2. A SELECTIVE UPDATE ON DEVELOPMENTS IN LIFE AND PENSIONS LAW DURING THE PAST YEAR

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The past year (September to September) has been fairly uneventful as far as life assurance law 'proper' is concerned althought the activities of the Financial Services Act Regulators continue to have an important and wide-ranging influence on the way in which life assurance business is conducted. Developments in connection with pensions have been of a rather more substantive nature. I shall seek to deal with both life and pensions in turn.

LIFE

There has been little 'proper' law (by which I mean either statutory or case law) decided during the past year and those cases which have been reported, have all involved the Regulators.

In *R-v-LAUTRO, ex parte Ross* (i), Mr Ross a director of the Winchester Group plc, an appointed representative of the Norwich Union, applied to the Court for an order of *certiorari* on the grounds that the Board of LAUTRO had failed to observe the rules of natural justice in exercising its power of intervention so as to prohibit the Norwich Union from accepting new business from the Winchester Group. The Norwich Union had not appealed against the Intervention Notice as they were entitled to do and instead, had given Winchester notice of termination of their appointed representative agreement. The application to the Court failed. The LAUTRO Rules provided for a right of appeal to the member of LAUTRO but went no further, nor, in the Court's view, was there any need to imply any such provision for the purposes of the rules of natural justice.

The LAUTRO rules were in place to protect the investors and the Court found that:

> "Once it was recognised, as inevitably it had to be, that a self-regulating organisation might have to act with urgency in order to achieve its purpose, then it would be undesirable to cumber it with the necessity to make a judgement as to whether time admitted of an opportunity to make representations".

The Court observed, interestingly, that under the provisions of the Financial Services Act ("FSA"), Sections 97 and 99, if a person was named in an intervention notice served by SIB, that person did have a right to refer the matter to the Financial Services Tribunal. No such right existed under the LAUTRO Rules. This is not surprising:

LAUTRO continually seek to distance themselves from the appointed representatives of their members; their action is focused very much upon the members themselves.

The case of *SIB-v-FIMBRA* (ii) was concerned with the time from which the Investors Compensation Scheme should take effect. The Scheme was established under Section 54 of the FSA although the legislation was unclear as to its effective commencement date. Various commencement dates might have been possible: the Court decided that the operative time was 18th December 1986 when the provisions of the FSA which gave meaning to the words "investment business" (Section 1 and Schedule 1) came into effect.

For those who enjoy a little schadenfreude at the expense of their professional colleagues, the case of *SIB-v-Pantell and others* (iii) will provide some interest. The case consisted of an action being taken by SIB against a foreign company, Pantell SA, and a firm of English solicitors, for dishonestly promoting shares in a US company to English investors. The allegation against the solicitors was that they had been "knowingly concerned" in Pantell's contraventions of Sections 3, 47, 56 and 57 of the FSA. Whilst we are informed by the FT report that Messrs Barlow Lyde and Gilbert appeared for the defendant solicitors, we do not, unfortunately, learn the identity of the defendants (after Barlow Lyde and Gilbert's name is reported, we are informed that they are "not the defendant solicitors"). This action had been brought by the solicitors to strike out SIB's statement for claim calling for appropriate compensation from Pantell and the solicitors, on the basis that, assuming the allegations were true, SIB was not entitled to the relief claimed against the solicitors.

The application was not successful: the Court held that under the terms of the sections, the Court could make such an order were the facts so proved i.e. that a party (the solicitors in this case) was knowingly concerned in a contravention and that a compensation order could be made as a result.

Finally, as far as 'proper' law is concerned, the effect of section 62 of the FSA which gives parties a right of action for damages who suffer loss as a result of any contravention of the Act, has been restricted in accordance with Section 62A of the Act. That Section provides that those rights shall be restricted to "private investors" only which is defined by The Financial Services Act 1986 (Restriction of Right of Action) Regulations 1991 (iv).

