Internal dispute resolution: Is this the best we can do?

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Abstract Internal dispute resolution (IDR) is shortly to celebrate its first birthday. One of the numerous offspring of the Pensions Act 1995, IDR's place in the family making up the pensions complaints framework was being queried by its elder sibling, the Pensions Ombudsman, even before its official birth. The DSS is already proposing revisions to the governing regulations which would change the relationship of IDR to the Pensions Ombudsman's jurisdiction. But will this be enough to support and nourish the younger and less articulate child?

In this paper, the original intention behind IDR is compared with the actual result, and a number of legal problems are mentioned with a view to provoking a more wide-ranging review of the IDR structure in the context of the larger dispute-resolution family.

Keywords: *Pensions Act 1995, internal dispute resolution, Pensions Ombudsman, OPAS, litigation*

Background to IDR

Pre-Pensions Act 1995 position

At the beginning of the 1980s, the only choice for a scheme member who believed that he or she had a justifiable pensions grievance against the employer or the scheme trustees was to seek redress through the courts. Many scheme rules included an arbitration clause, but in practice the arbitration option was rarely invoked. The fact that it would be expensive and time-consuming for a scheme member to bring a court action was hardly a deterrent for the defending

employer or trustees. Very few pension cases did reach the courts in the course of that decade — and those that did (eg *Cowan v Scargill*,¹ *Stannard v Fisons Pensions Trust Limited*,² *Courage*³) tended to involve whole classes of members, with significant cost-raising capabilities, rather than individuals seeking redress in relation to an alleged personal wrong. Only two years ago, one of the few judges to have adopted a specialised interest in pension cases was able to observe that while

'the social and economic importance

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of occupational pension schemes has been apparent for many years . . . it is only in the course of the last 10 years that pension schemes have come before the Court in significant numbers . . . there are only four important decisions of the Court of Appeal, and none yet of the Lords.⁴

New choices

In a remarkably short period of time, however, new choices became available as follows:

- 1983: establishment of Occupational Pensions Advisory Service (OPAS);
- 1990: establishment of office of Pensions Ombudsman;⁵
- 1997: introduction of internal dispute resolution requirement.

This paper examines the particular features of the internal dispute resolution (IDR) procedures prescribed by the Pensions Act 1995, and suggests that the speed with which the current arrangements were put in place may have been at the expense of coherence and efficiency.

PLRC recommendations leading to IDR

The Pension Law Reform Committee (PLRC) under Professor Goode, whose report was published in September 1993, was particularly concerned with the problems facing the individual in the field of dispute resolution. The PLRC report was written in the context of the procedures being operated by Dr Farrand's immediate predecessor as Pensions Ombudsman. Given the change brought about by Dr Farrand's appointment, it is interesting to remind ourselves of the self-imposed restrictions governing the Pensions Ombudsman's

policy on dispute resolution. In 1993, the Pensions Ombudsman did not consider disputes involving:

- the exercise of trustees' discretions;
- the amount of transfer values;
- disputes about scheme investments or investment performance (unless involving abuse or malpractice).

The emphasis was strongly on the individual wrong of the traditional maladministration type. Heavyweight legal analysis was avoided. Turnover was modest and leisurely.

Dr Farrand immediately swept all this away. In particular, he studiously ignored arguments that particular disputes brought to his attention were really class claims dressed up as individual disputes. The traditional understanding of maladministration was that an individual citizen had received high-handed or arrogant treatment by a monolithic public body. The current Pensions Ombudsman's interpretation is more far-reaching.

If Parliament had intended to restrict his jurisdiction to 'individual' disputes of the traditional maladministration type, then Parliament had every opportunity to have made this clear. But the issues simply do not seem to have been thought through when the Pensions Ombudsman's office was set up.

In making its final recommendations, the PLRC stressed that it believed that the numbers of disputes and grievances, both individual and collective, would be reduced by the implementation of a number of *other* proposals which were intended to be complementary to its IDR proposals.

