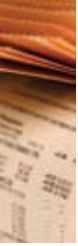




## ACE OPDU Elite

*Pension trustee  
liability insurance*



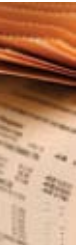
*In recent years there has been a gradual transformation of pensions from the gratuity once offered by a benevolent employer into the binding legal entitlement it represents today. Pensions have become the topic of debate in most executive boardrooms. Changes in legislation and recent court determinations are the latest culmination of a shift in the legal view of duties on pension trustees and others. This has resulted, explicitly and implicitly, in increasing the duties and obligations placed on trustees; a role which can attach personal liability if things go wrong.*

*Claims can arise from a variety of sources and for various reasons, but there are a number of protections available that can help reduce the liability exposure of a trustee. Trustees need to consider whether they are comfortable with the level of protection they are afforded should their decisions be challenged.*

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*“It is not surprising that many pension scheme trustees are thinking twice about whether the risk/reward ratio is appropriate.”*

Robin Ellison (Partner at Pinsents Mason), Financial Times, 19.07.04



### **Congratulations, you've just been made a trustee.**

Being selected as a trustee is regarded as a position of honour within an organisation and as such your new role brings with it a significant amount of kudos. Indeed, you may not realise it but as a population, trustees are fast becoming the most powerful people in the business world! Trustees look after the pension savings of millions of people, choose to back or sack some of the most talked-about fund managers in the financial world and can exert a vast amount of influence in company mergers and acquisitions. However, being a trustee can often be a thankless task in an increasingly complex industry. Considerable personal liability attaches to the role, so on appointment it is essential that you have a clear understanding of your obligations and rights so that you are in a position to discharge them properly.

- Trustees are faced with a greater number of statutory duties brought into force by the Pensions Act 1995.
- A duty of care was subsequently imposed on trustees under the Trustee Act 2000.
- More recently the Pensions Act 2004 has introduced a number of changes to the duties and obligations of trustees including a new statutory requirement for 'knowledge and understanding'.

Trustees who breach their duties or responsibilities may place their personal assets at risk should they be determined to be personally liable for any loss experienced as a result of their actions. They may also open themselves up to criminal penalties by acting improperly or fraudulently, or civil penalties by contravening statutory requirements. Add to this a generally more litigious society, scheme members becoming increasingly aware of their pension rights and the ever-increasing profile of pensions in the news of late, and it is easy to see why trustees may be feeling a little nervous.

*Irrespective of whether the claims are justified or not, the trustees may have to pay legal costs and expenses incurred whilst investigating and defending a claim . . .*

### **How can claims be generated?**

The main types of claim that a trustee may face can be categorised as follows:

- **Breach of trust/fiduciary duty**  
The most common source of litigation in the past has come mainly from scheme members and beneficiaries, and in particular relate to:
  - Actions arising from an alleged failure to pay the right people the right amount, at the right time;
  - Actions concerning the loss or diminution of trust assets.
- **Contractual claims**
  - Actions brought by those with whom the trustees contract.
- **Breach of statutory duty**
  - A failure to act in accordance with statute, although in practice such claims are likely to be brought by beneficiaries and coupled with claims for breach of trust.
- **Tort**
  - A breach of duty of care owed in tort for negligence. Such claims can be brought by third parties who are not beneficiaries or in any contractual relationship with the trustees.

Of all the cases referred to the Pensions Ombudsman during a calendar year (often over 3,000 in total), typically 98% are from members of pension arrangements, with the remaining 2% of cases coming from employers, trustees and managers.

### **How might a claim arise?**

Dissatisfied members or beneficiaries most frequently make claims ranging from a complaint progressing through the scheme's internal dispute resolution procedure to

referrals to the Pensions Ombudsman, the Pensions Regulator, or even the Courts. Irrespective of whether the claims are justified or not, the trustees may have to pay legal costs and expenses incurred whilst investigating and defending a claim brought against them in connection with their duties. These regulatory bodies have a wide collection of powers ranging from the ability to direct trustees to take certain actions to initiating proceedings for severe fines and penalties against them personally.

The most frequent enquiries directed to the Pensions Ombudsman, the Pensions Regulator or the Courts relate to:

- **Transfers**
  - Both individual and bulk transfers can give rise to complaints. In the former, these tend to be personal pension-related rather than occupational. The latter tend to be brought by individuals who believe they have suffered loss as a result of the 'incorrect' transfer of funds following a bulk transfer of membership e.g. through pension scheme mergers or new pension set ups.

