Pensions Ombudsman Update - July 2019

Welcome to our latest CMS Pensions Ombudsman Update. Our quarterly Updates are designed to help you get to grips with the Ombudsman's thinking, to keep track of decisions on individual topics and to identify underlying trends. This month we consider developments including the latest High Court appeals and a million pound-plus liability award.

Betting on the wrong horse: trustees lose out for multiple breaches of trust

PO-7292 Mr L and others (29 March 2019) was an extensive determination in which the Ombudsman found that the trustees had committed multiple breaches of trust and maladministration in their running of a DC occupational pension scheme: and were personally liable for seven-figure losses which had arisen as a result.

The trustees' actions: The scheme was established in 2008 as a vehicle for Mr D, a trustee and its only member, to trade financial products. However, over the next few years it was joined by a number of Mr D's associates. By the autumn of 2012 the scheme had 58 members, although Mr D and his wife were the only trustees.

The trustees invested member funds with a Swiss investment manager, entering into an asset management agreement in 2012 for a *"very dynamic"* line of investment in contracts for difference. The contract recorded performance and annual management fees as "*TBA*".

For three years, members struggled to obtain information about their investments, although the trustees provided quarterly statements reflecting the manager's assurance that member funds were growing at 1% per month. It was not until 2015 that the trustees got to the bottom of the matter and were forced to admit that of the £1.3m originally invested, only £106,000 remained (largely because the manager - which went into liquidation shortly afterwards - had taken £1.1m in fees and commission).

The trustees had also spent scheme funds on preference shares in a company set up by Mr D, which was then appointed as a consultant to the trustees and paid from scheme funds; and on making £800,000 worth of loans to several start-up companies, all of which defaulted without a single loan being repaid.

The Ombudsman's findings: Perhaps unsurprisingly, the Ombudsman was satisfied that the trustees had breached their duties of care and skill in multiple respects. The risk to member funds was akin to *"placing a bet on a horse in the Grand National".* In addition to sending out unverified statements of account, the trustees had failed to conduct adequate due diligence, take independent advice or have regard to the need for diversification. And Mr D would be held to a higher standard than an ordinary trustee in relation to investment duties, on the basis that he had held himself out to prospective members as having substantial investment experience.

The trustees had failed to exercise due care or skill in negotiating the asset management agreement, and ignored the Regulator's DC Code of Practice, which urges trustees to draw up clear and comprehensive contracts with service providers (the Ombudsman has a statutory duty to take into account relevant provisions of Codes). The manager effectively had the right to charge the trustees whatever it liked, and it was unreasonable for the trustees to have agreed to the manager having the right to terminate the contract with immediate effect, without providing for what would happen next.

The reckoning: The trustees were held personally liable for the substantial losses to scheme funds. They were ordered to pay, within 28 days, the full losses on the investment with the Swiss manager (up to £1.3m); the £800,000 lost in loans; the £175,000 investment in Mr D's company; the £115,000 paid to that company in fees; and interest at the judgment rate of 8%.

For good measure, the Ombudsman found that the trustees' incompetence amounted to maladministration. He directed them to pay £5,000 to each of the 14 applicants before him, in recognition of the exceptional level of non-financial injustice they had suffered. And, as a final flourish, he reported the trustees to the Pensions Regulator.

An interesting coda was that the Ombudsman declined to determine the validity of an indemnity given by members when they joined the scheme, holding the trustees *"fully indemnified in respect of their decisions".* The Ombudsman opined that this was *"a commercial agreement between the members and the trustees"* and that they would have to enter into separate proceedings to establish whether it allowed the trustees to recover any sums from members.

> *Comment:* The facts are atypical, but the case highlights the Ombudsman's sweeping powers to impose liability. Issues with wider resonance include the emphasis on Regulator Codes; the examination of trustees' contractual terms with third parties; and the willingness to hold a trustee to a higher duty of care over a particular strand of trusteeship (in this case investment) when that trustee had, accurately or not, presented himself to members as an expert in the field.

Ombudsman cannot rule on questions member has not raised

Sheffield v Kier Group Plc [2019] EWHC 986 (Ch) was an appeal in the High Court from an Ombudsman determination. The Ombudsman had upheld the member's complaint about the failure to calculate interest payable on his pension under the Local Government Pension Scheme regulations. However, the Ombudsman then directed the parties to re-calculate his pension to reflect the fact that those regulations required benefits to have been paid from his 75th birthday, with arrears calculated from that date. This contradicted an understanding between the member and his employer that he would be treated as having a different, later scheme retirement date.

The High Court agreed with the member that the Ombudsman had been asked to resolve the single 'question of principle' of whether interest was payable on the arrears: not the date the member retired from the scheme, the amount of the pension, or the due date for the first payment. The Ombudsman could only determine a dispute referred to him by a member, and had no inquisitorial function letting him investigate and determine questions which the member had not asked.

