

THE FACULTY OF ACTUARIES AND INSTITUTE OF ACTUARIES

SECTION 67 PENSIONS ACT 1995

JOINT OPINION

1. Introduction

1.1 We have been asked to advise the Faculty and Institute of Actuaries on several issues relating to Section 67 of the Pensions Act 1995 ("section 67"), in order to assist their members on its application in various circumstances.

1.2 By way of introduction, it is worth noting what was said by Mr William Hague MP (then Minister for Social Security) in relation to the then Pensions Bill

“The clause serves two purposes. The first is to provide protection against scheme amendments that would detrimentally affect the accrued rights of scheme members. It achieves that by placing restrictions on the making of amendments by requiring either an actuarial certificate that amendment is not detrimental or the consent of each individual member. The hon. Gentleman asked whether that was necessary or whether the requirement already existed in law. In fact, **we are putting on a statutory basis what has been understood to be the present position under trust law....**

Secondly, the clause provides a practical means whereby trustees can overcome the difficulty of untraceable members in those schemes where rules require the consent of all members before amendments may be made.”¹

1.3 And in response to a question about accrued rights, he said this:

“...The hon. Gentleman asked whether accrued rights meant only early-leaver rights. They do, but the Government have tabled an amendment to the definition of accrued rights because it would be unreasonable to protect members and impose costs on employers in respect of rights that have not yet been earned. Early-leaver rights are those which have accrued. That is in line with the recommendations of

¹ Standing Committee D, 8th June 1995 col 469 (emphasis supplied)

the Goode committee.”²

1.4 We set out:

1.4.1 in bold at the head of each Section, each of the primary issues on which we have been asked to advise,

1.4.2 in italics as and when they arise in the discussion, the particular questions arising under each of the issue headings on which we are specifically asked to consider

2. The Width of “Scheme”

2.1 Introduction

2.1.1 Section 67 provides that:

“This section applies to any power conferred on any person by an occupational pension scheme (other than a public service pension scheme) to modify the scheme.”

2.1.2 “Occupational pension scheme” is defined by reference to the following definition set out in s.1 of the Pension Schemes Act 1993 (see s.176 of the 1995 Act)

“any scheme or arrangement which is comprised in one or more instruments and which has, or is capable of having, effect in relation to one or more descriptions or categories of employments so as to provide benefits, in the form of pensions or otherwise, payable on termination of service, or on death or retirement, to or in respect of earners with qualifying service in an employment of any such description or category”

2.1.3 The above definition is a very wide one, and is apt to cover arrangements which pensions practitioners may not intuitively regard as pension schemes: for example:

² *Ibid* col 470

- in *City and County of Swansea v Johnson*³, the court held that a local authority industrial injury allowance scheme, whereby the employer bound itself to pay on a no-fault basis compensation on termination of employment as a result of injury sustained or disease contracted in the course of employment, fell within the above definition;
- in *Parlett v Guppy's Bridport Ltd (No.2)*⁴, the Court of Appeal held that a resolution of a company recorded in the minutes of the company's AGM, by which the company undertook to pay to the managing director a pension on his retirement, fell within the above definition.

2.2 Which of the following arrangements would Counsel consider to be a "scheme" for the purposes of section 67:

- *voluntary augmentations to benefits made by employers directly out of their own assets rather than through what would normally be regarded as an occupational or personal pension arrangement;*
- *an unfunded scheme;*
- *an unapproved scheme;*
- *a redundancy plan;*
- *a disability plan;*
- *an accident plan;*
- *a death in service only plan; and*
- *an employee share plan.*

³ [1999] Ch 189

⁴ unreported, 8 October 1999

2.2.1 In our opinion, the definition of “scheme” can (but not in all cases) include these types of arrangement, except that we do not consider that an employee share plan (and similar plans) could be regarded as within the definition.

2.3 *Is the “scheme” what the member(s) have been promised? Can the “scheme” be wider than the content of any formal trust deed and rules?*

2.3.1 The “scheme or arrangement” referred to in the definition is one which is comprised in “one or more instruments or agreements” and which “provides benefits...”. The provisions of those instruments and agreements - including the benefit structure and the administrative provisions - are what make up the scheme; the scheme can in one sense be viewed as the vehicle by which benefits are delivered and assets invested and administered.

2.3.2 The provisions of a scheme can change from time to time in a number of ways. For instance in the case of a trust scheme having a trust deed and rules

(i) Administrative powers may be altered pursuant to a power of amendment. The scheme does not change its identity: it is simply that the provisions of the scheme are altered and, where as would be usual such an amendment is made by deed, that deed becomes one of the instruments in which the scheme is comprised.

(ii) Benefits may be increased perhaps even in a way (*eg* by a trustee resolution) which requires neither instrument nor agreement⁵. There is no doubt that the increases become part of the provisions of the scheme from the time they are granted. The identity of the scheme does not change: it remains comprised in the original trust deed and rules but so that the “instruments or agreements” which make up the scheme are read in their altered form (*ie* including the benefit increases).

⁵ It is arguable that such a resolution would be an “agreement” but we proceed on the footing that it is not.

2.3.3 Similarly, if benefits are changed as a result of actions outside the formal provisions of the trust deed and rules in such a way as to be legally binding on the trustees and the employer, those changes become provisions of the scheme just as much as alterations under the rules themselves.

The type of case we have in mind here is where an estoppel arises as a result of announcements and booklets on which all the parties have acted for a long period of time as in *Icarus (Hertford) Ltd v Driscoll*⁶.

2.3.4 Two possible meanings of “scheme” have been suggested by one commentator⁷:

- (i) the “rigid” view is that a scheme at its root is a set of monetary promises;
- (ii) the “flexible” view is that a scheme may be a set of promises but they should be viewed as being promises which are inherently flexible if the right is reserved to change their shape. There is on this view no modification if the fundamental promise stays the same.

2.3.5 We do not think that either of these approaches fully describes or encapsulates the nature of a scheme. In relation to this, it will be apparent from what we have said that, conceptually, the “scheme” is not simply what the members have been promised. Certainly the benefits which they have been promised (in such a way as to be binding on the trustees and the employer) are benefits which are payable as part of the scheme (and that is so whether the obligation arises under the provisions of the scheme or as the result of an estoppel outside the formal provisions): the promises arise under or indeed because of the scheme, but they are not the scheme itself. The scheme itself encompasses more than that and includes all the administrative powers and provisions relating to the trust assets and collection of contributions.

2.4 *Would any of the following features have become part of the “scheme”?*

⁶ [1990] PLR 1

⁷ See “Deconstructing Section 67” by Dan Schaffer, British Pension Lawyer March 1999 p3 at Section B p 6

- (i) *early retirement/cash factors expressed to be variable at the discretion of the actuary but which have been promised to the members in the scheme booklet or in a letter from the pensions manager*
- (ii) *If trustees have declared an intention to make future pension increases in line with inflation, subject to the availability of funds (which may permit the scheme to be funded to a higher level than Revenue restrictions would otherwise permit)*
- (iii) *if the employer promised a higher level of benefit to certain individuals than ordinarily provided under a scheme without making that benefit conditional on the scheme being altered*

2.4.1 As to (i), if the promise has been made in such a way that it is binding, then the relevant factors must be reflected in the benefits of the members concerned when those benefits come to be paid. To that extent, they are part of the scheme in the way that any other benefit under the rules is a part of the scheme. But it must be borne in mind that the scheme is not simply the benefits: rather the benefits are payable under the provisions of the scheme so that the scheme itself is conceptually something different from the benefits.

2.4.2 As to (ii), if the intention has become a promise then it will have to be implemented (funds permitting): and to that extent the position is just the same as under paragraph 2.4.1. above. But this is not a likely scenario: statements of this sort are usually no more than statements of intent which do not create legally binding obligations. In such a case, the intention would not be reflected in the benefit entitlement and could not in any sense be regarded as part of the scheme.

2.4.3 As to (iii), this would be an example of an obligation relating to pensions which arose outside the scheme *eg* an employer might promise a pension based on 1/30ths where the scheme itself only provides for 1/60ths and where the excess is simply an unfunded promise made by the employer. This would seem to us to create a separate scheme or supplementary scheme.

3. Width of “modification”

3.1 Introduction

3.1.1 Section 67(1) applies to

“...any power conferred on any person by an occupational pension scheme.....to modify the scheme”

3.1.2 To state the obvious we are concerned with a power

(i) which is conferred on some person by the scheme

(ii) to modify the scheme.

3.2 *What is the scope of the requirement for the power to modify being **conferred by the scheme**?*

3.2.1 Not all modifications to a scheme are affected by powers conferred by the scheme. For instance, statute may confer a power. Or the court may approve a compromise between trustees, employer and members of some dispute between them; the compromise might result in a change to benefits, but that change would not result from a power conferred by the scheme.

3.2.2 Less clear are the cases referred to in paragraph 2.4 above. However, we doubt very much that a change in benefits resulting from an estoppel by convention between the trustees, the employer and the members would ordinarily be as the result of the exercise of any power conferred by the scheme. Rather, in holding that an estoppel by convention exists, the court is prohibiting the parties bound from resiling from their shared understanding (express or implied), notwithstanding that that understanding is wrong as a matter of fact. That seems to us to be something quite different from the exercise of a power conferred by the scheme.

3.2.3 We think that the result would be the same in a case such as *South West Trains v Wightman*⁸

⁸ [1998] PLR 113.

where a contractual arrangement between the members (through a collective bargaining procedure) and the employer resulted in the members being able to claim only the benefits which they had bargained for and not the larger benefits which the scheme rules on their face provided.

We do not think that the decision is any authority for the proposition that the contract bringing about that result would be a modification within section 67⁹.

3.2.4 Similarly, changes in contractual documents would not in an ordinary case amount to a modification of the scheme. For instance, suppose that an existing pay structure is altered to reduce (pensionable) fixed pay and to replace it with (pensionable) basic pay and (non-pensionable) performance-related pay; the actual level of pensionable pay may, as a result of the change, be reduced and thus the amount of a member's accrued rights might be reduced.

But there has, we think, been no modification to the scheme: its provisions have not been changed in any way; rather, the facts against which the provisions of the scheme are applied have changed but the scheme itself remains unmodified.