It is therefore worthwhile noting some of these other recommendations, and comparing them with the outcome in the Pensions Act 1995.

Proposal 1

OPAS should be given sufficient financial support to enable it to employ professional conciliation staff and generally 'upgrade' its dispute-resolving facilities.

Outcome

Not adopted, primarily as a result of OPAS's express preference to avoid the bureaucracy inherent in 'professionalising' a service which otherwise appeared to operate rather effectively.

Proposal 2

That the Pensions Ombudsman's jurisdiction should be extended to include disputes between employer and the trustees or among the trustees themselves.

Outcome

Accepted.⁶

Proposal 3

The Ombudsman should be given the power to enforce his determinations directly.

Outcome

Not accepted, but in practice determinations are enforceable by the successful party through the county court.

Proposal 4

The Pensions Ombudsman's determinations should be published.

Outcome

Accepted in principle. Copies of determinations are in practice readily available through membership of the Society of Pension Consultants (SPC).

Proposal 5

The Pensions Ombudsman should be given specific power to make 'distress' payments.

Outcome

Rejected on the basis that the Ombudsman could already order restitution for *financial* loss. 'It is not considered appropriate to allow the Ombudsman to order the payment of compensation'.⁷ The power of the Ombudsman to award 'distress' payments has nevertheless been upheld by the courts on the basis of the *existing* legislation.⁸

Proposal 6

Schemes should be required to establish a formal internal disputes procedure *of a nature approved by the Regulator*.

Outcome

Accepted, *except* as regards the need for the Regulator to approve the arrangements. Whatever the nature of the 'approval' envisaged by the PLRC, there would have been an enormous bureaucratic exercise involved in vetting the dispute procedures for every scheme to which the requirement would apply *unless* IDR had operated on a general code of practice basis — a point which will be returned to later.

Legal framework of IDR

From such origins the internal dispute resolution procedures were born. The broad requirement is set out in s. 50 of the Pensions Act 1995. The detailed framework is set out in the Occupational Pension Schemes (Internal Dispute Resolution Procedures) Regulations 1996.⁹

Section 50 requires that trustees or managers of a scheme must secure that IDR arrangements are made and implemented. As is well known, the basic IDR structure involves a two-stage process (if the complainant wishes to avail himself or herself of the opportunity

of an appeal). In the words of the statute:

- ‘The arrangements must —
- (a) provide for a person, on the application of a complainant of a prescribed description, to give a decision on such a disagreement [ie a disagreement between prescribed persons about matters in relation to the scheme], and
 - (b) require the trustees or managers, on the application of such a complainant following a decision given in accordance with paragraph (a), to reconsider the matter in question and confirm the decision or give a new decision in its place.’

Problems

Legal status of decisions under IDR

In law, a determination by OPAS is effectively no more than a recommendation to a scheme that a particular course of action should be taken (or that the complainant is not justified in his claim). A determination by the Pensions Ombudsman, as noted earlier, is enforceable through the county court. A decision by the High Court is automatically enforceable.

In the case of IDR, however, the position is unclear. There is no machinery for enforcing a decision made under the IDR procedures. Nor is it clear whether a decision made by the ‘nominated person’ is automatically binding on the trustees or managers of the relevant scheme.

If the decision by the nominated person is entirely in favour of the complainant, what more need the complainant do to ensure that something is done about the original complaint? Even if the decision is in favour of the complainant, the nominated person must

still draw the complainant’s attention to the right to refer the disagreement to the trustees (Regulation 5(2)(d)). If it was intended that the favourable decision (so far as the complainant was concerned) should be the end of the matter, why should such a statement be necessary? If, on the other hand, the ‘appeal’ system is intended to operate only against unfavourable decisions, what mechanism is there for the trustees to vet the original decision by the nominated person before deciding whether or not they agree with it? A one-way appeal system hardly represents a level playing-field.

Whatever the original intention, the best that one can make of the legislation is to operate on the basis that the first-stage decision *will* bind the trustees unless the trustees restrict the scope of the nominated person’s powers.

