Better workplace pensions: further measures for savers

RESPONSE FROM ICAS TO THE DWP

15 May 2014
Introduction

The ICAS Pensions Committee welcomes the opportunity to comment on The Department of Work and Pensions Command Paper on better workplace pensions: further measures for savers.

Our CA qualification is internationally recognised and respected. We are a professional body for over 20,000 members who work in the UK and in more than 100 countries around the world. Our members represent different sizes of accountancy practice, financial services, industry, the investment community and the public and charity sectors.

Our Charter requires ICAS committees to act primarily in the public interest and our responses to consultations are therefore intended to place the public interest first. Our Charter also requires us to represent our members’ views and to protect their interests, but in the rare cases where these are at odds with the public interest, it is the public interest which must be paramount. For example, the ICAS Pensions Committee has published two high profile reports on pensions in an independent Scotland in the context of the Referendum debate. Our reports which have been published under the banner “Scotland’s pensions future” have successfully raised important issues on the implications of independence for the State pension, public sector pensions and private pensions.

Key points

We have the following key points to raise on the Command Paper:

- We would not favour the introduction of a compulsory system of accreditation for pensions administrators. There are forms of assurance and accreditation available or in the pipeline which are designed to enable customers to assess the standard of the administration. Ultimately, we believe that competition will remove poor administrators from the market.

- We believe that the proposals that mastertrusts should have a minimum of four independent trustees could be costly and we are not convinced that the proposal that the chair of trustees should be recruited through a recruitment consultant will deliver value for money.

- We do not believe that the DWP has sufficient evidence to justify the inclusion of minimum quality standards within regulations and that the proposed quality standards would not be fit of purpose.

- The proposal for an audited annual statement on compliance with the proposed minimum quality standards is flawed and suggests a lack of understanding of audit and assurance engagements.

- We are generally supportive of measures to increase transparency and appreciate that there is a relationship between transparency and the ability of employers and employees to assess the quality of a pension scheme or product. However, we are becoming increasingly aware that the selection of auto-enrolment solutions by smaller employers is becoming a compliance exercise, with the choice of auto-enrolment solutions limited by a number of factors: the cost of compliance; difficulties accessing professional advice; and the need to ensure compatibility with existing payroll arrangements. We do not have a comprehensive picture of the extent to which payroll solutions may be unduly limiting the selection of an auto-enrolment solution and we would welcome more visible engagement between DWP and TPR with payroll providers on this issue.

Any enquiries should be addressed to Christine Scott, Assistant Director, Charities and Pensions, at cscott@icas.org.uk.
Consultation questions

Administration

Question 1. We would welcome views on the potential benefits of accreditation of administrators, and what role the Government and regulators could play in supporting this.

Answer 1. As things stand at the moment we would not favour the introduction of a compulsory system of accreditation for pensions administrators. Ultimately, we believe that competition will remove poor administrators from the market.

There is already an option available to administrators to demonstrate to customers the quality of their internal controls. Administrators may obtain a report on their internal controls following assurance work carried out under ICAEW’s technical release AAF 01/06. An AAF 01/06 engagement involves the administrator appointing a reporting accountant (in practice, an auditor) to issue a report on the specific control procedures it has in place. Normally, the reporting accountant’s report is made available to its customers and the auditors of those customers.

We are also aware that the Pensions Administration Standards Association (PASA) is developing an independent accreditation system through which defined benefit and defined contribution schemes (whether trust-based or contract-based) can demonstrate that they meet certain standards. The intention is that the accreditation process will ensure that schemes meet minimum required standards of administration and that underlying processes satisfy the Pension Regulator’s (TPR’s) requirements. In October 2013, PASA published its ‘Guide to Accreditation’.

On 1 May 2014, ICAEW and TPR published a voluntary assurance framework for mastertrusts ‘TECH 07/14 AAF: Assurance reporting on mastertrusts’: the quality of administration falls within the scope of this framework. The foreword to the framework states:

“While there is no standalone legislative or regulatory standard to which mastertrusts specifically need to operate, it is TPR’s belief that mastertrust providers and trustees of mastertrusts (which may include individual trustees and corporate trustees) would find it beneficial to be able to report on and thereby enable scheme members and customers (employing companies) to obtain a better understanding of the governance and administration arrangements of the mastertrusts.

This [framework] therefore sets out what is expected from assurance reports provided by independent practitioners on specified control procedures over a mastertrust’s governance and administration, as set out in [TPR’s] DC code of practice and DC regulatory guidance. The control procedures are assessed in the light of control objectives that are set out in this [framework].

