



CONTRIBUTION RULE

EXECUTIVE SUMMARY

The Trustee introduced a contribution rule in March 2015 which widened the scope of employers obliged to support the funding of the With Profits Section. This allows the Trustee to take a wider group of employers into account when assessing the covenant supporting the With Profits Section.

SECTION 48 OF THE ADMINISTRATION OF JUSTICE ACT 1985 APPLICATION

The Trustee introduced a contribution rule using its existing amendment power on the basis of legal advice from Leading Counsel¹. The rule is now included in the consolidated version of the Trust Deed dated 19 February 2023 available on the Cheviot website.

The Trustee applied to the Court under s48 of the Administration of Justice Act 1985 for authorisation to use its amendment power in this way. The Court Order was granted in February 2015. The Trustee used the s48 route to provide reassurance and greater certainty whilst minimising legal costs.

After careful consideration, the Trustee concluded that it was not appropriate to risk any wider waiver of legal privilege by publicising a copy of the legal opinion which supported the application. Since the Court Order was granted, further case law² has also supported the Trustee's decision that introducing a contribution rule was appropriate.

IMPACT ON EMPLOYERS

With Profit Employers have a contractual obligation to fund any deficit in the With Profits Section if the Trustee considers it appropriate to require contributions. In particular the contribution rule gives the Trustee discretion to require employer contributions when the With Profits Section is underfunded, on an ongoing basis. The rule also gives the Trustee power to require an additional lump sum on certain trigger events such as employer insolvencies, wind-ups or mergers.

REASONS FOR ITS INTRODUCTION

The key factors considered by the Trustee were:

1. The With Profits Section³ was classified as a cash balance scheme and falls outside the definition of money purchase scheme introduced in the Pensions Act 2011. It is subject to the scheme specific statutory funding requirements. The first actuarial valuation was undertaken as at 31 December 2014.
2. The funding of the Section is supported by investment returns and any contributions payable by employers. In this context, it was considered important to extend the scope of employers with funding obligations to the Section as widely as possible.
3. Employers who were contributing in 2002 when the Section closed to new contributions are liable under the legislation to support the funding of the With Profits Section. Since 2002, many employers have changed corporate identity, including many partnerships which have converted to Limited Liability Partnerships. Some benefits under the With Profits Section relate to other employers, which were not participating in 2002.
4. The introduction of a contribution rule allowed the Trustee to go wider than the statutory provisions, so as to include (within the overall funding 'covenant') employers which are not statutory employers for the purpose of the legislation, but to which liabilities within the With Profits Section can reasonably be attributed. As a result, if contributions are required at any time in the future, liability can be imposed on the employer which incurred the liability (or its successor) rather than liability being imposed only on employers falling into the limited statutory definition of employers.

¹ Nicolas Stallworthy KC

² The decision in *Merchant Navy Ratings Ltd v Stena Line Ltd* where the Court held that it was permissible for the trustee to amend the scheme rules to introduce a contribution obligation on employers where no such obligation previously existed

³ See definition of With Profits Employer in Section 1 of Schedule 1 of the Trust Deed dated 29 December 2022.



IMPACT ON VALUATION RESULTS

As required by the statutory valuation process, the Trustee regularly commissions an independent review of the covenant supporting the With Profits Section. This review is undertaken on the wider group of employers which are now subject to a balance of cost obligation under the contribution rule. The combined covenant is assessed as strong. This assessment is reflected in the Trustee's investment strategy.

The latest valuation as at 31 December 2020 is available on the website.

CONSULTATION WITH EMPLOYERS

Clause 6.3.4 permits the Trustee to take decisions on behalf of employers in relation to the scheme specific funding basis. The Trustee consults with employers before finalising each valuation. This usually includes an employers' meeting.

We recommend that you read the list of frequently asked questions, which is available on www.cheviottrust.com.