#### **Claim example:**

**Trustees were responsible for a transfer of funds into a new pension scheme following the sponsoring employer's disposal of a subsidiary. The rules required the amount to be such 'as the trustees, after consulting with the actuary, decided to be just and equitable'. As such they consulted an actuary. However, just prior to the transfer date the value of the fund was enhanced by a strong stock market rise taking the scheme from a deficit position to one of surplus, the result being that the scheme members sued the trustees for not taking**



*“Trustees are now more likely to be sued, prosecuted or fined. It won’t be long before there is a serious lawsuit.”*

Donald Duval (Head of Consulting at Aon), Financial Times, 19.07.04

**this increase into account within the transfer payment. Defence costs alone were estimated to be approximately £2 million with several weeks in court, with the final costs being in the region of £5 million in total.**

- Discretionary decisions e.g. death benefits
  - Trustees are generally given discretion to decide how benefits should be distributed. However, relatives or dependants of the member may well assert competing claims. They may further claim that the trustees have not exercised their discretion properly.

**Claim example:**

**The children of a member complained that the trustees should have exercised their discretion to award benefits on the death of their father in their favour in line with his expression of wish form. Instead, a proportion of the lump sum death benefits (£80,000) were paid to his co-habitee, with the balance being placed under trust from which she would receive an income for life, with the capital going to the member’s children on her death. However, she was not a dependent within the meaning of the pension fund rules. Thus, the Pensions Ombudsman held that the trustees’ decision constituted maladministration and each trustee was ordered to pay compensation to the children, in addition to the death benefits being paid over to them. The Pensions Ombudsman’s decision was upheld in court.**

■ Ill-health cases

- Ill-health pensions have been and continue to be a common source of complaints. It is not always understood by members that different criteria may apply in deciding whether their employment should continue versus whether an ill-health pension can be paid. For example, an employer may fairly dismiss an employee because the latter’s state of health means that he or she is not presently able to do the job, but whether an ill-health pension can be paid might depend on whether the employee’s ill-health is likely to be permanent. Similarly, different criteria may apply in deciding whether the scheme member is entitled to draw benefits from the state on the basis of incapacity.

**Claim example:**

**An individual complained to the Ombudsman regarding his application for incapacity benefit. The rules of the scheme stated that no incapacity pension was payable unless the retirement was ‘in the opinion of the trustee, due to incapacity’. The Ombudsman upheld the complaints of maladministration because the trustees relied too heavily on medical advice in deciding whether the applicant satisfied the requirements of incapacity. In addition, the awarding or not of an incapacity pension is a decision of fact and is open to challenge. The trustees’ failure to provide an explanation for its reasons to reject the application fell short of the standards required by good administration. The trustees were ordered to pay compensation to the member in respect of the maladministration and were ordered to reconsider the matter.**



*It may only be a matter of time before the focus falls on investment decisions and diversity.*

- Winding up
  - Where a final salary pension scheme is being wound up, there may be a deficit in the funding. In the case of an insolvent employer this may result in a reduction in benefits, in which case the members are more likely to involve the trustees in litigation. Conversely, if the scheme is in surplus, the trustees often have the power to decide how surplus pension fund assets should be utilised. They may decide to augment benefits, perhaps of one class of beneficiary only, if they feel this is fair. However, another class of beneficiary may claim that the trustees' decision was unfair.

**Claim example:**

**A claim for breach of trust was brought against a set of trustees following a transfer of surplus assets to the employer. Despite having received legal advice that their course of action was proper and having correctly amended the scheme rules to permit the repayment, the Pensions Ombudsman determined that the way in which the trustees made the transfer amounted to an act of maladministration. The sponsoring employer was ordered to refund the surplus to the scheme.**

- Calculation of benefits
  - This heading covers a broad range of matters from simple calculation errors to allegations that promises / guarantees have not been kept and to problems caused by benefits being quoted of higher amounts than eventually turn out to be payable. Receipt of an incorrect quotation does not usually give rise to a right to receive a pension at the misquoted amount. What the member is entitled

amount. What the member is entitled to receive is a pension, which has been correctly calculated in relation to the rules of the pension arrangement. However, where an inaccurate quotation has led to a member making financial commitments that they are subsequently unable to honour, a further payment to redress the error may be due. For example, if a member has acted to his or her detriment as a result of receiving the wrong information it can be claimed that a financial expectation has been created. This is particularly relevant if the error has not been corrected within a relatively short period of time.