3.3 *The meaning of "to modify": the competing theories*

3.3.1 "Modify" and "modification" are defined for section 67 purposes by section 124(5) incorporating the definition in section 181(1) Pension Schemes Act 1993. It is a wide definition, including additions, omissions and amendments. There is no reason to think that modification powers are restricted to commonly found general scheme amendment powers - often expressed as power to alter or to amend any provision of the scheme - even in the case of case of a scheme with a trust deed and rules¹⁰. There are many powers which can be exercised in a way which affects benefits and, in considering whether the proposed exercise of such a power will

⁹ Even if it were a modification, it ought to be possible to structure the changes in such a way that the consent requirements are satisfied.

¹⁰ In this context, we should make the obvious point that, whilst section 67 applies to every power to modify (see section 67(1)), not every exercise of such a power gives rise to a need to fulfil the certification or consent requirements. It is only an exercise of the power in a manner which "would or might affect any entitlement, or accrued right" which does so.

“modify” the scheme, we think it is the substance of the change which must be considered. In other words, the question whether a given power is a power to modify the scheme must be answered by reference to the results which can be brought about by its exercise.

3.3.2 In some cases, it may not be straightforward to decide whether the particular power is one to modify the scheme or not. For instance, a power (however expressed) which could be used to introduce an entirely new benefit (*eg* dependants’ pensions where none is provided) would be a power to modify the scheme¹¹: we do not, at present, see any contrary argument to that conclusion. But the obligation/power of trustees to decide how to distribute a lump sum death benefit held by them upon discretionary trusts would probably not be a power to modify the scheme. Those two examples illustrate a distinction which, it seems to us, ought to be drawn in the context of benefits provided under a scheme: that is to say a distinction between the exercise of a power which changes the benefits which would otherwise be payable and the exercise of a power which is inherent in establishing the amount of the benefit in the first place. This distinction can be seen in our consideration of certain aspects of section 67 considered later.

3.3.3 It has been suggested¹² that a “numbers” test is possible so that a power is one to modify if it is capable of being exercised in favour of a class but not if exercisable only in favour of individuals. Whilst we can see that it is an attractive result in the sense of reducing the practical difficulties encountered in relation to section 67, we do not consider that an argument along those lines would find favour with the Court.

3.3.4 Nor do we think that the “rigid”/“flexible” dichotomy suggested¹³ provides a solution. The concept of the “fundamental promise” will, we think, prove to be rather elusive.

¹¹ Although not, we think, an amendment caught by section 67(2).

¹² See footnote 7 above

¹³ See paragraph 2.3.4 above

3.3.5 The difficulties of construction which arise in relation to section 67 are illustrated by the practical example of the exercise of augmentation powers: we consider this at paragraph 6 below.

3.4 *Can the exercise of an existing power under the scheme be excluded?*

3.4.1 We understand this to be directed essentially at the question whether a power which already exists under the scheme can be exercised regardless of section 67 on the basis that the change it brings about is already inherent in the scheme. Put that widely, the answer is “No” since section 67 clearly applies to the exercise of an ordinary power of amendment exercised *eg* to reduce accrued benefits. It will be apparent from what we have written above that our view is that any other power which changes, rather than defines, rights is also within section 67(1)¹⁴.

The contrast is shown by considering the position if the power were not exercised:

- (i) if the beneficiaries have defined rights in the absence of the exercise of the power and those rights are affected by an exercise of the power then there is a modification
- (ii) but if the beneficiaries have no defined rights in the absence of the exercise of the power, so that its exercise is necessary to define their rights, there is no modification.

3.4.2 This again is the distinction we have drawn attention to in paragraph 3.3.2 above.

3.5 *Can an employer announcement effectively modify **the scheme** where the trustees, in whom the power to amend is vested under the scheme rules, become aware of the announcement and either do nothing or act upon it without taking any formal action to amend the scheme?*

¹⁴ Although whether the actual proposed exercise of the power will fall within section 67(2) is, of course, a separate question.

3.5.1 It can only be said that the position is not clear and will depend on the precise facts of the relevant case. Absent questions of conventional estoppel (which we have considered to some extent already in the context of what constitutes a scheme) section 67(2) would appear to render ineffective any purported amendment made without compliance with the certification or consent requirements¹⁵. Were it not for section 67, it may well be that the facts in a case such as that mentioned would be sufficient to establish that the trustees had resolved, or are to be treated as having resolved, to make the amendment.

4. When do the trustees need a certificate?

4.1 *Whose task is it to identify which rules have been modified for the purposes of giving a section 67 certificate?*

4.1.1 This is particularly relevant where part or all of the current rules have been re-written. Our own experience shows this to be an area which causes difficulty. This is because the rewrites of this sort are not intended to change the benefits at all, either up or down. If that intention is effected, then the amending power is not being exercised in a way which “would or might affect any entitlement, or accrued right”. So, say some actuaries and lawyers, if there is no change, there is no need for a certificate: indeed, some actuaries suggest that they cannot give a certificate since the section does not apply. Nonetheless, trustees often ask for the comfort of a certificate because if, contrary to their honest belief, the rewrite does affect benefits, they are subject to civil penalties if there is an amendment without compliance with the statutory requirements.

4.1.2 We shall return to that dilemma in a moment. But one thing is clear and that is that where a certificate is needed - for instance, matters may go slightly beyond rewrite and include some small change to benefits not simply by way of improvement - the section and the Modification Regulations¹⁶ require the actuary to express his own opinion. Before he can do that, the actuary

¹⁵ We leave aside for the moment the question whether those requirements can be satisfied retrospectively

¹⁶ The Occupational Pension Schemes (Modification of Schemes) Regulations 1996 SI 1996/2517

will have to satisfy himself that there is no adverse effect on the member in respect of his accrued rights; and to do that, he will have to know what changes to benefits are being made. In ascertaining the extent of benefit changes, the actuary might rely among other matters on:

- (i) his own ability to read a document and understand it;
- (ii) advice from the trustees' lawyer and
- (iii) his own independent legal advice.

4.1.3 Very often, (i) will be sufficient. But if the document is either very long or very complex, the actuary may want to rely on (ii) or (iii). In practice, if this is necessary, it is preferable - save in unusual circumstances - for the actuary to be able to rely on the trustees' legal adviser, but that adviser would have to agree that his advice could be relied on by the actuary. There is, unfortunately, sometimes an element of buck-passing here: the actuary says he needs help understanding the document and the lawyer says it is up to the actuary to form his own opinion.

4.1.4 However, if the case is one where the actuary cannot be expected to form a view about the meaning and effect of the document as compared with the predecessor provisions without legal assistance, it is clear that he is entitled to help, when forming his opinion as an actuary, on the legal effect of the document and that he is entitled to rely on legal advice in forming his opinion for the purposes of certification.

4.2 *A dilemma: where the trustees want a certificate but the actuary does not think one is required*

4.2.1 In this situation, the trustees may need actuarial assistance at two levels.

- (i) they may want actuarial - as well as legal - advice that the amendment does not affect

accrued rights in order to satisfy themselves that they do not need an actuarial certificate;

- (ii) if the actuary advises that the amendment does affect accrued rights, then the trustees will require his certificate for the purposes of section 67.

4.2.2 In the first case, where advice is sought, we see no difficulty in the actuary giving his advice in the form of a certificate which would satisfy section 67: if for wholly innocent reasons it turns out that the amendment does (adversely) affect accrued rights, then the trustees are protected by the certificate and the actuary's responsibility is, we think, no more and no less than if he had simply given advice. The position here is really no different from the following case namely:

an amendment will affect accrued rights but it is believed not adversely; a certificate is given; it turns out that the amendment does adversely affect accrued rights. The trustees are protected by the certificate provided that they have acted responsibly, although the actuary may be responsible if he has acted negligently.

4.2.3 The position is slightly different where the trustees, having taken legal advice, instruct the actuary that the amendment will not affect accrued rights. We do not consider that the actuary need give a certificate in such circumstances. However, if he is instructed to form his own opinion whether the amendment will affect accrued rights - taking such legal advice as he requires or relying on the trustees' legal advice - the case is then the same as discussed in paragraph 4.2.2 above and the actuary may as well give his confirmation in the form of a certificate complying with section 67.

4.3 *Is the actuary required to give a certificate on the demand of the trustees, where the modifications are such that there can be no effect on members accrued rights and entitlements?*

4.3.1 We will consider the special cases of rectification and setting aside documents later in this

Opinion. As a general proposition, however, where an amendment (eg to administrative powers) will not affect accrued rights, no section 67 certificate is necessary. The trustees cannot really insist that the actuary give a certificate in these circumstances. However, we would repeat the preceding paragraph in this context.

4.4 *Is there a conflict between:*

- *section 67(4)(a), which states that the prescribed requirements for the purpose of securing that no power to which section 67 applies “is exercised in any manner which, in the opinion of the Actuary, **would** adversely affect any member ...”; and*
- *the certification regulations, which state that “an actuary shall certify to the trustees of the scheme that, in his opinion, the exercise of the power in the proposed manner to modify the scheme **would not** adversely affect the member ...”*

does the use of the negative in the regulations impose a more stringent test than the section?

4.4.1 We do not consider that there is such a conflict.

4.4.2 We analyse the provisions as follows:

- (i) Section 67(2) precludes the exercise of a power in any way which “would or might” effect any entitlement or accrued right of a member subject to the certification or consent requirements. There is no reference to the Actuary or, indeed, to any other person who might make a judgment whether a proposed amendment would or might have such an effect; nor is there a reference to adverse¹⁷ effect.
- (ii) Section 67(4)(a) describes the purpose of the certification requirements *ie* to secure that the modification power is not exercised in a way “which, in the opinion of an actuary, would adversely affect...” the member “in respect of his entitlement or accrued

¹⁷ See further in this context paragraph 5.2 *et seq* below.

rights...”. The subsection thus has two important elements: first, it is concerned with adverse modifications; and second, it provides for the actuary to be the judge¹⁸.

- (iii) Regulation 3 specifies, as the prescribed requirement, that the actuary shall certify that “in his opinion the exercise of the power in the proposed manner....would not adversely affect any member...in respect of his entitlement, or accrued rights....” The Regulation puts the matter negatively where the section puts it positively. It should be noted that the Regulation does not envisage the actuary warranting that the modification will not (or, using the grammar of the Regulation would not (*ie* if made) adversely affect benefits. He is not asked to certify that the modification will not adversely affect benefits: he asked simply to certify that, in his opinion, it will not do so. In other words, he is asked to express an opinion about what will happen not what could happen.