The definition is not entirely straightforward and was the subject of much debate (hence, no doubt, the need for specific regulations on the point) and covers individuals who are not carrying on investment business and any other person providing that they are not carrying on business of any kind. Regulation 3 does provide for circumstances in which a person who is not a private investor may still bring an action under Section 62 and includes three specific contraventions: where insider dealing may be involved, the breach of fiduciary duties and any attempt to exclude a liability which the FSA imposes and states to be incapable of exclusion.

The Financial Services Act Regulators have been busy throughout the year. Since Mr David Walker (as he then was) took over at SIB from Sir Kenneth Berrill in 1988, SIB has been moving away from providing a fully detailed rule book (with which the self-regulatory organisations were obliged to provide "equivalence" in their rule books) to a new three tier approach. The first tier, the "Principles", were established in April 1990. Consultative paper 42, was published in July 1990 and contained proposals for the Core Rules.

These rules, as their name suggests were intended to provide the "core" or basis for the third tier of rules to be provided by each SRO taking into account the requirements of their own particular members. Although the Core Rules have been made, they have not yet been brought into force. Many commentators seem to agree that although this new "simplified approach" may have been admirable originally, the change at this stage simply appears to add more complexity to the existing regulatory position and may well be the case of "too much, too late".

A typical example of what might be described as the fickleness of SIB in its regulations can be seen from its attempt to regulate "broker funds". These, in simple terms, are funds owned by a life office or operated by a unit trust company but managed by an insurance broker or associate. The subject of much abuse in the past for overcharging, under-performing, and being given, in some cases, preferential treatment at the expense of other policy holders, it was not surprising that this area should demand careful attention from SIB.

SIB has already tried two sets of rules in this area including the muddled attempt at distinguishing between "company" and "investor broker fund advisers". In November 1990, Consultative Bulletin No. 48 contained a new set of draft rules introducing what would have been SIB's third set of rules on the subject. This included a new distinction between "closed" and "open" funds i.e. those in which the fund manager was limited to investing in the funds of a life office or the unit trusts of a particular provider only or those where there were so such restrictions. By May of this year, a policy statement had been issued indicating that that idea, plus others, was not being pursued further. Emphasis was to be placed on disclosure rather than proscription. To date, no new rules of SIB have been published although the relevant SRO's have been the policy statement into account for the purposes of their rules.

A new IMRO Rule book has just been published. Most of the provisions come into effect from 30th November 1991. The new rule book attempts to simplify the existing rules in accordance with the new SIB approach, without major revision.

LAUTRO have also been busy during the past year. Their Rules Bulletin No. 38, published in October 1990 was of particular interest. This introduced new rules with regard to the compensation of independent intermediaries for extra work done by intermediaries as a result of administrative failures or other negligence on the part of life offices. Perhaps partly because of the recession, many intermediaries may have thought that during troubled times when business levels were low, the life offices would provide additional sources of income. Many cases of this kind were reported. The existing LAUTRO rules strictly control the amount of commission (which is widely defined to include almost any payment) payable to intermediaries. These new rules permitted compensation to be paid by intermediaries but only in circumstances where they have either instituted or would have grounds for instituting legal proceedings and lawyers have advised the Life Office that in their opinion:

> "It would be sensible and economical for the claim to be settled on the basis of a payment, which may be made without an admission of liability".

This is actually achieved by excluding such payments from the meaning of commission, hence the general restrictions do not apply. Interestingly, the one area which does not seem to be covered by the bulletin is the possibility that intermediaries could be taking secret profits from the life office without knowledge of their client. It appears clear in a number of cases that intermediaries have pursued such compensation without informing their client who might well feel that if any compensation were available, they should be one of the recipients.

Rules Bulletin 41 introduced new rules in connection with both appointed representatives and the powers of the disciplinary committee. The new rules regarding appointed representatives are generally designed to strengthen the degree of control of LAUTRO members over their appointed representatives. Specific provision has been made in order to limit the amount of credit that can be made available to representatives so as to:

> "Inhibit the malign effects of debt build-up on the sales techniques of representatives"

Further provisions are aimed at raising the standards of the "fit and proper" checks, to strengthen the rules on compliance procedures and to make it more clear to the public what kinds of business a representative is authorised to conduct.

