

The Pensions Bill (HL): Pension Fund Regulation

[Bill 87 of 1994/95]

Research Paper 95/46

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The Pensions Bill (HL) [Bill 87 1994/95] was published on 21 March 1995 after completing its first stages in the Lords. The Bill sets up for the first time a statutory framework for regulating occupational pension schemes. It also provides for the equalisation of the state pensionable age for men and women, and applies certain judgments of the European Court of Justice on equal treatment.

The Bill is covered by three Library Research Papers. This paper (which updates RP 95/10) focuses on the administration and investment of occupational pension schemes, including trustee board composition, funding and the new regulator. Research Paper 95/47, Social Security Aspects, covers changes to the state pension scheme, including pensions for war widows. Research Paper 95/48, Non-state benefits, deals with the Bill's effect on non-state pension benefits, including pensions and divorce and equal treatment.

Christopher Blair
Business & Transport Section
House of Commons Library

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I Introduction

The Pensions Bill, which was published on 15 December 1994 following its first reading in the House of Lords, sets up for the first time a statutory framework for the regulation of occupational pension schemes. At the moment such schemes operate under a complex web of trust law, social security legislation and rules determined by the Inland Revenue. As well as legislating for the occupational pension sector, the Bill also provides for the equalisation of the state pensionable age for men and women, starting from 2010, and applies certain judgments of the European Court of Justice which require that men and women are treated equally by occupational schemes.

During its passage through the Lords the Bill was amended substantially. Although many amendments were of a technical nature, important changes to the way pensions are handled in matrimonial cases, and to the rights of recipients of the war widow's pension were made. The extensive regulation-making powers of the Bill were also criticised, both by the Lords chamber and by the Delegated Powers Scrutiny Committee. Amendments were passed which require the Government to consult appropriate organisations before making regulations under the Act, and the power to create by order criminal offences for breaches of Part I of the Bill was made subject to the affirmative procedure.¹

This paper is limited to the administration and investment of occupational pension schemes. It describes the main events in that field which have led up to the Pensions Bill, and examines a number of the major issues in greater detail. There is also a partial Bill summary and a bibliography of the main documents which have preceded this Bill. Two further Research Papers, produced by the Education and Social Services Section of the Library, treat other aspects of this Bill: The Pensions Bill: Social Security Aspects (Paper 95/47) covers state-pensions and especially the changes needed to equalise the pensionable age; the war widow's pension is also discussed. The Pensions Bill: Non-state Benefits (Paper 95/48) deals with questions on the pension benefits derived from occupational pension schemes and the relationship of an occupational scheme to the state earnings related pension scheme (SERPS). Pensions and divorce fall within the scope of that paper also. Note further that on 24 April the Social Security Committee is publishing extracts from memoranda which it has received on the Bill: this paper is available from the Vote Office as HC 336.

In 1991, according to Government estimates, some 10.7 million employees were active members of occupational pension schemes in the United Kingdom. It is estimated that there are nearly 150,000 different schemes in operation. Although the majority of these schemes by number are private sector schemes, the public sector schemes accounted for more than 4 million active members alone. Most of the schemes are governed by trust law: they are run by trustees who administer the scheme in accordance with powers set out in the trust deed

¹See clauses 108(1) and 156(2)(c)

and the scheme rules. Much of this paper, and the Bill to which it relates, is devoted to these trust schemes, but some of the Bill's provisions also apply to public sector schemes.

There are two main types of occupational scheme: defined benefit or earnings-related schemes, and defined contribution or money purchase schemes. In an **earnings-related** scheme, the pension which will be paid on retirement depends upon the salary which the individual attains before retirement. The length of the individual's pensionable service may also affect the pension. Contributions towards the scheme may be made by the employer only (non-contributory) or by both the employer and the employee. Although a rate will be set at which contributions need to be made, the value of the pension is determined not by the investment performance of the pension fund, but by the individual's salary and employment record. In earnings-related schemes it is ultimately up to the employer to fund the pension properly, since the employer is liable if the fund is not sufficient to pay the promised benefits. Many of the provisions of the Pensions Bill are specifically aimed at controlling this type of scheme, since although they potentially offer a very good pension for their members, their nature makes them vulnerable to abuse or bad management.

The other primary type of occupational scheme is a **money purchase** or defined contribution scheme. As the name suggests, the contributors - the employer and/ or the employee - pay in contributions at a set rate. The value of the final pension is not related to salary or length of service. Instead it depends on the investment performance of the assets in the fund. The employer takes on no risk in such a scheme - since there is no pension promise to meet beyond the accrued value of the individual's contributions. The would-be pensioner assumes the investment risks of his pension, but benefits in theory at least from professional management at low cost. Regulations on fund management, trustee responsibilities and scheme information all apply to this type of scheme, but rules which are connected with a salary-related promise - like the minimum solvency proposal - do not.

In addition there are a number of schemes which combine features of both types of scheme. These are known as **hybrid schemes**, and depending on how they are constituted may be closer to one or other of the main types.

Although all are discussed in greater detail in the pages which follow, it is worth drawing attention to the three main sources used in this paper.

- The Goode Report.² Following the Maxwell affair and a number of other high profile failures in occupational pension schemes, the Pension Law Review Committee was set up in June 1992 by the Secretary of State for Social Security, the Rt Hon. Peter Lilley, to conduct a thorough investigation of the law relating to occupational pensions. The committee's chairman was Professor Roy Goode. Their report, *Pension Law Reform: The report of the Pension Law Review Committee*, forms the groundwork for and much of the substance of this Bill. It is usually referred to as the Goode Report.

²*Pension Law Reform: The report of the Pension Law Review Committee*, 2 vols (HMSO, September 1993) [Goode]

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- The Social Security Committee.³ Although the present Committee and its predecessor have produced a number of influential reports, this paper relies mainly on their response to the Goode Report: *The Report of the Pension Law Review Committee (The Goode Report)*, Fourth Report from the Social Security Committee.
- The White Paper.⁴ The Government published its proposals for pension reform, drawing on the Goode Report where appropriate, in June 1994. The White Paper is in two volumes: the second contains a point by point comparison of Goode's recommendations with the Government's proposals.

Pension law and administration has its own lengthy vocabulary which can be offputting to those who are not familiar with the terms. Although this paper tries to explain any jargon, readers may find the glossary which is appended to volume one of the Goode Report, and that in volume one of the White Paper, useful points of reference.

³*The Report of the Pension Law Review Committee (The Goode Report)*, Fourth Report from the Social Security Committee, Session 1993-94, 25 May 1994, HC 436 [Social Security Committee]

⁴*Security, Equality, Choice: The Future for Pensions*, Secretary of State for Social Security, 2 vols, June 1994 [Cm 2594] [White Paper]

II The Maxwell affair and other weaknesses of the present system

The death of the publisher Robert Maxwell in November 1991 was followed by revelations that substantial assets were missing from the pension schemes of various Maxwell companies. At the time of writing most of the claims against various financial institutions for their roles in the Maxwell affair have been resolved in an out of court settlement which should restore a significant proportion of the missing assets to the pension funds. Criminal charges are, however, still pending against a number of individuals, including Robert Maxwell's sons.

An outline of the Maxwell affair was given in the Goode Report: those paragraphs are reproduced below:

The Maxwell affair

4.10.3 Robert Maxwell was the chairman and, through other companies, the majority shareholder of two public companies, Maxwell Communications Corporation (MCC) and Mirror Group Newspapers (MGN). Both companies were ultimately controlled by a Liechtenstein trust, the Maxwell Foundation, which itself was controlled by Maxwell family interests. Each company had a large pension fund for its employees. Certain investments of the two pension funds, together with portfolios managed by certain external managers, were eventually merged into the Common Investment Fund (CIF), of which Bishopsgate Investment Management Ltd (BIM) was appointed trustee. Maxwell was the chairman of BIM, which was owned by the Maxwell Charitable Trust, itself controlled by Maxwell family interests. BIM was authorised by IMRO as an occupational pension scheme member, so that its authorisation was limited to in-house scheme management. The great bulk of the CIF was administered directly by BIM. The remainder was placed by BIM in the hands of different external managers, one of which was London and Bishopsgate International Investment Management plc (LBI), a fund manager authorised by IMRO to conduct investment business and controlled by Maxwell through Headington Investments Ltd.

4.10.4 Maxwell also controlled some 400 trading (or in some cases, non-trading) companies which he referred to as 'the private side'. Various holding companies acted as the treasury to the trading companies.

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4.10.5 The private companies accumulated huge debts. To enable these to be met, money was borrowed from banks against shares in MCC and MGN and substantial amounts of cash and other assets belonging to those two companies and to the CIF and certain of the individual pension schemes were applied for the benefit of the private companies. These included assets which were centrally managed and assets externally managed. Investigations after Maxwell's death revealed that some £298 million of assets was missing from the CIF and a further £155 million from individual pension schemes. Of the total losses of about £453 million, some £248 million represented assets disposed of through the private companies. The balance consisted of securities used as security for loans from banks to the private companies.

4.10.6 The methods by which assets were removed from the individual pension schemes and the CIF and used to the benefit of the Maxwell private companies have been described in various House of Commons Select Committee reports and are currently the subject of proceedings. We therefore say no more about them.

The Select Committee's Reports

4.10.7 Before these facts became public, the House of Commons Select Committee on Social Security had begun a review of pensions, focusing initially on the charging structure of personal pensions. However, in the light of the Maxwell affair the Committee decided to concentrate its inquiries on the ownership and control of pension funds in general and the Maxwell companies in particular. Evidence given to the Committee included a copy of the report submitted to the directors of BIM by the auditors to the CIF drawing attention to a number of accounting control weaknesses: the absence of formal authorisations or review of investment transactions by the board; the lack of a formal system or procedures to review or monitor the external fund managers' activity; the absence of

formal documentation of certain stock lending arrangements administered by LBI; and the fact that there was no formal regular review of the level of stock lending transactions or of the level and quality of collateral provided for them.

4.10.8 In its Report the Committee identified a range of weaknesses in the regulatory framework and made numerous recommendations. These included a recommendation for the establishment of a Departmental Committee or Royal Commission which led to our Committee being set up. The Select Committee has since continued to investigate the particular circumstances surrounding the Maxwell affair and has produced several more reports, though these do not cover occupational pensions in the wider context.

[Goode, 4.10.3 - 4.10.8]

Mr Brandon Gough of Coopers & Lybrand Deloitte told the Social Security Committee how despite the scale of the frauds, in essence the deals were very simple:

"As I look at the methods they are strikingly simple ... Approximately £235 million is simply money owing by private Maxwell companies from securities sold by the pension fund. There was one particular transaction of £100 million involving an unlisted Israeli company ... It happened sadly to be a very good investment but the money did not come into the fund ... Similarly there was an arrangement to dispose of shares in MCC worth about £50 million ... Again, they were sold for some reason, we do not know why, through a Maxwell private company and the money was not paid. There was thirdly a realisation of a portfolio of investments [worth £50 million] managed by a company called London & Bishopsgate International in the Maxwell empire ... and again for some reason outside the control of the trustees, let me say that the money was left in Maxwell's private companies."

[*The Operation of Pension Funds*, Second Report from the Social Security Committee, HC 61-II 1991/ 92 para 3]

Although the Maxwell affair was by far the most notorious of the pension scandals, several other cases where the existing system of regulation was shown to be ineffective served to reinforce the case for a thorough examination of the legislation which controls the operation

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of occupational pension funds. The Goode report described briefly the problems with the Belling, Burlington International Group, and the Lewis's Group pension funds:

4.10.10 The Maxwell affair is not the only example of a loss of pension scheme assets. Indeed, it is in a sense atypical, not simply because of the scale of the loss but also because of the concentration of control of so many functions in a single person, Robert Maxwell, who dominated the employer company, the trustee board and the management of the funds by and through the in-house fund management company. There were other major failures, if on a less spectacular scale. They include, for example Belling, Burlington International Group, and the Lewis's Group.

4.10.11 Belling went into receivership in May 1992. It was discovered that in May 1991, £3.5 million had been withdrawn from the pension scheme and paid to a solicitor to secure a refinancing arrangement for the company. The refinancing did not take place, and the money paid is irrecoverable. In November 1991, the trustees of the pension scheme purchased one of the company's subsidiaries for £5.5 million, which at the time represented twenty per cent of the scheme's assets. A significant part of the subsidiary's trade was with the parent company, and a substantial loss is expected on the sale of the investment.

4.10.12 Receivers were appointed at Burlington International Group in March 1992. Of the pension scheme's gross assets of £32 million, £12.9 million or forty per cent were in employer-related investments. Because of the insolvency of the employer, the realisable value of those assets is now estimated to be £3.2 million. As a result, there is a shortfall of assets against the scheme's liabilities of some £6.5 million, leaving an average deficit of fifty per cent of deferred members' accrued benefits.

4.10.13 The Lewis's Group went into receivership in January 1991. The pension scheme, which had assets of about £12.5 million, had purchased a property from a subsidiary of the employer for £2.4 million. The property is derelict and has produced no income for the scheme. It is now proving difficult to sell. The scheme trustees had also made an unsecured loan of £1.25 million to the company.

[Goode, 4.10.10 - 4.10.13]

Among other failings of the current regime, the Goode Report commented on cases where pension scheme members have suffered from unfair treatment, inadequate and misleading information, and delays in the payment of contributions and benefits. They also drew attention to the question of who owns and controls a pension fund's assets, and whether the members of a scheme should be able to participate to a greater extent in the management of their scheme.⁵

⁵Goode, 1.1.11

III The Pension Law Review Committee Report (Goode Report)

On 8 June 1992 the Secretary of State for Social Security, Peter Lilley, announced that he was establishing a committee to investigate the law relating to occupational pension schemes.⁶ The committee's wide-ranging brief was to look at, among other matters, the rights of scheme members and employers, and at the questions of the ownership of pension funds and the accountability of their managers and trustees.