- (iv) This distinction is illustrated by the answers to two closely related, but different, questions asked of the actuary:
 - (1) “Will this modification adversely affect benefits?” [or: “Would this modification, if made, adversely affect benefits?”] and

 - (2) “Will this modification, in your opinion, adversely affect benefits?”

- (v) In response to question (1), he might be able to say that there are no circumstances in which there could be an adverse effect; in which case he will answer both questions in the negative. But there will be many cases where he will be unable to give such an answer. There is then a range of possible observations he could make, including
 - (a) in most circumstances, there will be a beneficial effect; I can envisage

¹⁸ There is also a third factor which is mentioned in paragraph 6.2.2 below: section 67(2) focuses on the exercise of a power which would or might affect the benefit whereas section 67(4)(a) focuses on the exercise of a power which would adversely affect the member in respect of such benefit.

- circumstances in which there would be an adverse effect, but I think that they are very unlikely and even if they occur the effect will be very small;
- (b) as in (b), but I think the effect will be significant in that unlikely event;
 - (c) there are many circumstances in which the benefit will be adversely affected;
 - (d) it is not possible to say with any degree of confidence.
- (vi) Clearly, in none of these circumstance could he answer question (1) in the negative in the sense of giving an unqualified answer applicable to all circumstances.
- (vii) But when he comes to answer question (2), he may be prepared to express a professional opinion. In case (a), for instance, he may be willing to express the opinion that there will be no adverse effect whilst acknowledging that unlikely - but possible - events may come to pass which will prove his opinion to be wrong. If he is willing to express that opinion, and if it is an opinion which a competent actuary could hold, then we consider that the actuary can properly give a certificate according the test imposed by the Regulations. But if he is unwilling to express an opinion at all, for instance because he simply cannot make a sensible judgment in the light of a number of imponderable factors, he cannot give a certificate.
- (viii) In forming his judgment, the actuary may seek to draw a distinction between future economic events (*eg* changes in the rate of inflation) and other contingencies (*eg* the effect of a modification on a death benefit payable only in certain events). The actuary may feel able to express a professional opinion in relation to the effect on benefits of the former (economic factors) but not the latter (other factors). However, we do not see any distinction in principle between these types of factor; but in practical terms, the actuary may refuse to give his certificate if he feels unable to make a judgment and that may be more likely to be so in relation to non-economic factors.

- 4.4.3 Applying this approach, we do not see a conflict between the section and the Regulations. Section 67(2) simply sets the scene - no changes at all are allowed which might affect accrued rights except ones satisfying the requirements of section 67(3). That subsection then sets out the requirements, one of which is that the certification requirements or the requirements for consent are satisfied. Section 67(4)(a) then sets out the purpose of the certification requirements which is to preclude an amendment which would in the opinion of the actuary adversely affect the member in respect of his accrued benefits.
- 4.4.4 When we come to the Regulations, that purpose is effected by the need for a certificate that the proposed amendment would not in the opinion of the actuary adversely affect the member in respect of his accrued benefits. Except in a case where the actuary is unwilling to express an opinion at all, the purpose of section 67(4)(a) is precisely reflected in the requirement for the certificate required by the Regulations.
- 4.4.5 We accept that the Regulations prohibit an amendment which the actuary is unwilling to certify under those Regulations notwithstanding that such an amendment is not one which, in the opinion of the actuary, would adversely affect accrued benefits (and is thus not an amendment within the express purpose of the certification requirements as stated in section 67(4)(a)). However, the fact that the Regulations, to this limited extent, go beyond that purpose would not lead a Court to strike down the Regulations as *ultra vires* as the overall purpose of the Regulations is not subverted by that extension.

5. What are “accrued rights”, “entitlement”, “adversely affect” and “benefits”

5.1 Introduction

- 5.1.1 The issues raised in this Section of the Joint Opinion raises some very difficult questions in relation to which it is not possible to give answers which we can express with a great deal of confidence.

5.2 *How do contingent and future interests fall within the definitions of “entitlements” and “accrued rights”*

5.2.1 Our own view is that “entitlements” refer to benefits the right to payment of which (whether immediately or in the future) has arisen or commenced. Thus a lump sum which has become due but has not yet been paid is an “entitlement”, as is a pension (both as to past and future instalments) which has commenced payment. But contingent rights *eg* a member’s own deferred pension which will come into payment in the future on attaining normal pension age or a widow’s pension in respect of a living member already in receipt of his pension, is an “accrued right”.

In this context, future instalments of a pension in payment are not contingent even though they are payable only so long as the pensioner survives. The pension for life is, we think, to be treated as single interest much like the interest of a life tenant under a family settlement. On this analysis, future instalments of a pension are not “future” benefits so as to fall within “accrued rights”. It may be that the “entitlement” of a member whose own pension has commenced payment includes the benefits for dependants while still contingent. We do not think that that is so, although they do turn into member’s entitlements for section 67 purposes once the member himself is dead, as a result of Regulation 2 of the Modification Regulations.

5.3 *What are the entitlements and accrued rights of an active member? Are they restricted to accrued rights (as defined in section 124(2) and thus restricted to the rights as if the member had opted out of pensionable service)? Or do they include something wider as well, such as the revaluation of benefits? Should the actuary solely consider the accrued rights and entitlements of members immediately before and immediately after the modification takes effect?*

5.3.1 We consider that the purpose of the section 67 is to protect only the accrued rights of an active member within the definition. The most that can be said in favour of the wider view is that the provisions are ambiguous: reference to *Hansard*¹⁹, permitted under *Pepper v Hart*²⁰ in these

¹⁹ See the passage set out in paragraph 1.3 above

circumstances, strongly supports the conclusion which we favour as a matter of construction.

5.3.2 The definition of “accrued rights”, read literally, includes both statutory revaluation and any revaluation expressly provided for by the scheme rules. In the case of a deferred pensioner, this does not give rise to any particular problem for section 67 purposes. But the position is much more difficult in the case of an active member because the section seeks to provide protection by reference to a benefit which the member does not in fact enjoy. The active member would in fact become entitled to his “accrued rights” only if he left service. He does not, therefore, become entitled in fact to revaluation. These difficulties can be illustrated by some examples:

- (i) Consider the case of a proposed amendment reducing the accrual rate from $1/60^{\text{th}}$ to $1/120^{\text{th}}$ for future service. One might ask how that could possibly affect accrued rights since all it does is affect future accruals. If the position is to be judged immediately before and immediately after the amendment, the accrued rights are not affected at all since the same benefit - and the same revaluation - would arise on the notional opt-outs at those two instants of time. But the section does not - or at least does not clearly - provide for any adverse effect to be judged in that way.
- (ii) Suppose for instance that an amendment is proposed under which benefits for persons leaving service more than a month after the amendment are to be reduced (*eg* by a change of accrual rate for past service from $1/60^{\text{th}}$ to $1/120^{\text{th}}$ - assume that there is power to this and that the circumstances are unusual so that the trustees could properly agree to this course from a trust-law perspective). Since a member opting out of pensionable service immediately before and immediately after the amendment will have precisely the same benefits and entitlement to revaluation, it would follow that there is no adverse effect on accrued rights if this temporal test is to be applied. We would find that a very surprising result - although we acknowledge that it could be argued that

since the member can in fact elect to opt out his position in respect of his past service is not prejudiced. We do not think that that is what the section is aimed at all. We think that an active member must be entitled to remain an active member and at the same time have his accrued rights protected.

(iii) In this example, it might, alternatively, be argued that the modification takes place at the time the change in benefits comes into force, a month after the deed of amendment; and that the comparison test is to be made between the position immediately before and immediately after the change comes into effect. We do not consider that that is a satisfactory analysis. It meets the particular example we have given, but has to rest on the basis that no amendment is made, for the purposes of section 67, when it is actually made but only when it takes effect. That would be a practically impossible approach to operate generally in relation to actuarial certification and/or member consents.

(iv) We think that there are three possible answers:

(a) The first answer is that revaluation has nothing to do with “accrued rights”. Rather, the accrued right of a member in the examples above at that time of the amendment is *eg* to a pension, at NRD, of $n/60^{\text{th}}$ of FPS at the date of the amendment, so that if he remains in service, his benefits when he actually leaves service or retires, must include the right to that amount of pension in respect of his pre-amendment service. Under that approach, the amendment in (i) above does not adversely affect accrued rights: but the amendment in (ii) above does so, because, if the member serves beyond the one month period, his benefits in respect of pre-amendment service will be reduced.

(b) The second answer is that revaluation is included in “accrued rights” but that a rather different comparison must be made. Under this approach, a comparison is to be made between (i) the benefits on opting-out revalued (at the scheme rate or statutory rate as the case may be) to the time as of which the

comparison is being made and (ii) the benefits to which the (active) member would in fact be entitled under the scheme if he were to opt out at that time. If the latter exceeds the former, there is no adverse affect of the amendment; but it must be possible to say that, at all times until retirement or previous leaving service, that the comparison will favour the scheme benefit²¹. In practice, that will probably not be so unless the amendment includes an underpin to that effect.

- However, such an underpin can, we think, be limited to the benefits which would have been provided under the scheme if the amendment had not been made. There is an obvious conceptual difficulty in protecting accrued rights by reference to a hypothetical benefit (the opt-out benefits) to which the member did not in fact become entitled and which may exceed his actual benefits if the scheme had not been amended; we do not, however, see how it can be said that an amendment adversely affects any accrued benefit if the scheme continues to provide as good a benefit as prior to the amendment. For example, even in the absence of amendment, a member may be better off by opting out and receiving revaluation of his pension rather than by remaining in pensionable service and receiving future service accruals: if he in fact remains in service, he cannot claim a larger benefit as if he had left service. His position should not be any better in a case where an amendment is made. Thus an amendment which affects benefits may in the events which happen leave the member who remains in service with benefits which are equal to or in excess of the benefits he would have received if the amendment had not been made but with less than if he had opted out: he should not, we think be able to claim the opt-out benefit on the basis that it is protected by section 67.

²¹ But note that if the scheme or statute require future accruals to be allocated exclusively to future service, it may not be possible for those accruals to be taken into account in the comparison.

- This second answer leads, however, to the curious conclusion, assuming that it is not correct simply to make a comparison at the time of the amendment, that a reduction in the future accrual rate could have an adverse effect on accrued rights, since revaluation from the time of the amendment may be more valuable than accrual at the reduced rate (depending on the age and service record of the member).

