ASSOCIATION OF
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Conflicts of Interest team
The Pensions Regulator
Napier House
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Dear Sirs

Consultation on Conflicts of interest guidance

I am writing on behalf of the Association of Consulting Actuaries in response to the consultation document issued by the Pensions Regulator dated February 2008 containing draft guidance on conflicts of interest.

Members of the ACA provide advice to thousands of pension schemes, including most of the country's largest schemes. Members of the Association are all qualified actuaries and are subject to the code of professional conduct of the Faculty and the Institute of Actuaries. Advice given to clients is independent and impartial. ACA members include the scheme actuaries to schemes covering the majority of members of defined benefit pension schemes.

The ACA is effectively the 'trade association' for consulting actuaries, whilst the Faculty and Institute of Actuaries are the professional bodies.

We have found it more appropriate to respond to your consultation in free-form. Our responses to your specific questions are set out in the appendix to this letter.

Initial remarks

We come across potential conflict situations in our day-to-day roles of advising trustees and our comments below are given against this background.

We find that we are generally very supportive of the concepts and ideas that are set out in this consultation document. We note that this is an issue that you wish to tackle as part of your role of boosting trustee governance. We acknowledge that a number of trustee boards will find that they fall short of the principles that you outline, although our overwhelming experience is that trustee boards behave with great integrity in relation to conflicts even if they do not follow your suggested approach to the letter.

We do have some concerns over the length of the guidance. At nearly fifty pages there is a danger that busy trustees will not be able to digest it all or take away the key messages.

Status of guidance

Set against this background one of our key concerns is the status of this guidance and indeed other guidance that has been issued by the Pensions Regulator recently. The drafting itself seems to support the contention that its status is uncertain. On the one hand you say that the primary objective of the guidance is to promote the importance of good scheme governance arrangements in respect of conflicts of interest. So it would appear to have a "best practice" flavour to it. But on the other you say that following the publication of the guidance you would hope to see you a marked improvement in the governance of conflicts (although, as indicated earlier, we are not convinced that the need for such improvement is widespread). Going further, some of the phrases within the guidance suggest compulsion and indeed paragraph 15 suggests that there are actions that must be undertaken by all trustee boards. If so then this guidance is more than best practice.

We ask that you make plain what the intended status is of this guidance and, if there is any element of compulsion, you clearly state your locus for so doing.

It would be useful if you could indicate whether at some point in the future you intend to turn this guidance into a code of practice.

Compliance costs

We are somewhat concerned at the costs that could be involved if trustee boards choose or are indeed strongly encouraged or required to adopt your five principles. There could be significant time involved for trustees and their delegates in addressing these principles. Furthermore, it would appear that particularly when you get to principle four you are envisaging a lot of legal input. In this regard we are not sure why lawyers should always be the guardians of expertise on conflict issues or why independent trustees might be *"the only option"* (principle 4.4). Is there a danger that your experience of problem cases could colour your views as to the relative strengths that independent trustees bring?

Whilst on principle four, a possible addition would be the need to ensure transparency when dealing with a conflict.

In relation to the principles there are some matters which require clear action by the trustee board if they are to be compliant. For example, 2.1. that requires trustee boards to agree and document their conflicts of interest policy and 2.2. that requires such policies to be kept under regular review. Principle 3.1. requires trustees to consider in advance any conflicts that may arise and principle 3.4. requires trustee boards to maintain an up-to-date register of each trustee's interests. While all of these seem to be eminently good practice our question is the degree of compulsion the trustees should feel under once this guidance is finalised and if compulsory the process for evidencing compliance.

Role of senior management

In paragraphs 31 and 32 you come near to suggesting that senior employees of the sponsoring employer should not be appointed as chair to the board of trustees and that in this situation an independent trustee is ideally positioned. We fear that this is an oversimplification of the issue given the expertise that a senior employee could have brought and the possibility that the independent trustee could bring their own conflicts as a service provider to the trustee board. There are senior employees who do an excellent job as trustee chairmen – better than some of the best independent trustees – in terms of ensuring that the trustee board fully addresses each issue that should be addressed. It does not seem sensible to remove such trustees just for appearances' sake.

We do not believe that in conflict situations independent trustees are always a solution or are necessarily the best solution.

Sharing advisers

We found the section on sharing advisers with the sponsoring employer (paragraphs 112 to 115) to generally be well balanced. We agree that trustees should give careful consideration to situations where the same firm or individual provides advice in situations where the interests of the scheme and employer diverge. However, this does not mean that models such as the Y model that you mention cannot successfully address the potential for conflicts in the majority of these situations.

The role of the pension manager

Regarding the role of the pensions manager that you outline in paragraphs 121 to 125 we felt that possibly more could be said here as the pensions manager being privy to confidential information could be under huge conflicts even if he or she is not giving advice to the trustees.

Declaring interests – Appendix C

Some of the information in the suggested disclosure seemed rather odd. We wondered whether this form had been adapted from a non-executive director disclosure, which focuses more on relationships with competing firms rather than the relationships that might result in trustee conflict. Our specific comments are:

- We suggest that the title refers to “new trustee” rather than “elected trustee”, to avoid the appearance that the guidance does not apply to company-appointed trustees, for example.
- We were unsure why there was a reference to shareholding in a “public” company. It seems rather unlikely that shareholdings in an unassociated company will give rise to a conflict, except perhaps in the very rare case where the trustees are involved in selecting specific shares for investment or disinvestment. Presumably this was intended to cover situations where the trustee is a shareholder in the sponsoring employer or its associates where there could be a potential conflict? We suggest either amendment or deletion of this part of the wording. If, however, shareholding is relevant, why is private shareholding not? The undertaking to notify on a continuing basis changes in shareholdings in all companies could be rather onerous.
- We were surprised that there is no record of the trustee’s status as a scheme member (employee, deferred pensioner, pensioner).
- We would expect the form to record the status of the trustee as an employee of one of the participating companies.

Conclusion

To conclude, we found the principles that you have set out in your draft guidance to be balanced and the issues that you raise to be of interest to most trustee boards especially those that have not sat down to think about conflict issues. However, in its application there is an almost exclusive focus on conflicts from an employer perspective. In the interests of balance we would have expected more on personal conflicts and conflicts as a scheme member.

We ask when finalising the guidance that you make clear its status and you have regard to the compliance costs that could be involved if as you intend, there is a marked improvement in the governance of conflicts evidenced by trustees complying in a meaningful way with the principles that you have outlined.

We hope that you find our comments of assistance.

Yours faithfully

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Appendix

This Appendix follows the structure for comments set out in Appendix E of the consultation document.

Structure and layout of the guidance

1. Yes, the guidance clearly describes a conflict of interest and how trustees can be affected.

2. Yes, the guidance provides a clear background to each of the five principles underpinning the process for managing conflicts.

3. We were able to extract the relevant information, but as your audience is trustees, rather than pensions professionals, we think that you do need to shorten the document or make clearer those areas where you expect trustees to take action. At nearly fifty pages you may well find that many trustees do not have time to read the document. One way in which you could shorten it is to remove those matters that are peripheral to conflicts.

Guiding principles

4. The principles appear to cover all the key areas relating to conflict management arrangements.

5. The principles appear to provide sufficient guidance on how to approach the subject. However, we are not sure whether the order of the principles is correct. It would seem to be more practical for trustees to address principle 2, which is essentially about documentation, after they have stepped through all the other principles. If principle 2 comes before principles 3 to 5 the result might be an over-theoretical policy.

Case Examples

6. We found the case examples helpful.

Options for managing conflicts of interest

7. The various options outlined for managing conflicts all seem suitably explained to us.