

	<p><b>DETERMINATION NOTICE</b>  <b>under section 96(2)(d) of the</b>  <b>Pensions Act 2004 (the “Act”)</b></p> <p><b>The Derfshaw Limited Retirement</b>  <b>Benefits Scheme</b>  <b>(“the Scheme”)</b></p>	<p>The Pensions  Regulator  case ref:</p> <p><b>TM5691</b></p>
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## 1. Decision

The Determinations Panel (the “Panel”) granted the application (the “Application”) made by Thomas Eggar Trustee Corporation Limited (the “IT”) on 27 February 2007 for an order to be issued under section 11(1) (c) of the Pensions Act 1995. The Panel determined that an order be issued in the following terms:

The Pensions Regulator hereby authorises:

1. that the Derfshaw Limited Retirement Benefits Scheme commence wind up with effect from 9 March 2009 subject to the provisions of Section 96(5)(a) of the Act;
2. this order is made because the Pensions Regulator is satisfied that it is necessary in order to protect the interests of the generality of the members of the Scheme that it be wound up pursuant to section 11(1)(c) of the Pensions Act 1995. In accordance with section 11(4) of the Pensions Act 1995, the Regulator authorises that the Scheme be wound up in accordance with the provisions of sections 73-75 of the Pensions Act 1995 (as modified by the Occupational Pension Schemes (Winding Up) Regulations 1996) and any relevant provision of those regulations, or such other statutory provision and regulations as may be in force from time to time and may be applicable to the winding up of the Scheme.

## 2. Parties

The Warning Notice specified the following parties as being directly affected by the regulatory action outlined in the Warning Notice:

- (a) Thomas Eggar Trustee Corporation Limited;
- (b) Frederick Henry Shaw as individual trustee for the Scheme;
- (c) John Edward Simpson as individual trustee for the Scheme;
- (d) Roy Benyon as individual trustee for the Scheme (respectively the “Legacy Trustees”);
- (e) Derfshaw Limited as Principal Employer to the Scheme (“the Principal Employer”);
- (f) The Pension Protection Fund.

At the oral hearing, on 9 March 2009, the IT was represented by Mr Nicolas Stallworthy of Counsel. The Regulator was represented by Mr Sebastian Allen of Counsel. The Principal Employer and the Legacy Trustees were represented by Mr Frederick Shaw who appeared in person.

### 3. Details of the Scheme and the Principal Employer

The Scheme was established by the Employer on 27 April 1983 by an Interim Trust Deed of the same date and commenced on 1 May 1983. The Scheme is a contracted out, defined benefit scheme which is paid up and has approximately 57 members. The size of the fund is £1,510,000.

The Principal Employer is an engineering company. The number of its employees is unknown. Aside from the Principal Employer there are two current participating employers, namely Kestner Engineering Co Limited and Lennox Foundry Co Limited, (respectively the "Employers"). A third participating employer namely, Kestner DJM Pollution Control Limited, entered liquidation on 11 July 2000 (references to the Employers includes, where material, references to Kestner DJM Pollution Control Limited).

None of the Employers has contributed to the Scheme since December 1999, and it is understood that the Employers are neither willing nor able to support the Scheme.

The Scheme is governed by a definitive trust deed dated 19 March 1984 along with a schedule of rules annexed to the definitive deed (respectively the "Deed and Rules").

### 4. Background

None of the parties tendered any witness statements. Therefore, all of the facts had to be ascertained from the documentation provided to the Panel. A brief summary of the facts, as to which there was no dispute, is summarised below.

In 1998 the Principal Employer began taking advice from Sun Life (the "Scheme Actuary") in relation to its funding obligations to the Scheme. The Scheme Actuary advised that due to changes in pension legislation, the Employers would face significant increases in their funding obligations to the Scheme particularly since a recent actuarial valuation had revealed a significant deficit.