- (c) The third answer is that revaluation is again included in “accrued rights” but that the comparison is to be made throughout the period after the modification between (i) that part of a member’s accrued rights acquired before the modification on the footing that the modification had not been made and (ii) that part of his actual accrued rights acquired before the modification. This is to read section 67(2) as meaning “...would or might affect at any time in the future” the accrued right at any time in the future of a member. On this approach, it can be asked at any time after the modification (a) what a member’s accrued rights are at that time and (b) what part of them were acquired before the modification was made. It is then necessary to make a comparison: the only candidate for comparison is the corresponding part (*ie* acquired before the modification was made) of the accrued rights on the assumption that the modification had not been made. In order to give his certificate, the actuary must be able to say that in his opinion that comparison will always result in (ii) equalling or exceeding (i).

- (v) We illustrate this third approach by reference to the examples in (i) and (ii) above. Assume in each case that the member in question has 10 years’ service (accruing pension at the annual rate of 1/60ths final pensionable salary). Consider then the position 5 years later when the member has accrued an additional 5/120ths rather than the additional 5/60ths he would have accrued had the amendment not been made. His actual “accrued rights” at that time then include, in example (i), a deferred pension,

carrying revaluation, or 20/120ths of his then pensionable salary. His notional accrued rights” had the amendment not been made would have been a total of 15/60ths of his then pensionable salary. It is next necessary to ask what part of those actual and notional accrued rights were “acquired” before the amendment was made. We think that the answer, in respect of those notional accrued rights and in the light of the definition of “accrued rights” in section 124(2)(b) Pensions Act 1995, is 10/60ths of pensionable salary at the date of the amendment.

- (vi) Accordingly, according to the third answer, the amendment in (i) above does not adversely affect the member in respect of his accrued rights since the accrued rights acquired before the amendment remain 10/60ths; but the amendment in (ii) does so since, if the comparison is made after the end of the one month period, it can be seen that the member’s deferred pension, if he were to leave service, acquired before the amendment is reduced from 10/60ths to 10/120ths.
- (vii) On this analysis, revaluation (whether statutory or provided for by the express terms of the scheme) forms part of the member’s accrued rights; and a reduction in the scheme’s rate of revaluation to statutory revaluation for all service would adversely affect the member in respect of his accrued rights acquired before the reduction. This is so because, if the amendment had not been made, his accrued rights acquired before the amendment would have included the right to the higher rate of revaluation.
- (viii) Also on this analysis, a change in the definition of pensionable salary is permissible provided that the pension attributable to service up to the date of the amendment remains based on the level of salary at the date of the amendment²². It is only this level of benefit which has been “acquired” before the amendment.

²²

Or possibly, if lower, salary at the date of actually leaving service according to the pre-amendment definition: although the actual level of benefit attributable to pre-amendment service may be less than the accrued right at the date of the amendment, the reduction would not be due to the amendment but would instead be due to an actual reduction in the level of (old definition) pensionable salary.

5.3.3 Our own view is that it is not correct to make a comparison simply at the date of the amendment. The view that a comparison can be made of the position immediately before and immediately after the amendment is held by some and is well-arguable. It produces the result - one we consider to be a sensible result - that a reduction of future service accruals is permissible without need to rely on some sort of underpin (which is necessary under the second possible answer considered in (iv) above); and it prevents, as we consider in principle ought to be the case, an amendment reducing an express rate of revaluation in respect of past service to the statutory rate. However, we consider that it faces serious problems in the light of the possibility of amendments being made to take effect at a future date.

5.3.4 We were initially attracted by the view that revaluation is not to be taken into account in considering whether an amendment adversely affects the accrued rights of active members for the following reasons.

- (i) The purpose of section 124(2) appears to be to quantify what part of the benefits of a member has accrued before and after a particular time. For a deferred pensioner, clearly all his benefits have accrued by the time he leaves service: his benefits in fact include revaluation so that he is protected from adverse affect by amendment of his benefit and its revaluation.
- (ii) But sections 67 and 124 are not intended to replace the concept of pension accruing over a period of time. When a person retires or leaves service, his benefits, ascertained at that time, can be regarded as having accrued over the period of his service.
- (iii) But there are different ways of regarding that accrual: for instance benefits can be regarded as accruing uniformly or there can be attributed to each year a proportion based on that year's salary. Section 124(2)(b) is telling us, we think, no more than that of the eventual benefit payable, a certain part is to be treated as having accrued up to the time in question (*ie* for section 67 purposes, the time of the amendment). It is looking at the manner of apportionment between past and future service but only so far

as is consistent with the actual benefit eventually payable. The eventual benefit actually payable when a member serves to retirement does not reflect any revaluation from any date, and for a member who leaves service at some date after the amendment, receives revaluation only from that date. It is not consistent with the benefit actually payable to bring into account a notional benefit which is revalued over a period when in fact no revaluation took place. In practice, the most important consequence of this approach is that accrued rights are based on service to and salary at the date of the amendment.

5.3.5 However, we now recognise that an approach which ignores revaluation altogether fails to deal adequately with the case where a scheme provides a rate of revaluation which is better than the statutory rate, and where there is a proposed amendment to reduce that rate of revaluation to the statutory rate in respect of the whole period of service of a member who leaves service after the date of the amendment. It is this recognition, coupled with our continued reservations about the “immediately before and after” test, that leads us to the second and third answers. Both of these answers contain, as a special case, the “immediately before and after” test but meet the reservations which we have to it.

5.3.6 We now think that the third answer provides the correct solution. It gives a sensible answer to a number of problems. Where there is an amendment reducing the future accrual rate the third answer results in there being no adverse affect on the member in respect of his accrued rights. This is the result we would intuitively expect to be correct. The need for an underpin, as required by the second answer, is avoided. And it protects the member from any adverse effect, in relation to pre-amendment service, of a reduction in the rate of revaluation. It also provides a sensible reading of sections 67 and 124(2) as explained in paragraph 5.2.3(v) (vi) and (vii) above. But as we have already said, the “immediately before and after” test is a well-arguable approach and may be correct. And the second answer which we have identified cannot be ruled out.

5.4 *In considering the effect of a modification on members’ benefits, should the actuary consider its effect on each member separately and on each benefit separately, or apply*

a value test, i.e. consider the overall impact of the modification on the member's pension benefits

- 5.4.1 In our opinion, the section and the regulations are looking at each member separately: it is not possible to look at scheme liabilities as a whole and set off an improvement for one class against a detriment to another class.
- 5.4.2 An amendment is allowed if the certification requirements are satisfied. These are contained in Regulation 3 of the Modification Regulations and require the actuary to certify that in his opinion the amendment

“would not adversely affect any member of the scheme (without his consent) in respect of his entitlement, or accrued rights, acquired before that power is exercised.”

On balance, we think that this requires each benefit in respect of a member to be looked at separately in relation to any particular modification. Thus it is necessary to look separately at the effects of a modification on benefits on death after withdrawal from service and on pension benefits at normal retirement. However, it is well arguable that the Regulations envisage a value test in respect of the totality of the benefits of the member concerned, although that is not the DSS view. This argument can be based on the fact that Regulation 3 does not expressly refer to an adverse effect on a benefit or even benefits collectively: rather, it refers to an adverse effect on the member in respect of his accrued rights. It can then be argued that there is no adverse effect on the member if some benefits go up and some go down. If our view (which accords with the DSS view) is right, we can see no distinction based on the wording of the Regulations between the effect of a modification on benefits payable on different contingencies (*eg* death after withdrawal from service and surviving to normal retirement) and different benefits payable on the same contingency. We therefore consider that the effect of a modification such as change in the definition of pensionable salary has to be looked at in respect of each component benefit of the package of benefits payable on that contingency.

- 5.4.3 We agree that where there are two changes to the same benefit (*eg* a change in the definition

of pensionable salary and a change to the accrual rate) it is the combined effect of the overall amendment which has to be considered; it is not necessary to look at each change as though it were a separate amendment.

5.5 *Is the contingent beneficiary protected in the right of the member while the member is alive, not in his or her own right?*

5.5.1 Yes, but see also under **Contingent Benefits** below.

5.6 *Is the member's statutory or scheme right to a transfer value an "entitlement" or "accrued right" for the purposes of section 67? What is the status of the "transfer test"?*

5.6.1 Under the heading "benefits" the question arises whether a member's right to a transfer value (whether under the "cash equivalent" legislation or pursuant to express rules in a scheme) is an "entitlement, or accrued right" for section 67 purposes. If it is, then an adverse change in transfer value factors in respect of past service would be incapable of actuarial certification under the section (subject to the provision of suitable underpins), at least in cases where the scheme provides expressly for fixed factors and not simply for the application of such factors as the actuary considers appropriate from time to time. If it is not, then, without any change in the benefits under the scheme, the transfer value factors could be changed without affecting accrued rights.

5.6.2 If it is assumed (as we have advised is correct) that an active member has only "accrued rights" and not an "entitlement", then those accrued rights at a given time are

"the rights which have accrued to or in respect of him at that time to future benefits under the scheme" [section 124(2)(a)]

and those rights

"are to be determined as if he had opted, immediately before that time, to terminate

that [pensionable] service”. [section 124(2)(b)]

5.6.3 When a person opts out of pensionable service, he becomes entitled to a package of benefits: they will become payable to the member himself (*ie* rights to future benefits accrued to the member himself) or payable to his spouse/dependants (*ie* rights to future benefits accrued in respect of - but not to - the member). A similar distinction between rights which accrue to the member and rights which accrued in respect of him is to be found in the provisions of section 94 Pension Scheme Act 1993, providing the right to a cash equivalent. That cash equivalent relates to

“any benefits which have accrued to or in respect of [the member] under the applicable rules”

5.6.4 The right to a cash equivalent, at least under the legislation and probably under an express scheme provision, is not in our view a right which has accrued - either to the member himself or in respect of him - to future benefits under the scheme. The benefits are what become payable to the member and those claiming through him; the right to a cash equivalent is one, which if exercised, effects a discharge of the scheme from those benefits but is not part of those benefits.

5.6.5 As with so many aspects of section 67, this is not a view we can express with confidence. Indeed, it seems that many commentators and advisers are of the view, or have simply assumed, that the right to a cash-equivalent is an accrued right within section 67.