The new rules on the powers of the disciplinary committee enable the committee to fine a member following a finding of misconduct. A similar power has recently been exercised by IMRO on two occasions levying fines of £50,000 and £100,000. Perhaps community service should also be an option?

FIMBRA have also started to publish their new rule book although at the moment, reference is still necessary to the old version in many areas. Entirely new catagories of membership have been established in an attempt to simplify the previous categories which were complicated and in certain cases somewhat arbitrary in their application.

Finally in connection with life business generally, a passing note should be made of the EC draft third life (framework) directive. The directive will provide for a single licence for authorisation which would be obtained from a company's home state and be valid throughout the Community. The directive provides for supervision and co-operation between member states and this will clearly involve much technicality: it would appear likely, for example, that each company would need to comply with the marketing rules and regulations applicable in the state where products are marketed, hence in this country, the LAUTRO rules on the subject would cover all products marketed here whatever their country of origin. Other provisions deal with, for example, the control of technical reserves and investments, disclosure to policy holders, and freedom of establishment and freedom to provide services. Implementation of the directive is not expected until 1994 or 1995.

PENSIONS

The Social Security Act 1990 was passed just over a year ago, but many of its provisions have come into force only during the past year. The Act introduced a number of disparate provisions, of which perhaps the most interesting have been: the obligation placed upon insolvency practitioners to appoint an independent trustee where an employer becomes insolvent: the establishment of the Pensions Ombudsman; the registration of occupational and personal pension schemes and the introduction of Limited Price Indexation ("LPI").

The new provisions with regard to independent trustees resulted from two cases in which the liquidator or receiver of an employer which was also the trustee of the company's occupational pension scheme had sought to exercise a discretion under the pension scheme to distribute its surplus. The decisions in these cases *(Mettoy -v- Evans & others* (v) and *Icarus -v- Driscoll (unreported)* were to some extent conflicting: In *Icarus,* the Court upheld the exercise of the discretion whereas in

Mettroy, the Court held that the exercise of the discretion clearly involved a fiduciary duty which could not properly be discharged by a liquidator/receiver who had conflicting duties to creditors. The new provisions insist upon an independent trustee being appointed. This statutory function is entirely new. There appear to be a number of unusual features and possible deficiencies in the Act and governing regulations (vi) one of which seems to be that whilst Schedule 4 to the Act appears to give the insolvency practitioner the right to appoint an independent trustee under the insertions to Section 57C to the Social Security Pensions Act 1975 ("the Pensions Act"), the position is by no means clear and does not even refer to any requirement that such appointment should be in writing.

Although there are some provisions which seek to ensure a degree of independence on the part of the independent trustee, in view of the fact that an insolvency practitioner, who acts for the creditors, has the power of appointment, there is obviously room to question just how genuine this 'independence' will really be in practice.

The office of the Pensions Ombudsman is established by inserting new provisions into the Pensions Act and by new regulations (vii). This statutory basis contrasts with the office of the Insurance Ombudsman which was established on a voluntary basis by the insurance industry alone. Decisions of the Pensions Ombudsman will be binding on both parties (unlike the Insurance Ombudsman which binds the insurer only). There would also seem to be some overlap between the two "Ombudsmen" with e.g. personal pension contracts. A simultaneous referral by an aggrieved investor to both Ombudsmen, suggests an interesting possibility.

LPI was intended to provide a system whereby deferred pensions and pensions in payment should increase annually at the rate of 5% or at RPI if less. The former provision was introduced on 1st January 1991 but the escalation of pensions in payment has been deferred by the Government for the time-being in view of the uncertainties caused by the *Barber* judgement (on which more below).