As a result the Principal Employer began to explore the possibility of closing the Scheme and establishing, as an alternative, a money purchase arrangement. This is clear from a letter from the Legacy Trustees to the Scheme Actuary dated 14 January 1999 which states:

*"Further consideration will be given to the way forward, including discontinuance and moving to a money purchase scheme. **As you will be aware the scheme has to give three months notice to members of any change.** The trustees*

*and employer have agreed, however, that any alteration would not take place until 30<sup>th</sup> June 1999.” (emphasis added)*

The Scheme Actuary responded on 20 January 1999 stating:

***“You mention in your letter that the scheme may well be terminated with effect from 30 June 1999. I am aware that you have already discussed this possibility at some length with Doug Steer-Smith. I would reiterate that if a scheme does wind-up with a deficit then the trustees are obliged to seek extra funding from the employer to make good the deficit ...***

***... I am not clear whether a definite decision to wind the scheme up has yet been made.”*** (emphases added)

On 16 April 1999 the Employers wrote to the members of the Scheme notifying them that:

*“.....we now have to advise you that the Company has to discontinue participation in the scheme as at 30 June 1999.”*

Subsequently, on 1 July 1999, the Legacy Trustees wrote to the Scheme Actuary stating that:

***“.....employers have now issued notices to contributing members that they may have to discontinue their participation in the scheme.***

*Currently, a logical time to do this would be 30 September, to enable a money purchase scheme which has been discussed in depth with Sun Life and others to be firmly in place to take the place of the final salary scheme.*

***Your response to this letter will enable the employers to make a final decision”.*** (emphases added)

The Panel noted that there then followed a series of letters to the Legacy Trustees from the Scheme Actuary requesting urgent confirmation as to the status of the Scheme. On 2 August 1999 the Legacy Trustees responded to the Scheme Actuary in the following terms:

*“The employers have therefore no option but to discontinue the scheme, and the precise date is notified to you as 30<sup>th</sup> September 1999. Would you kindly treat this as formal notification of termination of the scheme.”*

In December 1999 the Principal Employer paid a contribution of £275,000 to the Scheme which Mr Shaw has described as a special contribution

In the view of the IT and the Regulator the Scheme has not subsequently been administered as if it were in wind up.

## **The Regulatory Background**

On 13 December 2005 the Panel appointed the IT to the Scheme with exclusive powers pursuant to Section 7 of the Pensions Act 1995. The circumstances of the IT's appointment are not relevant for the purposes of the Application.

The IT began to review the affairs of the Scheme and concluded that there were significant questions as to whether the Scheme was, as the Legacy Trustees contended, in wind up. Specifically the IT queried whether the requirements of the Rules had been observed. In response to the IT's enquires the Legacy Trustees asserted that the letter sent to the Scheme members on 16 April 1999 constituted notice (the "Alleged Notice") as required by the Rules.

Having taken the advice of Counsel, the IT made the Application (there is no power for the IT to wind up the Scheme in the absence of the Employers' co-operation.).

The Panel heard the Application on 9 April 2008 and made an order authorising the Scheme to be put into wind up. Mr Shaw in his capacity as a director of the Principal Employer, and as a Legacy Trustee, referred the Panel's decision to The Pensions Regulator Tribunal on procedural grounds. The Regulator conceded that there were a number of procedural defects in respect of the service of documents and accordingly consented to the Application being reheard by the Panel.

At the oral hearing there was no suggestion that any of the procedural defects remained outstanding.

### **5. The Issues**

From the skeleton arguments and the submissions of the parties three key issues emerged. These were:

- a. was the Scheme in wind up as the Employers and the Legacy Trustees contended?
- b. if the Scheme was not in wind up, should it be wound up pursuant to Section 11 (1) (c) of the Pensions Act 1995?; and
- c. if the Scheme should be wound up, from when should it be wound up?

It was clear to the Panel that (a) above was the central issue. The Panel was of the view that there were two parts to the question as to whether the Scheme was already in wind up namely:

- (i) did the cessation of contributions by the Employers in 1999 trigger the Scheme to enter wind up pursuant to the provisions of the Rules?; and
- (ii) did the Alleged Notice comply with requirements of the Rules?

Mr Shaw argued, on behalf of the Principal Employer and the Legacy Trustees, that the answer to both (i) and (ii) above was in the affirmative. The IT and the Regulator contended to the contrary.