The Ombudsman had misdirected himself and the member's appeal would be allowed.

At the time of writing, we understand that the court's decision may be subject to appeal.

> *Comment:* Member complaints can be hard to decipher (here, the original one was *"a narrative document running to some twenty-eight pages, with appendices*"). Parties must establish early in the process precisely what the member is - and is not - complaining about. This can save cost and confusion further down the line.

Awarding costs and giving reasons

The court in Mr Sheffield's case went on to analyse how the Ombudsman had approached the member's claim for reimbursement of his legal fees. The Ombudsman rejected the request, stating that access to his office (and to TPAS) was available free of charge. On appeal, the member argued that this reasoning suggested the Ombudsman would never exercise his power to make a costs direction in a complainant's favour. The respondents sought to reopen the question of whether the Ombudsman had power to make a costs direction at all.

The court held that case law supported the Ombudsman's power to make an award for costs, under his broad jurisdiction to direct that parties "*take such steps*" as he may specify. The Ombudsman also had a statutory duty to give reasons for his decisions. The judge seemed to recognise that the Ombudsman's reasoning on costs (a single sentence in his determination) was somewhat sparse, but cited Court of Appeal authority that his reasons *"should not be subjected to minute, meticulous or over-elaborate critical analysis in an attempt to find a point of law on which the disappointed party to the reference can appeal."*

It was reasonable to assume that the Ombudsman knew what factors he needed to consider in deciding whether to make a costs direction, and that these included the particular circumstances of the case before him. On the judge's reading, the Ombudsman had properly concluded that any factors which might justify a costs direction in this case were outweighed by the availability of free advice and access to the Ombudsman.

> *Comment:* The pragmatic approach on display here indicates judicial reluctance to unpick Ombudsman decisions merely due to an economy of language.

Member wins investment loss appeal

Tenconi v James Hay Partnership [2019] 6 WLUK 162 concerned a member who complained about delays by his SIPP provider that prevented him from investing in stocks around the time of the Brexit referendum.

The Ombudsman agreed there was undue delay in making the member's funds available but found that any lost opportunity to invest before or after the referendum result was not within the provider's reasonable contemplation. He also suggested that any loss was not measurable as there was no certainty over which shares the member would have bought, what their prices would have been, and the effect the referendum result would have had on them.

The High Court held that when a member asked to transfer their pension funds, it was obviously possible that this was for investment purposes and that delay might cause a lost opportunity to invest over a given period. If there were foreseeable spikes in the market in that time, it was foreseeable that the delay could cause loss.

The Ombudsman had also set too high a bar for measurability. It was possible for an investor to say they did not know exactly which shares they would have bought, but had anticipated a likely spike in the market and with ready money would have taken advantage of it.

The matter was remitted to the Ombudsman, who should focus on the date at which the funds should have been available, absent maladministration, in order to assess damages. At that point the member had the burden of showing what he would have done on the relevant date, on the balance of probabilities. If it was accepted that he would have invested the money, he did not have to show precisely which shares he would have bought; the Ombudsman could look at factors such as his investing patterns and the nature of his portfolio at the time.

> *Comment:* This is a useful reminder of key principles on the ability to claim for potential investment loss.

The Ombudsman as "competent court"

In January we noted the High Court's (non-binding) view in Burgess v BIC that the Ombudsman was not a 'competent court' under section 91 of the Pensions Act 1995. Section 91 prevents trustees from recovering payments by recouping them from future pension instalments if the member disputes the amount owed, except where the issue has been resolved by "*order of a competent court*".

The Ombudsman has now issued his own factsheet in response, setting out 'non-exhaustive reasons' why in his view the judge was wrong. It emphasises the Ombudsman's view that his role is judicial, that he is a tribunal with the characteristics of a court of law, and that his office is a "lower court" for the purposes of the Civil Procedure Rules.

> *Comment:* In January we expressed the hope that this point would be considered in this year's Court of Appeal hearing in the BIC case. In the event that Court did not need to address the point, and so we have no definitive judicial authority on it. In contrast, the Ombudsman's view is crystal-clear. It would be useful if the point could be settled in the relevant legislation.

CMS and the Pensions Ombudsman

CMS has had a market-leading Pensions Ombudsman Unit for many years, led by Mark Grant. Mark wrote the only text book on the Ombudsman's role and established and chairs the Pensions Ombudsman Liaison Group, an industry body that meets with the Ombudsman and seeks to improve understanding, relationships and communications between his office and key stakeholders. CMS is also a stakeholder in the Pensions Ombudsman's Legal Forum.