6. Powers of Augmentation and Section 67

6.1 How does Section 67 apply to augmentation powers?

6.1.1 At this point, we would like to consider an example which illustrates some of the difficulties of construction which arise in relation to section 67:

- (i) suppose two schemes (A and B) are identical save that scheme A has a power exercisable by the trustees with the consent of the employer to alter (up or down) the benefits of the scheme but Scheme B has no such power: both schemes have wide powers of amendment which could be utilised to alter benefits (up or down).
- (a) There can be no doubt that the wide powers of amendment are powers to modify the scheme within section 67. We think that there can be little doubt that the power in scheme A to alter benefits is also a power to modify the scheme: it is capable of being used to increase or reduce benefits which are expressly provided by the pre-existing provisions of the scheme and, if the “substance” approach which we have described is correct, it is therefore capable of being used to “modify” the scheme²³.
- (b) We do not think that the express power in scheme A can be regarded other than as a power to modify on the basis that it is only a power to alter an existing benefit. On that approach, a distinction would have to be drawn between that power and one which was wider *eg* in also authorising the introduction of a new benefit: as to the latter, we consider²⁴ that it is clearly a power to modify. It would be an extraordinary result if a change (whether up or down) in the level of benefits pursuant to the express power in scheme A would not be a modification and yet the identical reduction pursuant to the wider power would be. Whilst on any construction of section 67 it may be that some surprising results will flow, we do not consider that the Court will be prepared to draw that sort of distinction.
- (ii) Assume now that the circumstances of each of schemes A and B are such that the trustees and the employer wish to alter accrued benefits in such a way that certain of

²³ The position might be different if benefits were defined only by reference to a trustee’s discretion but that will not be the case in relation to the vast majority of benefits with which we are concerned.

²⁴ See para 12 above.

those benefits would be adversely affected²⁵. Clearly, the exercise of the amending power in scheme B would be a modification: and, for the reasons given, we think that the exercise of the specific enabling power in scheme A would also amount to a modification. Section 67(2) then applies since the modification is one which would adversely affect accrued rights: the alteration cannot be made, therefore, unless the consent requirements are fulfilled. There is nothing surprising about that result: it is the policy of the legislation that adverse changes to accrued rights should not be made without the necessary member consents.

- (ii) Next make a different assumption - that the trustees and the employer want to augment certain benefits.
 - (a) For the reasons already given, we consider that such augmentation is a modification to the scheme whether effected, as in scheme A, by use of the express power of augmentation or, in scheme B, by use of the wide power of amendment.
 - (b) Accordingly, the certification or consent requirements must be fulfilled unless it can be said that the augmentation is not one which “would or might affect any entitlement, or accrued right”, the issue to which we now turn.

6.2 *Is the augmentation of benefits a modification which “would or might affect any entitlement or accrued right”?*

6.2.1 It has been a widely expressed view that section 67(2) applies in any case where benefits might be affected even where it can be clearly seen, without the aid of actuarial assistance, that there can be no adverse effect *eg* the introduction of (or improvement in the rate of) fixed-rate increases to pensions once they have come into payment. If that view is correct, then it follows

²⁵ Assume that the trustees would be acting properly in making the change.

from our analysis of powers to “modify” that the exercise of a discretionary power to augment benefits would give rise to a need for the certification or consent requirements to be fulfilled.

We do not consider that the distinction between powers which change the benefits and powers which are inherent in establishing the amount of the benefit (considered in paragraph 3.3.2 above) assists; a discretionary increase to an existing benefit falls within the former category unless as a matter of construction, the exercise of the discretion gives rise to a new benefit. The position may be different where, on a winding up, there is an obligation on the trustees of a scheme to augment benefits, when it can be argued that the member has an existing right which is simply quantified in the course of the winding up.

6.2.2 However, we consider that there are arguments against that widely held view and in favour of a more restrictive meaning, according to which the exercise of a power of modification in a way which can, in any circumstances, operate only to improve a benefit does not “affect” that benefit for the purposes of section 67(2).

(i) First, the structure of section 67 draws a distinction between (i) (in section 67(2)) the exercise of the power in a manner which might “affect any entitlement, or accrued right, of any member” and (ii) (in section 67(4)) the exercise of the power in a manner which would, in the opinion of an actuary, “adversely affect any member of the scheme...in respect of his entitlement, or accrued rights”. In case (i), the focus is on the effect, if any, on the benefit; in case (ii) the focus is on the effect, if any, on the member.

(a) We should comment here that it seems to us clear that section 67 is concerned with protecting individuals: there can be no offsetting of benefit to one member against detriment to another. This appears from the reference in section 67(2) to the entitlement or accrued right “of any member” and is consistent with policy: see again William Hague MP:

“The hon. Gentleman also asked about offsetting improvements and decreases and I have covered that. [Section 67] will prevent amendments detrimental to individual scheme members. It will

not be permissible to offset improvements to some against decreases to others without the consent of each individual concerned.”²⁶

- (b) A change to a particular benefit might, in some circumstances adversely affect that benefit, but in other circumstances might improve it (*eg* a change from fixed rate increases to LPI increases on pensions once in payment). Such a change would clearly fall within section 67(2) because there may be circumstances in which the particular benefit is adversely affected. The change can only be made if the certification or consent requirement are fulfilled - in the context of section 67(4)(a) only if the actuary can express the opinion²⁷ that it will not adversely affect the member.
- (c) The purpose of section 67 can then be seen to be to protect the member from changes which might adversely affect him unless the actuary can express his view that the change in his opinion will not do so. This could happen (*eg* the change from fixed rate increases to LPI increases to pensions once in payment mentioned in (b) above) where a change to a benefit might, or might not, have an adverse effect on that benefit but will not, in the judgment of the actuary, in fact adversely affect the member. It can therefore be argued that section 67(2) is looking only at changes which are at least capable of having an adverse effect on the benefit, and not at cases which could only ever result in an improvement.
- (ii) Second, although this is perhaps only another way of making the same point, an improvement in a benefit leaves the original benefit unaffected and simply provides for an addition to it; this is to be contrasted with a reduction in the benefit, which of necessity affects the original benefit. On this way of looking at matters, the

²⁶ Standing Committee D, 8th June 1995 col 471

²⁷ It is his opinion which is required, not his warranty: see further at paragraph 4.4.2 above.

improvement of an existing benefit is treated in the same way as the introduction of a wholly new benefit (*eg* dependants' pensions in a scheme which does not already provide for them). As to an improvement of that latter type, it is difficult to see how section 67(2) could apply: although the introduction of a new benefit would be a modification of the scheme, the accrued rights of a member acquired before the introduction of the new benefit are left untouched so that the modification does not "affect" them at all²⁸. Note that the argument here is that the increase does not affect the benefit; it does, in our view, modify the scheme.

(iii) Against those points, it can be argued that:

(a) the result is to do no more nor less than to read in the word "adversely" before "affect any entitlement" in section 67(2); and that it is not possible to do so since section 67(4)(a) shows that the draftsman intended to draw a distinction between "affect" and "adversely affect"; and

(b) to do so would be to make a nonsense of the section since an actuary could never be satisfied that the member would not be adversely affected, as contemplated by section 67(4)(a), in a case where the modification "would...[adversely] affect" the entitlement or accrued right of the member. This would mean that there never could be a circumstance where both (a) the modification would (in contrast with might) affect the benefit and (b) the actuary could be satisfied that the modification would not adversely affect the member; but - so the argument runs - the section clearly contemplates such a possibility so that the points made in (ii) above cannot be right.

6.2.3 We do not think that those arguments are conclusive because we do not accept the premise on which they must be based *ie* that the approach is effectively to read the word "adversely" into section 67(2). There could, for instance, be an amendment of which it could be said that it

²⁸ Assuming that security of benefits is not an issue: as to which see paragraph 8 below.

certainly would affect the benefit (*eg* a change from fixed rate increases to LPI increases on pensions once in payment where the change does not leave the original benefit untouched in the sense of only adding something to it); or there could be an amendment of which it could be said only that it might affect the benefit (*eg* the removal of a widow's pension for a man who is unmarried at the date of the modification - it is only if he marries that the modification will have any effect on the benefits payable to or in respect of him under the scheme²⁹). A sensible meaning can therefore be given to section 67(2) without the need to read the word "adversely" into the subsection.

6.2.4 Unfortunately, that is not the only sensible meaning of section 67(2). The words "which would or might affect" can perfectly sensibly - and on one view more naturally - be read as referring to any modification which changes in any way, including improvement of, the entitlement or accrued rights of a member. If, for instance, a pensioner is awarded a one-off increase of 3% to his pension in the exercise of a wide power of amendment (there being no specific power for this purpose) the answer he would give to the question "Has the amendment affected your pension?" would surely be "Yes; it has increased it".

6.2.5 Our own view is that the more restrictive reading of section 67 is correct and that a modification which can only result in an improvement to a benefit is not within the scope of section 67(2).

We can, however, express that view only as an "on balance" view; indeed, our views about which is the correct conclusion have changed over the course of time.

6.2.6 The principal criticism of this restrictive reading of section 67 is that it does not sit easily with the way in which the section is drafted, and involves an element of "the tail wagging the dog":

- (i) section 67(2) is intended to be the filter mechanism by which the trustees determine whether or not the actuary is to become involved in the certification process;

²⁹ We realise that this example raises another central issue *ie* the meaning of accrued rights and the extent of the protection afforded by section 67(2), as to which see above

- (ii) reading section 67(2) in isolation from section 67(4), the meaning is clear: a benefit augmentation might affect an entitlement or accrued right of a member;
- (iii) the above interpretation of section 67(2) is, however, dependent upon reading it in conjunction with section 67(4), at which point in time the actuary has become involved in the process;
- (iv) yet the point of the exercise is to avoid the involvement of the actuary at all: in other words, the consideration of section 67 should begin and end with sub-section (2), and should not go on to consider sub-section (4).

6.2.7 Our preferred interpretation of section 67 is therefore reliant upon the Court adopting a purposive construction of the section to reach a result contrary to the widely-held view as expressed in paragraph 6.2.1 above.

6.2.8 Further, we must point out that this view depends critically on the view that security for benefits has nothing to do with section 67: if that were not the case, then security issues would have to be looked at in the context even of an amendment which improved existing benefits or, indeed, introduced an entirely new benefit³⁰.

6.3 *Other powers*

6.3.1 Whichever view is correct on the limited question of augmentation powers, we do not think it can be said that every power which can impact on members' accrued rights is necessarily a power to modify. Consider, for example, commutation. Different schemes adopt different approaches. Thus

³⁰ We consider the question of security at paragraph 8 below.