There was no dispute between the parties that, if the answer to (a) above was in the negative, then the answer to (b) should be in the affirmative. Further, there was no dispute as to (c) given that the parties agreed, subject to the Panel agreeing that the Scheme was not in wind up and that it should be in wind up, that the date should be 9 March 2009.

Before assessing whether the Scheme was already in wind up, thereby obviating the need for any further order, the Panel considered the relevant provisions of the Rules.

## 6. The Rules

The winding up provisions of the Scheme are set out in Rule 13. The relevant terms of Rule 13 are as set out below:

*“1. The Principal Employer or any Participating Employer may give three months notice to the Trustees of intention to cease paying contributions to the Scheme and on the expiry of the three months the contributions of the Employer giving notice and of its Employees shall cease. Unless the circumstances are as set out in sections ... 4 of this Rule,*

- (i) benefits under the Rules shall continue to be provided in respect of Members who have retired, reached Normal Retirement Date, or who retain benefits under Rule 11 and;*
- (ii) Members in the employment of the Employer at the date of cessation of contributions shall be regarded as having ceased to be employed in pensionable employment in accordance with Rule 11.1 but shall not be permitted nor invited to continue in full membership as other provided therein.*

*The Principal Employer and the Trustees may however decide that the trusts of the Scheme in so far as they apply to Employees of the Employer giving notice shall determine absolutely and that the procedures described in sections 5 and 6 of this Rule shall be followed in respect to the Employees of that Employer who are Members and the appropriate part of the assets of the trust fund.*

.....

*4. In the event of all Employers ceasing to pay contributions to the Scheme or on the business of the Principal Employer ceasing to be carried on (unless its successors in business shall take the place of the Principal Employer for all the purposes of the Scheme) the trust fund shall be dissolved and wound up and the trusts under the Scheme shall determine absolutely.”*

## 7. Submissions as to the correct construction of Rule 13

### The submissions of the Employers and the Legacy Trustees

Mr Shaw submitted that the notice requirements of Clause 1 were obviated in circumstances in which Clause 4 applied, i.e. in situations in which the Employers ceased to pay contributions. Put differently, he submitted that Clause 4 was a standalone provision and should not be read in conjunction with Clause 1.

His rationale was founded on the presence of the word “unless” in Clause 1. His argument was that notice was required (as set out in Clause 1) “*Unless the circumstances are as set out in sections .... 4 of this Rule*” applied. Mr Shaw argued that since the circumstances of Clause 4 had arisen, namely that all of the employers had ceased to pay contributions, then there was no need for there to be any notice and the Scheme entered automatic winding up as a result.

### The submissions of the IT and the Regulator

The IT and the Regulator submitted that this construction was incorrect and that Clause 4 was not a standalone power and had to be read in conjunction with Clause 1. The key points, as they appeared to the Panel, can be summarised as follows:

- (a) the reference in Clause 4 to “*all Employers ceasing to pay contributions to the Scheme*” must contemplate and cross refer to the cessation of contributions pursuant to the mechanisms prescribed by Rule 13 as a whole including Clause 1;
- (b) Clause 1 expressly cross refers to Clause 4 which strongly implies that both ought to be read together;
- (c) the formality for the requirement of valid notice under Clause 1 is required to provide certainty and to distinguish a cessation of contributions under Rule 13 from circumstances in which no contributions are paid i.e. because the Scheme is in surplus and a contribution holiday is taken;
- (d) the formality for the requirement of valid notice under Clause 1 is required to provide a precise date on which contributions and accrual can be said to have ceased and therefore a precise date for the commencement of winding up can be determined;
- (e) if Clause 4 is read in isolation then the employers can effectively avoid the notice requirement, as provided by Clause 1, and therefore the purpose and the protection of Clause 1 is frustrated
- (f) the purpose of winding up of a pension scheme is a significant one with potentially serious consequences for the members of that scheme. Therefore it is a process which ought not to be effected in an informal

manner with potentially serious consequences for the members of the scheme in question.

Before resolving which interpretation of Rule 13 ought to be preferred the Panel first considered the principles of construction referred to by the IT and the Regulator.

## 8. Principles of construction

A number of helpful authorities were placed before the Panel which set out the principles of construction which ought to be borne in mind when approaching the construction of pension scheme rules.