Mr Lilley told the House:

The Maxwell fraud is shocking because it is so exceptional. Most private pension schemes have served their members well. They have expanded considerably over the past decade. This Government are committed to reinforce their role. They provide substantial additional benefits to those in retirement, and have contributed significantly to the growth in pensioners' incomes which we have seen over the past decade. More than half of all employees are members of such schemes. We are determined to ensure that their standing is maintained and enhanced, and the security of their members protected.

The Maxwell affair has focused attention on the whole framework of pension scheme law. It has raised questions about issues, many of which may have played no part in that crime, but which none the less need answering. I therefore agree with the Select Committee on Social Security that there should be a thorough review of this area.

I propose accordingly to implement our manifesto pledge by establishing an independent committee with the following terms of reference:

to review the framework of law and regulation within which occupational pension schemes operate, taking into account the rights and interests of scheme members, pensioners and employers, to consider in particular the status and

⁶HC Deb. 8 June 1992, cc.19 - 21

ownership of occupational pension funds and the accountability and roles of trustees, fund managers, auditors, and pension scheme advisers, and to make recommendations.

I believe that those terms of reference will enable the Committee to consider all the issues raised by the Select Committee in its valuable report. I am pleased that Professor Roy Goode QC, Professor of English Law at Oxford University has agreed to chair the review. I shall announce the names of members of his committee shortly.

The committee will invite evidence from all interested parties and hold a number of public hearings. I have asked Professor Goode to report within 12 months or earlier if possible. If the committee finds changes which should be initiated urgently I have asked it to report them to me before it concludes its work.

I should emphasise that the committee will not be asked to carry out an investigation of the Maxwell affair. That involves crime and fraud and is rightly being investigated by the Serious Fraud Office.

[HC Deb. 8 June 1992, cc. 20-21]

The ten member committee, under the chairmanship of Professor Roy Goode, first met on 6 July 1992. In September it issued a consultation document, *Consultation Document on the Law and Regulation of Occupational Pension Schemes*, which generated more than 1,600 written responses. The Committee also held public meetings, and took evidence from 137 witnesses representing 37 organisations. In addition, they commissioned research from Social & Community Planning Research: a quantitative survey of public perceptions of occupational pension schemes, and a qualitative survey of the views of employers and employees.⁷

The Pension Law Review Committee's report was published at the end of September 1993 under the title, *Pension Law Reform*. This report is usually referred to as the Goode Report. Described in the Commons by the Secretary of State for Social Security as 'immensely

⁷The research is reproduced in Goode, vol ii.

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thorough, comprehensive, lucid and long', the report made some 218 recommendations.⁸ Its key points included the following:

(i) A New Pensions Act

Trust law should continue to be the basis of pension fund law but should be clarified and reinforced by a new Pensions Act, providing for the first time a proper statutory framework for occupational pension schemes [4.19.2 - 4.19.19].

(ii) Strengthening the scheme of governance including compulsory member trustees

The report recommended fundamental changes to the method of appointment of trustees. Typically, appointments are in the hands of the employer. The report proposed that "active" members (ie. current employees) should have the option of appointing up to two thirds of the trustees, depending upon the type of scheme [4.5.1 - 4.5.65].

(iii) Minimum solvency standards

The accrued rights for pension scheme members should be protected by a minimum solvency standard, which would be phased in over a 5 year period [4.4.45 - 4.4.47].

(iv) Better information for members

Current disclosure requirements should be extended to include:

- details of registration with the pensions regulator
- greater details of contributions, benefits and the methods by which these are secured
- details of the policy on pension increases
- details of trustees
- details on powers of amendment, use of surplus, treatment of deficits and procedures on winding-up

⁸HC Deb. 3 November 1993, cc.354-56

- rights to further information.

Moreover, the report stressed the need for this information to be clear. It also proposed that the current requirement to provide annual statements to active members should be extended to pensioners [4.12.1 - 4.12.45].

(v) A new pensions regulator to be established to oversee the system and enforce it

The proposal was that the Regulator should enforce the new Pensions Act, and replace the current Occupational Pensions Board. The Regulator would be given significant powers to deal with breaches of statutory duties some of which would be treated as criminal offences.

The Regulator should be properly resourced and should work alongside existing financial regulatory bodies. His powers would include:

- spot checks and investigations, including the power to obtain information through the courts;
- power to fine or remove trustees;
- controls over the payment of surplus assets to employers;
- power to trigger a wind-up of a scheme and also approve certain changes to speed-up the winding-up process (and deal with any remaining surplus on a winding-up of the company).

The Regulator would also be involved in the monitoring of scheme management. This would include: appointing trustees in the insolvency of an employer; ensuring the production of scheme accounts; monitoring contributions and solvency within new standards and agreeing to plans to deal with deficits [4.19.22 - 4.19.39].

(vi) An industry-wide compensation scheme should be set up to cover employees whose pensions were threatened by "fraud, theft or other misappropriation"

A pensions compensation board should be established alongside the new regulatory framework. Compensation would cover all funded occupational pension schemes, and would be financed by a post-event levy on all schemes. Compensation would be limited to cases where the employer is insolvent, and would be payable at the rate of the lesser of 90% of "lost assets" or 90% of the actual scheme deficit. [paras 4.11.76 - 4.11.78].

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Peter Lilley, Secretary of State for Social Security, welcomed the report in the Commons, pointing out that it represented just one stage in the process of pension reform. He said that the government was still considering the report and would issue discussion papers as a basis for "detailed exchanges with interested parties":⁹

"We aim to create a framework for occupational pensions which is secure, stable and fair and to encourage people to make provision for their retirement. The report aims to modernise and improve the framework of law affecting occupational funds to bring about fair balances between the interests of scheme members, pensioners and employers. The government certainly shares these aims".

[HC Deb. 3 November 1993, cc. 354-56]

IV The Social Security Committee

In 1991/ 92 the Social Security Committee had called for the scrapping of trust law as the basic legal framework for pension scheme regulation, and its replacement by something more simple.¹⁰ The present Committee accepted, however, that the Government intended to retain trust law - in line with the Goode Report's recommendations - and therefore concentrated its attention on 'strengthening the approach the Government looks likely to adopt'.¹¹ Another principle which informed the Committee's deliberations was the danger of excessive regulation discouraging employers from setting up occupational pension schemes. They were told by one of their witnesses:

"I know of one very large plc where the view has been expressed privately to me that further legislation and the imposition of costs due to solvency may cause it to abandon final salary pension arrangements and move over to low-cost money purchase schemes. I feel that it will only take one very large company to take that step to start the bandwagon rolling."⁶

[Social Security Committee, para 6]

⁹Ibid.

¹⁰HC 61, 1991/ 92

¹¹Social Security Committee, para 7

The Committee feared that if the Goode Report was implemented in all its details the Government 'would need to produce a major bill of around 150 clauses and set in hand sheaves of regulations. The new Act and the subsequent regulations would be imposed upon an area already creaking under the weight of past Acts and regulations. It would be ironic - to say the least - if the new Act brought about to safeguard pension schemes following Maxwell's theft of assets resulted in fewer employers offering occupational pensions.'¹²

To highlight this danger, the Committee set out nine issues which it believed a Pensions Act ought to address:¹³

- Scheme information. Members should have the right to information about their scheme which is 'succinct, easily understood and timely'. This should include a short annual statement of the value of their current pension rights and a projected value at retirement; details of the scheme's solvency level; and the form in which its assets are held as well as their location. The Committee argued that encouraging the active interest of the members in the running of their scheme was one of the key ways of ensuring that a scheme would be well run.
- The aim should be for all schemes above a certain size to have at least one third member trustees. Trustees need to be properly trained and to understand that their duty is to the trust, not to the interests of the employer, employees or pensioners.
- The relationship between the fiduciary principles of trust law and statutory regulatory rules must be clarified. It must be clear which code takes precedence.
- The Pensions Regulator should be well-resourced, and appointed by the Secretary of State. Although he should take a pro-active stance, the information which schemes are required to lodge with the Regulator should be kept to a minimum. The Regulator should be a source of best practice for schemes and an ally for those who believe schemes are being run improperly. He should have the power to disqualify unfit trustees.
- Pension scheme members should be able to take action against trustees who are not performing their duties properly. If the Regulator and a Chancery Master agree, the legal costs of such action should be payable in advance to aid the members.

¹²Ibid., para 6. The Pensions Bill as originally published ran to 154 clauses.

¹³Ibid., para 9

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- The limited circumstances in which scheme surpluses can be run down should be set out in the Act. A commitment to an earnings-related pension, and the availability of the funds to meet this promise are more important than the question of ownership.
- Deficiencies in the Goode Report's minimum solvency standards mean that if enacted the standards might seriously threaten the future of many occupational schemes. A new, more workable standard should be applied which is both practical for the scheme administrators and yet offers additional safeguards to the members.
- A compensation scheme should be introduced along the lines suggested by Goode.
- To safeguard the assets of a pension fund, the assets should be held by an independent custodian. Where the assets are not held by such a custodian, then they should be clearly designated as belonging to a pension fund. This proposal would seek to correct the uncertainty about the beneficial ownership of pension fund assets which facilitated the depletion of fund assets in the Maxwell schemes.

Some of the Social Security Committee's recommendations are discussed in more detail later in this paper.

V The White Paper

On 23 June 1994 The Secretary of State for Social Security, Peter Lilley, published the Pensions White Paper, *Security, Equality, Choice: The Future for Pensions*. In a statement to the House he outlined the provisions of the White Paper, which, he said, implemented all the main proposals of the Goode Report:

My top priority is to restore confidence in the security of pension funds. Following the Maxwell affair, I set up the pension law review committee under Professor Goode. Its report has been widely welcomed-and rightly so. I have since been consulting on its recommendations. As a result I have decided to implement all the committee's main recommendations. We will reinforce trust law as the basis for pensions law; we will bring the management of all schemes up to the level of best practice; we will give members more influence in the running of their schemes; we will introduce a minimum solvency requirement to ensure the adequacy of

pension fund assets; we will appoint a strong regulator; and we will set up a compensation scheme.

As the Goode committee and the Social Security Select Committee recognised, the great majority of schemes are secure and well run. We must not burden them with over-complex administration or unnecessary extra costs. The arrangements that I propose will achieve the security that the pension law review committee intended, while minimising burdens on pension schemes.

I do not believe that any single measure can provide a satisfactory defence against fraud. It is better to strengthen every possible line of defence. The first such line is the scheme members. They have the greatest interest in ensuring that their scheme is well run, so I will give members the right to clear and relevant information, the right to select at least a third of the trustees and access to a procedure to resolve disputes.

The second line of defence is the trustees. Pension funds will continue to operate under trust law, so the role of trustees is crucial. I will make it clear that their role is quite distinct from that of the employer and will set out clearer guidelines for their day-to-day management of schemes. I will give the pensions ombudsman new powers to resolve disputes between employers and trustees. Trustees who are scheme members will be entitled to paid time off for training and trustees' meetings.

The third line of defence lies with the professionals-such as the auditors and actuaries. They will report to the trustees, not the employer, and will have a duty to whistleblow to the regulator.

The fourth line of defence is solvency. I agree with the pension law review committee that a minimum solvency requirement is needed to make sure that funds are available to provide the pensions promised to employees. The Institute and the Faculty of Actuaries have suggested modifications of the pension law review committee's proposal for valuing pension scheme liabilities. After consulting widely, I have taken the actuaries' approach on board. The vast majority of schemes already meet such a solvency requirement. I propose a transition period of five years to help other schemes adjust. From then on, any scheme that falls below the requirement will have three years to reach 100 per cent. solvency. I think that that is fair, prudent and right.

The fifth line of defence will be the new regulator. It would be neither feasible nor desirable for any regulator to police

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more than 150,000 schemes on a daily basis. A regulator should not have to dissipate energy on unnecessary bureaucracy among the vast majority of well-run schemes. Instead a regulator should focus on schemes where there is some reason for unease, ready to take swift and decisive action. The regulator that I propose will have powers giving the full force of the pension law review committee's recommendations: the power to make schemes comply with their statutory obligations; the power to impose sanctions; the power to carry out spot checks; and the power to suspend and disqualify trustees. The regulator will be tough, incisive and able to act at the first sign of trouble.

If, despite all those measures, fraud occurs and the employer is insolvent and cannot meet the loss, members will none the less be protected by a compensation scheme. It will be administered by an independent compensation board, chaired by the pensions ombudsman. The regulator and the compensation board will be completely independent of each other. Both will be funded by a levy on pension schemes.

A more insidious threat to the value of pensions than fraud or theft is inflation. The best cure for that is low inflation. Inflation is now at its lowest for a generation and the Government are determined to keep it low. At present, there is no obligation to protect the whole pension against inflation. I propose that the whole of any occupational or appropriate personal pension rights built up after 1997 must be in line with inflation, up to 5 per cent. a year. As now, schemes may choose to go further. Early leavers from salary-related schemes will have the whole of their deferred pension revalued on a similar basis and we will require more consistent valuation and more efficient administration of transfer rights.

In salary-related schemes, the employer is responsible for making good any deficit that may emerge in a scheme, to enable it to fulfil the pension promise. So it is reasonable that employers should still be able to receive payments from any surplus that builds up. But the circumstances in which that is permitted will be strictly defined in legislation and members will have a right of appeal to the regulator.

[HC Deb. 23 June 1994, cc.359-360]

Replying for the Opposition, Donald Dewar objected that the White Paper represented a boiling down rather than a 'distillation' of the Goode Report. He queried why the reforms would not come into force until 1997, when the problem was so immediate, and was unhappy with the White Paper's lack of specificity. In particular, he drew attention to the plans to require only one third of trustees to be elected by the membership, even in money-purchase schemes: Goode had suggested a quota of two thirds for these schemes. He expressed concern that the Regulator was described as a 'long stop' and that his role had been reduced. Mr Dewar maintained that the Regulator should be actively involved in policing the minimum solvency requirement, and that it was a mistake to have abandoned the proposal that the Regulator should be funded by the Government in order to secure his independence from the industry which he was meant to regulate. On the minimum solvency question itself, he feared that the new formula for assessing solvency was weaker than that operating in many schemes at present; there was a danger that the formula would encourage a levelling downward.