- (i) Scheme A: fixed rate which would require scheme amendment to alter.
- (ii) Scheme B: fixed rate but with power for trustees (with advice of actuary) to alter.
- (iii) Scheme C: rate fixed by actuary from time to time (*ie* so that rate applies until actuary changes it).
- (iv) Scheme D: rate determined by actuary on each occasion of retirement.

6.3.2 Suppose that in each case the trustees, the employer and the actuary all consider that there should be a worsening of the rate to reflect changing market conditions. In our view, the position would be as follows:

- (i) Scheme A: an amendment is required and the case clearly falls within section 67.
- (ii) Scheme B: the same as Scheme A: the substance is the same as the amendment in Scheme A. This result would be the same, in our view, even if the power was vested in the actuary alone since section 67 refers to a power vested in any person.
- (iii) Scheme C: where the position is that the rate fixed by the actuary is to apply unless and until he changes it, the position is in substance the same as under schemes A and B. However, in some schemes, the rules may be silent about the commutation rate or simply provide for commutation at a rate to be determined by the actuary; but the trustees may, nonetheless, in practice apply a rate fixed by the actuary from time to time in order to avoid consultation him on each and every retirement. In these circumstances, we think the position is the same as under scheme D, as follows.
- (iv) Scheme D: in this case, there is no change to the provisions of the scheme at all and therefore no “modification”. A person retiring at a particular time has no right at all to have his commutation ascertained by reference to the rate which was applied on a previous occasion in relation to another individual

6.3.3 The difference between schemes A to C on the one hand and scheme D on the other hand is this. For schemes A to C, if there is no formal change to the commutation rate, then a retiring member is entitled to commute at the rate applied previously; for scheme D, the member is not entitled to commutation at any particular rate but only at the rate determined by the actuary on that occasion. The change required in the former case is a modification; there is no change at all in the latter case. This reflects the distinction to which we have drawn attention in paragraph 3.3.2 above.

6.3.4 Similar considerations apply in the cases of early retirement reductions and transfer values, in each case where those are an “entitlement” or “accrued right”³¹.

7. **Form of certificate**

7.1 *Should actuaries include in the certificate additional information relevant to their opinion as to the effect of the modification, such as legal advice received or assumptions used?*

7.1.1 From the trustees’ point of view an unqualified certificate, without setting out any assumptions in it, is most satisfactory. Since the actuary has to express his own opinion, there is an obvious risk of challenge if a stated basis for the certificate turns out to be wrong.

7.1.2 However, we think there could be little risk of challenge if the actuary were to set out his actuarial assumptions provided that he also states that in his opinion they were reasonable and appropriate. The actuary may also rely on legal advice when giving his certificate, a matter not within his own expertise. There is, perhaps, a distinction to be drawn between a certificate which states “I give this certificate on the basis of [effect of legal advice]” and one which states “In forming my opinion, I have taken legal advice to [effect of advice]”: it may be more difficult in the second case than the first for a challenge to be made on the basis that the legal advice was

³¹ See further at paragraph 5.6.2 *et seq* above in relation to transfer values.

wrong.

- 7.1.3 We think it is preferable not to make any reference to the advice in the certificate, although the client should be informed of the substance of the advice on which the actuary relies (as well as the actuarial assumptions which he makes as required by the Professional Conduct Standards).

8. Security of Benefits

- 8.1 *Is the security of benefits an issue which ought to be taken into account by the actuary when considering the effect of the modification?*

8.1.1 This has been an area of considerable debate among lawyers and actuaries. The only thing which can be said with certainty is that there is no clear answer. The issue of whether security of benefits needs to be considered in relation to the giving of a certificate under section 67 is tied in with the extent to which cash-equivalents form part of a member's "accrued rights" within section 124(2).

8.1.2 Assuming, contrary to our view, that the right to a cash-equivalent is an accrued right, then it must follow that an amendment to the scheme which reduces security to the extent that cash-equivalents have to be reduced would be an amendment requiring certification (and in respect of which a certificate could not be given). The fact that security is capable of being a section 67 issue in these special (albeit unlikely) circumstances lends some support to the view that security generally can be an issue and is a matter which the actuary will have to take into account. In particular, it cannot be argued that section 67 is only ever concerned with benefits and never at all with assets.

8.1.3 In contrast, if the right to a transfer value is not an accrued right, we are of the view that security of benefits is not an issue for the purposes of section 67. Security is dealt within the statutory framework by other protective provisions - notably the MFR and the debt on the employer

provisions. Security of benefits is no doubt a real issue - trustees need to take account of security and funding when they effect amendments to the scheme - but that goes to the propriety of a proposed amendment and not, in our view, to the power of the trustees to make it. These dual protections - MFR/debt on employer and trustee duties - make further protection under section 67 inappropriate in the context of the 1995 Act. It is certainly the case that section 67 says nothing express about security. It is expressed in terms of modifications which affect entitlements or accrued rights the natural reading of which is, we think, that it says nothing impliedly about security either.

8.1.4 Moreover, if security is an issue, it is very difficult to see precisely how it is to be taken into account.

- (i) For instance, if the “immediately before and after” test in relation to adverse effect on a member is correct, consistency of approach would suggest that security is to be judged at the same time. But is this to be done by reference to the adequacy of the reserves actually held to meet the buy-out cost of the accrued rights or must the assets be at least 100% of the scheme’s liabilities using the scheme’s valuation basis or some other basis? Whatever the correct answer is, it would seem that a certificate could not be given where, before the amendment, the scheme was 100% or better funded on both a buy-out basis and the scheme’s valuation basis and where the amendment moved the scheme into less than 100% funded on both those bases.
- (ii) Or, if the approach we favour (the third answer as we have described it) is correct, consistency of approach would suggest that the actuary should make a wider judgment whether or not the amendment will in his opinion be adversely affected. He should be looking to the future and the effect of possible events on the scheme. If the actuary has no reason to think that the scheme will be wound up in the foreseeable future and every reason to believe that the employers will fund the scheme on a proper basis, he may form the opinion that the amendment would not adversely affect accrued rights. And this could, in theory, be so even if the immediate effect of the amendment is to move the

funding from above to below 100%

(iii) The width of the necessary enquiry and the practical difficulties facing the actuary suggest that security is not in fact relevant in the context of section 67.

8.1.5 But the contrary is plainly arguable - indeed, strongly so if the right to a transfer value is an accrued right. Beneficiaries are interested in what they receive from the scheme, not just in what is said on paper they are entitled to. For instance, suppose a scheme is about to go into winding-up with an insolvent employer and the trustees propose to amend the scheme to change the priority of benefits in the winding-up. It would not be at all surprising to find section 67 prohibiting such an amendment which would be to the disadvantage of those whose benefits are moved lower down the list, and trust law may be ineffective to prevent it (the trustees may have good and proper reasons for wishing to make the change).

8.1.6 There is a danger that through constant repetition of the view that section 67 is not concerned with security - and that is the commonly expressed view in our experience - lawyers and actuaries generally come to accept that view as the “better” view. It must be remembered that the (real) doubts about the effect of the section in relation to security do not become less over time simply because more and more people accept that view. Ultimately, the answer will depend on what the Courts say; and they are unlikely to be impressed by the fact that there is a commonly held view.

8.2 *Is it relevant whether or not the scheme is in, or is about to go into, winding up?*

8.2.1 Either security is an issue or it is not. If it is not an issue, then it makes no difference whether or not the scheme is in winding up or whether one is imminent. If it is an issue, then each case needs to be looked at on its own facts; if the scheme is in winding up amendment is unlikely in any event, but if for some reason amendment is contemplated, it should be possible to determine with some certainty whether or not the amendment would³² impinge on accrued benefits *ie* it

³² In this context “would not” is looking forward to a proposed amendment; the effect of those

should be possible to tell if the result of the amendment will be that there are insufficient assets to meet any particular benefit.

8.3 *In considering whether a change to winding up priorities would adversely affect members' accrued rights and entitlements, should the actuary who is aware that the scheme is likely to go into winding up in the near future take a different approach to the one which would otherwise be taken?*

8.3.1 We fear the position may be rather more complicated if, contrary to our view, security is an issue. In all cases, we think it will be a matter of actuarial judgment whether accrued rights will be adversely affected. As we have already said, if the actuary has no reason to think that the scheme will be wound up in the foreseeable future and every reason to believe that the employers will fund the scheme on a proper basis, he may form the opinion that the amendment would not adversely affect accrued rights.

9. Contingent Events

9.1 *To what extent must the actuary take into account contingent events in forming his opinion, e.g. where the modification is likely to be prejudicial only in very unusual circumstances?*

9.1.1 Take the following example: an amendment is proposed which would only prejudice a pensioner or deferred member who is a widower with a handicapped child aged 16 or over. At the time of the amendment there is no such member but the amendment may potentially affect a member who is married with a handicapped child: should the actuary taken into account the possibility that the married pensioner's wife might predecease him and the child?

9.1.2 In our opinion, these contingent rights are "accrued rights" provided that they can potentially become payable in respect of a deferred pensioner. If they can only become payable in respect of an active member, they are not "accrued rights" since such rights are to be ascertained as if the member had left pensionable service. Our view is that the actuary does have to consider

words is we think the same as "does not" in relation to an amendment which has just been made.

whether or not such contingent rights might be adversely affected. But see paragraph 5.4 above as to whether a value test can be applied.

9.2 *Should the actuary, in relying on information provided by trustees and employers, take into account when assessing the contingency the possibility that they may not be aware of all aspects of members' personal circumstances?*

9.2.1 The actuary can only form an opinion on the basis of the information available to him and it is true that the trustees and the employer may not know all the detailed circumstances of each and every member and would not necessarily be in a position to know whether an amendment would or might adversely affect that member's accrued rights.

9.2.2 The actuary, however, has to express his opinion that the amendment would not adversely affect any member of the scheme.....in respect of his accrued rights. We do not see how the actuary can properly form that opinion unless he knows what the benefits of a member are. In practice, he must make reasonable enquiries himself unless there is an express provision in the scheme requiring the member to notify the trustees of relevant special circumstances. What is reasonable will depend on the facts of the case. For instance, if a deferred member's whereabouts are not known, the actuary may be entitled to assume that certain benefits are not payable.

9.2.3 Having said that, we are not at all clear how this problem could arise in practice since benefit entitlement may change with time. For instance, a deferred member may not have a dependent entitled to benefits today, but he may have tomorrow: his accrued rights may well include benefits in respect of the future dependent so that his actual current circumstances are not all that need to be considered.