The relevant principles are neatly summarised in *Armitage v Staveley Industries Plc* [2005] EWCA Civ 792 at paragraph 29. The Panel found the following principles particularly helpful namely:

*“(3) The interpretation must be one that is practical and purposive, rather than detached and literal;*

*(4) If more than one interpretation is possible, the correct choice may depend on the practical consequences of choosing one interpretation rather than another.”*

In addition the Panel had regard to a principle of construction as elucidated by Lady Justice Arden in *Stevens v Bell* [2002] EWCA Civ 672, at paragraph 32, where she stated:

*“... a pension scheme should be interpreted as a whole. The meaning of a particular clause should be considered in conjunction with other relevant clauses. To borrow John Donne’s famous phrase, no clause “is an island entire of itself.”*

The IT and the Regulator submitted that the requirement of notice as provided by Clause 1 should be formal and deliberate and not casual or informal. In other words the requirement for there to be notice from all of the Employers was a strict formality that had to be observed. In support of these submissions the IT and the Regulator relied on a number of authorities. The points arising from these authorities can be summarised as follows:

- (a) in circumstances in which notice does not have to be in writing (Clause 1 does not state that the notice must be in writing) the Panel should construe the requirement of notice as the giving of formal and deliberate notice with the intention of giving notice to the required recipient. The Panel was referred to *Ex p. Oastler, In re: Friedlander* (1884) Vol 13 QBD 471, and in particular the comments of Lindley LJ at 475, and *Burgh v Legge* (1839) 5 M & W 418;
- (b) the necessity that notice be actual and direct in the context of a pension scheme received support from Neuberger J (as he then was) in *Capital*

*Cranfield Trust Corporation v Sagar* [2001] 54 PBLR at paragraph 40 where he stated that:

*“Third party rights and, in a case such as this, very important third party rights, pensions to employees, no doubt of mostly modest means, would have been appreciated as liable to be affected by a notice such as that contemplated by clause 18. In my judgment, someone in the position of a beneficiary should be able to know for certain that such a notice had been given. The facts of the present case indicate how important it is. Twenty years on this has become an issue. The beneficiaries do not know what happened and are at the mercy of the available paper trail.”*

(c) Neuberger J (as he then was) reinforced these views in *Bestrustees v Stuart & Anor* [2001] PLR 283 at paragraph 33 where he stated that:

*“In this connection I bear in mind that a pension scheme is likely to continue for a substantial period of time and that those most affected by them and entitled to protection from the trustee, the employer and indeed the court, will be people who are comparatively poor, who will not have easy access to expert legal advice, and who will not know what has been going on in relation to the management of the Scheme. In those circumstances, it seems to me that the protection of the beneficiaries requires the court to be very careful before it permits a departure from the plain wording and plain requirements of the trust deed.”*

In addition to the authorities, as referred to above, the IT and the Regulator made two additional points.

Firstly, that the absence of a requirement for written notice militates strongly in favour of deliberate and formal notice being required so as to afford the necessary certainty and protection for the members' rights.

Secondly, that on the plain reading of Clause 1 the use of the transitive verb “give” is conspicuous in the phrase “*The Principal Employer or any Participating Employers may give three months' notice to the Trustees*”. This, it was submitted, connotes a deliberate giving of notice.

## 9. Reasons

### **Is the Scheme in wind up?**

The Panel considered that the requirement of notice, as required by Clause 1, existed in order to protect the Legacy Trustees and the members of the Scheme in arguably one of the most serious situations that the Scheme could face, namely when the Principal Employer and the Participating Employers are attempting to bring the Scheme to a close.

Accordingly the Panel felt that the requirement for notice should not be casual or informal, but should be formal and deliberate. This approach was consistent with the legal principles to which the Panel had been referred. The Panel felt

that the need for formal and deliberate notice was all the more important in this context given that there was no requirement for the notice to be given in writing.

The Panel felt that this approach was not unduly pedantic, particularly because of the protection that the notice requirement provided to the members of the Scheme when they needed it the most, i.e. when the Employers were trying to bring about an end to the Scheme. The Panel's approach is consistent in this regard with the comments of Neuberger J as set out in paragraph 40 of *Capital Cranfield* and paragraph 32 of *Bestrustees* respectively.