The main proposals in the White Paper were:

A. Trustees and minimum solvency

Although trust law will be retained as the basis for controlling schemes, its role will be reinforced, and in places modified. The scheme's professionals - the actuary, fund managers and legal advisers - will be responsible to the trustees and not to the employer. The trustees will be responsible for the investment of the fund, to the standard expected of a prudent person. These powers can be delegated to authorised individuals, and the employer must be consulted about the investment strategy. No more than five per cent of a scheme can be invested in the parent company, and loans or other financial assistance to the employer will be forbidden. Scheme assets must be segregated from those of the employer. [1.15 - 1.19]

A minimum solvency requirement will apply to all tax-approved defined benefit schemes.¹⁴ This is designed to protect accrued rights, and to set a schedule for future contributions. Solvency will be calculated according to the cash equivalent of the accrued entitlement to benefits: this is similar to the transfer value which a member would receive if he were to leave the scheme early. Discretionary benefits are excluded from the solvency calculation. For younger scheme members, the cash equivalent would assume future growth based on the

¹⁴Some schemes are not approved for tax purposes because the benefits that they offer are in excess of the limits imposed by the Inland Revenue. Schemes which are backed by a guarantee which is at least as good as the minimum solvency requirement, such as public sector and local authority schemes, are also exempt from the solvency requirement.

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investment return offered by equities; for older members the return would be based on the less volatile but lower returns offered by investing in gilts. [1.20 - 1.21]

The solvency requirement would be phased in over five years, from 1997. When in operation, all schemes would be required to have a schedule of contributions in place which would maintain funding at no less than 100 per cent of the minimum solvency requirement. The trustees would have to obtain a full actuarial valuation of the scheme at least every three years, and obtain a less thorough actuarial certificate every year. If the annual certification revealed a deficiency, then a full valuation would be required. Where there is a deficiency, a revised schedule of contributions must be agreed between the trustees and employers to restore funding to the 100 per cent level within three years. If a shortfall of below 90 per cent is revealed at the valuation, then emergency action must be taken to build the fund up to at least 90 per cent solvency within three months. The Regulator will be able to relax these time limits at the trustees' request if by following them the employer might face unnecessary pressures, such as potential insolvency. [1.22 - 1.24]

Good practice for scheme management will not be the subject of legislation: instead the Government believes a code of practice could be implemented by the industry. Any codes of practice produced by professional bodies (on accountancy, audit and actuarial matters) would be binding on scheme professionals. [1.26]

B. Members

Members will have the right to select a minimum of one third of the trustees in their scheme. The minimum number will be two (or one if the scheme has fewer than 100 members). Existing arrangements will be allowed to continue if they have the support of the scheme's members. Trustees are allowed paid time off for training and trustee duties. [1.27]

All information for members must be available in a clear and comprehensible form. Schemes must provide information on the rules and benefits of the scheme. Members will be entitled to annual statements of benefits, as well as the accounts. Schemes will be encouraged to consolidate their trust deeds or rules at least every five years. [1.28] There must be a formal internal dispute resolution procedure, and members will also be able to refer problems to the Occupational Pensions Advisory Service (OPAS) or to the Pensions Ombudsman. The Ombudsman's jurisdiction will be extended to include disputes between the employer and the trustees. [1.30]

If a scheme has to be wound up, then the scheme rules will be over-ridden to ensure that every member receives the cash value of their accrued rights. Remaining assets will then be allocated according to scheme priority rules. If there are insufficient assets, then pensions already in payment will not be reduced, but other members will have their entitlements reduced proportionately. [1.31] Transfer values will be calculated on a basis that is at least as good as that used for assessing solvency, but although schemes will be encouraged to include the value of discretionary benefits (benefits which are customary but not mandatory) there will not be legislation on this point. [1.32]

C. Employers

In salary related schemes employers are responsible for making good any funding deficiencies. They will be allowed to receive payments from funds so long as the rights of members are protected. The trustees will decide about making payments from surpluses, in accordance with prescribed criteria. If the scheme's rules do not allow payments to be made to the employer, then the trustees can apply to the Regulator for permission to amend the rules. The members can ask the Regulator to intervene whether the rules allow payments or not, although if payments are allowed, then the challenge is based on whether the prescribed criteria have been observed. [1.35] Although accrued rights from past service are protected, employers will be free to change benefit levels for future service. [1.36]

D. Occupational Pensions Regulator

An Occupational Pensions Regulator will be set up. The Regulator will lead the new Regulatory Authority which will replace the existing Occupational Pensions Board (OPB). The Authority will be an independent, statutory body which is accountable to Parliament through the Secretary of State. As well as a full time Chairman, there are to be six part-time members: of these two will have general pensions knowledge; one will be a pension funds specialist; one will be a life assurance specialist; one will be chosen after consultation with employees' associations; and one will be appointed after consultations with employers' associations. [Appendix 3]

Members can report their concerns about their scheme to the Regulator, and scheme actuaries and auditors will have a duty to whistle-blow. [1.38] The Regulator will be paid for by an annual levy on all occupational schemes, calculated according to the total membership of each scheme. The existing levies which fund the tracing registry, OPAS and the Pensions Ombudsman will be absorbed into this levy. [1.42]

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The Regulator's main role is to ensure that schemes comply with their statutory obligations, but he will also be responsible for advising the Secretary of State, liaising with other regulatory bodies, and making modifications to scheme rules in certain circumstances. According to Appendix 3 of the White Paper his involvement would extend to the following areas:

- minimum solvency;
- payment of contributions;
- member trustees;
- information for trustees and professionals;
- disclosure of information to scheme members;
- surplus;
- scheme wind up;
- internal dispute resolution procedures;
- transfers and preservation;
- equal treatment;
- indexation of pensions in payment;
- scheme registration.

[White Paper, Appendix 3.7]

E. Compensation

A new compensation scheme, administered by the Pensions Ombudsman and a Compensation Board, will cover losses resulting from the dishonest removal of assets from the pension fund. Compensation will only be payable if the scheme employer is insolvent. Compensation will be limited to the lower of 90 per cent of the missing assets and 90 per cent of the amount required to restore the scheme to 90 per cent solvency. Interim payments will be allowed to enable ongoing commitments to be met. [1.40] Compensation would be funded by a post event levy on all schemes, again based on total scheme membership (not the scheme's total liabilities). [1.43]

F. Divorce

The Goode Report discussed the complicated issue of pension rights after divorce and recommended that further research be conducted. Obviously, if pensionable rights are extended beyond the present position then schemes will face greater costs. The Government promised to undertake further detailed research into this issue. (Pension rights on divorce are covered in the Goode Report at 4.16.1 - 17 and in Research Paper 95/48.)

G. Deviations from the Goode Report

The second volume of the White Paper consists of the Government response to each of the 218 recommendations made by the Pension Law Review Committee in the Goode Report. The major departures from Goode are highlighted here: the numbering refers both to the layout of the White Paper [Cm 2594 - II] and of the Goode Report [1.2].

- **Rec. 13** Goode wanted the Regulator's approval whenever payments were being made from a pension fund's surplus, even if such payments were allowed by the scheme's rules. The White Paper does not require the Regulator's approval if the scheme's rules allow payments from surpluses, although prescribed criteria must be followed.
- **Rec. 16** Under Inland Revenue rules, schemes with surpluses in excess of that permitted by the Revenue have five years in which to eliminate this surplus. Goode wanted to extend this period to a maximum of fifteen years. The Government object that this period would be unjustifiably long, and argue that the Revenue's rules are already quite flexible.
- **Rec. 26** Goode recommended that any shortfall beneath 100 per cent solvency must be reported to the Regulator immediately by the trustees or the actuary. The White Paper imposes a duty to report such shortfalls only if the employer fails to take remedial action and the employer and the trustees cannot agree to an appropriate remedial schedule of contributions.
- **Rec. 38** Goode suggested that member trustees should constitute at least two thirds of the trustee board in money purchase schemes, and hybrid schemes which do not involve a significant earnings-related component. The White Paper imposes a flat rate of one third for all types of schemes.
- **Rec. 102** Trustees should be required to make an annual return to the Regulator consisting of the accounts, an audited statement of contributions, the actuarial certificate of scheme solvency, and a certificate of the scheme's ability to meet its Guaranteed Minimum Pension (GMP) obligations (where appropriate). The White Paper requires instead such information to be lodged with the trustees, and to be made available to the Regulator only on request.
- **Rec. 116** The Regulator should lay down a Code of Practice for pension fund investment, which if deviated from would enable the Regulator to intervene in the

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management of the offending scheme. The White Paper said: 'The role, if any, of codes of practice is subject to further consideration'.

- **Rec. 149** OPAS (the Occupational Pensions Advisory Service) should be funded to allow for a paid conciliation service. According to the White Paper, OPAS, which relies on unpaid volunteer advisers, objected to this proposal. The Government is still committed to funding OPAS.
- **Recs. 151, 152** The Ombudsman should be able to enforce his decisions directly, and should be able to include sums for distress, delay and inconvenience as well as financial loss in his awards. Both proposals were rejected.
- **Rec. 164** There should be a right of appeal for cases in public service schemes where pensions rights are forfeited after the commission of certain serious offences. The White Paper thought such a right unnecessary: a decision on forfeiture is subject to judicial review at present. Treason and Official Secrets Act convictions may lead to forfeiture.
- **Rec. 212** Goode wanted the costs of the Regulator to met by the State. Arguing that those who benefit from regulation should bear the cost of paying for it, the White Paper provides for costs to be met by an industry levy instead.

H. Developments after the White Paper

Following the issue of the White Paper, the Department of Social Security issued consultation documents on the rules regarding member trustees and the structure of the levies which would be needed to fund the Regulator and the compensation scheme.¹⁵ In a policy speech to a CBI conference on pension reform, delivered on 22 September 1994, the Social Security minister William Hague indicated a relaxation of some of the White Paper's proposals. Instead of requiring that a ballot on member trustees should be held in every case, Mr Hague suggested that the requirement to hold a ballot would be triggered by a request from the scheme's members. This would avoid the requirement for a costly ballot where the members were satisfied with existing arrangements. He also appeared to soften the impact of the minimum solvency requirement, by allowing schemes to value their equity assets against equity prices

¹⁵*The Future for Pensions: The Selection and Appointment of Member-nominated Trustees*, DSS consultation paper, June 1994; *Non-state Pension Reform: The Structure of the Levies*, DSS Consultation Paper, July 1994

over a period rather than on a single day. This would make it less likely that a scheme would fail a solvency test simply because of short-term stock market movements.¹⁶

Further refinements appeared in a written answer to a question asked by Peter Butler MP, and in a letter from Peter Lilley to John Butterfill MP which was placed in the Library of the House of Commons.¹⁷ The changes announced were:

- The largest defined benefit schemes would be allowed to use equity-based returns for a proportion of their pensioner liabilities when calculating their solvency for the minimum solvency requirement.
- The time limits for restoring a scheme to solvency were relaxed. Schemes will have one year to regain the 90 per cent level (instead of three months), and five years (instead of three) to restore 100 per cent funding.
- When calculating solvency, assets would be allowed to be valued using market values averaged over a number of months rather than market values on a single day.

The Pensions Bill [HL 14] was published on 15 December 1994. It had its Second Reading in the Lords on 24 January 1995; Committee stages were taken on 7, 13, 16, 20, and 21 February; the Report stages were held on 13 and 14 March; and the Third Reading debate was on 21 March 1995. A summary of those clauses which fall within the scope of this research paper is included later in this paper. The next section, however, considers a number of prominent issues within the Bill at greater length.

¹⁶Government backs down on pension trustees', *Financial Times*, 23 September 1994

¹⁷HC Deb. 8 December 1994, cc.368-69w; Rt Hon. Peter Lilley MP to John Butterfill Esq., MP, 8 December 1994, Deposited Paper /3 770

VI Issues in pension fund reform

A. Bulk transfers

When individuals leave an occupational scheme, they are able to transfer an element of their accrued rights to their new scheme. In certain circumstances, however, a group of pensioners may move all at once from one scheme to another. The Goode Report described two different scenarios where members will move from schemes in large numbers. The first, which they termed bulk transfers, normally occurs when all or part of a company is taken over, and the members of its pension scheme are moved as a unit into an existing scheme. There are legal protections for the rights of the members in such cases, although there is no requirement that the members of the scheme give their consent to the transfer.

If the members have not consented to the transfer, then the trustees or managers of the transferring scheme are obliged to obtain a certificate from an actuary to the effect that the new scheme is, broadly speaking, at least as favourable as the old scheme. Many schemes have, as part of their normal practice, a number of discretionary benefits which may boost significantly the value of the scheme's benefits to its pensioners. The actuary is required to take into account, when calculating the transfer's effect on the members, the value of such benefits, working on the assumption that the discretionary benefits would continue to be paid in the same way as before. The rules for such transfers are set out in *The Occupational Pension Schemes (Preservation of Benefit) Regulations 1991* (SI 1991/167), as amended by *The Occupational Pension Schemes (Preservation of Benefit) (Amendment) Regulations 1993* (SI 1993/1822).

The Pension Law Review Committee considered making it compulsory for all members to give their consent before this kind of bulk transfer could be effected. They rejected this on two grounds: it would be administratively very difficult to obtain the consent of all members, and this requirement might cause employers to wind up a scheme instead of transferring it. Secondly, they did not find widespread abuse of the use of bulk transfers. In their opinion the certificate provides adequate protection for members. The Government accepted this recommendation.¹⁸

There is another sort of bulk transfer where a single employer decides to rationalise, for whatever reason, the pension schemes he operates, by merging schemes together. The Goode

¹⁸Goode Report, 4.7.26; White Paper, vol. 2, p.12

Report called this manoeuvre a merger. In this case the transferring scheme is wound up, and all the members are moved into another scheme operated by the same employer. No actuarial certificate is required that the benefits are of broadly comparable value; the consent of the members is not required. This loophole allows an employer to move employees into a less generous scheme. Since in many cases the surplus of a scheme on winding up is payable to the employer, in effect the loophole permitted employers to cash in the surplus of an existing scheme, and at the same time to move the scheme's members into a new scheme which would not have a surplus, and which might provide less valuable benefits to its members than the previous scheme.

