibits occupational

pension schemes from providing life assurance only benefits unless an employee is either in a waiting period to join a scheme, has opted not to join the scheme, or a link can be established with e.g. a personal pension or stakeholder scheme. Breach of this section could result in an imposition of a fine on trustees.

Member-Nominated Trustees

The provisions set out in sections 241 to 243 of the Pensions Act 2004, which provide that arrangements must be put in place to ensure that at least one-third of trustees are nominated and selected by members, came into force on 6 April 2006. However, for schemes currently operating a member-nominated trustee/director "opt-out" under the previous provisions of the Pensions Act 1995, the new requirements will not apply until the earlier of the expiry of the existing opt-out or 31 October 2007. From 2009, the Department for Work and Pensions proposes that schemes will have to have 50% member-nominated trustees/directors. Processes should have been developed in order to meet this requirement by the proposed deadlines.

Modification of accrued pension rights and consultation on future amendments

From 6 April 2006, trustees of most occupational pension schemes will need to check whether any proposed modification to benefits that have accrued is a 'regulated modification' and, if it is, decide whether to go down the member consent or actuarial equivalence route. Modifications to members' future service rights will be subject to the employer consultation requirements set out in sections 259 to 261 of the Pensions Act 2004. Trustees are required to inform employers of any proposed 'listed change' (e.g. increasing normal pension age, closing scheme to new members, changing a defined

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benefit scheme to a defined contribution scheme etc.) so that the employer may comply with this duty to consult. Implementation of consultation requirements is staggered; they affect employers with 150+ employees from 6 April 2006, employers with 100+ employees from 6 April 2007 and employers with more than 50 members from 6 April 2008. The Pensions Regulator will have power to impose civil penalties where procedures are not followed.

Scheme Funding

The new scheme funding requirements came into force with effect from 30 December 2005. These will apply retrospectively to any scheme valuation with an effective date on or after 23 September 2005 and signed after 30 December 2005. They require trustees to produce a variety of documents, examples of which have been published on the Pensions Regulator web site. Charlie Massey, strategic development director at the Pensions Regulator, stresses that 'it is important that trustees understand their obligations – they will need to make key funding decisions negotiating with the employer to reach agreement, as well as obtaining and questioning professional advice'.

Trustee Knowledge & Understanding

The Pensions Act 2004 sets out the basics of the requirement for Trustee Knowledge and Understanding (TKU). The Code of Practice published by the Pensions Regulator provides further information on how trustees are required to be conversant with their own scheme documents, and to have knowledge and understanding (appropriate to their role as trustee) of trusts and pensions law and of the principles of funding and investment. Whilst the Code is not a legally enforceable document, the Pensions Regulator, the Pensions Ombudsman or a Court would take compliance with the TKU Code into account when considering whether the TKU requirement has been met (for example, in the context of a maladministration claim). TKU came into force from 6 April 2006, and gives Trustees appointed on or after that date up to 6 months to complete the required

learning. Existing trustees (other than professional trustees) have until 6 October 2006 to comply. The Pensions Regulator has launched its Trustee Toolkit, an e-learning programme, to assist in this.

Impending Legislation

Whilst the majority of announced legislation has already been introduced, the following section focuses on legislation that is due to come in over the next 6 months.

Age Discrimination

Subject to parliamentary approval, the employment equality (age) regulations will come into force on 1 October 2006. The regulations extend to trustees of occupational pension schemes and an overriding non-discrimination rule is to apply to every scheme. The regulations provide exemptions for many pension scheme practices, but where scheme rules fall outside of these exemptions, employers and trustees must rely on objective justification or the length of service exemption. Failure to do so could result in a case being brought against the trustees or employer for unlawful conduct.

Winding Up Procedure Regulations

The Government has issued draft Regulations on winding-up procedures, (The Occupational Pensions Schemes (Winding Up Procedure) Regulations 2006), for consultation. The Regulations apply to an occupational pension scheme that is required to have a recovery plan in place under the new statutory funding regime and which enters into wind-up during the recovery period. It contains a requirement for trustees of such schemes to put in place, review and implement a winding up procedure, which includes establishing scheme liabilities, recovering any assets, indicating the extent of any benefit reductions, how liabilities will be discharged and the timeframes for doing so. The Pensions Regulator will have the power to impose civil penalties where trustees have failed to take reasonable steps to comply with these requirements.

Cross Border Schemes - Changes Announced

The Pensions Regulator has recently issued revised guidance on the cross border scheme requirements, which expands the categories of member who could make the scheme a cross border scheme. Glyn Ryland of Wragge & Co recently confirmed that it is crucial that employers and trustees ascertain whether or not their scheme would qualify under these new guidelines, and if so what action to take, as soon as possible due to the requirement to fully fund these types of schemes on the scheme funding basis.

Disclosure Regulations - Delayed

Amendments to the main set of disclosure regulations that will, in conjunction with a code of practice, replace the statutory timing requirements with 'reasonable periods' for the provision of information to occupational pension scheme members, are now not due to take effect until October 2006.