9.3 *If security of benefits is an issue, must the actuary form a view of future levels of security, such as by reference to future economic factors and changing scheme membership, or can he base his opinion solely upon security immediately before and immediately after the modification?*

9.3.1 The answer to this depends largely on the correct comparison to make, an issue which we have discussed at length. We have also considered³³, in the context of security, whether and how the actuary is to take into account future events. We are left with the unsatisfactory conclusion - unsatisfactory because it gives no real guidance - that it is a matter for his professional judgment.

10. Contingent Benefits

10.1 Are benefits payable to a particular class of beneficiaries at the discretion of the trustees the “accrued rights” of those beneficiaries? What is the effect of changes to the size of the class to be considered by the trustees in the exercise of that discretion or the size of benefits payable to those beneficiaries so selected?

10.1.1 It is probably the case - and certainly wise to proceed on this basis - that benefits payable at the discretion of the trustees amongst a class fall within the definition of “accrued rights”³⁴. Such a benefit may be for instance a lump sum death benefit or a dependant’s pension. Note that the “accrued rights” of a member includes rights payable in respect of him: Section 124(2)(a). But Regulation 2 extends the meaning of “member” for the purposes of Section 67 where the member has died. Where there is genuinely a discretion, so that no person has any right to benefit until the discretion is exercised, we think that the accrued right in respect of the member (whether a pensioner, deferred pensioner or active member) for the purposes of Section 124(2)(a) includes the “right” to have the discretion properly exercised. Contrast the case (as in paragraph 10.3 below) where the right in respect of the member is to payment of a benefit

³³ See paragraph 8.1.4(ii) above.

³⁴ We are not concerned with death in service benefits: they are not “accrued rights” of the member since such rights are ascertained on the basis that the member opts out of pensionable service

to an identified person (such as his surviving spouse).

10.1.2 Where an amendment does not affect the total amount of the benefit (*eg* of a lump sum benefit) but changes the class among which it may be distributed (either by extending or limiting it) we think that the accrued right is probably not adversely affected. Contrast the case of a pension, dealt with in paragraph 10.1.3 below. However, if the class is narrowed, there may be circumstances where the benefit will be adversely affected and no certificate could be given: this could occur where the benefit is not payable at all when the discretionary class is empty, rather than being paid to the estate of the member.

10.1.3 Where an amendment might affect the amount of a benefit, the position is different. For instance, where dependants' pensions are truly discretionary - in the sense that the trustees have a choice about to whom they will pay the pension - a change in the class of discretionary object could well result in a different, and less valuable, benefit being provided *eg* where the recipient is the person added to the class and the benefit turns out to be of a shorter duration. It does not necessarily follow that the member is thereby adversely affected in respect of his accrued right: it could, for instance, be argued that the member is advantaged - and not disadvantaged at all - because the trustees have greater flexibility about whom to benefit. Our view, however, is that an amendment which changes the composition of a class is clearly a modification to the scheme and also one which affects the benefit: a pension payable at the discretion of the trustees to A or to B for his or her respective lifetime is different from a pension payable to A, B or C for his or her respective lifetime. The "accrued rights" of the member include, under Section 124(2)(a), the right in respect of him to future benefits, *ie* the right to have a pension paid to A or B. This right is modified to a right to have a pension paid to A, B or C; the modification does, in our view, affect the accrued rights in respect of the member. Accordingly, such an amendment can be made only if the certification or consent requirements are fulfilled. The actuary therefore needs to decide whether the amendment will, in his opinion, adversely affect the member. In many cases he may be able to give that certificate on the basis that the benefit, after the amendment, is in fact as (actuarially) valuable³⁵ as it was before.

³⁵

Since it cannot be said in advance either to whom the benefit will in fact be paid or how long

10.1.4 Although the focus of section 67(4)(a) and of Regulation 3 is on the member in respect of his accrued rights or entitlement, we do not think that the mere fact that the class is being extended necessarily entails that the member is not adversely affected in respect of his accrued rights, since the effect of the modification may be to reduce the value of the benefit if the trustees exercise their discretion in a particular way (eg if a discretionary class is extended to include the parents of a member and the discretion is exercised to benefit the (elderly) parents rather than the (young) partner of the member). In this context, we point out that the Section and the Regulation are not concerned only with the member's own position; they are also concerned with the effect on the member in relation to other benefits payable in respect of him.

10.1.5 We have considered in paragraph 4.4.2 above the approaches which the actuary might take in deciding whether he can give a certificate. The effect of the amendment will need to be examined in relation to each member separately. It may well be that the actuary is simply unable or unwilling to express the view that the amendment would not adversely affect the member. We do not consider that the potential duration of the benefit if payable to the additional member of the class can simply be ignored.

10.1.6 In practical terms, it seems to us that certification problems could be avoided by making use of that part of Regulation 3(1) which in effect allows the actuary to give a certificate even if it has an adverse effect on the member provided that it does not do so without the consent of the member. In other words, the change to the class of discretionary beneficiaries could be expressed to take effect only if the member consents to that change at some later date (eg by signing a nomination form consenting to an addition of further beneficiaries to the discretionary class).

10.2 *Could a certificate be given where the modification:*

the recipient will live, the only test which can be applied is one of value rather than quantum of the benefit.

- (i) *widened the class of people prospectively entitled to the benefit without reducing the amount of benefit;*
- (ii) *reduced the scope of the relevant class of contingent beneficiary*
- (iii) *reduced the duration of payment of benefits to a contingent beneficiary (for example, by reducing the maximum age for payment of a benefit to a child in full-time education from 25 to 23);*
- (iv) *changed a discretion to pay a spouse's benefit from "any beneficiary" (including the legal spouse) to the legal spouse or, if there is no legal spouse, to any other beneficiary*

10.2.1 In relation to these cases, the position we think is as follows:

- (i) a certificate can be given in the case of a lump sum benefit; in the case of a pension benefit, the actuary will have to make a judgment about value - see paragraph 10.1.3 above.
- (ii) section 67 applies but a certificate could not, in many cases, be given;
- (iii) benefits would be adversely affected and a certificate could not be given;
- (iv) the effect of this change could be adverse. Section 67 applies and the actuary may decide that he cannot give a certificate. The effect could be adverse since a pension payable to a surviving spouse may be expected to be of shorter duration than a pension payable to another member of the class, *eg* a younger partner.

10.2.2 In some of these cases - for instance adding a "common law spouse" to a discretionary class - it may be possible to draft an amendment in such a way that the actuary can give his certificate by providing for the change to take effect only with the (subsequent) consent of the member, relying on the words "(without the consent of the member)" in Regulation 3(1) of the Modification Regulations.

10.3 *What of a modification which removed the right of a member's legal spouse to be paid a spouse's pension, replacing it with a provision that, where a member had a legal spouse but is living with a common law spouse, part or all of the benefit should go to the latter?*

10.3.1 Similarly, in this example, it seems to us that the actuary could not give a certificate: although the monetary amount of the benefit would be the same regardless of the modification, its duration (as to the part going to the common law spouse) will be different and may be less. Even if the actuarial value of the benefit does not immediately change as a result of the amendment, there is (in contrast with the position under paragraph 10.2.1(iv) above) an actual accrued right *ie* the widow's benefit, which clearly is adversely affected and it is far from clear that a value test can be applied in these circumstances. This is because the widow's benefit forms part of the member's accrued rights as defined in Section 124(2)(a) as a right accrued in respect of him to future benefits under the scheme. The amendment clearly adversely affects that right even if it is replaced with another right of equal value (*eg* to a benefit payable to a wider class at the discretion of the trustee). Whereas the extension of an existing discretionary class (as in paragraph 10.2.1(iv) above) is properly to be regarded simply as a change to an existing "right", we think that the replacement of a widow's right to a benefit by a discretionary benefit is the creation of a new "right". The position is, in principle, no different from that of an amendment replacing, compulsorily, part of a member's own pension with a surviving spouse's pension.

11. Benefits contingent on future economic circumstances

11.1 *What factors are to be considered by the actuary when considering a proposed modification to guaranteed pension increases?*

11.1.1 It has been suggested that the "adverse effect" of such a modification can be judged simply by reference to current market conditions. We do not agree with that, but we do consider that this is one circumstance where a value test is to be applied. In other words, using his judgment

about future rates of inflation the actuary should form his opinion whether the change to the particular benefit of the individual member concerned (having regard to his age and to the length of time over which the pension will be payable and the date of its commencement where it is not already in payment) adversely affects the benefit. The actuary will, no doubt, take some account of the possibility of unlikely circumstances *eg* rates of inflation of 25% or more, but in forming his opinion he may discount that possibility even to the extent that he considers it can be ignored.

11.1.2 The actuary might judge as follows:

“It is possible that inflation will be so high or so low that the change will have an adverse effect on the benefit at some time in the future: but my opinion is that that is very unlikely. In my opinion, the benefit will not be adversely affected but I accept that events could prove me wrong.”

It seems to us that an actuary forming that sort of judgment in the sort of case now under consideration could properly give a certificate.

11.1.3 Similar considerations apply to cases where there is a proposed change to the basis period by reference to which pension increases are to be awarded *eg* where there is an increase by reference to the RPI between two dates. In the case of a pensioner, his entitlement is clearly affected immediately at the time of the amendment; in the case of an active member or a deferred pensioner, the amendment will not take effect until the pension falls into payment. The task for the actuary, in each case, is to form his opinion whether the change adversely affects the member and in doing should take account of his view of future likely inflation. In the case of a pensioner, the actuary can probably assess with some confidence whether the proposed amendment will or will not have an adverse effect on the next increase. If he can see that the effect will be adverse, that may have a considerable influence on whether he feels he can express the opinion that the amendment will not, overall, have an adverse effect on the member.

11.2 *Can an actuary give a certificate where the method of GMP revaluation is altered (whether it is effected by the exercise of an existing power or by way of scheme amendment)?*

11.2.1 It will be apparent from what we have already said that we do not accept the premise that because a change is effected using an existing power under the scheme it is therefore not a modification. We think that there is a real risk that a change in the basis of valuation is a modification within section 67 and that, subject to any statutory exclusion, the certification or consent requirements must be satisfied. The matter is then one of judgment.