**Claim example:**

**In this case, the complainant decided to take early retirement based on a quotation, which later was determined to be incorrect in respect of the lump sum payment. The complainant produced evidence of careful financial planning which took into account the lump sum which he had been led to believe was available from the scheme. As such, it was clear that the individual had made plans that relied on this lump sum. The Ombudsman directed that, if the individual's application for early retirement was accepted, the trustees should pay him the lump sum figure representing the figure originally quoted less compensation already given.**

- Self-investment / loans
  - Whilst trustees are permitted to participate in self-investment and loans, as governed by legislation, these activities are always sensitive topics, particularly if anything should go wrong.



*“Pension fund trustees should be given access to liability insurance if high quality candidates are to continue to take on the role.”*

Julian Aylmer (Partner at Reynolds Porter Chamberlain), Press Release, 11.07.03

**Claim example:**

**Pension scheme trustees were required to make good a deficit in the pension scheme and thus it was agreed that payments of £5,000 a month would be made by the employer. However, the employer’s cash flow position was unstable and as a result the trustees (who were also directors and shareholders of the sponsoring employer) at the same time lent back £5,000 a month to the company. The company then went into administration. A member complained and the Pensions Ombudsman held that the loans were maladministered by the trustees and ordered them to pay the loans from their own resources (a total sum of £50,000). The trustees appealed but were dismissed.**

Whilst these are the most common issues at present, it may only be a matter of time before the focus falls on investment decisions and diversity. A respected pensions consultant told delegates at the 2004 Pensions Management Institute’s autumn conference that allowing scheme members to make investment decisions was “hugely dangerous” and could result in a large number of lawsuits in 20 years’ time. He said: “It is hugely dangerous and companies are going to have a legal or moral obligation to do something about it. If people find their retirement income is far less than they expected, they may blame the company.” In addition, given that 85% of members in a defined contribution scheme opt for the default fund (often a ‘lifestyling’-type fund), trustees must ensure that this is suitable for their membership profile and represents the best of modern thinking in terms of dynamic, asset allocation based life-styling. Furthermore, the trustees must determine the optimal number of funds to offer; too many and the choice is too complicated, too few and the choice is too restrictive.

**So what protections are available?**

- Section 61 Trustee Act 1925
  - A trustee who has been in breach of trust can try to make use of section 61 of the Trustee Act 1925:  
“If it appears to the Court that a trustee, whether appointed by the Court or otherwise, is or may be personally liable for any breach of trust...but has acted honestly and reasonably and ought fairly be excused for the breach of trust and for omitting to obtain the directions of the Court in the matter in which he committed such breach, then the Court may relieve him either wholly or partly from personal liability for the same.”
- Of course for the trustee, the problem is that section 61 does rely heavily upon the Court’s opinion as to whether they acted honestly and reasonably and ought fairly to be excused. In particular, there is the catch-22 situation that if in doubt as to whether they committed a breach of trust, a trustee ought to have made an application to the Court. Clearly such an application would only be appropriate if the trustee realised there may be a problem in the first place.
- Exoneration and indemnity clauses
  - For many years trustees have sought protection from liability by insisting upon the incorporation in trust deeds of exoneration and indemnity clauses. These clauses generally operate to excuse liability other than for an act or omission that occurs through wilful default. However, cover is likely to be narrow. A number of cases have tested the validity and construction of exoneration clauses.

*A simple  
and effective  
protection  
for trustees  
is pension  
trustee  
liability  
insurance.*

Some main points to emerge are:

- A trustee cannot be exonerated for actual fraud or subjective dishonesty.
- An exoneration clause cannot exclude statutory liability (note the new statutory requirement for 'knowledge and understanding' within the Pensions Act 2004).

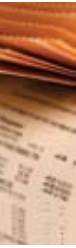
Sentiment has swung against total reliance upon such provisions as their successful operation usually entails loss to the fund, and thus to the beneficiaries thereof. Furthermore, it is difficult to ensure that the wording of an exoneration clause includes every conceivable eventuality. Where an indemnity is provided by a participating employer, it depends upon the continued existence of that employer in a state of financial health, something that cannot be taken for granted these days.

- Insurance
  - A simple and effective protection for trustees is Pension Trustee Liability Insurance.

Depending on the specific coverage afforded, this product can provide a means of protecting the assets of individual trustees, the pension scheme, the sponsoring employer and their employees against claims of wrongdoing. Where the trust deed and funding allows, the cost of this insurance can be paid for out of the fund assets. Where the latter is not allowed, or where the policy also covers fines and penalties imposed by the Pensions Act 1995 or 2004, the sponsoring employer may wish to purchase the protection on behalf of those who would be insured.



