Trustees of pension schemes often have to exercise discretionary powers to decide who should get what benefits. Often these focus on ill health and death benefit cases, emotive matters for members and the trigger for hundreds of complaints to the Pensions Ombudsman. Here, our pensions experts remind you of the key issues.

Key action points for trustees

1. Process is key

Pension scheme trustees often have to exercise a discretionary power. When exercising a discretion, process is key.

2. Role of the Pensions Ombudsman and the Courts

The Courts and The Pensions Ombudsman are clear that they won't interfere with the outcome of trustees' decision-making, but they will examine the process by which the trustees got there.

3. Secure decisions
So, to make secure decisions, trustees need to be aware of the issues to consider and the process they must go through.

**What are discretions?**

Do your rules say you “may” do something? Or that a particular benefit can only be paid “with trustee consent”? These and similar provisions are discretionary powers. In other words, they are powers the trustees can exercise, or benefits the trustees can pay, but you cannot be required to do so. An important part of the role of any trustee of a pension scheme will include the exercise of discretionary powers set out in the deed and rules of their scheme.

Common discretionary powers may relate to whether or not to pay a benefit, who a benefit may be paid to, or the value of the benefit. Common discretionary powers in scheme rules include:

- deciding on the recipients of a death benefit lump sum;
- deciding whether the member meets the test for ill-health early retirement;
- deciding who receives a survivor's pension where there is more than one potential beneficiary;
- and
- paying benefits before normal retirement age with or without reduction for early payment.

Decisions under discretionary powers are often contentious, and are the most commonly seen type of decision being challenged in front of the Pensions Ombudsman.

**Process**

The law is clear that trustees must consider all relevant matters and must leave out of account any irrelevant matters.

The law also requires trustees to reach a “reasonable” decision. Specifically, a decision “which is not so unreasonable that no reasonable body of trustees could have made it”. Which is a fairly generous target area, but one that rules out the patently unreasonable.

It is wise for trustees to keep records of decision making that are sufficient to show that this has happened (though careful consideration needs to be given to precisely what is recorded and how much detail is given). You can read more about this below under the section on the Pensions Ombudsman.

As part of this process, trustees should also consult and take appropriate advice from their professional advisers (this might be the scheme actuary, lawyers or administrators or a combination).
A policy for decision-making?

Must you consider the use of the power on each occasion? Or can you set a policy for how to use the discretion?

Setting a policy is acceptable, and can be helpful where there may be large volumes of decisions and policy criteria that will help to streamline processes.

A policy might help by listing the type of information that the trustee will ask for in certain cases (in a death case, things like the deceased’s will, details of his or her family and their financial circumstances, for example, among other information).

A policy might also help by setting guidelines, but the trustee needs to be careful not to restrict its ability to make a reasonable decision based on the facts. For example, a policy for use in relation to ill-health early retirement cases might require a certain number or type of medical reports, but subject to a proviso that the trustee can use other medical reports where it decides that is appropriate.

If a policy is adopted, it is critical to keep the policy under review and ensure that revisions are made, as and when required. Use of an outdated policy could in itself potentially be grounds for complaint, if it has led the trustees to make an unreasonable decision.

In addition, an open mind should be kept as to whether the circumstances of a particular case might make a departure from the general policy appropriate.

Where they have delegated any discretions, for example to a sub-committee or to the external scheme administrator, trustees should ensure that appropriate processes are in place, including a clear understanding of the principles set out here.

Risks in decision making: the Pensions Ombudsman

Given the complexity and sensitivity of many aspects of a trustee's discretionary powers, not to mention the margin for people to consider the same facts and reach different conclusions, it is unsurprising that this is a subject often considered by the Pensions Ombudsman.

This has led the Pensions Ombudsman to issue its own guidance on how trustees should exercise their discretionary powers, which can be accessed here. A specific element of the trustees’ discretionary powers, ill-health early retirement, has also been given its own guidance on the Ombudsman's website.
It is important to note that the Ombudsman does not need to agree with the trustees’ decision; it will only examine whether the process used in reaching that decision was correct.

The Pensions Ombudsman may ask to see all of the information that the trustees had at the time of making the decision, and any records of meetings where the matter was decided and other details considered in making the decision.

**Exercising Trustee Discretions - Checklist**

1. **Is this a discretion?**
   
   What do your Rules say? If they use words like "the Trustee may" or "with the Trustee's agreement", it's a discretion. It is not a discretion if something happens (such as the member automatically becoming entitled to the benefit) when certain conditions are met.

2. **Who has the power to exercise the discretion?**
   
   What do your rules say? Is it as trustee power, an employer power or a joint power?

3. **Do you need to consider any legislation?**
   
   Your rules might say (for example) that any benefit which, prior to the Finance Act 2004, was a member right will, after 6 April 2006, be payable only at trustee discretion if making the payment could constitute an unauthorised payment.

4. **Ask relevant questions**
   
   You need to have all the facts and information that might be relevant to the decision you are making, before you consider making the decision.

5. **Wait for the answers**
   
   Don't risk prejudicing your decision by considering the case before you've received responses to your questions.
6. Consider all relevant factors

Your duty is to consider all relevant factors and to disregard all irrelevant factors.

7. Take advice

You should consult and take appropriate advice from your professional advisors.

8. Reasonable decision

You must make a decision that is not unreasonable.

9. Record your decision

Trustees should keep a record of their decision, with careful thought given to exactly how much detail is set down.

10. Be regular

Where you have a discretion to do something on a regular basis (for example, to make discretionary increases to pensions in payment) consider whether to exercise the discretion regularly (even if you decide against exercising it).

11. Review policy

Where you adopt a policy about how you will approach the exercise of a discretion, review the policy regularly.