The Goode Report found no justification for this loophole, and recommended that unless the members had consented to the merger, then no such merger should be permitted unless an actuarial certificate was obtained indicating that the value of the benefits would remain broadly the same in the new scheme. In other words, the existing regime for bulk transfers would apply to mergers also. The Government has accepted this recommendation.

Bulk transfers between the schemes of a single employer following the wind-up of one scheme should be permitted without the consent of the relevant members only on the basis of an actuarial certificate.

Accepted.

Acceptance will increase member protection and place on a level playing field the requirements for all bulk transfers.

[White Paper, vol. 2, Rec. 72]

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B. The Pensions Regulator

The Goode Report had recommended that a new pensions regulator should be funded by the state [4.19.33], and this was echoed by the Social Security Committee [para.76]. The Goode Report commented:

'Because in a contracted-out scheme the member is losing the right to a guaranteed state benefit, it is right that government should meet the cost of protecting the alternative provision.'

[Goode Report, 4.19.33]

The White Paper rejected this recommendation; it suggested instead:

'Costs to be met by an increased levy on schemes. This ensures that those who benefit from the regulatory framework pay for it.'

[White Paper, vol.2, Rec. 212]

If the scheme is funded by a compulsory levy on the pensions industry, it is arguable that the regulator is not independent, but is instead a creature of the industry which pays his bills. The funding arrangement, however, is analogous to that which supports the self-regulatory scheme of protection for investments under the *Financial Services Act 1986*. This is a double-edged comparison, since not everyone is convinced by the record of self-regulation in the financial services industry.

There is a perception that the Goode Report had proposed a more pro-active role for the regulator than the one outlined in the White Paper: the Government has challenged this interpretation. Announcing the White Paper, Peter Lilley responded to precisely this charge from Donald Dewar:

'The hon. Gentleman suggested that the role of the regulator was much diminished below that recommended by the pension law review committee. That is not so. It will have all the powers, in full, which were, in essence, recommended by the Goode committee. What the regulator will not be is encumbered by certain bureaucratic procedures which could have flowed

from some of the recommendations of the PLRC and he will, therefore, be more effective by being better focused on areas of concern, rather than spending all the time responding to forms coming in from 150,000 different pension schemes, the vast majority of which are well-managed.'

[HC Deb. 23 June 1994, c.365 - 66]

In fact, the Goode Report and the White Paper appear to concur on the need for the regulator to be able to 'carry out spot checks and detailed investigations independently of any complaint' [Goode Report 4.19.24].

The Regulator's primary responsibility will be to ensure that schemes comply with their statutory obligations. So, in the case of transfers, for example, the Regulator's role will be to make sure that an actuarial certificate is obtained where necessary.

The difference is that whereas the Goode Report recommended that the trustees should make an annual return to the Regulator, consisting of the accounts, an audited statement of payment contributions, an actuarial certificate of scheme solvency, and a certificate of the scheme's ability to meet its guaranteed minimum pension (GMP) obligations, the Government decided that such records should merely be available for inspection by the Regulator. Moreover, the Goode Report recommended that the trustees and the actuary of a scheme should be under a statutory duty to report any shortfall in the scheme's solvency level to the Regulator as soon as they become aware of it. The Government thought these proposals were too demanding.

The Bill in the Lords. An amendment was introduced (but withdrawn) at Committee stage by Baroness Hollis of Heigham which would have required the Regulator to be funded by the Government rather than by an industry levy (HL Deb. 7 February 1995, cc.141 - 151). (A similar amendment was defeated at Report Stage by 95 votes to 135: see HL Deb. 13 March 1995, cc.567 - 575).

Amendments requiring active supervision of schemes by the Regulator were introduced at Committee Stage by Baroness Hollis of Heigham (HL Deb. 7 February 1995, cc. 106 - 113: amendment withdrawn); and by Lord Ezra at Report Stage (HL Deb. 13 March 1995, cc.559 - 567: amendment defeated by 93 votes to 120).

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C. The ownership of pension funds

The background to this problem is the existence of large surpluses in some pension funds. These surpluses have originated from a combination of better-than-expected share price performance and changed levels and patterns of employment, especially in industries which used to be labour-intensive. Some employers have taken advantage of surpluses either to reduce, or temporarily suspend the level of their own contributions to their scheme. This is known as taking a contributions holiday. There has also been concern that companies with schemes in surplus may use the surplus to pay off other company debts, and even that companies may become takeover targets, with the acquiring company chiefly intent on realising the surplus in the pension scheme. Not unreasonably, pensioners have been worried about both the misapplication of pension funds, and the direction of the benefits of the surplus. Some employers have used their surpluses to increase pension benefits, but many have not. Pensioners argue that since the money has accrued from their contributions, it is they, not the employers, who should derive the benefits of unexpected surpluses.

The question of who owns the funds in a pension scheme has proved particularly intractable. The consensus seems to be that the assets in the pension fund belong neither to the pensioners nor to the employers. Assets in a scheme are vested solely in the trustees, and can only be withdrawn subject to the trust deed, or the law. Although the pensioners cannot be said to own the assets, they obviously have an interest in them. The assets are the security for future payments as well as the source of current payments. The pensioners therefore have an interest in the fund as a whole, although they do not have any claim on the assets. Their entitlement is to a pension, and not to the assets which enable that pension to be paid. Equally, although the employer will also have made contributions to the fund, the assets no more belong to him than to the pensioners.

The next question, which follows on from this, is 'who do the surpluses belong to?'. This is still more complicated. The legalistic opinion, expressed by the Goode Report, is that a surplus only arises when a scheme is wound up. At that point, all the liabilities and assets crystallise, and a surplus (or deficit) can be confidently measured. The scheme's trust deeds may provide for allocating the surplus on winding-up: it is usual for such surpluses to be assigned to the employer, although there may be provision for increasing the benefits to members as well. In an ongoing scheme, though, the surplus is less tangible: it is an actuarial estimation of how the estimated assets in the fund relate to its estimated current and future liabilities.¹⁹ Such things as better or worse-than-expected asset price performance, the length of time that current contributors stay with the scheme, and the lifespan of its pensioners can

¹⁹Ibid. 4.3.2

all serve to throw these calculations out. So, in a sense, it is a futile exercise to try to apportion ownership to a notional sum. What is more important is the safeguarding of the assets in a scheme (which may fund a notional surplus) and the delivery of the promised benefits to those who are entitled to them.

The Goode Report did not 'consider that sweeping changes are needed in the law in this area'.²⁰ Similarly, the Social Security Committee acknowledged that the question of ownership of pension schemes was a secondary matter. They had been told by Professor Goode:

"The pension promise is a promise to provide a pension; it is not a promise to hand over a share of the assets."

[Social Security Committee, para. 88]

A similar line was taken by the pensions officer of the GMB, Paul Moloney, who appeared before the committee on behalf of the TUC:

"A lot of people say that the fundamental question is the ownership of pension funds and surpluses. To us the fundamental question is: what level of pensions will people get out of their pension schemes? The discussion about the ownership of pension funds and surpluses flows from that."

[Social Security Committee, para. 89]

Although the Goode Report did not feel that sweeping legislative changes were required to deal with the treatment of surpluses, it made two recommendations. In the case of schemes where the trust deed allows a payment to be made to the employer, Goode suggested that the approval of the Regulator should nevertheless be required, and that this approval should only be given in strictly defined circumstances.

The approval of the Regulator should be required even where the trust deed or any amendment to it permits payments to be made to the employer and there is an adequate margin. Approval should be given only where limited price indexation (LPI) has been introduced for past and future service, the trustees have obtained written legal advice that the proposed payment was proper and the Regulator is satisfied that the members' accrued rights under the scheme remain fully secure and that contribution holidays would not eliminate the surplus within a reasonable period. '

²⁰Ibid. 4.3.28

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[Goode Report 4.3.30]

The Government did not accept this recommendation. Rather than require the Regulator's approval in all cases, the White Paper proposes that it will be up to the trustees to decide whether the payment meets defined criteria. The members will be able to challenge the trustees' decision if they think the criteria have not been followed, and they can refer the proposal to the Regulator in such cases:

Where scheme rules allow a payment to be made to the employer, the trustees will decide subject to satisfying prescribed criteria. Members will have a right to challenge the trustees' decision and seek the intervention of the Regulator if the criteria have not been complied with. Where scheme rules do not allow a payment, the Regulator will have power to modify as does the OPB currently.

[White Paper, vol 2, Rec. 13]

The effect of this proposal depends rather on the prescribed criteria, but it would appear less rigorous than Goode, in that the Regulator is not automatically involved. Clause 34 of the Pensions Bill as printed requires the following criteria to be satisfied before payment can be permitted by the Trustees: proposals for the payment must conform to para 6(1) of Schedule 22 to the *Taxes Act 1988* (on the reduction of pension fund surpluses); it must be in the interests of the members for the power to be used in the manner which is proposed; pensions under the scheme must have been increased by the required percentage; and the members of the scheme must have received proper notice of the proposal to use the power to make payments to the employer. It is interesting to speculate on how the requirement that the payment be in the interests of the members will be interpreted in practice.

As for those schemes where a payment is not permitted under the trust deed, the White Paper accepts Goode's recommendation that there should be a mandatory requirement for the employer to notify the scheme members of the proposed payment so as to allow them to make representations to the Regulator, and to require the employer to state why the Regulator should permit the payment.

Perhaps the final word on the question of surpluses and ownership should go to Peter Lilley. When he announced the publication of the White Paper, on 23 June 1994, he defended the right of employers to make use of surpluses in certain circumstances:

In salary-related schemes, the employer is responsible for making good any deficit that may emerge in a scheme, to enable it to fulfil the pension promise. So it is reasonable that employers should still be able to receive payments from any surplus that builds up. But the circumstances in which that is permitted will be strictly defined in legislation and members will have a right of appeal to the regulator.

[HC Deb. 23 June, c.360]

D. Member-nominated trustees

The Goode Report made the following recommendations:

After considering these conflicting views we have concluded that, for earnings-related schemes (including hybrid schemes where there is a significant earnings-related component) active members should be entitled (but not obliged) to appoint from among their number at least one-third of the trustees, with a minimum of two, and the employer should be able to reserve the right to appoint the remainder. There are already some schemes which go further than this, with 50/50 appointment of trustees, and in some cases a majority. On the other hand, for money purchase schemes (including hybrid schemes which do not contain a significant earnings-related component) where the employer has no liability beyond the employer's contributions, scheme members should be entitled (but not obliged) to appoint at least two-thirds of the trustees, with the employer being able to reserve the right to appoint the remainder. These recommendations on the composition of the trustee board should not, however, apply to small schemes, defined for this purpose as schemes with fifty or fewer active members and pensioners.

[Goode Report, 4. 5. 40]

Earnings-related schemes pay a pension with a benefit which is defined in relation to the earnings of the member, usually as a proportion of his final salary. This is also known as a defined benefit scheme. Under a money purchase scheme (or defined contribution scheme), the pension rights accrue in relation to the sums which a member has paid into the scheme

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(plus investment gains). Because under a money purchase scheme the member takes most of the investment risks himself, unlike an earnings-related scheme where the employer would have to make good any shortfall, Goode thought that these schemes should have a higher proportion of member trustees.

The White Paper rejected this distinction in favour of a single, more simple system:

All schemes to be required to appoint one-third member-nominated trustees with a minimum of two (minimum of one for schemes with fewer than 100 members), unless alternative arrangements gain the support of a majority of members. Subject to further consultation.

[White Paper, vol 2, Rec. 38]

Introducing the White Paper in the House, Peter Lilley defended this simplification:

The hon. Gentleman asked why we did not go further than a third of trustees being appointed by members. That was the broad recommendation of the Goode committee and, obviously, individual schemes will be able to go further. If they want some different system of representation of their members - some have successful schemes involving pension committees, their various subsidiaries, and so on - they would have to get that agreed by the members as a whole before the new scheme was introduced. Obviously, if people made their objections known to the regulator about a particular scheme, he could repudiate it.

We did not go for two thirds of member trustees in the case of contracted-out money purchase schemes, partly for reasons of simplicity, partly because of the complexity that that would cause to hybrid schemes, which were part one and part the other, and partly because we did not want to convey the impression that trustees, when appointed, are

purely representatives of an interest. They may be appointed by the members, but once they act as trustees, they have to act on behalf of the whole fund.

[HC Deb, 23 June 1994, c.365]

The government position is arguably stricter than that of the Social Security Committee. The Committee, in all its deliberations, gave considerable weight to the twin facts that occupational schemes tend to produce better benefits than other schemes, and that the number of occupational schemes is declining. They were mindful of the danger of encouraging this decline by imposing burdensome regulation which would act as a disincentive to the continuation of occupational schemes. Employers are not, of course, obliged to offer an occupational scheme. Accordingly they stressed the importance of training trustees. Only when training proposals had been developed did they think it appropriate for there to be a compulsory proportion of member trustees:

55. This Committee is very aware that the appropriate composition of trustee boards is seen by many as being a crucial factor in ensuring the successful future of occupational pension schemes. A number of the witnesses who appeared before this Committee put forward significantly differing views on this subject. We are conscious that there is a concern amongst members that they should be entitled to significant representation on trustee boards and that they should be entitled to nominate half the membership of the trustee board. Alternatively there is anxiety amongst many employers, even from those who already have significant member representation, that for the Government to introduce compulsory member representation and in turn to prescribe how those member trustees should be selected could affect the future of a number of schemes.

