1997 No. 665

PENSIONS

The Occupational Pension Schemes (Pensions Compensation Provisions) Regulations 1997

Made - - - -	*6th March 1997*
Laid before Parliament	*13th March 1997*
Coming into force	*6th April 1997*

The Secretary of State for Social Security, in exercise of the powers conferred upon him by sections 56(3), 81(1)(c), (2) and (7) 82(1) and 3(a), 84(1)(b) to (3), 86, 124(1), 125(2) and 174(2) and (3) of the Pensions Act 1995**(a)**, and of all other powers enabling him in that behalf, having consulted such persons as he considers appropriate**(b)**, by this instrument, hereby makes the following Regulations:-

Citation, commencement and interpretation

1.—(1) These Regulations may be cited as the Occupational Pension Schemes (Pensions Compensation Provisions) Regulation 1997 and shall come into force on 6th April 1997.

(2) In these Regulations, unless the context otherwise requires–

"the audited accounts" means the accounts prepared by the auditor;

"the 1988 Act" means the Income and Corporation Taxes Act 1988**(c)**;

"the 1993 Act" means the Pension Schemes Act 1993**(d)**;

"approved scheme" means a scheme which is approved or was formerly approved under section 590 or 591 of the 1988 Act, or in respect of which an application for such approval has been duly made which has not been determined;

"the auditor" means an individual or a firm appointed by the trustees as auditor of the scheme;

"base rate" means the rate for the time being quoted by the reference banks as applicable to sterling deposits or, where there is for the time being more than one such base rate, the rate which, when the base rate quoted by each bank is ranked in a descending sequence of four, is first in the sequence;

"beneficiary" means a person, other than a member of the scheme, who is entitled to the payment of benefits under the scheme;

"Board" means the Pension Compensation Board**(e)**;

"compensation provisions" has the meaning given by section 81(3);

"ear-marked scheme" means an occupational pension scheme which is a money purchase scheme under which all the benefits are secured by one or more policies of insurance or annuity contracts and such policies or contracts are specifically

(a) 1995 c.26. Section 124(1) is cited because of the meaning ascribed to "prescribed" and "regulations".

(b) *See* section 120(1) of the Pensions Act 1995.

(c) 1988 c.1.

(d) 1993 c.48.

(e) The Pensions Compensation Board is established under section 78(1) of the Pensions Act 1995.

allocated to the provision of benefits for individual members or any other person who has a right to benefits under the scheme;

"guaranteed minimum pension" has the meaning given in section 8(2) of the 1993 Act;

"the loss" means the reduction falling within section 81(1)(c);

"money purchase benefits" has the meaning given in section 181(1) of the 1993 Act;

"money purchase scheme" means an occupational pension scheme under which all the benefits that may be provided other than death benefits are money purchase benefits;

"normal pension age" has the meaning given by section 180 of the 1993 Act;

"reference banks" means the four largest institutions for the time being which–

(a) are authorised by the Bank of England under the Banking Act 1987**(a)**,

(b) are incorporated in and carrying on within the United Kingdom a deposit-taking business (as defined in section 6, but subject to any order under section 7, of that Act), and

(c) quote a base rate applicable to sterling deposits;

"relevant insurer" means, in relation to an annuity contract or policy of insurance under which scheme benefits are or were secured, the person with whom the contract is made;

"scheme" means an occupational pension scheme which is a trust scheme;

"unallocated assets" means any assets of a money purchase scheme which have not been specifically allocated for the provision of benefits to or in respect of members (whether generally or individually).

(3) Unless the context otherwise requires, any reference in these Regulations to a numbered section is to the section of the Pensions Act 1995 bearing that number.

Schemes to which the compensation provisions and these Regulations do not apply

2.—(1) The compensation provisions and these Regulations shall not apply to–

(a) a scheme which has fewer than two members and not beneficiaries;

(b) a scheme the only benefits provided by which are death benefits and under the provisions of which no member has accrued rights;

(c) a scheme which provides relevant benefits, but is neither an approved scheme nor a relevant statutory scheme;

(d) a scheme whose members are fewer than 12, all of whom are trustees and under the rules of which all trustee decisions must be made by unanimous agreement, save that the non-participation of a pensioner trustee in any such decision shall be disregarded;

(e) a public service pension scheme;

(f) a relevant lump sum retirement benefits scheme;

(g) a scheme in respect of which any Minister of the Crown has given a guarantee or made any other arrangements for the purpose of securing that the assets of the scheme are sufficient to meets its liabilities;

(h) a section 615(6) scheme.