Prevention is better than cure. Training and a thorough understanding of the scheme trust deed and rules are essential. Careful delegation to experts in certain fields needs to be considered (e.g. investment managers, third party administrators etc.). However, delegation does not remove responsibility. Trustees have collective responsibility and no one is infallible. Moreover, it is important to consider that claims are often made whether justifiable or not; in these cases insurance can be invaluable to cover legal defence costs, let alone any extra costs incurred.



*Pension trustee liability insurance is gaining in significance. The recently published Code of Guidance for Independent Trustees asks independent trustees “to ensure that trustees consider whether appropriate indemnity cover is available and in place.”*

**ACE OPDU Elite pension trustee liability insurance policy**

**ACE OPDU Elite** provides a cost-effective means of protecting the assets of individual trustees, the pension scheme, the sponsoring employer and their employees where an actual or alleged wrongful act may have placed the pension scheme assets at risk.

Whilst attention is usually focused on the potential size of a settlement, it is often the costs involved in investigating and defending the action that prove to be prohibitive.

**ACE OPDU Elite** can advance funding to cover defence costs, in addition to providing cover for settlement of an action if required.

**ACE OPDU Elite** brings peace of mind, and provides trustees and the sponsoring employer with the confidence to perform their roles secure in the knowledge that they have considerable protection from one of the world’s leading insurance and reinsurance companies.

**ACE OPDU Elite** cover is far reaching and includes:

- Past, present and future trustees.
- Employees involved in the provision of services to the scheme.
- Their respective lawful spouses, domestic or civil partners, estates, heirs or legal representatives in the event of death, incapacity, insolvency or bankruptcy.
- The pension scheme.
- A corporate trustee company.
- The sponsoring employer company.
- Directors and officers thereof.

**ACE OPDU Elite** offers protection against a comprehensive range of allegations, including:

- A breach of trust.
- A breach of duty.
- A breach of statutory provision.
- Maladministration.
- Negligence.
- Administrative errors.
- Wrongful omissions.
- Misstatements.
- Misleading statements.

**Triggers**

In addition to the long-standing accountability of pension trustees and employers to court actions, there are now a number of other types of forum in which these individuals can face proceedings. **ACE OPDU Elite** responds to all of the following:

- A civil or arbitral proceeding.
- A criminal proceeding.
- An administrative or regulatory proceeding asserting legal liability for a wrongful act.
- A written demand.
- An official investigation.
- An extradition proceeding.
- A fact-finding investigation or proceeding by the Pensions Ombudsman, the Pensions Regulator, or equivalent body.
- A contribution notice as issued by the Pensions Regulator under Section 38 of the Pensions Act 2004.



*This innovative contract is the benchmark for excellence.*

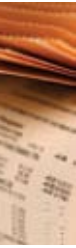
**Other key highlights**

**ACE OPDU Elite** also offers the following:

- Cover for damages, judgments, settlements, defence costs, legal representation expenses and awards (including distress awards and compensation as determined by the Pensions Ombudsman, the Pensions Regulator or any other regulatory body).
- Cover in respect of loss to the sponsoring employer or pension scheme as a result of the indemnification of trustees or others.
- Cover against loss to the pension scheme as a result of exoneration of trustees or others.
- Cover for acts committed prior to the inception of the policy.
- Cover for named pension schemes including the facility to add new pension schemes if the company is merged with or acquires another company during the policy period.
- Continuous cover in the event that the sponsoring employer company merges with or consolidates into another entity (any subsequent name changes to the sponsoring employer company and or pension scheme must be advised) or enters administration.
- Cover for schemes during wind-up with the potential to provide an extended period of cover after the wind-up has been completed.
- The ability to include coverage for a broad variety of employment benefit and welfare plans in addition to pension schemes.
- Provision to advance defence costs up to the policy limit.
- Provision for allowing notification of circumstances that are not yet a claim but may in the future give rise to a claim.
- The ability to authorise either the sponsoring employer company or the trustees to act on behalf of the other insured parties. Where the authorised party is the sponsoring employer, prior written agreement of all trustees must be obtained in order for them to effect cancellation or termination.

