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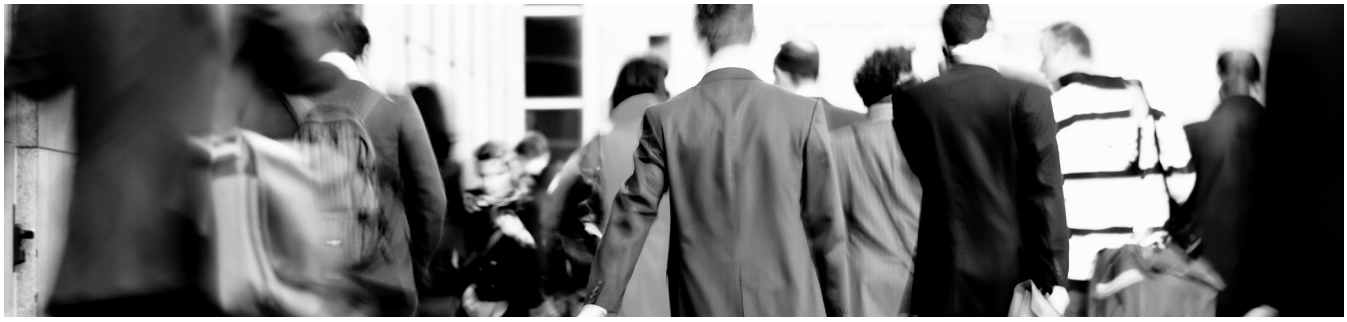

Pensions

Construction: the foundation for a fresh approach to correcting mistakes?

Briefing

March 2016

In a recent case, *Re BCA Pension Plan* [2015], the trustee sought successfully to correct a mistake in scheme documentation by making a Court application under section 48 of the Administration of Justice Act 1985. The Court was asked to issue an order that the trustee be permitted to administer the Plan as though words in the pension increase rule had not been mistakenly deleted during a consolidation exercise.

Introduction

Mistakes are surprisingly common in formal pension scheme documentation and, once discovered, should be corrected to ensure that members receive the benefits to which they are entitled. Frequently, the correction of such mistakes involves a full hearing of all the evidence and the application by the Court of the equitable doctrine of rectification. This is the usual remedy where the rules make sense but they happen to say something which the parties did not intend when the trust deed was executed.

However, sometimes it may be possible for trustees to take advantage of an alternative, cheaper route available under section 48 of the Administration of Justice Act 1985 (section 48). This latter course was the action taken in the recent case of *Re BCA* Pension Plan [2015], which we examine more closely in this briefing.

A reminder of the doctrine of rectification

In broad terms, the equitable remedy of rectification is available if two conditions are met:

- as the result of a mistake, a written instrument fails to express the true common intentions of its parties at the time it was executed
- the mistake cannot easily be corrected by other means.

Often in pension schemes where a mistake is discovered, it has the effect of awarding greater benefits than intended to members and, therefore, the scheme amendment powers are of no assistance, as any changes would fall foul of section 67 of the Pensions Act 1995.

In order for a rectification claim to succeed, the parties to the document (usually, the scheme's trustees and the principal employer) must provide credible evidence that the document in question does not reflect their true and common intentions, and this is judged objectively. The Court must also consider that making a rectification order is appropriate and equitable in all the circumstances of the case. The burden of proof falls on the party seeking the rectification, usually the scheme's employer. Representative beneficiaries are normally appointed to ensure that the interests of each class of members are considered by the Court.

It is not unusual for rectification hearings to be long and costly, as proof of the parties' intentions may not be easily established, and the hearing may involve evidence from several witnesses, including experts. Where representative beneficiaries are appointed to ensure all classes of members' interests are considered by the Court, witness statements will also be required from each of them, adding to the costs and complexity of the case.

However, it may still be possible to apply for summary judgment. This is a Court judgment, given at an early stage, without a full trial of the issues. The test for whether summary judgment is appropriate is high: the representative beneficiary or beneficiaries must have no real prospect of successfully defending the claim and there must be no other compelling reason why the case should be taken to full trial.

An alternative to rectification – a 'construction application' under Section 48 of the Administration of Justice Act 1985

An alternative to a full-scale rectification hearing is a section 48 Court application for a declaration as to the construction of an ambiguous provision in a scheme's trust deed and rules – a 'construction application'. This rarely-used process requires significantly less evidence, as it relates primarily to an issue of legal interpretation. There are no special rules governing the construction of pension scheme documents and the same general principles are applicable to the trust deed of a pension scheme as they are to other written instruments.

Essentially, section 48 provides that where there is a question as to how the scheme's rules should be construed and a counsel of at least 10 years' call has provided a written opinion about that question, then the Court may make an order authorising the trustees to take certain steps in reliance on that counsel's opinion.