(2) In this regulation–

"lump sum benefits" does not include benefits paid by way of commuted retirement pension;

"pensioner trustee" has the meaning given in regulation 2(1) of the Retirement Benefits Schemes (Restriction on Discretion to Approve) (Small Self-administered Schemes) Regulations 1991**(b)**;

"public service pension scheme" has the meaning given by section 1 of the 1993 Act;

"relevant benefits" has the meaning given in section 612(1) of the 1988 Act;

"relevant lump sum retirement benefits scheme" means an approved scheme–

(a) 1987 c.22.
(b) S.I. 1991/1614.

(a) which has been categorised by the Board of Inland Revenue for the purposes of its approval as a centralised scheme for non-associated employers;

(b) which is not contracted-out; and

(c) under the provisions of which the only benefits which may be provided on or after retirement (other than money purchase benefits derived from the payment of additional contributions by any person) are lump sum benefits which are not calculated by reference to any member's salary;

"relevant statutory scheme" has the meaning given in section 611A of the 1988 Act**(a)**;

"section 615(6) scheme" means a scheme with such a superannuation fund as is mentioned in section 615(6) of the 1988 Act.

Relevant offences

3. For the purposes of section 81(1)(c) (cases where compensation provisions apply: reduction to be attributable to prescribed offence), the prescribed offence is any offence involving dishonesty, and for the avoidance of doubt dishonesty shall include an intent to defraud.

Applications for compensation

4. An application for compensation under section 82 in respect of a scheme may only be made by–

(a) the trustees of a scheme, or their representative;

(b) a person concerned with the administration of, or the provision of benefits under, the scheme, or his representative; or

(c) a member of, or beneficiary under, the scheme, or his representative.

Amount of compensation

5.—(1) If the Board decide to make a payment or payments to the trustees in accordance with section 83, the amount of any such payment or (if there is more than one) the aggregate must be determined in accordance with paragraph (2).

(2) The amount shall be the lower of the amounts specified in paragraphs (a) and (b) of section 83(3), less the amount of any payment already made under section 84(payments made in anticipation), except to the extent that any such payment has been recovered by the Board.

(3) For the purposes of section 83(3)(a) (compensation not to exceed 90 per cent. of the shortfall at the application date), and subject to paragraph (4), the amount of the shortfall at the application date shall be calculated in accordance with the formula–

$$P - Q$$

where–

(a) P is

(i) the value of the assets as stated in the audited accounts which most immediately precede the loss, adjusted by the auditor so as to take into account subsequent alterations in their value (if any) which occur prior to the application date, but disregarding the alteration in their value attributable to the loss itself, or

(ii) if there are no such audited accounts, the value of the assets on such date as immediately precedes the loss, as reported by the auditor, adjusted in the same manner as for the calculation under head (i), and

(b) Q is the value of the assets immediately before the application date, as reported by the auditor;

and the same principles are used to value the assets for the purposes of P and Q.

(4) In the case of an ear-marked scheme, the amount of the shortfall at the application date for the purposes of section 83(3)(a), shall be calculated in accordance with the formula–

(a) Section 611A was inserted by section 75 of and Schedule 6, Part I, paragraphs 1, 15 and 18(1) to the Finance Act 1989 (c.26).

P + R – Q

where–

(a) P is the value of the assets on such date as immediately precedes the loss, adjusted so as to take into account the loss and other alterations in their value (if any) between that date and the application date, as certified by the relevant insurer,

(b) R is the value of the assets constituting the loss on such date as immediately precedes its occurrence adjusted so as to reflect any alteration in the value of those assets which would have occurred had they remained in the scheme until immediately before the application date, as certified by the relevant insurer,

(c) Q is the value of the assets immediately before the application date, as certified by the relevant insurer,

and the same principles are used to value the assets for the purposes of P, R and Q.

(5) For the purposes of section 83(3)(b) (amount required to secure assets equal to 90 per cent. of liabilities), the value of the assets and the amount of the liabilities of the scheme on the settlement date shall be determined under an actuarial valuation carried out in accordance with regulations 3 to 9 of the Occupational Pension Schemes (Minimum Funding Requirement and Actuarial Valuations) Regulations 1996**(a)** and the mandatory guidelines on the minimum funding requirement contained in Guidance Note 27(GN27), prepared and published by the Institute of Actuaries and the Faculty of Actuaries**(b)**.