11.2.2 This is now subject to the provisions of 6(1)(c) of the Modification Regulations³⁶.

12. Modifications incorporating Guarantees or Underpins

12.1 *Which of the following guarantees/underpins would be effective to allow a certificate to be given in the context of a change to the definition of pensionable earnings and/or final pensionable earnings under a scheme which might otherwise affect accrued rights:*

(a) *for benefits accrued to the date of modification, calculate final pensionable earnings as the greater of:*

- *that calculated on the **new** definition at the date of (subsequently) leaving pensionable service; and*
- *that calculated on the **old** basis at the date the change is introduced, without any revaluation;*

benefits after the date of the modification accruing on the new basis;

(b) *for benefits accrued to the date of (subsequently) leaving pensionable service, calculate benefits as the greater of*

- *those calculated for all pensionable service on the new definition; and*

³⁶ Inserted by Regulation 9 of The Personal and Occupational Pension Schemes (Miscellaneous Amendments) Regulations 1999 (SI 1999/3198).

- *those calculated for pensionable service to the date of modification, on the old definition;*
- (c) *as (a), but the guaranteed minimum amount is increased in the same way in which a deferred pension would be, so that on subsequent retirement or withdrawal from service the pension on the new definition is compared with the guaranteed amount increased by statutory revaluation;*
- (d) *grant a pensionable service credit (or debit) such that the combination of a new pensionable service definition and a new final pensionable earnings definition gives the same benefits at the date of modification as under the current definitions (without adding any revaluation to the guarantee on subsequent withdrawal or retirement from service)*

12.1.1 We think that we have dealt with the difficulties illustrated by the above examples in paragraph 5 above. We think that all of the guarantees set out in paragraph 12.1 above enable the actuary to give a certificate unless the second answer we have considered (*ie* the answer contained in paragraph 5.3.2(iv)(b)) is, contrary to our view, correct, in which case only underpin (c) would be effective. In the cases of the other solutions which we have considered (*ie* the “immediately before and after” test and the first and third answers contained in paragraphs 5.3.2(iv)(a) and (c)), each of the guarantees would be adequate.

13. Rectification of earlier errors and other legal imperatives

13.1 *Would section 67 apply to a rectification of a scheme (whether by deed or by Court Order) which operated to reduce the level of benefit provided under the provisions as originally drafted?*

13.1.1 In some cases, the error requiring rectification may be so obvious that it can be corrected as a matter of construction; in other cases, it may be necessary to rectify the deed. This Opinion is not the place to review the requirements which have to be fulfilled in order to obtain an order for rectification: it is sufficient to say that there has to be very clear evidence:

- (i) that an error has been made in transposing an expressed intention of the parties into

written form;

- (ii) that the parties maintained that intention up to the time of execution of the document;
and
- (iii) that the document as rectified would accurately reflect that intention.

13.1.2 If an order for rectification is obtained from the Court, it is effective from the date of the document. The order does not itself effect a modification but establishes that matters are as they were always intended. In some cases, it is not clear whether or not an action for rectification would succeed; in others, one can be reasonably confident that it will succeed; and occasionally, it is possible to advise almost with certainty that a rectification action would succeed. In relation to all of these cases, the question arises whether the trustees can avoid an application to the court by amending the scheme pursuant to an express amending power to give effect to the original intention by way of confirmation.

13.1.3 In all of these cases, it can be said that such an amendment either does or does not affect accrued rights. It is obvious, of course, that the amendment affects the wording of the scheme provisions relating to benefits, but that may be different from actually affecting the benefits themselves. Thus it is argued by some people that if there is a right to rectification, the actual benefits (*ie* even before an order for rectification is obtained) of the scheme are those which would be in accordance with the relevant wording after rectification. Accordingly, the argument goes, a formal amendment does not effect any change to the actual benefit entitlements.

13.1.4 As we see it, there are two real questions: one theoretical and one practical.

- (i) The theoretical question is this: assuming that a rectification action would succeed, what are the benefits which apply until an actual order is obtained?
- (ii) The practical question is this: is it safe, in the circumstances of any particular case, to act on the basis that rectification would be granted if it were sought, to make an express

amendment to formalise the position and not to make an application to the Court?

13.1.5 In our view, it is for the actuary to judge - to form his opinion - whether the change will have an adverse effect on the member.

(i) As to the theoretical question

(a) We think it is probably the case that a beneficiary would be able to claim only the benefits to which he would be entitled if the order for rectification were obtained. This is because if he sued the trustees who refused to provide him with anything in excess of the intended benefit, he would be met with a counterclaim for rectification which, on the hypothesis under consideration, would succeed. However, there is a respectable contrary argument for saying that a document should be given effect to unless and until rectified. For instance, the court will not order rectification when to do so would not affect the rights between the parties *eg* when they have already corrected the error out of court by agreement. This loss of right to rectification can effect the position *vis a vis* third parties such as the Inland Revenue which will be entitled to levy taxation on the basis of the unrectified agreement. This suggests that there is a real distinction between a right to rectify (which may only be effective as between the parties to the document and those claiming under them and which can be lost) and actual rectification.

(b) Assuming that the rights of beneficiaries are governed by the provisions of the deed as rectified even before an order for rectification is obtained, we are of the view that the entitlement and accrued rights for section 67 purposes are likewise the rights which would subsist under the deed as rectified. Accordingly, an exercise of the amending power to give formal effect to those rights would not affect - let alone adversely affect - any entitlement or accrued right. If that is correct, then the case is not within section 67 at all and a section

67 certificate is unnecessary. This, perhaps, is one case where the actuary should not be expected by the trustees to give a certificate: it should not be for the actuary to judge whether legal advice that an action for rectification would be bound to succeed is correct. We do not agree with those who consider a section 67 certificate is needed because the power is one to modify the scheme: it is not every exercise of a power to modify a scheme which falls within section 67, but only one which would or might affect any entitlement or accrued right.

It is true that an exercise of the power in the circumstances now under consideration modifies the wording of the document and in that sense modifies the scheme: but it does not do so in such a way as would or might affect any entitlement or accrued right.

- (ii) The practical question is when a trustee or employer could ever be advised that the case for rectification is so clear that a formal amendment will clearly not affect accrued rights. We think that such cases are bound to be rare. And there seems to us to be a risk, even in a clear case, of dealing with the matter out of court. The risk is that a beneficiary, perhaps many years later, will attack the corrective measure as a breach of section 67, effectively raising the question whether rectification is - or perhaps would have been - available. The trustees and employer may then face two problems in particular. First, it will be asserted that it is too late to obtain rectification and that such equitable relief should have been sought in good time. Second, the evidence on which the rectification claim would have been based may either not be available or may not be open to being tested. We accept that in some cases, oral evidence would be irrelevant and that the documentary evidence (which can be preserved) is all that is necessary to convince the court that rectification should be ordered. In other cases, oral evidence may be essential: and whilst that evidence can be preserved in the form of statutory declarations, the opportunity for cross-examination, for the testing of that evidence, declines as memories fade and eventually is lost altogether on the death of the witness. That is why we think it is only in the most exceptional case that trustees and employers could be advised that the case is so clear that an out of court corrective

amendment can safely be effected. But as we have already said, we do not think that this is a matter for the actuary and consider it unlikely that a certificate would ever be appropriate.

13.2 *What if the amendment reflects an overriding legal imperative, such as a statutory requirement to modify the scheme?*

13.2.1 Where an amendment is made pursuant to a statutory power outside the scheme, section 67 does not apply. But if the amending power is found within the scheme even though its exercise may be compelled by legal requirements (eg under *Barber* or Inland Revenue requirements) it still falls within section 67.³⁷

14. **Retroactivity**

14.1 *Does section 67 require the certificate to be signed by the actuary before the power modify is exercised?*

14.1.1 We think that the only safe course is to obtain a certificate before the amendment is made. In this context, one needs to examine the power to see when it is exercised. Some powers of amendment have to be exercised by deed and be executed by trustees and employers; other may be exercised by resolution. Section 67(2) restricts the exercise of the modification power: it “cannot be exercised...” unless the [certification or consent requirements] are satisfied. We read that as requiring that the consent or certificate is acquired before the amendment is made; and civil penalties arise under Regulation 8 of the Modification Regulations in such a case.

14.1.2 Given that view, we do not express a final view on the difficult question of the effect of a certificate given in relation to, but after the purported making, of an amendment. At the

³⁷ The Personal and Occupational Pension Schemes (Miscellaneous Amendments) Regulations 1999 provide that section 67 does not apply to modifications required by the Revenue to ensure that the scheme can remain exempt approved

moment, we incline to the view that the exercise of the power is a nullity.

- 14.1.3 Trustees can obtain a certificate for a modification which changes members' accrued rights or entitlements from an earlier date, provided that there is no adverse effect and the change is otherwise permissible under the terms of the scheme.

15. When things go wrong

- 15.1 *In what circumstances may an actuary's certificate be successfully challenged for non-compliance with section 67? What is the effect of such a challenge on the modification?*

15.1.1 If the actuary gives a certificate which is given in good faith and reflects his true opinion, then in our view an amendment made in reliance on that certificate is immune from challenge for non-compliance with section 67, although it may be open to challenge on other grounds *eg* by invocation of the *Hastings-Bass*³⁸ principle.

15.1.2 Subject to such other challenges, the amendment would stand even if there was an adverse effect on a member. Indeed, this may even be the result where the actuary has been grossly negligent in giving his certificate but the trustees have acted in good faith. The contrary view - that the certification requirement would not be fulfilled when the certificate is given in bad faith or perhaps even when it is simply negligently given - would expose the trustees to civil penalties when they had done nothing wrong and indeed could not reasonably be expected to have discovered the error in the certificate themselves. It is no answer to that, we think, to say that in practice OPRA would not take any action in such a case.

16. The role of professional guidance

³⁸ [1975] Ch 25

16.1 To what extent is it possible to give actuaries guidance on the matters raised in this Opinion? What would be the risks for actuaries in following such guidance or for the profession in giving it?

16.1.1 We will be brief and to the point on this aspect. We do not consider that it is any part of the function of the Faculty or the Institute to give legal advice to their members. We think there is little, if anything, in the advice which we give in this Opinion which is appropriate to be reflected in a Guidance Note; certainly the most careful consideration needs to be given before such a course is taken. That is not to say that the profession cannot be given information on current thinking, as was done in relation to the Joint Meeting Note, but it has to be made clear that individuals are responsible for taking their own advice and should not rely on such information as an accurate representation of the legal position in conducting their practices.

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11 April 2000