On one argument, the nominated person will effectively be acting as agent of the trustees within the statutory framework. It has been suggested that it might be prudent to try to define the precise types of dispute which the nominated person has power to determine, eg disputes over benefit calculations, but not over ‘class claims’ involving complex merger terms. The problem here is in actually defining what is, and what is not, a dispute of an individual, administrative nature, and what may constitute a class claim even though only one individual may at the moment be affected.

One halfway house might be to attempt to circumscribe the nominated person’s authority so that the decision made at the first stage will be framed as a recommendation to the trustees that the disagreement is resolved in a particular way. This addresses the issue of ‘binding the trustees’ without contravening what appears to have been the spirit of the original PLRC proposals.

Role of nominated person

The Pensions Ombudsman can refer points of law to the High Court. The High Court can refer points of European law to the ECJ. The nominated person, in contrast, will be *obliged* by the regulations to give a decision. Moreover, the decision must be given within two months (or at some later date which remains unspecified). In short, the nominated person must 'have a go'. There appears to be no scope for the nominated person to say 'this is far too difficult for me'.

In 'having a go', however, we come back to the uncertain relationship between the nominated person and the scheme trustees or manager: if the trustees are unhappy with the nominated person's decision (assuming that they get to hear about it), there is no *statutory* mechanism for them to change it. This again suggests that an approach based on recommendations may redress the apparent inequity in the current framework under which there is no statutory right of appeal to or by the trustees where the first-stage decision supports the complainant.

Giving explanations

The original draft of the IDR regulations required both the nominated person and the trustees to give an *explanation* of the decision. This would have prevented them from hiding behind the principle of trust law which holds that trustees are not obliged to give reasons for the decisions arising from the exercise of their discretionary powers.¹⁰ In the final version of the regulations, this requirement was dropped. Instead, both the trustees and the nominated person are free to provide merely a 'statement' of the decision. It is true that the statement must be accompanied by details of any legislation and scheme rules relied upon (including

any rules giving a discretion). But this falls short of a requirement to give a lengthy explanation of the *reasons* for the decision.

One of the traditional reasons for not giving explanations is that it exposes the decision maker's reasoning to scrutiny. One of the purposes of IDR is to defuse disputes. If the reasons are good enough, why not give them? The position can be contrasted with that of trustees exercising a discretionary power. The trustees will be concerned that the exercise of the power cannot be attacked. A discretionary power automatically involves a spectrum within which a range of different, but equally valid, decisions can be taken.

In the case of IDR, however, the issue should have a right or a wrong answer. The complaint may concern a challenge to the exercise of the trustees' discretion, but a typical 'disagreement' will be that the complainant does not agree with that decision. The nominated person should be wary of falling into the trap of substituting his or her own views for those of the trustees. The *ITB* case underlines the point that where trustees have a discretion, the fact that someone else, be it the Pensions Ombudsman, a judge or, *a fortiori*, a nominated person under the IDR procedure, disagrees with the decision on grounds of alleged unfairness or partiality does not of itself make that decision invalid. A little reasoning given at the IDR stage may go a long way in forestalling a much lengthier investigation by OPAS and the Pensions Ombudsman.

Liability of nominated person

Suppose that the nominated person simply gets the law wrong: can he or she be sued for negligence? This is a fairly basic question, one would have thought, but it is a question which is unfortunately left open by the

regulations. Obviously there can be no claim where there is no loss, but rights which are lost — say as to whether a particular benefit should be included on winding-up of a scheme — would constitute loss for this purpose.

Until 1974, professionals who were engaged in the exercise of skill or judgment in relation to the resolution of disputes were generally considered to be immune from negligence claims. The public policy reasoning which was invoked to justify the position was summed up by one judge as being based on the rationale that it would be unfair for the adjudicator to be exposed to being ‘shot at by both sides’.