The requirement of formal and deliberate notice informed the Panel's conclusion that the provisions of Clause 1 and 4 of Rule 13 ought to be construed together, i.e. Clause 4 is not a standalone provision.

The Panel felt that, if the cessation of contributions by the Employers could bring about an unavoidable wind up of the Scheme, then the members and the Legacy Trustees would be deprived of the protection provided by Rule 13(1). Further, that it could not be correct that the Employers could sidestep the notice requirement by just ceasing to pay contributions. Such an approach would frustrate the purpose of Rule 13(1) and undermine the protection that it sought to provide.

For instance, if the Employers took a contribution holiday then, should Mr Shaw's construction be preferred, the Scheme would enter wind up. This would be a very surprising result and a potentially disastrous situation for the Scheme and those involved in it. It is the requirement of notice that lends certainty to the process.

Accordingly the Panel considered that Rule 13(1) and Rule 13(4) ought to be read together and that accordingly the cessation of contributions, without the notice required by Rule 13(1), would not trigger the wind up of the Scheme.

The Panel then considered whether the Alleged Notice complied with the requirements of Rule 13(1) (notwithstanding the fact that the Panel had never seen a letter sent to the members from Kestner DJM Pollution Control Limited). The view of the Panel was that the Alleged Notice did not satisfy the requirements of Rule 13(1) in a number of significant respects.

Firstly, the Alleged Notice was addressed to the members of the Scheme and not to the Legacy Trustees. This is not surprising given that this accords with the understanding of the Legacy Trustees as set out in their letter, dated 14 January 1999, which stated "*As you will be aware the scheme has to give three months notice to members of any change.*" The Panel took the view that the Employers had not appreciated to whom notice had to be given.

Further, the Alleged Notice was expressed to expire on 30 June 1999 which was less than the requisite three months as required by Clause 1. In addition, the Alleged Notice only stated that the Employers intended to "*discontinue participation in the scheme as at 30.06.99*" which is substantively different from

giving a notice of an intention to “*cease paying contributions*” as required by Rule 13(1).

Subsequent correspondence also makes it clear that as at the date of the Alleged Notice no final decision had been reached regarding the winding up of the Scheme which further undermines the validity of the Alleged Notice.

The letter to the Scheme Actuary from the Principal Employer, dated 1 July 1999, stated “*Your response to this letter will enable the employers to make a final decision*”. This letter demonstrates that, as no decision had been made by 1 July 1999, it is inherently unlikely that the Employers, at 16 April 1999, had determined to, and did, give the requisite notice. The Panel noted that the contribution, in December 1999, was inconsistent with the contention that the Scheme had entered wind up on 30 September 1999.

For all of the above reasons the Panel concluded that the Alleged Notice did not comply with the requirements of Rule 13(1) and accordingly the Scheme had not entered wind up.

#### **Additional submissions on behalf of the Principal Employer and the Legacy Trustees**

Mr Shaw stated during the course of the oral hearing that the Legacy Trustees were aware of the Employers’ intentions during 1999. He did not adduce any evidence to this effect and he did not pursue this line of argument any further. However, the Panel was of the view that, even if the Legacy Trustees were aware of the Employers’ intentions (two out of three of the Legacy Trustees were directors of the Employers), then mere passive knowledge was not sufficient notice for the purposes of Rule 13(1).

The Panel noted that should such an assertion be made it would be inconsistent with Mr Shaw’s assertions to the Regulator in his letter dated 11 March 2005 in which he stated:

*“Could we explain that we never use the telephone on important matters and always commit our thoughts to paper. This tends to remove the “who said that, when” syndrome from our files”.*

Finally Mr Shaw submitted that for various reasons the Application was defective due to a number of alleged errors contained in a number of documents. The Panel did not agree that any of these alleged errors, if they could be considered as errors, vitiated the Application.