Finally, in connection with the Social Security Act, the Government has established the Register of Occupational and Personal Pension Schemes (viii). The general intention behind these provisions is to ensure that individuals do not lose track of pension entitlements from previous employers. Currently, a large number of individuals simply fail to take up their pension rights because they have been unable to trace their entitlement under previous schemes.

The case of *Barber -v- G R E* (ix) received wide-spread publicity after the European Court judgement on 17th May 1990. The general effect of the case has been clear: an insistence upon equality between men and women in pension provision. The great unknown, however, has been in connection with "retrospection" i.e. from which date such equality should take effect.

The National Association of Pension Funds (NAPF) obtained a joint opinion from counsel (Jeremy Lever Q.C. and Nicholas Warren) in connection with the precise effect of retrospection although leading pensions lawyer John Quarrell has described obtaining such an opinion as "a waste of time and of their members' money". Indeed, the attempt to 'interpret' a translation of a judgement given in French on a point which clearly was not being considered fully by the judges at the time (it was not relevant to Mr Barber's circumstances) does not seem destined for a satisfactory conclusion. The view of Counsel was that the necessity to provide equal benefits should only apply to benefits accruing after 17th May 1990. This would mean that the effect of the judgement would not fully work itself through until 40 years or so into the future (i.e. when young people with some pension benefits which accrued before the 17th May 1990, finally retired). A number of cases where this issue is relevant are now being prepared for further hearing before the European Court (x). The Government is known to be lobbying hard in favour of this restrictive interpretation in view of the effect on company pension schemes and the need for employers to inject further resources to meet these increased liabilities.

The case of *Imperial Group Pension Trust -v- Imperial Tobacco* (xi) was an important case in the development of pensions/trust law. The heady days of the 1980's had seen a surplus arise in the Imperial Group Pension Scheme of £130m. The company was not, however, permitted to receive any part of the surplus. It sought to place pressure upon members to abandon existing rights and transfer their entitlement to a new scheme where the company could participate in a distribution of the surplus, by refusing to agree to annual increases in pensions. Under the rules of the schemes, the employer's consent was required for such increases. The question was raised as to whether the employer was entitled to refuse consent obsolutely or whether there were any implied obligations upon the employer in considering its consent.

The court had enquired as to why the company had sought to encourage members of the scheme to transfer to a new scheme rather than consent to the increases: no answer was given by the employer and the reason must have been fairly obvious. The Court held that the company's right to give or withhold its consent was subject to an implied term that such right was not validly exercisable in breach of the obligation of good faith which should exist between employer and employees.

Finally, as with the life side, a draft EC directive has recently been published, the first in connection with the "co-ordination of laws, regulations and administrative provisions relating to pension funds". Judging by the reference to the kinds of schemes covered, the draft is still in early form in that the definition of UK schemes covers, "pension funds for approved pension schemes including those set up under irrevocable trusts", would seem to merit a certain amount of possible expansion and refinement. Member states will not be permitted to restrict freedom of pension funds to choose an investment manager or custodian from another member state. Article 4 of the draft provides for various principles of investment which are largely in line with the provisions of existing English law. The final provision restricts self-investment to a "prudent level" which is the subject matter of a recently published draft statutory instrument.

The Directive in its present form seems unlikely to have much general effect upon pensions business in the UK.

(i) *The Financial Times* 17th July 1991, *The Times* 22nd July 1991.

(ii) *The Times* 9th July 1991, NLJ 1035

(iii) *The Financial Times* 9th August 1991

(iv) 1991 SI No. 489

(v) *The Financial Times* 9th February 1990

(vi) The Occupational Pension Schemes (Independent Trustee) Regulations 1990 SI No. 2075

(vii) The Personal and Occupational Pension Schemes (Pension Ombudsman) Regulations 1991 SI No. 588

(viii) Register of Occupational and Personal Pension Schemes Regulations 1990 SI No. 2278

(ix) (1991) 1 QB 344

(x) See *Pensions Lawyer,* July 1991 for a recent summary

(xi) *The Times* 6th December 1990