Litigation

'Cautionary Tail'

Julian Aylmer of Reynolds Porter Chamberlain recently reported that 'a claim against a trustee for breach of duty in the course of his trusteeship will be a claim for breach of trust that, in certain circumstances may not become time-barred for decades if not centuries'. Furthermore, trustees seeking contribution from the other professionals involved, such as the pension administrators, auditors or actuaries, will be faced with different limitation periods applying for breach of contract or tort, which could expire before the claim is brought against the trustees, leaving trustees to face the music alone.

Pensions Ombudsman Determinations

a) Incorrect Retirement Quotation

During his term of employment, Mr M was temporarily appointed to a higher post following the incumbent being posted elsewhere for a period of 16 months. During this period Mr M received a higher salary commensurate with this post. One year

after he had returned to his original post, Mr M requested and received early retirement quotations from his employer. He retired some three months later at age 60 to take advantage of the enhanced pension that he was informed he would receive following his tenure in the acting post. However, one month after his early retirement he discovered that the quotation on which he had based his decision was incorrect. The pension Mr M actually received was £20,334 per annum as opposed to the sum of £22,914.95 originally quoted. Mr M brought his complaint to the Pensions Ombudsman on the basis that his employer provided an incorrect estimate of early retirement benefits on which he then relied to his financial detriment. The Pensions Ombudsman determined that the employer was accountable and the complaint of maladministration was upheld. He further determined that had it not been for the incorrect estimate, Mr M would have continued in his position of employment until he was 65. Consequently, the Pensions Ombudsman directed the employer to either: a) purchase an annuity to provide Mr M with an income of £2,580 per annum with 3% escalation and 50% spouse's benefits; or b) arrange for the occupational pension scheme to increase Mr M's pension by £2,580 per annum with effect from the date of his retirement (in order for this to be cost neutral to the scheme the employer would be required to pay a lump sum to the fund to cover the cost of this enhancement).

b) Transfer Payment Delay

Mrs G was a member of her employer's pension scheme. Upon taking up new employment, Mrs G became a member of her new employer's scheme and requested a transfer of her previously accrued pension benefits to the new pension scheme. The time between the receiving scheme first making contact with the previous employer and the transfer actually taking place was approximately 1 year and 7 months. Mrs G alleged that due to the delay by her previous employer, her transfer value purchased less service in the scheme to which she

Whilst the focus of these pension ombudsman cases is on the size of settlements, the extra cost of investigating and defending the action must not be forgotten. Pension trustee liability insurance could help

transferred than would otherwise have been the case. The Pensions Ombudsman determined that the delays did constitute maladministration and so upheld the complaint. He directed that the previous employer was to pay the receiving scheme the sum of £12,200 to purchase a further service credit that would place Mrs G in the position she would have been had the previous employer dealt with the matter properly.

c) Wind-Up Issue

Mr H was the only active member of a final pension scheme at the time when the administrators of the scheme wrote to the trustees and suggested that the trustees should consider an alternative pension arrangement for Mr H and wind up the scheme. Just under one year later, the administrators wrote to a firm of financial advisers about the benefits available to Mr H from the scheme. The letter suggested there may be a surplus of assets in the scheme and that the trustees could either enhance the benefits to Mr H or take a refund of the sum, less tax. It was made clear that the latter option would require Inland Revenue approval but this should not be problematic 'provided that we can demonstrate to the Revenue that the scheme liabilities have been met by way of a non-profit buy-out'. After three months, a sum of £49,308.36 (which included the £6,000 surplus) was transferred to a personal pension. Mr H asserts that this transfer was undertaken without his full consent as he was not advised of the alternative options available to him and that the assets would have been sufficient to secure his entitlement under a non-profit deferred annuity. The Pensions Ombudsman determined that by failing to draw the alternatives to Mr H's attention the employer and trustees were guilty of maladministration. As a result, he directed the trustees to pay Mr H: a) a sum of £16,135 plus interest for past payments;

b) purchase an annuity policy to provide a future pension of £6,925 per annum together with 3% increases and 50% spouse's benefit; and c) a sum of £350 to redress Mr H for the considerable financial hardship and inconvenience suffered as a result of the maladministration.

d) Delay in Annuity Purchase

Ms J was originally a member of the employer's final salary pension scheme until she transferred to their money purchase arrangement invested with Insurance Company A and B. Ms J asserts that she made it known to the trustees that she wished to take her benefits at age 60, however annuities were not purchased from the Insurance Companies until some 4 and 5 months after her normal retirement date, respectively. She also claimed that the trustees were in breach of the disclosure regulations, as she was not advised of her retirement benefits until 8 days before her normal retirement date. The Pensions Ombudsman found that the trustees were not guilty of breaching disclosure regulations. However, despite the fact that there was a history of lost correspondence from both parties, given that the trustees purchased the annuities with payment backdated to the normal retirement date indicated that the trustees were trying to make amends for the delay in setting up the pension. Consequently the Pensions Ombudsman ordered the Trustees to pay Ms J £3,260 in recognition that she is receiving less in the way of pension than she might otherwise have done if the avoidable delays had not occurred.

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CONTACT US
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