In two leading cases, however, the House of Lords has severely restricted the public policy principle.¹¹ In these cases, the court ruled that the previously understood policy of granting adjudicators a blanket indemnity against claims of negligence had to be balanced against another principle of public policy: that someone who holds himself or herself out to undertake a particular function has fundamental duties towards those who are obliged to place reliance on the outcome of their deliberations. While judges are immune from negligence claims, and magistrates enjoy specific statutory exemption,¹² the extent of the immunity beyond this is:

‘very dubious . . . the fact that someone is entrusted to resolve a dispute between parties will not of itself afford him immunity from actions for negligence.’¹³

The Pensions Ombudsman also enjoys statutory immunity from defamation claims.¹⁴ Suppose that the nominated person casts all the blame for a particular mistake on his or her predecessor, and the predecessor gets to hear about it. They might well feel that their own

integrity (and job prospects) was being unjustly impugned. Since the nominated person will not enjoy the same absolute immunity as the Pensions Ombudsman, the best that the nominated person can hope for is that the courts will support a defence based on what is known as ‘qualified privilege’. To plead this defence successfully, the nominated person will have to demonstrate that he or she was discharging a legal duty.

It may be advisable for the nominated person to seek an indemnity from the employer or (if they have power) the trustees in relation to any liability arising from the exercise of the statutory IDR function. Such an indemnity would not be caught by the prohibition on indemnities from the scheme in s. 31 of the Pensions Act 1995, which applies only in relation to indemnities against fines or penalties. The nominated person under the IDR framework is not exposed to the risk of incurring fines or penalties in the same way as the trustees themselves are.

Conflicts

In many cases one finds that the nominated person is the pensions manager. In many cases too, the complaint concerns a matter on which the pensions manager has either already given a view, or in relation to which the pensions manager has otherwise had some responsibility (eg the issue of an incorrect or misleading benefit statement).

It is a fundamental legal principle that a judge is disqualified from deciding a case in which he may be biased. This principle applies where the bias may reasonably be suspected, even if it does not actually exist: justice must not only be done, but it must be seen to be done.

There is, however, an exception in cases of ‘necessity’. In these cases, the person exercising the judicial or

administrative function is the only person empowered to hear the case. The problem with the nominated person category under the IDR framework is that it does not quite fit the exception. The nominated person is not appointed by statute. He or she is selected by the trustees. One possibility might be to appoint an alternate nominated person where there is a conflict.

Jurisdiction

Another potential trap in the IDR framework relates to jurisdiction. The PLRC's original recommendation was that IDR should provide a mechanism for dealing with disputes arising in relation to a pension scheme. There is nothing in the report which suggests that Professor Goode intended to limit the scope of IDR to disputes between members and *trustees*.

Many pensions-related disputes involve the conduct of the employer. A common example is the employer's refusal to consent to the grant of an incapacity pension. Technically, such cases will fall outside the jurisdiction of the nominated person, since there will not be disagreements between the member and the trustees. In practice, however, many IDR cases will involve a mixture of complaints about the conduct of the trustees and the employer, and it is often difficult to disentangle the two in a way which does not appear to the member to be a snub or a provocation to further action.

Trustees and nominated persons might prefer to take a pragmatic view of such cases. Although the DSS chose to prescribe a relatively detailed framework for IDR, it seems to go against the spirit of what IDR is meant to be about if advantage is taken of the technicalities of that framework to deny a member the opportunity to have his or her

disagreement considered as a whole. If this involves suggesting to a member that he does take up his case with the employer, then that, surely, is a useful outcome of the first-stage IDR process. As so often, what matters is the tone of the decision as much as its actual content.

Relationship to Pensions Ombudsman

A further troublesome issue has been the interface between IDR and the Pensions Ombudsman. As originally structured, the Pensions Ombudsman has been obliged to insist that complaints are put through the IDR process before he can consider them. The DSS is now proposing — apparently at the suggestion of the Pensions Ombudsman — that the regulations are changed to allow the Pensions Ombudsman to dispense with the IDR requirement, probably on a discretionary basis.