(6) For the purposes of section 83(3)(a)–

(a) the prescribed rate of interest shall be–

(base rate plus 2 per cent.) x 90 per cent.; and

(b) the prescribed period by reference to which the rate of interest specified in sub-paragraph (a) is calculated shall commence on the application date and end on the settlement date.

Payments made in anticipation

6.—(1) The prescribed class of liabilities referred to in section 84(1)(b) (liabilities the trustees would not otherwise be able to meet) are–

(a) any liability for payment of pensions which has arisen at the application date;

(b) any liability which arises between the application date and the settlement date for payment of–

(i) guaranteed minimum pensions,

(ii) pensions, other than guaranteed minimum pensions, payable to persons reaching normal pension age,

(iii) pensions payable to beneficiaries,

(iv) ill-health retirement pensions;

(c) in the case of a scheme where some or all of the benefits that may be provided are money purchased benefits, any liability such as is specified in paragraph (2).

(2) The liability referred to in paragraph (1)(c) is the approximate amount of any monthly pension that would have been payable in respect of money purchase benefits prior to the settlement date but for the loss.

(3) Except where any liability for payment of a pension arises in connection with terminal illness, such liability shall not for the purposes of this regulation include any liability for payment of a lump sum, whether or not deriving from the commutation of pension rights.

(4) For the purposes of paragraph (3), a person shall be regarded as terminally ill where his expectation of life is less than one year, and the expression terminal illness shall be construed accordingly.

(5) Payments made in anticipation shall be calculated–

(a) so that, so far as the Board is reasonable able to achieve, the extent to which liabilities specified in paragraph (1) are satisfied after the Board has made a payment under section 83, is undiminished;

(b) so as to counter-balance any payments in anticipation made previously which were too great or too small;

(a) S.I. 1996/1536.

(b) Copies of GN27 may be obtained from the Faculty of Actuaries, 17 Thistle Street, Edinburgh EH2 1DF.

(c) so as not to exceed the amount required to enable the trustees of the scheme, prior to the settlement date, to meet such liabilities as are specified in paragraph (1); and

(d) so as not to exceed 90 per cent. of the shortfall at the application date.

(6) For the purposes of section 84(3), the prescribed circumstances in which any payment made under section 84(1) may not be recovered, in whole or in part, are where such recovery would cause pensions in payment to be reduced.

Mixed benefit schemes

7.—(1) This paragraph applies where some, but not all, of the benefits that may be provided under a scheme are money purchased benefits.

(2) Where paragraph (1) applies to a scheme, and the assets out of which money purchase benefits are provided–

(a) are distinct from the assets out of which other benefits are provided, and

(b) cannot be used for the purposes of providing any other benefits,

then the compensation provisions and these Regulations shall apply as if the assets out of which money purchase benefits are provided, and the proportion of the liabilities which is attributable to the provision of money purchase benefits, were the assets and liabilities of a separate scheme.

(3) Where paragraph (1) applies to a scheme, and the assets out of which money purchase benefits are provided–

(a) are not distinct from the assets out of which other benefits are provided, or

(b) are so distinct but can be used for the purposes of providing other benefits,

then the compensation provisions and these Regulations shall apply as if the proportion of the liabilities which, in the opinion of the Board, is attributable to the provision of money purchase benefits, and a like proportion of the assets, were the liabilities and assets of a separate scheme.

Multi-employer schemes

8.—(1) Where a scheme applies to earners in employments under different employers–

(a) section 81(1)(b) shall have effect as if the words "the employers are insolvent" were substituted for the words "the employer is insolvent"; and

(b) section 81(3)(c) shall have effect as if the words "the last employer became insolvent" were substituted for the words "the employer became insolvent".