Furthermore, the policy can be tailored to meet the specific requirements of each individual circumstance by optionally extending the policy to provide:

- Public relations expenses (up to a specified sub limit) for the reasonable fees and related expenses of a public relations, crisis management or law firm engaged to prevent or limit adverse effects or negative publicity which it is anticipated may arise from a Claim or Investigation.
- Civil fines and penalties, where insurable, made against the insured by a regulatory body such as the Pensions Regulator provided the premium is paid without recourse or reimbursement from the pension scheme or any of its assets.
- Court application costs (up to a specified sub limit) for the reasonable legal and professional charges, costs and expenses incurred as a result of a actual or proposed proceeding to seek a declaration or direction from the Court or arbitral proceeding as to how the Trustee should act in a particular set of circumstances or in relation to a complaint made or dispute referred to the Pensions Ombudsman.
- Emergency costs provision (up to a specified aggregate limit) such that defence costs, investigation expenses, prosecution costs, mitigation expenses, public relation expenses or bail bond costs can be incurred with retrospective approval.



*Because we endeavour to understand the risks you are exposed to, we are able to share in the responsibility for some of those risks and increase your opportunity for success. With ACE as your partner, your business can move forward with greater speed and surety.*

- Employer benefit programmes and/or employee share ownership programmes as listed in the schedule or by endorsement to the policy.
- Cover for costs including defence costs, bail bond costs and public relation expenses incurred in relation to an extradition proceeding.
- Costs (up to a specified sub limit) incurred in replacing or restoring pension scheme documents in the event of their loss, damage or destruction.
- Prosecution costs (up to a specified sub limit) for the legal and professional fees, costs and expenses incurred to resist any application for or to bring legal proceedings to obtain the discharge or revocation of, for example, an order disqualifying a Trustee, an interim or interlocutory order, confiscating, freezing or creating a charge over real property or personal assets, or the deportation of an Employee or Trustee.
- 12 years of cover for trustees and employees who retire prior to the expiry of the policy should no alternative cover be put in place.
- Cover for costs incurred in the pursuit of legal proceedings against an advisor of the pension scheme for the purpose of establishing a breach of professional duty of care (up to specified sub limit).
- Theft and fidelity of pension scheme assets (up to a specified sub limit).

This innovative contract is the benchmark for excellence. It is written in plain language and provides comprehensive cover. This summary only describes the main features of the policy. The precise coverage afforded is subject to the terms and conditions of the policy as issued.

#### **More than just insurance . . .**

**ACE OPDU Elite** goes further than conventional insurance, with value-added services that include:

1. Access to specialist services provided by the Occupational Pensions Defence Union (OPDU). The Advisory Service provides trustees and administrators with general guidance and advice on matters affecting the day-to-day administration of the pension fund. It aims to facilitate good governance. The confidential advice line is staffed by lawyers and provides access to the Advisory Panel Experts where appropriate. The Advisory Service is complementary to **ACE OPDU Elite** policy holders.
2. A pack containing helpful information for the trustees, received on inception of the policy.
3. A newsletter from time to time containing information on topical pensions issues, regulatory items and recent Pension Ombudsman, the Pensions Regulator and Court determinations.



*ACE is one of the most innovative providers of insurance products and services in today's global marketplace.*

#### **Why choose ACE?**

ACE has earned its leading position in the fiduciary liability pension marketplace by consistently providing superior service, exceptional expertise and a commitment to its clients. In particular, we pride ourselves on our:

- **Stability**
  - ACE Europe is a leading provider of insurance and reinsurance in Europe. Headquartered in London with a network of offices across 14 European countries, ACE Europe is part of The ACE Group of Companies, one of the world's largest providers of property and casualty insurance, reinsurance and financial services. Established in 1985, the ACE Group has grown rapidly by building long-term partnerships with our brokers and clients in each of the world's major insurance markets.
- **Innovation**
  - ACE is one of the most innovative providers of insurance products and services in today's global marketplace. We pride ourselves on the quality and experience of our staff, who are specialists in their individual fields. Using this experience, we focus on products and services in market segments where this specialised knowledge creates a natural alliance with customers. In addition, we tailor our products and services to support the key business goals of those select segments.
- **Experience and expertise**
  - ACE Europe has a highly respected underwriting team holding a significant degree of knowledge on pensions and experience in the pensions industry. We work with brokers and clients to provide

quality cover and a claims service, which meet the needs of trustees and employers in a rapidly changing environment.

#### **Other products available from ACE:**

We offer a wide range of products to diverse sectors of industry and can tailor policy wordings to meet our clients' individual needs. We have professional, experienced underwriters specialising in areas such as directors & officers liability, employment practices liability, crime, accident, health and business travel insurance.

To find out more about **ACE OPDU Elite** pension trustee liability policy, or any of the above listed products, contact your insurance broker or nearest ACE office.

Please note this information is descriptive only. The precise coverage afforded is subject to the terms and conditions of the policy as issued.



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