The facts in *Re BCA Pension Plan* [2015]

This case concerned the BCA Pension Plan (the Plan), established in 1996. The original rules provided for limited price indexation (LPI) increases of 5 per cent for benefits relating to post-April 1997 service. In 2005, a deed of amendment introduced 2.5 per cent LPI increases for benefits relating to post-April 2005 service. Fixed increases of 3 per cent applied to all benefits attributable to pre-April 1997 service.

In 2011, a new consolidating deed was produced and executed. However, the part of the original rules which identified the elements of pension to which the different rates of increase applied was omitted in error. This meant that, following the consolidation exercise, it was unclear whether an increase of 5 per cent LPI, 2.5 per cent LPI or 3 per cent fixed was intended to apply to any particular pension or part of a pension.

The trustee's application

Rather than pursuing formal rectification proceedings, the trustee made a section 48 application to the High Court, asking for an order that it be permitted to administer the Plan as though the mistakenly deleted words in the increase rule had not been omitted from the consolidating deed. This was the way in which the trustee had, in fact, been administering the Plan both before and after the 2011 consolidation.

The trustee obtained a QC's opinion which stated that the relevant rule provided for different rates of increase to apply to certain benefits, without indicating which pension or part of the pension was to be increased by each stated amount. This lack of direction made the consolidated rules unworkable and the Court could therefore conclude that something had gone wrong with the drafting.

Although the submitted construction involved reading a whole sub-paragraph into the consolidated rules, it was argued that this did not contravene the principle in an earlier case, *Cherry Tree Investments*, as the inclusion would operate to make sense of what had been rendered a nonsensical provision by the consolidation drafting. It would not change the meaning of the document but would give practical effect to its existing meaning. It reflected that a clear mistake had been made and it was obvious how to correct it.

The decision

The trustee's application was granted. Having allowed the original rules and the deed of amendment to be admitted in evidence, Snowden J considered it obvious to an objective observer that there had been a mistake in drafting the increase rule in the consolidation process. The increase rule no longer made sense and it was clear that the consolidated rules did not intend to bestow on members a choice of the most favourable rate of increase each year. There was no mechanism in the rules for such an election and giving members this option would have been a radical alteration to the Plan.

Snowden J therefore agreed it was obvious that the wording in the original increase rule had been omitted in error. He was satisfied that this solution did not infringe Cherry Tree Investments as 'the consequence was not to create a new contractual provision in rules that would work without it; its inclusion is necessary to make the existing rules work.'

The Judge also made clear that, although the order would protect the trustee against any complaint that it had wrongly administered the Plan, it would not bind members, who were free to contend that a different construction of the consolidated increase rule should apply.

Unlike a rectification claim, there is no requirement under section 48 to appoint a representative beneficiary. Snowden J originally proposed to make the section 48 order conditional upon the trustee giving notice to the members and also to allow any member to apply to have the order set aside or varied within two months. However, he accepted the trustee's further argument that it was impractical to notify all members individually of the change. It was relevant that the implementation of the order would maintain the increases in benefits which the trustee had been paying all along.

Snowden J did not accept that the members should not be told of the existence of the order at all as, where a section 48 order relates directly to benefit levels, members should be informed of it unless there was a compelling reason not to do so. He then accepted that this could be achieved with an appropriate notice in the next regular communication to members which would be 'sensible and proportionate'.

Comment

When mistakes are discovered, practitioners have always considered whether construction is an appropriate remedy, but it is relatively narrow in its application, and the fact that it does not bind members is a disadvantage. As a result of this case, it may be that the option of making a construction application to correct mistakes in pension scheme documents becomes more viable, as the extent of the caution against inserting whole clauses in the *Cherry Tree Investments* decision has been clarified. In *Re BCA*, Snowden J considered that the effect of reading the additional words into the increase rule was necessary to make the rules work, and not to create a new contractual provision.

Clearly, construction would not apply where there is an error in documentation which cannot be construed as simply 'correct' or 'incorrect'. However, it is easy to see why scheme employers would prefer to avoid a full rectification trial, with its attendant high costs and the requirement for extensive evidence of the parties' intentions, and numerous witness statements, including those from representative beneficiaries. Such evidence is often difficult to obtain, given the length of time which has frequently lapsed between the execution of the deed in question and the realisation that the resultant document is inaccurate.

However, the hurdles trustees and employers must negotiate for a successful construction application are high, and to consider this an easy option would be wrong. In *Re BCA*, there was clear evidence that wording essential to the correct application of the increase rule had been omitted in the consolidation process, as the rules made no sense without it. The earlier versions of the rules were admitted as evidence and an objective observer would have noticed the consolidated rule was unworkable. Such clear evidence may not always be readily available.

It seems that section 48 may not gain rapid popularity, as it may be unsuitable in the majority of cases. In situations where the rules actually make sense but happen not to reflect the parties' intentions, the appropriate course of action will still be rectification. In these circumstances, the Court would still need to examine evidence of the parties' intentions at the time the deed was executed and the simpler section 48 route of obtaining counsel's opinion will not be sufficient. However, there may be some cases in future where the line between rectification and construction is blurred.

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