56. We have considered this whole issue in great detail. We acknowledge that a significant number of schemes already have member representatives, including pensioner trustees. We do, however, conclude on balance that there should be some element of compulsion introduced along the lines expressed by the PLRC. We therefore recommend that, over time, as the training proposals have taken root, both final salary schemes and money purchase schemes should be required to have trustee boards which include a minimum of one third member trustees. It could be that over the longer term, as more employers come to appreciate the value of member trustees

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that this requirement could be increased. As we have stated in our previous Reports, we would wish ideally that such member representation would always include a pensioner trustee; however, we accept that this should not be included in legislation.

[Social Security Committee, paras. 55, 56]

On the 22 September 1994, in a speech to the CBI, the social security minister William Hague indicated some changes of opinion. In addition to moves to make solvency checks less onerous, he also suggested that in response, again, to representations, the Government was considering amending the requirement that all schemes have one third of member-nominated trustees. The White Paper had already suggested that schemes would be allowed to opt out of this requirement if they could show that a majority of members were happy with an alternative arrangement. Both pensioners and active members would be consulted before a scheme was allowed to opt out: there would have to be a referendum in order to demonstrate that opting out was what the members wanted.

The DSS consultation paper, *The Future for Pensions: The Selection and Appointment of Member-Nominated Trustees*²¹, goes into greater detail on the envisaged procedures for electing member-representatives. The current trustees would be responsible for determining the procedures by which member-nominated trustees would be elected, but their procedures would be open to challenge. This might take the form of 10 per cent of active and pensioner members registering their discontent. The trustees would then have to re-examine their procedure, and put either it or a proposed alternative procedure to a vote of confidence. All active and pensioner members could vote in this referendum. If there was not a voting majority for a procedure following a referendum, then a 'default procedure' would come into effect. This default procedure would be set out in legislation. A suggested default mechanism, in the DSS consultation paper, allows all active members to nominate candidates: pensioners appear not to have a right of nomination. Pensioners, active members and non-members will be eligible to be nominated: nominations will require a specified number or percentage of supporters, such as 10 per cent of active members, or ten members, whichever is less. Active members only, not pensioners, will vote if a ballot is required. Any elected member-nominee would be statutorily appointed to the board.

Mr Hague's speech, however, indicated a willingness to accede to respondents who had complained that it was an unnecessary burden to oblige all schemes to hold an initial ballot

²¹*The Future for Pensions: The Selection and Appointment of Member-nominated Trustees*, DSS consultation paper, June 1994

for member-trustees. Instead, it will be up to members to trigger the procedure for electing member-trustees. Under clause 17 of the Pensions Bill, an employer will make proposals to continue with the existing arrangements, or to adopt new arrangements for selecting the trustees. A statutory consultation period will then begin during which active and pensioner members can determine whether they wish to accept the proposals. If they reject the proposals, or the procedure is not carried out properly, then the arrangements for electing member trustees (as provided for by clause 16) will apply to the scheme. If the proposals are accepted, then there will be no requirement to hold a ballot under clause 16. Part of the argument for this change is that many pension schemes, 60 per cent of the members of the National Association of Pension Funds for instance, already have member trustees.²² For them to be obliged to hold a ballot would be illogical, and a waste of money. On the other hand, pension scheme members must now adopt an active stance if they wish to enforce their right to member-trustees, whereas the White Paper had proposed to oblige schemes to implement this right (unless the members expressed their satisfaction with the existing regime in a ballot).

The training of member trustees has also been the subject of debate. The Social Security Committee made the strongest recommendation on training, calling for a certificated qualification, with funding available from the Regulator to allow trustees to attend. They also thought that schemes should make a statement in their annual report on the progress of their trustee training programme. The Committee stopped short of calling for such training to be compulsory.

54. We understand that some employers will be fearful of having to include member representatives and we believe that those concerns must be allayed before any changes are introduced. This Committee believes the key to this issue is a policy of comprehensive training for trustees which should ideally commence before they take up the role and should continue throughout their time in post. We emphasised the vital importance of trustee training in our Report on the Work of the Maxwell pension fund trustees. We stated our belief that training should consist of both an introductory training course as well as regular updates. We would also support the proposal that trustees should be strongly encouraged to obtain a certificate of qualification in trusteeship. We reluctantly accept it is not possible to make such training a compulsory requirement, however we would recommend that all schemes should be required to state in their Annual Report and the annual statement to members

²²Ibid.

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the level of progress the scheme has made in training its trustees. The Regulator should be able to finance training for trustees of small schemes. We consider if such steps are taken, that over time all employers will accept, as a number of employers already have done, that a trustee board with significant member representation should not be seen as a threat to their position but as an ally.

[Social Security Committee, para. 54]

The Goode Report also felt that it was not practical to require compulsory training, though it recommended that schemes arrange such training. Its only formal recommendation in this area was that member trustees should be allowed to undertake training without losing pay.

Several submissions emphasised the need to raise the general level of knowledge among trustees and to make them more aware of their responsibilities. Increasing attention is being devoted to the question of training, and several organisations are now offering courses for pension trustees. We do not consider it would be practicable to require all trustees to complete even a preparatory training course, but we strongly recommend that schemes arrange this as a matter of good practice and that there should be continuing education for trustees in relation to scheme management and their role and responsibilities. We recommend that employers should be required to allow member trustees reasonable time for training without loss of pay.²⁴

[Goode Report, 4.5.65]

The Government accepted this recommendation in their White Paper.

The Bill in the Lords. Several amendments were introduced to increase the proportion of member nominated trustees on trust boards. At Committee Stage Baroness Dean of Thornton-le-Fylde withdrew an amendment which called for a majority of trustees to be member-nominated, and Baroness Hollis of Heigham's amendment requiring at least half the trustees to be scheme members was defeated by 116 votes to 129 (HL Deb. 13 February 1995, cc. 441 - 456). At the same stage, Baroness Seear's call for at least one of the member nominated trustees to be a pensioner member was defeated by 115 votes to 131 (HL Deb. 13 February 1995, cc. 457 - 463). At Report Stage, Baroness Hollis' amendment requiring two thirds of the trustees in money purchase schemes to be member nominated (in line with the Goode report) was defeated by 74 votes to 129 (HL Deb. 13 March 1995, cc. 604 - 610); also on Report, Baroness Seear withdrew her amendment which would have required there to be a pensioner trustee nominated by pensioners in mature schemes (where pensioners are in the majority) (HL Deb. 13 March 1995, cc. 611 - 616); and Baroness Hollis withdrew an

amendment which would have required a majority vote by scheme members before a scheme could opt out of the member nominated trustee provisions of clause 16 (HL Deb. 13 March 1995, cc. 617 - 622).

Several amendments were tabled which would have required compulsory training for trustees. At Third Reading Baroness Turner of Camden's amendment on this topic was defeated after debate by 77 votes to 158 (HL Deb. 21 March 1995, cc. 1132 - 1138).

E. Solvency or funding

In most occupational schemes a fund of assets is built up by a mixture of contributions from the individual's employer and contributions (usually in the form of deductions from salary) made by the individual. At the same time, the assets in the pension fund will be drawn upon to pay for the pension benefits which have been earned by those who used to contribute to the scheme when they worked for the employer but who have now retired. Any fund is judged to be 100 per cent solvent when it has sufficient assets to meet all its legal liabilities. Although this concept sounds simple, it actually involves complex actuarial work, first to determine precisely what a fund's liabilities are, and then to calculate the value of the assets.

Goode defined the total liabilities for active or deferred pensioners (that is, those who are still working and contributing, and those who have contributed in the past, but although not yet retired are no longer contributing to the scheme) as being the cash equivalent of all members' accrued rights.²³ For those who are pensioners of the scheme, the full solvency requirement is the current cost of purchasing an annuity which would pay for their benefits, plus the cost of any promised increases in their benefits. So, under Goode, the solvency requirement is the sum of the cash equivalent of accrued rights plus the cost of purchasing immediate annuities.²⁴

The Goode Report accepted that the levels of funding would go up and down all the time, corresponding to fluctuations in the stock market and other asset markets. It is realistic to distinguish between minor funding inadequacies which can easily be remedied, and major funding shortages which require more drastic or long term solutions. Accordingly, Goode suggested that a solvency band be set up between the 100 per cent solvency level, and a so-called base level of 90 per cent. All schemes would have to adhere to a plan to fund

²³Goode Report, 4.4.46

²⁴Ibid. 4.4.46

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themselves at the 100 per cent level; if the scheme fell below 90 per cent, then an immediate injection of cash would be required. [Goode Report 4.4.20]

Goode suggested that the trustees or actuary should inform the Regulator on every occasion when the funds fall below either of these two thresholds. The Government rejected this. Instead, the White Paper proposed that such deficiencies need only be reported to the Regulator where either the employer fails to take appropriate remedial action or where the trustees and the employer cannot come to an agreement about a contributions schedule to restore full funding. This proposal is meant to avoid expensive - and perhaps unnecessary administrative work except in cases of real need. [White Paper vol. 2 Recs. 25-26]

The solvency proposals have attracted a good deal of controversy. On the one hand, it has been argued that the notion of a minimum solvency standard is inherently potentially misleading, in the way that, for example, a company's pre-tax profit figure is. By flagging up a headline figure and associating it with such concepts as full funding and 100 per cent solvency, there is a danger of implying a guarantee. In reality there can be no such guarantees, and even funds that might pass one particular measure of solvency may nevertheless still be unable to meet their liabilities in full.²⁵ At the same time, the remedial measures which are required to restore schemes to 100 per cent solvency have been attacked for threatening the viability not just of pension schemes but also of the companies which fund them.

As has been discussed earlier, the Government has moved to relax the time periods during which underfunded schemes must restore their funds to solvency. Announced in a letter from Peter Lilley to John Butterfill MP, the changes are:²⁶

- Schemes will have one year to regain the 90 per cent level (instead of three months), and five years (instead of three) to restore 100 per cent funding.
- When calculating solvency, assets would be allowed to be valued using market values averaged over a number of months rather than market values on a single day.

²⁵See for instance 'Workers at Swan Hunter face cut in pensions', *Financial Times*, 20 September 1994, where according to the writer the Swan Hunter scheme is unable to meet its future liabilities despite apparently being able to pass the sort of solvency test proposed by the White Paper.

²⁶HC Deb. 8 December 1994, cc.368-69w; Rt Hon. Peter Lilley MP to John Butterfill Esq., MP, 8 December 1994, Deposited Paper /3 770

Another significant change which was revealed at the same time points to the other controversy posed by solvency requirements. In order to assess solvency, the assets have to be matched against the liabilities. Because pension funds operate as if they are going to remain in operation, rather than be wound up tomorrow, they are able to make assumptions for future levels of return on their assets which effectively offset their future liabilities. The solvency test is more akin to an immediate winding up: it asks can the fund pay its immediate liabilities with its immediate assets. Historically the return on equities has been much higher than the return on fixed interest stocks, but fixed interest stocks are also much less volatile. Although the potential rewards of gilt investment are lower than equity investment, the risks are correspondingly lower too. This would suggest that if a fund wishes to be confident of always being able to meet its liabilities whenever it is called upon to do so it should hold gilts in preference to equities. Yet because the return on gilts is lower than that on equities, if a fund were to hold gilts in preference to equities, that would imply additional contributions to the fund. In other words, the price of the increased security offered by gilts is the higher cost (in comparison to holding equities) of achieving the same return.

The White Paper allows the solvency calculations to be based on equity returns for younger members of schemes, whilst requiring that older members and pensioners have their benefits matched by gilt-based returns. The change announced on 8 December in Mr Lilley's letter to John Butterfill would permit the largest funds (those with assets running into hundreds of millions of pounds) to match up to 25 per cent of their pensioner liabilities against equity returns rather than gilts. The reason given is that such schemes would in all probability never be - and probability could not be - wound up, so the gilt-based method is inappropriate. Rather than purchase annuities to provide the benefits accrued by their members, a large scheme would instead be run as a closed fund, and retain an equity element in its ongoing investment portfolio.

The costs of the minimum solvency requirement, as assessed in the White Paper, were, the Government has accepted, too low. The modifications to the solvency requirement since then, however, mean that those figures (albeit on a different basis) are still broadly correct. In particular, the costs to employers of having to increase or bring forward contributions in order to meet the solvency requirement are estimated at £230m a year over the twelve year period until the minimum solvency requirement is fully in place. The costs of any adjustment to investment strategy implied by the minimum solvency standard are assessed at between £60m and £170m each year the over same period.²⁷ The Compliance Cost Assessment estimates, on a conservative basis, that the overall asset holdings of private sector salary-related schemes will see little change in the value of UK equity, property and cash holdings, a fall in holdings

²⁷*Pensions Bill: Compliance Cost Assessment*, Department of Social Security, 1994. Published with the Bill.

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of foreign equities and bonds of about ten per cent, and an increase in holdings of fixed interest gilts and indexed gilts of 40 per cent and 65 per cent respectively.²⁸ Given the timescale involved and the advance notice, it is unlikely that the devastating effects on the stock markets that some have predicted will occur.

The Bill in the Lords. The most notable change resulted in the Minimum Solvency Requirement (MSR) being rechristened the Minimum Funding Requirement (MFR). The Opposition argued for schemes' solvency to be regulated on a different basis altogether. Lord Eatwell suggested that instead of the Solvency or Funding requirement, there should be a Minimum Contribution Requirement which would require the employer to make to the scheme contributions which would be sufficient to meet the benefits to which members were entitled. He argued that because the Government's proposals were reliant on assessing schemes on a discontinuance basis, they would result in both higher contributions being required from members and at the same time would yield lower benefits. His proposed alternative was a contribution requirement, based on best actuarial practice, which would assess schemes on an ongoing basis. Such a basis would avoid the reduction in benefits and increased costs implied by the Government scheme. To provide against scheme insolvency (a situation which the discontinuance basis is more appropriate for), Lord Eatwell proposed a central discontinuance fund in which the assets of insolvent schemes would continue to be managed on an ongoing basis.