It will be interesting to see whether this effectively kills off IDR in its infancy. Why go through the rigmarole of the highly prescriptive IDR system and await a decision of (possibly) dubious enforceability, when at no extra cost you can go straight to the Pensions Ombudsman?

Does IDR work?

Original intention

In order to assess whether IDR works, one needs to look at what IDR set out to achieve. As discussed at the beginning of this paper, the PLRC recommendation was extremely general. The Regulator would have been given an overriding power to approve the IDR framework. This would have given scope to the Regulator to issue some general guidelines along the lines of 'best practice', having regard to the widely

differing types of scheme and types of dispute which are likely to arise. Would this have been such a bad outcome?

Problems with prescriptive approach

What we have instead is a classic example of what some may regard as the primary shortcoming in the Pensions Act 1995 approach, ie the potential loss of the general principle in the obsessive search for prescription and detail. True, the IDR regulations are mercifully shorter than the MNT regulations. The prescriptive approach, however, seems to seek to impose a template which unnecessarily over-formalises the process of dispute resolution at a very early stage. Some other technical legal problems arising from the prescriptive approach have been discussed earlier. The author's personal view is that IDR is the one area under the Pensions Act 1995 where a code of practice would have adequately met the perceived need — and most closely matched the solution envisaged by the PLRC.

Too early to judge?

Despite these shortcomings and difficulties, we do now have a requirement for IDR which did not exist a year ago. It is easy to criticise the end product without having allowed it the test of time to prove itself. The compliance culture in which all those involved in the pensions industry must now live does not easily lend itself to flexible solutions. All trustees now live in fear of maladministration claims, and given the prescriptive nature of the IDR regulations, they will wish to ensure that

they stick to the terms of the regulations to the letter.

Only time will tell whether any of the potential problems and pitfalls identified above will be the subject matter of the next wave of investigations by the Pensions Ombudsman. But one is perhaps entitled to conclude that the DSS might have done a little better first time around. Second-stage decisions are not *necessarily* the best decisions.

References

- 1 *Re Mineworkers Pension Scheme Trusts* [1985] Ch. 270.
- 2 [1990] PLR 225.
- 3 *Ryan v Imperial Brewing & Leisure Limited* [1987] 1 All ER 528.
- 4 Walker, Sir Robert, 'Some trust principles in the pensions context', paper delivered at the Conference on Trends in Contemporary Trust Law, University of Cambridge, January 1996, 1996 [PLR] 107.
- 5 Under s. 59B Social Security Pensions Act 1975, as inserted by s. 12(1) and Schedule 3 Social Security Act 1990. See also the comments on jurisdiction and interference with exercise of discretionary powers in *Edge v Pensions Ombudsman* ('the ITB case') — [1998] PLR 15, currently the subject of appeal to the Court of Appeal.
- 6 Section 157 Pensions Act 1995.
- 7 White Paper [1994] 'Security, Equality, Choice: The Future for Pensions', Cmnd 2594, June.
- 8 *Westminster City Council v Haywood and Pensions Ombudsman* [1996] PLR 161, although on appeal Millett, L. J. reserved the position of the Court of Appeal on the point on the basis that the issue would be likely to arise for full consideration in a future case. The High Court recently re-addressed the issue when laying down guidelines to the effect that distress awards should be capped at £1,000 except in (undefined) 'exceptional circumstances'.
- 9 S.I. 1996 No. 1270.
- 10 See *Wilson v The Law Debenture Trust Corporation p.l.c.* [1995] 2 All ER 337.
- 11 *Edge v Pensions Ombudsman* [1998] PLR 15 (but note outcome of appeal is currently awaited). *Sutcliffe v Thackrah* [1997] AC 727, *Arenson v Arenson* [1997] AC 405.
- 12 Courts and Legal Services Act 1990.
- 13 Clerk & Lindsell on Torts (1995) (17th Ed., Sweet & Maxwell, p. 420).
- 14 Section 151(7) Pension Schemes Act 1993.