(2) Where a scheme in relation to which there is more than one employer is divided into two or more sections and the provisions of the scheme are such that–

(a) different sections of the scheme apply to different employers or groups of employers (whether or not more than one section applies to any particular employer or groups including any particular employer);

(b) contributions payable to the scheme by an employer, or by a member in employment under that employer, are allocated to that employer's section (or, if more than one section applies to the employer, the section which is appropriate in respect of the employment in question); and

(c) a specified part or proportion of the assets of the scheme is attributable to each section and cannot be used for the purposes of any other section;

or where–

(d) a scheme which has been such a scheme as is mentioned in sub-paragraph (a) to (c) is divided into two or more sections some or all of which apply only to members who are not in pensionable service under the section;

(e) the provisions of the scheme have not been amended so as to prevent the conditions mentioned in sub-paragraphs (a) to (c) being satisfied in relation to two or more sections; but

(f) those conditions have ceased to be satisfied in relation to one or more sections by reason only of there being no members in pensionable service under the section and no contributions which are to be allocated to it, the compensation provisions and these Regulations shall apply as if each section of the scheme were a separate scheme.

(3) For the purposes of paragraph (2), there shall be disregarded any provisions of the scheme by virtue of which contributions or transfers of assets may be made to make provision for death benefits; and where that paragraph applies and contributions or transfers so made to a section ("the death benefits section"), the assets of which may only be applied for the provision of death benefits, the death benefits section shall also be treated as if it were a separate scheme for the purposes of the compensation provisions and these Regulations.

(4) For the purposes of paragraphs (2) and (3) there shall be disregarded any provisions of the scheme by virtue of which, on the winding up of the scheme or a section, assets attributable to one section may be used for the purposes of another section.

Partially approved schemes

9. Where a scheme is not an approved scheme but contains a section which, by virtue of section 611(3) of the 1988 Act, is treated by the Board of Inland Revenue as an approved scheme, the compensation provisions and these Regulations shall apply to that section as if it were a separate scheme.

Modifications for money purchase schemes

10.—(1) In the case of a money purchase scheme, and subject to paragraph (2)–

(a) the compensation provisions shall have effect as if–

(i) for paragraph (d) of section 81(1) there were substituted–

"(d) in the case of a money purchase scheme, immediately before the date of the application the value of the assets of the scheme, as reported by the auditor, is less than 90 per cent. of their value immediately before the reduction falling within paragraph (c), where the value of the assets immediately before that reduction is adjusted by the auditor so as to take account of subsequent alterations in their value (if any) which occur prior to the date of the application, but disregarding the alteration in their value attributable to the reduction itself, and",

(ii) for paragraph (b) of section 83(3) there were substituted–

"(b) in the case of a money purchase scheme, must not exceed the amount, as reported by the auditor, which on the settlement date is required to be paid to the trustees of the scheme in order to secure that the value on that date of the assets of the scheme is equal to 90 per cent. of their value immediately before the reduction falling within section 81(1)(c), where the value of the assets of the scheme immediately before that reduction is adjusted by the auditor so as to take account of subsequent alterations in their value (if any) which occur prior to the settlement date, but disregarding the alteration in their value attributable to the reduction itself."; and

(b) these Regulations shall have effect as if for paragraph (5) of regulation 5 there were substituted–

"(5) For the purposes of section 83(3)(b) (amount required to secure that assets are equal to 90 per cent. of their pre-loss value), the amount required to be paid to the trustees of the scheme shall be calculated in accordance with the formula–

$$T \times 90\% - V$$

where–

(a) T is–

(i) the value of the assets (excluding unallocated assets) as stated in the audited accounts which most immediately precede the loss, adjusted by the auditor so as to take into account subsequent alterations in their value (if any) which occur prior to the settlement date, but disregarding the alteration in their value attributable to the loss itself, or

(ii) if there are no such audited accounts, the value of the assets (excluding unallocated assets) immediately before the loss, as reported by the auditor, adjusted in the same manner as for the calculation under head (i), and

(b) V is the value of the assets at the settlement date as reported by the auditor; and the same principles are used to value the assets for the purposes of T and V.".

(2) In the case of an ear-marked scheme–

(a) the compensation provisions shall have effect as if–

(i) for paragraph (d) of section 81(1) there were substituted–

"(d) in the case of an ear-marked scheme, immediately before the date of the application the value of the assets of the scheme, as certified by the relevant insurer, is less than 90 per cent. of their value immediately before the reduction falling within paragraph (c), where the value of the assets immediately before that reduction is adjusted so as to take account of subsequent alterations in their value (if any) which occur prior to the date of the application, including those which would have occurred if the reduction had not taken place, and",

(ii) after paragraph (b) of section 81(3) there were inserted–

"(bb) "ear-marked scheme" means an occupational pension scheme which is a money purchase scheme under which all the benefits are secured by one or more policies of insurance or annuity contracts and such policies or contracts are specifically allocated to the provision of benefits for individual members or any other person who has a right to benefits under the scheme,",