After a lengthy debate at Committee Stage, the amendment was withdrawn (HL Deb. 16 February 1995, cc. 813 - 831). At Report Stage a similar proposal for a minimum contribution requirement was again advanced by Lord Eatwell, and withdrawn (HL Deb. 13 March 1995, cc. 676 - 683). At the same time the Government accepted the Earl of Buckinghamshire's amendment which changed the minimum solvency requirement's name (cc. 683 - 84). At Third Reading Lord Eatwell introduced a revised proposal to allow schemes to assess their assets on either an ongoing basis, or a discontinuance basis: if an ongoing basis was used, however, schemes would also have to contribute to a central discontinuance fund. The amendment was again withdrawn (HL Deb. 21 March 1995, cc. 1157 - 1169).

²⁸Ibid. Note though that the foreign equities and bonds are aggregated: it is possible that an increase in foreign bond holdings may partially dampen sales of foreign equities. Note also that the gilt holdings are increasing from comparatively low levels.

VII Pensions Bill [HL] Bill 87 1994/95

Selected clause summary

Clauses 1 - 2: Occupational Pensions Regulatory Authority

These clauses relate to supervisory activities by the new Occupational Pensions Regulatory Authority (referred to also in this paper as the Pensions Regulator and the Authority).

Clause 1 sets up a new Occupational Pensions Regulatory Authority, referred to subsequently as the Authority. The Authority will have at least seven members, including a chairman: one will be chosen after consulting employers' organisations; another after consulting employees' organisations; one is to have life assurance knowledge; another knowledge of occupational pension schemes; and two are to be knowledgeable about occupational pension schemes in general. The members and employees of the Authority are only liable in damages for actions done as part of the work of the Authority if those actions (or omissions) were done in bad faith. The Authority's constitution is set out in Schedule 1. (More details on the Authority appear earlier in this paper in the section on the Regulator during the discussion of the White Paper.)

Clause 2 requires the Authority to prepare an annual report on its activities which must be sent to the Secretary of State; he in turn must lay a copy before both Houses of Parliament.

Clauses 3 - 15: Supervision by the Authority

These clauses relate to supervisory activities by the new Occupational Pensions Regulatory Authority.

Under **clause 3** (prohibition orders) the Authority can prohibit by order a trustee for a serious or persistent breach of his duties, or if he has infringed any of the provisions of Part I of this Bill. This is an amended form of the original clause which by using the term 'remove' rather than 'prohibit' might have allowed trustees to resign first and so escape sanctions. The effect of the measure is the same. Prohibition orders apply also to companies and Scottish partnerships. There is a right of appeal to the regulator by the prohibited trustee.

Under **clause 4** trustees can also be suspended for a period of up to twelve months (c.4(2)(b)); and that period can be extended by a further twelve months whilst the Authority considers

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whether to prohibit them. Suspension orders may also be used when proceedings for bankruptcy or dishonesty are in progress. There are provisions which would allow a scheme to function normally whilst a trustee is suspended. Taken together, clauses 3 and 4 are major sanctions by which the regulator can discipline trustees of occupational schemes.

When the Authority intends to prohibit a trustee the trustee must be given at least one month's notice of this intention; the other trustees must also be notified (**clause 5**). Notice can be given by post, and is valid if addressed to the recipient's last known UK address (c.5(5)). Immediate notice should be given of an intention to suspend (under clause 4).

It is an offence to act as a trustee whilst prohibited and suspended (**clause 6**), and is punishable by a fine (summary conviction) or a fine and/ or imprisonment (conviction on indictment). Note, however, that any actions carried out by someone who is prohibited or suspended do not become invalid simply because the individual is not currently a trustee (c.6(3)); nor does suspension or removal affect the potential liability of an individual who is purporting to act as a trustee of a trust scheme (c.6(4)).

If the Authority prohibits a trustee from a scheme, or if an existing trustee is disqualified from holding the office of trustee, then under **clause 7** it has the power to appoint by order another trustee. The Authority can also appoint a trustee to a scheme if it appears that the scheme requires additional expertise or numbers to function properly (c.7(3)). The order can require that such a trustee is paid from the resources of the scheme. An order under clause 7 can limit the powers of the trustee it appoints, and delegate powers exclusively to him (**clause 8**). If he is paid from the scheme's resources, the order can make such payments a debt due from the employer to the trustees.

The Authority has equivalent powers to the High Court (Court of Session in Scotland) to vest and transfer property as a consequence of the appointment and removal of a trustee (**clause 9**). Under **clause 10** the Authority has the power to levy a civil penalty (subject to a prescribed maximum) for the contravention or failure to comply with regulations made under Part I of the Act. Such penalties, collected by the Authority, are handed over to the Secretary of State. Where the trustee is a company or a Scottish partnership, there is a power to fine directors and officers or partners who are directly responsible. Along with clause 3, clause 10 is the main sanction which the Authority has against trustees.

Clause 11 gives the Authority the power by order to wind up occupational pensions schemes if it is satisfied that (a) the scheme ought to be replaced by a different scheme; (b) the scheme is no longer required; or (c) that it is in the best interests of the members of the scheme that it should be wound up. Orders on the basis of (a) or (b) can only be made on the application

of the managers or trustees, anyone else who has the power to alter the rules of the scheme, or the employer (c.11(2)). The order can direct the manner and timing of the winding up. The Authority may also apply for a public service pension scheme to be wound up, but only if it is in the best interests of the generality of the members.

Clause 12 permits Ministers and Government departments with relevant responsibilities to direct by order for a public service scheme to be wound up if they are satisfied that the scheme ought to be replaced by a different scheme, or that it is no longer required. Under c.12(4) as part of the order enactments which contain or provide for such schemes can be altered or repealed.

On application, under **clause 13**, to the High Court (or Court of Session), the Authority can apply for an injunction (or an interdict in Scotland) to prevent any person from misusing or misappropriating the assets of an occupational pension scheme. The court must be satisfied that there is a reasonable likelihood that a person will commit or repeat such an act.

Clause 14 provides for the restitution of assets which have been wrongly paid to the employer. If (a) assets appear to have been illegally distributed to the employer (in contravention of the provisions set out in clauses 34, 70, and 71), or (b) if loans or other financial assistance have been provided by the trustees to the employers (in contravention of clause 35), then the High Court (or Court of Session), on application from the Authority, can require the employer to make restitution by restoring the position to what it was before the illegal transaction was carried out. Clause 34 gives the trustees the power to make payments from pension scheme surpluses to the employer in certain circumstances. Clause 70 requires the consent of the trustees before the surplus of a scheme on winding up is distributed to the employer. Clause 71 provides further conditions which must be satisfied before assets which are undistributed after all liabilities have been met on the winding up of a scheme can be distributed to the employer. Clause 35 limits the powers of the scheme to invest in 'employer-related investments' to an amount set out in regulations. Employer-related investments include shares and other securities in the employer's company, property and land which is used by the employer, and loans to the employer. Currently schemes are required by the Inland Revenue to limit self-investment to 5 per cent and this is likely to be the prescribed figure.

The Authority also has the power to issue written directions in certain circumstances (**clause 15**). These include where the employer has failed to make the necessary arrangements for paying the benefits due to members (under clause 43(5)). The Authority can also require a statement which it has prepared to be included in a scheme's annual report, or, if such a report is not normally issued, require a statement to be sent by the trustees to scheme members.

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Clauses 16 - 18: Member-nominated trustees

Clause 16 provides for the selection of trustees by the members of the scheme: these trustees are known as member-nominated trustees. The trustees are responsible for ensuring that the requirements of this clause are implemented. Every scheme must have at least two member-nominated trustees (or at least one, if the scheme has fewer than 100 members). At least one third of the total number of trustees must be member-nominated. A member-nominated trustee, who has been nominated and selected by appropriate rules, becomes a trustee automatically by virtue of that selection. Above the minimum ratio, the employer has a right of approval over any other member-nominated trustees. Member-nominated trustees cannot be removed by the other trustees unless they all agree (16(3)(c)). The functions of a member-nominated trustee must not differ from those of other trustees: this is an essential requirement of trust law, since all trustees are equally responsible for the interests of all members of the scheme. If the members wish to nominate as a trustee an individual who is not a member of the scheme (a trade union official or a lawyer, say), then the employer can require the arrangements for his selection to provide that such a person must have the approval of the employer to qualify for selection (16(9)).

Member-nominated trustees must be elected by 'appropriate rules': these are either an off-the-peg prescribed set of rules, or scheme rules which have been approved under a statutory consultation procedure. For the latter, both active and pensioner members would need to have been consulted, and where the trustees wish, the deferred members also. The arrangements must make provisions for cases where the number of nominations is not enough for the vacancy to be filled. They must also determine a period of office for the member-nominated trustee: this must be between three and six years, with a right to be eligible for re-selection at the end of the period. If a member-nominated trustee is elected as a member of the scheme, then should he cease to be a member of the scheme he automatically ceases also to be a trustee.

Schemes can avoid clause 16's requirement for the nomination and selection of member-nominated trustees, if a valid proposal is made by the employer that the existing arrangements for selecting trustees continue, or that some new arrangements are adopted (**clause 17**). Such proposals will apply unless they are rejected within a prescribed period as part of the statutory consultations, which must include consultations with the active and pensioner members of the scheme, as well as the deferred members of the scheme if the trustees so choose. The sanctions available under clause 10 apply to any employer who does not implement the statutory consultation procedure (17(5)). Clause 17 is designed to allow schemes which want to retain their present trustee arrangements, or to alter their arrangements without the expense and bureaucracy of the procedures implied by clause 16. **Clause 18** allows time limits

to be set for the various arrangements under clauses 16 and 17; it also permits the Secretary of State to modify both sections by regulations for prescribed cases. The procedure for obtaining the views of members in schemes, as required, is to be prescribed.

Clauses 19 - 23: Independent trustees

These clauses govern situations where the employer (for the purposes of the scheme) is replaced by an insolvency practitioner or the official receiver acting as a liquidator or a receiver (as defined in **clause 19**). Under **clause 20**, where the employer's affairs are being handled by an insolvency practitioner or the official receiver, then the receiver or practitioner must either make sure that one of the trustees is independent or if necessary appoint an 'independent trustee' to the scheme. An independent trustee is defined as having no interest in the assets of either the employer or the scheme; moreover he must not be an associate or have a connection with the employer, the insolvency practitioner, or the official receiver. Provision is made for cases where more than one person is acting as an insolvency practitioner or an official receiver. Any member of a scheme can apply to the court for an order (under **clause 21**) requiring a receiver or practitioner to appoint an independent trustee, if they have failed to do so, as required by c. 20(1). Where the only trustee, in these circumstances, is the employer, then the employer ceases to be a trustee on the appointment of the independent trustee. The independent trustee takes on the discretionary powers of the trustees and any discretionary powers which are conferred by the scheme on the employer. Only an independent trustee (or a trustee acting with the approval of the majority of independent trustees, if there is more than one) can exercise these powers whilst clause 19 applies (**clause 22**). The independent trustee's fees are payable from the scheme's resources, and have priority over all other claims on those resources (c.22(6)). Under **clause 23** the receiver or practitioner is obliged to provide the trustees with any information which they may reasonably require, although if the costs of so doing cannot be recovered, and the trustees will not agree to paying, then he can refuse. The clause allows clause 19 to apply notwithstanding section 155 of the *Insolvency Act 1986*.

The clauses extend to partnerships, and include any debtor as defined under the *Bankruptcy (Scotland) Act 1985*. They are designed to offer even greater guarantees of a scheme's independence during a period in which the employer, active members and pensioner members might conceivably have sectional interests which could prejudice the scheme. All trustees have, in any circumstances, a duty to act in the scheme's best interest at all times.

Clauses 24 - 28: Trustees: general

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A trustee of a scheme (or anyone connected to a trustee) is not allowed to act as auditor or actuary to the scheme. Similarly, a firm is not allowed to act as an auditor or actuary to a scheme if any partner (or their connections and associates) is a trustee of the scheme (**clause 24**). Under **clause 25** it is an offence to contravene clause 24, and it is punishable by a fine not exceeding the statutory maximum (on summary conviction), or on conviction on indictment, by imprisonment or a fine or both. Acts done by auditors or actuaries who are ineligible for the position under clause 24 do not become invalid simply because the person was not entitled to hold that office.

Under **clause 26** the following persons are disqualified from being trustees of any scheme: if they have been convicted of any offence involving dishonesty and deception²⁹; if they are an undischarged bankrupt (or Scottish equivalent); if they have yet to be discharged from some other agreement with their creditors; or if they are subject to a disqualification order under the *Company Directors Disqualification Act 1986*, or an order following failure to pay under a county court administration order. Under clause 26(3), the Authority can by order extend a disqualification made by itself, or by the High Court (or Court of Session), from a single scheme to cover all schemes. The Authority may also, on the application of the disqualified person, waive or revoke a disqualifying order against a person (for one scheme, a class of schemes, or all schemes). Anyone who is disqualified under clause 26 immediately ceases to be a trustee (**clause 27**). It is an offence for them to act as a trustee whilst disqualified: the same punishments as in clause 25 apply. Acts done whilst purporting to be a trustee are not automatically rendered invalid by virtue of this fact; persons moreover remain liable for acts performed by them as trustees.

Under clause 27(7), the Authority must maintain a register of all persons who have been disqualified under c.26(3); when requested, they must disclose whether the name of a person who is specified in the approach is included on the register of disqualified trustees in respect of a specified scheme.

Schemes are not allowed to indemnify or reimburse trustees for any fines or civil penalties which are imposed on them. Schemes also must not pay the premiums for any insurance policy which covers the risk of such fines or penalties (**clause 28**).

²⁹Unless the offence is a spent conviction as defined by the *Rehabilitation of Offenders Act 1974*

Clauses 29 - 34: Functions of trustees

It is up to the trustees to decide whether their decisions need the approval of all trustees, or only a majority, to be passed (**clause 29**); the voting requirements can also specify different requirements for different types of occasions, as well as any quorums and periods of notice for meetings (where there is majority voting). The rights granted by this clause override all other legislation and agreements.³⁰ Whenever majority decisions are being taken (as opposed to unanimous ones) a prescribed form and period of notice must be observed.

