Private Edge Knowledge Bank

Legal pitfalls of pensions trusteeship

PENSION TRUSTEE LIABILITY

Complaints of maladministration before the Pensions Ombudsman and breach of trust claims can use up a substantial amount of trustee time and resources. Trustees must be aware of what protection they have under their scheme's governing documentation, in law and under any applicable insurance in order to effectively deal with the legal pitfalls of handling such complaints and claims.

Maladministration complaints before the Pensions Ombudsman

With trustee decisions now subject to ever increasing scrutiny from members, a complaint before the Pensions Ombudsman has the potential to consume a large amount of trustee time and resources. A complaint before the Pensions Ombudsman:

deals with disputes of fact or law;

maladministration involving those responsible for managing occupational or personal pension schemes.

There is a wide category of persons who can bring a complaint, although generally the Ombudsman will only investigate the complaint if the individual has exhausted the process under the scheme's internal dispute resolution procedure. Once written submissions are received by the Ombudsman, a written determination will be issued and the Ombudsman has statutory power to order parties to take or refrain from taking particular steps. There have been complaints that have resulted in the Ombudsman directing trustees to pay any compensation awarded personally, which is why it is important for trustees to know and understand the provisions of their scheme documents which cover exoneration and indemnity for personal liability.

Whatever the outcome of a determination from the Ombudsman, the trustees are likely to have spent a great deal of resources on dealing with the complaint, including obtaining legal advice. Trustees must therefore be aware of the protections they have for covering them for these expenses as well as understanding their own personal position, particularly where they are being accused of breach of trust.

Protection in law

Although there are limited statutory defences and discharges available to trustees they do not provide trustees with sufficient comfort that they will not be personally liable for mistakes made. Section 61 of the Trustee Act 1925 does provide that a court can relieve a trustee of personal liability if they have "acted honestly and reasonably" and "ought fairly to be excused". This is very much a protection of last resort and should never be considered by trustees as a replacement for exoneration, indemnification or trustee liability insurance.

Exoneration from mistakes

In the context of a trustee being sued by a member personally for breach of trust, it must be remembered that as a trust does not have legal personality, any claim will be against the trustees and under the concept of 'joint and several liability', one trustee could be held liable for a breach of trust committed by a fellow trustee.

Breach of trust claims cover a number of possible areas, including:

- failure to comply with the terms of the trust
- dishonesty
- negligence
- breaching any of their legal obligations under trust law and pensions legislation.

A breach of trust can occur even when the breach is not deliberate. For claims against trustees brought by scheme members, the first line of defence will come from an exoneration clause in the scheme's legal documents. Depending on how the clause is drafted, it may potentially exonerate a trustee from all forms of liability, except dishonesty. Trustees should review their own exoneration clause carefully and take legal advice if necessary to establish what liability is exonerated and what is not.

Indemnification

If a trustee is not directly exonerated by the scheme's own trust documentation or the exoneration clause does not otherwise apply it is possible that a trustee may also be covered by an indemnity provision. This could either be contained in the scheme's documentation or be separately provided (for example, in a deed of indemnity which covers trustees on the happening of a specific event or transaction). The wording of the indemnity is absolutely crucial as there is no one size fits all approach and indemnities can vary significantly from scheme to scheme.

Trustees must be clear on:

- who is providing the indemnity (is it from scheme assets, the scheme employers or both?)
- if multiple participating employers are providing indemnity coverage, how the cover is split between them
- what is covered under the terms of the indemnity e.g. negligence or just wilful default
- which expenses and liabilities are covered under the terms of the indemnity
- whether scheme assets be used to meet the claim
- does the indemnity only apply if there is no insurance cover in place and whether there are any other restrictions in place.

One issue for trustees relying on an employer indemnity is that it is only as strong as the entity providing it. Another is whether the indemnity continues to apply even if the scheme is wound-up (for example, because the benefits have been bought out with an insurer). In addition, if an employer becomes insolvent, the indemnity will not provide cover and the trustees will need to rely on other forms of protection. It should, however, be noted that there are important restrictions on the scope of exoneration and indemnity clauses. For example, a trustee's liability for failure to take care or exercise skill in the performance of their investment functions cannot be excluded or restricted by an exoneration or indemnity clause.

Insurance cover

It is now extremely common for trustees to put insurance cover in place to mitigate the risks involved in relying on an employer indemnity which might not provide them with sufficient cover in the future. Such insurance can be financed out of scheme assets although it is important to note that insurance cannot cover fines from The Pensions Regulator. The insurance can also be paid for directly by the employer.

Trustees may also remain exposed to claims even after they cease to be trustees so retired trustees may wish to consider whether independent insurance is required if adequate cover is not maintained for them after they retire. Any trustees considering purchasing trustee liability insurance should fully understand how the policy works alongside any existing exoneration and indemnity provided under the scheme rules and as part of their risk management process they should review all cover from time to time to ensure they are appropriately protected.

This guidance note is not intended to constitute a definitive, up-to-date, or complete statement of the law, nor is any part of it intended to constitute legal advice for any specific situation. You should take specific advice when dealing with specific situations and jurisdictions outside England & Wales.

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