#### **Is it necessary to wind up the Scheme?**

As set out in the penultimate paragraph of point 5 above, the parties agreed that, should the Panel find that the Scheme was not in wind up, then it was necessary to wind up the Scheme in the interests of the generality of the members pursuant to Section 11 (1) (c) of the Pensions Act 1995. The Panel agreed for the following reasons:

- a. authorising the Scheme to be wound up would resolve the status of the Scheme and provide the necessary certainty to the members and the trustees;
- b. the IT does not have the power to wind up the Scheme under the Rules and since the Employers maintain that the Scheme is already in wind up then further regulatory action can be avoided;
- c. further delay in winding up the Scheme will be to the detriment of the Scheme members resulting from priority drift as more members reach normal retirement date;
- d. winding up the Scheme guards against any further risk to the Pension Protection Fund.

### **The timing of the order**

Section 11 (4) of the Pensions Act 1995 provides that the Panel must include directions as to the timing of any order made pursuant to Section 11 (1) (c). There was no dispute between the parties that the order ought to take effect from 9 March 2009 and the Panel was content to make this order subject to the provisions of Section 96 of the Act.

#### **10. Statutory issues**

In making their decision the Panel had regard to the objectives of the Regulator as set out in section 5 of the Pensions Act 2004 and to the matters mentioned in Section 100, as set out in **Appendix 1**.

11. **Appendix 2** to this Determination Notice contains important information about the rights of appeal of the parties against this decision.

Signed: *Suzanne McCarthy*.....

Chairman: **Suzanne McCarthy**.....

Dated: 19 March 2009.....

**Section 5 of the Pensions Act 2004**  
**Regulator's objectives**

- (1) The main objectives of the Regulator in exercising its functions are –
- (a) to protect the benefits under occupational pension schemes of, or in respect of, members of such schemes,
  - (b) to protect the benefits under personal pension schemes of, or in respect of, members of such schemes within subsection (2),
  - (c) to reduce the risk of situations arising which may lead to compensation being payable from the Pension Protection Fund (see Part 2), and
  - (d) to promote, and to improve understanding of, the good administration of work-based pension schemes.
- (2) For the purposes of subsection (1)(b) the members of personal pension schemes within this subsection are-
- (a) the members who are employees in respect of whom direct payment arrangements exist, and
  - (b) where the scheme is a stakeholder pension scheme, any other members.
- (3) In this section-
- “stakeholder pension scheme” means a personal pension scheme, which is or has been registered under section 2 of the Welfare Reform and Pensions Act 1999 (c.30)(register of stakeholder schemes);
- “work-based pension scheme” means-
- (a) an occupational pension scheme,
  - (b) a personal pensions scheme where direct payment arrangements exist in respect of one or more members of the scheme who are employees, or
  - (c) a stakeholder pension scheme.

**Section 100 of Pensions Act 2004**  
**Duty to have regard to the interests of members etc**

- (1) The Regulator must have regard to the matters mentioned in subsection (2) –
- (a) when determining whether to exercise a regulatory function –
    - (i) in a case where the requirements of the standard or special procedure apply, or
    - (i) on a review under section 99, and
  - (b) when exercising the regulatory function in question.
- (2) Those matters are –
- (a) the interests of the generality of the members of the scheme to which the exercise of the function relates, and

(b) the interests of such persons as appear to the Regulator to be directly affected by the exercise.

**Referral to the Pensions Regulator Tribunal**

You have the right to refer the matter to which this Determination Notice relates to the Pensions Regulator Tribunal (“the Tribunal”). Under section 103(1)(b) of the Act you have 28 days from the date this Determination Notice is given to refer the matter to the Tribunal or such other period as specified in the Tribunal rules or as the Tribunal may allow. A reference to the Tribunal is made by way of a written notice signed by you and filed with a copy of this Determination Notice. The Tribunal’s address is:

The Pensions Regulator Tribunal  
15-19 Bedford Avenue  
London  
WC1B 3AS  
Tel: 020 7612 9649.

The detailed procedures for making a reference to the Tribunal are contained in section 103 of the Act and the Tribunal Rules.

You should note that the Tribunal rules provide that at the same time as filing a reference notice with the Tribunal, you must send a copy of the reference notice to The Pensions Regulator. Any copy reference notice should be sent to:

Determinations Support  
The Pensions Regulator,  
Napier House  
Trafalgar Place  
Brighton  
BN1 4DW.  
Tel: 01273 627698