(iii) after paragraph (f) of section 81(3) there were inserted–

"(g) "relevant insurer" means, in relation to an annuity contract or policy of insurance under which scheme benefits are or were secured, the person with whom the contract is made.",

(iv) for paragraph (b) of section 83(3) there were substituted–

"(b) in the case of an ear-marked scheme, must not exceed the amount, as certified by the relevant insurer, which on the settlement date is required to be paid to the trustees of the scheme in order to secure that the value on that date of the assets of the scheme is equal to 90 per cent. of their value immediately before the reduction falling within section 81(1)(c), where the value of the assets of the scheme immediately before that reduction is adjusted so as to take account of subsequent alterations in their value (if any) which occur prior to the settlement date, including those which would have occurred if that reduction had not taken place."; and

(b) these Regulations shall have effect as if for paragraph (5) of regulation 5 there were substituted–

"(5) For the purposes of section 83(3)(b) (amount required to secure that assets are equal to 90 per cent. of their pre-loss value), the amount required to be paid to the trustees of the scheme shall be calculated in accordance with the formula–

$$(T + S) \times 90\% - V$$

where–

(a) T is the value of the assets (excluding unallocated assets) on such date as immediately precedes the loss, adjusted so as to take into account the loss, and other alterations in their value (if any) between that date and the settlement date, as certified by the relevant insurer,

(b) S is the value of the assets constituting the loss on such date as immediately precedes its occurrence, adjusted so as to reflect any alteration in the value of those assets which would have occurred had they remained in the scheme until the settlement date, as certified by the relevant insurer,

(c) V is the value of the assets at the settlement date, as certified by the relevant insurer,

and the same principles are used to value the assets for the purposes of T, S and V.".

Signed by authority of the Secretary of State for Social Security.

Oliver Heald
Parliamentary Under-Secretary of State,
Department of Social Security

6th March 1997

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations relate to the payment of compensation to occupational pension schemes by the Pensions Compensation Board ("the Board"), as provided for under sections 81 to 85 ("the compensation provisions") of the Pensions Act 1995 ("the Act").

Regulation 1 provides for the citation, commencement and interpretation of the Regulations.

Regulation 2 provides for exemptions to the compensation provisions.

Section 81(1) of the Act specifies the conditions which must be met for a scheme to establish eligibility for compensation. Section 81(1)(c) of the Act provides that the value of the scheme assets must have been reduced and that there must be reasonable grounds for believing that the reduction is attributable to an act or omission constituting a prescribed offence. Regulation 3 provides that the prescribed offence is one involving dishonesty.

Regulation 4 sets out who may make an application for compensation.

Section 83(3) of the Act provides that the amount of compensation must not exceed, first, 90 per cent. of the reduction falling within section 81(1)(c) of the Act at the application date ("the shortfall") together with interest on the shortfall at the prescribed rate for the prescribed period, and secondly, in the case of a salary-related scheme, the amount required to restore the scheme to funding level of 90 per cent. at the date after which the Board determine further recoveries of value are unlikely to be made without disproportionate cost or within a reasonable time. Regulation 5 provides that the total amount of compensation paid shall equal whichever is the lower of those amounts, and makes provision as to the manner in which such amounts are to be calculated.

Regulation 6 concerns payments made in anticipation of a final payment of compensation. It specifies the liabilities which a scheme must be unable to meet, either fully or in part, before anticipatory payments can be made; lays down criteria by reference to which such payments are to be calculated; and prescribes the circumstances in which such payments may not be recovered.

Regulations 7, 8, 9 and 10 provide for modification of the compensation provisions, where some but not all the benefits that a scheme provides are money purchase benefits (regulation 7), where a scheme applies to earners in employments under different employers (regulation 8), where only part of a scheme is approved for tax exemption purposes (regulation 9), and where all the benefits that a scheme provides (other than death benefits) are money purchase benefits (regulation 10).

An assessment of the compliance cost for employers of the measures arising from the Pensions Act 1995, including these Regulations, has been placed in the libraries of both Houses of Parliament. Copies can be obtained by post from the Department of Social Security, Pensions and National Insurance Directorate, The Adelphi, 1-11 John Adam Street, London WC2N 6HT.