The next clauses deal with the investment powers of the trustees; their responsibilities for investment, and their powers to delegate investment to others. **Clause 30** prohibits any limitation of the trustees' liability to take care and exercise skill in the performance of investment functions. The trustees have the same powers to invest the assets of the scheme which they would have if they were themselves absolutely entitled to the assets of the scheme (subject to any restrictions imposed by the individual scheme) (**clause 31**). They may delegate any investment decisions to a fund manager who is authorised under section 191 of the *Financial Services Act 1986*. If they have satisfied themselves that the fund manager has appropriate knowledge and experience for this task, and that he is carrying out the task in accordance with clause 33 (making appropriate investments and obtaining proper advice), then the trustees are not responsible for any act or default made by the manager. The trustees can also choose to delegate investment decisions to two or more of the other trustees, or to a fund manager who is not an authorised person (under section 191 of the *Financial Services Act 1986*). In these cases, though, the trustees remain collectively liable for any acts or defaults of the delegated persons.

Trustees are required to prepare and keep up to date a written statement of the principles which govern the investment decisions of the scheme (**clause 32**). This must include their policies on choosing investments and maintaining solvency; the types of investments which they will hold; and policies on risks and returns. Trustees must take advice from a qualified person when they prepare and revise the statement, and they must also consult the employer. Where trustees neglect obligations under this clause, they are liable to the sanctions of clauses 3 and 10.

³⁰Note however that three provisions in this Bill are not overridden: special powers are reserved to Authority appointed trustees (c.8(4)(b)) and independent trustees in insolvency situations (c.22(2)); and under c.16(3)(c) member-nominated trustees can only be removed if all the other trustees agree.

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Clause 33 requires trustees and their managers to exercise their investment powers in accordance with this clause. They must bear in mind the need for diversification (rather than concentrating on one or a few types of investment), and consider the suitability of any proposed investments for the scheme's requirements. Before investing, the trustees shall take advice on whether these two criteria are met by the proposed investment (c.33(3))³¹. Trustees must also decide how often retained investments should be reconsidered, and take advice accordingly (c.33(4)). They must also take account of the principles set out in clause 32. In order to comply with this clause, the advice must either be written or have been confirmed in writing; in the case of 'investment business' it should come from an authorised person under section 191 of the *Financial Services Act 1986*, or, for other business, from a suitably qualified individual.

Clause 34 applies to ongoing exempt approved schemes, that is schemes which are approved by the Inland Revenue and which qualify for tax relief accordingly. If the scheme confers a power for anyone to make payments to the employer from the scheme's funds, this power is automatically conferred on the trustees. This power can only be exercised if the trustees are satisfied that proposals for the payment conform to para 6(1) of Schedule 22 to the *Taxes Act 1988*; that it is in the interests of the members for the power to be used in the manner which is proposed; that pensions under the scheme have been increased by the required percentage; and that the members of the scheme have received proper notice of the proposal to use the power to make payments to the employer (c.34(4)). Under subclause (5), which applies in prescribed circumstances only, the Authority must also be satisfied that the requirements of subclauses (3) and (4) are satisfied.³² The clause does not apply to payments which are not covered by s.601(2) of the *Taxes Act 1988*³³, and in prescribed circumstances, the application of the clause on certain classes of scheme may be modified by regulation.

³¹The requirement to take advice is waived where the investment is of the kind described in Part I of Schedule 1 of the *Trustee Investments Act 1961*.

³²c.34(3) prevents the power to make payments (c.34(1)(a)) from being exercised unless subclause (4), and *in prescribed circumstances* subclause (5), have been satisfied.

³³*ICTA* s.601(2) applies a tax charge of 40 per cent to payments to employers; s.601(3) exempts from this charge payments which would otherwise have been exempt, payments for which the Board of the Inland Revenue has been approached lest the payment could lead to withdrawal of approval under s.19(3) of the *Finance Act 1970*, or any payment of a prescribed description.

Clauses 35 - 36: Functions of trustees or managers

Clause 35 relates to self-investment. Since the employer is required to make contributions to an occupational pension scheme on behalf of the scheme's active members, and also to top-up the scheme if it cannot match its liabilities, it is clearly dangerous if the employer's company and the pension scheme are interdependent. If the scheme is invested back in the company, or has advanced loans to the company, then should the company fail, the scheme is also at risk. Current Inland Revenue rules impose a threshold for self-investment of 5 per cent of the scheme's assets: this limit is to be retained. Clause 35 limits the powers of a scheme to invest in 'employer-related investments' to an amount set out in regulations. Employer-related investments include shares and other securities in the employer's company, property and land which is used by the employer, and loans to the employer. Trustees face the sanctions of clauses 3 and 10 if the prescribed restrictions of c.35(1) are exceeded; it is also an offence for a manager or trustee to fail to take reasonable steps to secure compliance, subject to a fine, or imprisonment, or both (depending on the type of conviction).

Clause 36 deals with the documents which must be made available for members. Regulations can be made under this clause to require trustees or managers to make available to members and other specified persons at prescribed times certain documents relating to the scheme. These documents are the scheme's audited accounts; an auditor's statement on the contributions under the scheme; and an actuarial valuation and statement on the assets and liabilities of the scheme. Where schemes are subject to the minimum funding requirement (see clauses 50 - 55 below) they must provide the actuarial valuation and certificate required by clause 51 (stating whether the contributions meet and will continue to meet the level required to maintain or attain solvency over a certain period). As well as the scheme's members, prospective members, the spouses of members and prospective members, those who qualify or might qualify for benefits from the scheme, and trade unions with a recognised bargaining role for members and prospective members are all entitled to receive these documents. There are powers for regulations to prescribe the persons who may act as auditors and actuaries for the purpose of producing these documents, and for the form and content of the documents to be determined by regulations.

Clauses 37 - 40: Time off for trustees

Employers must allow employees who are trustees of their trust scheme time off during working hours for performing the duties of a trustee, and for undertaking relevant trustee training. Employees are allowed reasonable amounts of time off, based on the time required for trustee duties and training, but also on the circumstances of the employer's business and

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the effect of the employee's absence on the business (**clause 37**). Employees can make a complaint to an industrial tribunal if they have not been allowed time off in accordance with this clause (c.37(3)). Employees must be paid as if they had been working during the time which they had to take off (**clause 38**): a breach of this clause can be taken to an industrial tribunal also. There is, however, a time limit for complaints to be brought to tribunals under clauses 37 and 38: three months from the date of the failure, or if that is judged not to have been practicable, then within any further period considered reasonable by the tribunal (**clause 39**). The tribunals can award 'just and equitable' compensation where time off was not permitted; if it finds that the employee has not been paid in accordance with clause 38 whilst on trustee business, then the employer can be ordered to pay the due amount (**clause 40**).

Clauses 41 - 42: Advisers

These clauses provide for the professional advisers to a scheme: the auditor and scheme actuary; the fund manager and legal adviser. Under **clause 41** it is a requirement that every trust scheme have an auditor and an actuary, and - if the scheme has investments as defined by the *Financial Services Act 1986* - a fund manager. Such posts must be appointed by the trustees. Regulations can be made to specify the qualifications and experience which is required by professional advisers; regulations can also provide for the way such advisers are appointed, and their terms of appointment (c.41(5)). Subject to such regulations, it is for the trustees to determine the terms on which professional advisers are appointed. If trustees have not appointed an auditor or actuary, then the sanctions of clauses 3 and 10 may apply. Regulations may provide that the employer and the auditor and actuary be required to disclose information to the scheme's trustees and professional advisers; equally, regulations may impose duties on the trustees to disclose information and documents to the professional advisers.

If the scheme has any other appointed advisers, such as legal advisers or fund managers, *who have not been appointed by the trustees* then the sanction of clause 3 applies to any trustee who relies on the advice or judgement of such persons.

Clause 42 places the auditor and the actuary under an obligation to whistle-blow. If either of these persons has reasonable cause to believe that an employer, trustee, adviser or any prescribed person is not complying with a duty under the relevant legislation, and that this failure to comply is of material significance to the regulatory Authority's work, then they must immediately send a written report to the Authority. There is also an obligation for a written report of any prescribed matter to be sent in prescribed circumstances to the Authority. The

sending of such a report does not constitute a contravention of any duty which the auditor or actuary owes to the scheme. If they fail to send a written report in appropriate or prescribed circumstances, then they become liable to a civil penalty under clause 10. Auditors and actuaries who fail to whistle-blow can be disqualified by the Authority from similar positions at a specified scheme, schemes or all schemes. It is offence to act as an auditor or actuary to a scheme whilst disqualified under this section.

Clause 43: Receipts, payments and records

This clause deals with record-keeping and the making of payments and taking of receipts. Many of its clauses allow for additional regulations to be made, and are not themselves specific. Under **clause 43**, trustees must keep money which they receive in a separate account at a recognised bank. Trustees can be required by regulation to keep records of their meetings and to maintain books and records of prescribed transactions. Employers (and prescribed persons) may also be required by regulation to maintain records and books of prescribed transactions. The form and manner of these records can be prescribed by regulations. Regulations must require employers to pay into a separate account at a recognised bank payments of benefit which have not been made to members within a certain period. Sanctions apply to breaches of these clauses. It is also an offence under this section for an employer to make deductions from earnings for pension contributions and then not pay the amount deducted over to the pensions scheme's trustees or managers within a reasonable time.

Clause 44: Resolution of disputes

This clause requires the trustees and managers of a scheme to put in place a system for resolving disputes between prescribed persons about scheme matters. In the first instance there should be a person whom a complainant can apply to for a decision. This decision is then subject to confirmation (or a new decision) by the trustees or managers if a complainant wishes to refer the dispute to them after the initial decision. Both the application and decisions must be in writing. Regulations can be made under **clause 44** to provide for applications for decisions, and the procedure for reaching such decisions, including the setting of time limits. Existing schemes must have the appropriate arrangements in place at the commencement of this clause.

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[Clauses 45 - 49: Indexation

These clauses provide for pensions under occupational schemes to be increased annually by a certain percentage. They also amend the requirements under the *Pension Schemes Act 1993* relating to the Guaranteed Minimum Pension to take account of the effect of the indexation proposed here. For more information on these clauses see Research Paper 95/48, Section II. A]

Clauses 50 - 55: Minimum funding requirement

These clauses seek to ensure that pension schemes have sufficient assets to meet their liabilities; although the outline of the system which will enforce this match is available, the actuarial procedures, which are to be prescribed and on which so much depends, are not included on the face of the Bill (see also clause 111).

Clause 50 requires all occupational pension schemes to make sure that the value of their assets is at least as great as their liabilities. This was known as minimum solvency, but was renamed in the Lords 'minimum funding'. The way in which both assets and liabilities must be calculated will be prescribed. Money purchase schemes (which do not pay a guaranteed benefit) and certain other schemes are not subject to this clause. The two checks on a scheme's abilities to fulfil its obligations will be a full actuarial valuation of the scheme, complemented by an actuarial certificate which is less demanding to produce (**clause 51**). The full valuation will happen less frequently than the issuing of a certificate: the occasions and intervals at which both are required will be prescribed, as will their forms and contents. (The White Paper suggests that the certificate should be annual, and that the full valuation should happen at least once every three years.) The trustees of the scheme are responsible for seeing that the valuation and certification take place. The actuarial certificate must state the opinion of the scheme's actuary as to whether the level of contributions into the scheme is sufficient to ensure that the minimum funding requirement will continue to be met throughout the prescribed period, or if it is not currently met, that it will be met by the end of the prescribed period. Any other relevant changes to the scheme since the last full valuation must also be mentioned. If the actuary states in the certificate that the scheme does not or will not meet the minimum funding requirement, then the managers or trustees must obtain a full valuation within six months (or, in prescribed circumstances, within a prescribed period). A valuation or certificate must be made available to the employer within seven days of its receipt. The sanctions of clauses 3 and 10 apply if trustees or managers do not fulfil their obligations under this clause.

Clause 52 requires trustees to draw up a schedule of contributions to the scheme. These must be agreed with the employer, and certified by the actuary. The schedule should show the rate of contributions which are payable to the scheme (by the employer and the active members), and the dates on which the contributions are due. The schedule can be revised at any time if the revisions are agreed by the trustees or managers and the employer, and certified by the actuary. They have to be revised after each full valuation. The actuary cannot certify the contributions unless he is satisfied that the rates will ensure that minimum funding is maintained, or that it will bring the scheme into that state within a prescribed period. The Authority can extend this prescribed period, in prescribed circumstances. The sanctions of clauses 3 and 10 apply to this clause also.

If the agreed contributions schedule is not maintained, then the trustees or managers of any scheme covered by the funding requirement must inform the regulatory Authority of this fact within a prescribed period (**clause 53**). They must also inform the scheme's members. If the trustees or managers find that the minimum funding requirement is not met at the prescribed times, then they must prepare a report which has to contain prescribed information about why the funding requirement has not been met.

There are special procedures where an occupational pension scheme is revealed to be seriously underfunded. These procedures are triggered, under **clause 54**, when a full valuation shows that the assets of the scheme are less than 90 per cent of its liabilities. The difference between full funding and this 90 per cent trigger is known as the shortfall. When a shortfall is discovered after a full valuation, then the employer is obliged (c.54(2)) to increase the scheme's assets to wipe out the shortfall, either by a payment to the trustees or by another prescribed method. The increase in value has to be secured within a prescribed period (one year is the latest indication, extended from an original intention of 3 months), although the Authority can, in prescribed circumstances, extend the period which is allowed for payment. If the employer fails to make the necessary payment within the period allowed, then the trustees or managers must report this fact within fourteen days to the Authority and to the scheme's members. If the trustees fail to report this event, then clauses 3 and 10 apply to them. Under **clause 55** there is provision for regulations to modify the application of the clauses on minimum funding requirement in prescribed circumstances.

The length of the period during which employers will have to bring a seriously underfunded scheme back to full funding is very important. If the period is too short, then there is a risk of the employer's company being seriously damaged by the financial burden of the payments. If, however, too long a period is permitted, then schemes will be allowed to operate for a long time with inadequate funding and the clauses on minimum funding will offer very little protection to a scheme's membership. The Government has indicated that one year will be

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allowed for the emergency restoration to 90 per cent funding, and five years to attain full funding.

[Clauses 56 to 60: Equal treatment

These clauses apply an equal treatment provision to the membership of all schemes and to the treatment of all members. Benefits attributable to service on or after 17 May 1990 will also be subject to the equal treatment rule. This change derives from a ruling of the European Court of Justice in 1990 in *Barber v. Guardian Royal Exchange*. For a discussion of these clauses see [Research Paper 95/48, Section II.B](#)]

[Clauses 61 - 66: The Modification of schemes

These clauses provide, in general, for the protection of the entitlements and accrued rights of scheme members, by limiting the circumstances in which schemes can be modified. The Authority will be able to modify schemes, on application, in certain circumstances, including terms relating to the distribution and reduction of surpluses. For a discussion of these clauses see [Research Paper 95/48, Section II.C](#)]

[Clauses 67 - 71: The winding up of schemes

These clauses deal with the distribution of assets when a scheme is wound up, and with the priority order for the distribution of assets. Clause 70 requires the consent of the trustees before the surplus of a scheme on winding up is distributed to the employer. Clause 71 provides further conditions which must be satisfied before assets which are undistributed after all liabilities have been met on the winding up of a scheme can be distributed to the employer or to the members. For a discussion of these clauses see [Research Paper 95/48, Section II.C](#).]

Clauses 72 - 74: Pensions Compensation Board

These clauses establish a Pensions Compensation Board (its constitution is set out in [Schedule 2](#) of the Bill). The Board, like the Authority, will be funded from a levy on schemes (see clause 149); in the case of raising funds for compensating schemes, this will be a post-event

levy, raised as and when needed.³⁴ The Secretary of State will appoint a minimum of three members to this Board, including a Chairman (**clause 72**). One member will be appointed after consulting with employers' organisations, and another after consulting employees' organisations. The Chairman will also be consulted on these two appointments, and additional members can also be appointed. The Board has the power to borrow money. The Board is to publish an annual report which will be laid before Parliament (**clause 73**). Although the Board's decisions will be final, the Board can review its own decisions in certain circumstances (**clause 74**).

Clauses 75 - 80: Compensation

Under **clause 75**, compensation is available from the Board for trust schemes in the following circumstances only: where the employer is insolvent, the assets appear to have been depleted by a prescribed offence, and (for salary related trust schemes) where the scheme's liabilities exceed its assets by more than ten per cent.

Claims must be made within twelve months of the employer's insolvency, or within twelve months of the auditor, actuary or trustees discovering the reduction in the assets - whichever is the later (**clause 76**). The amount of compensation available is, for salary related schemes, enough to enable the scheme to meet 90 per cent of its liabilities; for other schemes 90 per cent of the reduction in the scheme's assets is available (**clause 77**). Advance payments can be made under **clause 78** though such payments (and overpayment) are repayable if the scheme is found not to be eligible for compensation. There is provision for the surplus funds of the Board to be distributed among occupational schemes, exercisable by order of the Secretary of State after consultation with the Board (**clause 79**). Compensation provisions for prescribed classes or types of scheme can be modified by regulation (**clause 80**).

Clauses 81 - 83: Money purchase schemes

In money purchase schemes, the benefits are not salary-related, but instead depend upon the investment performance of the accumulated payments into the fund by the employer and/ or the scheme members. Because such schemes do not produce a defined benefit which has to be paid to members when they become pensionable, the minimum funding provisions of clauses 50 to 55 do not apply to money purchase schemes (c.50(2)(a)). Clause 51 above included provisions for defined benefit schemes to have in place a contributions schedule

³⁴ See White Paper, Appendix 4

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which would allow the liabilities to be met. Clauses 81 to 83 require a modified contributions schedule for money purchase schemes. The trustees or managers must prepare and maintain a contributions schedule for money purchase schemes which shows what contributions are required and when they must be made. The schedule must have been agreed by the trustees or managers with the employer; or in the absence of such an agreement, by the trustees or managers (**clause 81**). If agreed payments are not made on time, then the trustees or managers must report this to the Authority within a prescribed period; unpaid contributions become a debt from the employers to the trustees or managers (**clause 82**). The sanctions of clauses 3 and 10 apply to trustees and managers who do not comply with their obligations under clauses 81 and 82. **Clause 83** determines the extent of the Secretary of State's obligation under section 124 of the *Pension Schemes Act 1993* to pay unpaid contributions in the event of the employer's insolvency.

[Clauses 84 - 87: Assignment and forfeiture

These clauses protect pension rights and entitlements by providing that they cannot be assigned or have a charge or any other claim set against them; they cannot pass to a trustee in bankruptcy; nor can they be forfeited. A new clause passed in the Lords (clause 85), however, deals with arrangements relating to pensions on divorce. For a discussion of some these clauses see Research Paper 95/48, Section II.D]

Clauses 88 - 89: Questioning the decisions of the Authority

Clause 88 lays down that the decisions of the Authority are final, although where trustees have been prohibited from office (under clause 3), fined (under clause 10), or disqualified from holding the position of trustee (under clause 26(3)) the Authority must review their decision if the affected person asks them to. The Authority can also review other decisions made by it on application if the circumstances have since changed, or the decision appears to have been made in ignorance of a material fact, or was wrong on a point of law. Under c.88(5) regulations can be made about the procedure for such reviews, following consultation with the Council for Tribunals (c.88(7)). The Authority can refer matters which involve a point of law to the High Court or the Court of Session (**clause 89**), and those who are unhappy with the Authority's determination of a decision on review, or of the Authority's refusal to review a determination, can appeal to the court.

Clauses 90 - 95: Gathering information

These clauses give the Authority a number of powers to enable it to carry out its work. **Clause 90** requires a trustee, manager, professional adviser, employer or any other person to produce any documents which are relevant to the Authority's functions if required to do so in writing. **Clause 91** gives the Authority's inspectors the right to enter and inspect premises and to require the production of documents and the examination of individuals. This power extends to any premises where members of an occupational scheme may be employed, or where work connected with the administration of a scheme may be carried out, or where documents connected with the administration of a scheme may be kept, except for private dwelling-houses which are not used for trade or business purposes. **Clause 92** provides for a justice of the peace to issue a warrant authorising inspectors to enter a premises and take possession of documents; persons named in the warrant must provide an explanation of such documents or state where they may be found. **Clause 93** provides penalties for those who neglect or refuse to comply with orders to produce information, or who knowingly produce false or misleading information. **Clause 94** provides that nothing in clauses 90 - 93 requires a person to incriminate themselves or their spouse, nor to set aside the protection of legal professional privilege. **Clause 95** authorises the Authority to publish the results or reports of investigations under Part I of this Bill in whatever form or manner they choose; such publication is to be regarded as privileged from an action for defamation.

Clauses 96 - 101: The Disclosure of Information

Clause 96 prevents information which has been gathered by the Authority under the Act ('restricted information') from being disclosed in a form which allows any individual concerned to be identified unless the information is already public knowledge, or the permission of the individual concerned and the person from whom the Authority obtained the information has been obtained. It is an offence to contravene this clause. **Clause 97** includes information supplied to the Authority by their corresponding overseas authorities within the terms of 'restricted information' under clause 96. Information from overseas authorities can only be disclosed in accordance with clause 96, or to allow the Authority to discharge its functions under the Bill, or to institute criminal proceedings. **Clauses 98** and **99** permit the disclosure of information, despite clause 96, if it is necessary for the Authority to do so to fulfil its functions, or if it needs to obtain specialist advice from a qualified person. Information can also be disclosed to other regulatory bodies and individuals to allow them to carry out specified functions: the bodies and their functions are specified in the table under clause 99. Neither clause 98 or 99 applies to information which has been obtained from overseas authorities. Clause 96 does not prevent the Authority disclosing to the Secretary of

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State information which is in the public interest or in the interest of members of occupational pension schemes (**clause 100**); information may also be released for various disciplinary purposes and to assist proceedings under specified acts; and also to assist corresponding overseas authorities carry out their functions, or to comply with a Community obligation. **Clause 101** permits the disclosure of tax information to the Authority, with certain safeguards.

Clauses 102 - 106: Gathering of information by the Compensation Board

These clauses apply similar provisions to clauses 90 - 95 (gathering of information by the Authority) to the gathering of information required by the Compensation Board. They require information to be disclosed (c.102); set penalties for failing to provide information, or for providing false or misleading information (c.103); and allow for the publication and dissemination of information gathered under these clauses in specified circumstances (cc.105-106).

Clauses 107 - 116: General Provisions

Clause 107 provides that where offences are shown to have been committed by an individual company officer or member, by a partner of a partnership, or an officer or member or governor of an unincorporated association then the individual is guilty of the offence as well as the corporate entity, partnership or association. **Clause 108** makes it an offence to contravene or fail to comply with any regulations made under Part I, subject to a fine on summary conviction not exceeding £5,000. Offenders cannot be punished under this clause and by means of civil penalties levied under clause 10 for the same offence. **Clause 109** provides that Part I and its subordinate legislation will override any contradictory provisions in the rules of an occupational pension scheme. **Clause 110** provides for regulations which can modify certain clauses in the Bill. **Clause 111** provides that the value of assets and liabilities under clauses 50(3), 67(3) and 69 can be calculated and verified against guidance which has been prepared or revised by a prescribed body, as long as the guidance has been approved by the Secretary of State. This important enabling clause means that the rules regarding the calculation of the minimum funding requirement can be delegated to another authority, outside Parliament. **Clause 112** (a new clause) requires the Secretary of State to consult appropriate organisations before making regulations under Part I. This requirement does not apply if the regulations are urgently required, or if they are made within six months of the relevant provision coming into force. **Clause 113** gives effect to the consequential amendments which are detailed in Schedule 3. **Clause 114** applies the definitions of connected and associated persons from bankruptcy legislation to clauses 20(2)(b), 24, 25 and 35. **Clause 115** introduces definitions of terms used in this Part of the Bill. **Clause 116** expands on the

interpretation of certain terms in this Part, by defining a salary related scheme; the clause also allows for regulations to be made altering the interpretation of the terms 'member' and 'employer'.

PART II

State Pensions

[Clauses 117 - 122. These clauses deal with the equalisation of the State Pension Age, and transitional provisions associated with the change. Clause 117 is a new clause passed in the Lords which restores the war widow's pension to previous recipients after a second bereavement or end of a second marriage. For a discussion of these clauses see [Research Paper 95/47](#)]

PART III

[Certification of Pension Schemes and the Effects on Members' State Scheme Rights and Duties

Clauses 123 - 135. For a discussion of the major issues behind these clauses see [Research Paper 95/48, Section II.E - G](#)]

PART IV

Miscellaneous and General

Clauses 136 - 138: Transfer values. [See [Research Paper 95/48, Section II.G](#)]

Clause 139: Breach of Regulations under the *Pensions Schemes Act 1993*

Clauses 140 - 144: Pensions Ombudsman. These clauses amend the powers of the Pensions Ombudsman. [See [Research Paper 95/48, Section II.G](#)]

Clause 145: Repeals sections 136 to 143 of the *Pensions Schemes Act 1993*

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Clauses 146 - 148: Personal Pensions. These clauses provide for annual percentage increases in contracted out personal pensions. [For a discussion of these clauses see Research Paper 95/48, Section II.A]

Clause 149: Levy. This clause replaces section 175 of the *Pensions Schemes Act 1993*. It adds the Regulatory Authority and the Compensation Board to the permitted items of expenditure covered by the levy on pension funds.

Clause 150: Pensions on divorce. [For a discussion of this and related clauses see Research Paper 95/48, Section II.D]

Clauses 151 - 2: Pensions for dependants of the Prime Minister and the Speaker.

Clause 153: Gives effect to Schedule 6 (minor and consequential amendments)

Clause 154: Crown employment. Applies Part I to those in Crown employment, except for those in Her Majesty's forces.

Clause 155: Gives the power for regulations or orders to be made by Statutory Instrument.

Clause 156: Provides that orders and regulations under this Bill shall be subject to the negative procedure, except for regulations under c.58(4) and c.72(6) (relating to exceptions of the equal treatment rule and the borrowing limit of the Compensation Board) which must be laid before and approved by both Houses. During the Bill's passage in the Lords, the power to make criminal offences by Regulations (under c.108(1)) was also made subject to the affirmative procedure.

Clauses 157 - 162 determine the Extent, applicability in Northern Ireland, Commencement and Short Title of this Bill. The following clauses come into force when the Bill receives Royal Assent: clauses 56 - 60 (equal treatment of members of occupational schemes); Part II (preparation for the equalisation of state pensionable age, subject to Schedule 4); clause 151 - 2 (pensions for dependants of the Prime Minister and Speaker). Clause 150 (pensions in matrimonial settlements) will take effect according to a statutory instrument issued for the purpose by the Lord Chancellor. The remaining provisions will be brought into force by statutory instrument issued by the Secretary of State and are expected to take effect (subject to phasing in procedures) from 1997.

SCHEDULES

Schedule 1: Occupational Pensions Regulatory Authority

Schedule 2: The Pensions Compensation Board

Schedule 3: Amendments consequential on Part I

Schedule 4: Equalisation.

Part I: Pensionable ages for men and women

Part II: Entitlement to certain pension and other benefits

Part III: Consequential amendments

Schedule 5: Amendments relating to Part III

Schedule 6: General minor and consequential amendments

Schedule 7: Repeals

Part I: Occupational pensions

Part II: State pensions

Part III: Certification of pension schemes

Part IV: Miscellaneous and General

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Economic policy & taxation

93/115	Financial Services: Regulators and Ombudsmen	10.12.93
94/70	Financial Services: Self Regulation and the Personal Investment Authority	16.05.94
95/10	Pension Fund Regulation	23.01.95

Social security

95/47	The Pensions Bill: Social Security Aspects	19.04.95
95/48	The Pensions Bill: Non-state Benefits	18.04.95