[TPR] has stated that it would expect mastertrusts to provide their first report in accordance with this framework for periods ending in the financial year 2014/15.”

Generally speaking, a mandatory system of accreditation would need to have clear objectives, represent value for money and offer something more effective than the other forms of assurance or accreditation which are currently available or in the pipeline. Such an accreditation regime is likely to be costly to establish therefore demonstrating that it provides value for money could be challenging.

Question 2. We would also welcome suggestions of other approaches to helping trustees and IGCs ensure that their scheme is being administered to a good standard.

Answer 2. See our response to question 1. There are options already available or in the pipeline which can assist trustees and IGCs assess the standard of administration.

Also, trust-based schemes are expected to comply with TPR codes of practice and we believe that there is a need to introduce a code of practice for contract-based DC schemes aimed at ensuring a consistent regulatory approach to schemes across the board. We understand that TPR and the Financial Conduct Authority are working together on such an initiative.
**Mastertrusts**

**Question 3.** Should mastertrusts have to meet the same independence standards as providers of contract-based schemes?

**Answer 3.** We are not in full agreement that mastertrusts should have to meet the independence standards set out in the Command Paper.

We believe that a requirement to have a minimum board size for mastertrusts of seven plus the implicit requirement to have a minimum of four independent trustees will add significant cost to the governance arrangements of mastertrusts.

In addition to the cost of paying for four or more independent trustees, the requirement to pay a recruitment consultant to search for an independent chair will be costly. We are not convinced that it will be possible in all instances for mastertrusts to identify a recruitment consultant with the necessary knowledge and skills to conduct the search for a chair. Therefore, we question the effectiveness of this proposed requirement as a means of ensuring mastertrusts are well governed.

We are keen that there is employee involvement in the trustee boards of mastertrusts. We recognise that there will be a requirement to ensure that members’ views are directly represented but that this would not have to be achieved by member representation on the board. We recognise that for mastertrusts, which have many members from a large number of different employers, securing member engagement and obtaining member views will be challenging. However, we believe that the tradition of member-nominated trustees should continue as part of any agenda for member participation in the governance of mastertrusts.

**Question 4.** We would welcome views on the proposed definition of ‘independent’ at Annex B.

We have concerns about the definition of ‘independent’ in relation to the overall structure of trustee boards and we set out our comments on this in our answer to question 3.

**Question 5.** Should the independence requirements be applied in different ways to different models of mastertrust? In particular, how should the independence requirements be applied to mastertrusts that use an independent trustee firm to act as their corporate trustee?

**Answer 5.** We have no additional comments to make on the application of independence requirements to different models of mastertrust.

**Trust-based governance**

**Question 6.** We would welcome views on the proposed quality standards for trust-based governance which are summarised at Annex B.

We view the introduction into regulation of minimum quality standards as overregulation compared to the requirements for defined benefit schemes and we do not believe that the DWP has made a case for introducing minimum quality standards into regulation.

TPR is in the process of updating its code of practice on funding defined benefit schemes and has issued a new code (November 2013) on the governance and administration of trust-based defined contribution schemes. Until TPR and the DWP have had the opportunity to assess the effectiveness of the new code, we do not believe there is an evidence base for introducing minimum quality standards into regulations.

We comment on the proposed minimum quality standards in our response to question 7.

**Question 7.** Are the requirements listed at paragraph 8 the right quality standards to be set in regulations for trust-based schemes?

The quality standards appear to be listed in paragraph 9 and again in Annex B. However, differently worded but similar quality standards are also set out in paragraph 5.
Setting aside our reservations about including these minimum quality standards in regulations, we do not believe that these quality standards have been well designed. Also, preparing two different but similar lists of quality standards gives scope for uncertainty about what the proposed standards are. If standards are to be placed within regulations the wording needs to be precise to ensure that they are clear and that any scope for unintended consequences is minimised. For example, paragraph 5 states that “the governing body must consider charges borne by scheme members” while Annex B states that “the trustees must assess the levels of charges borne by scheme members”. We do not believe that ‘considering’ and ‘assessing’ are equivalent terms and we believe that both are too vague to be included in regulations.

The requirement to include a statement on how the quality standards have been met with the audited report and accounts could be problematic. In paragraph 7, the following is stated “…the need for trustees to provide a clear, independently audited annual statement that they have also met the governance requirements [set out in paragraph 9]”. There are a number of difficulties with this material:

- Strictly speaking it is the accounts that are audited not the annual report. The correct terminology is ‘the annual report and audited accounts’. Auditors are required to provide positive assurance on the accounts but only undertake a consistency check on any material accompanying the accounts.
- The reference to the statement being audited is quite different from the auditor undertaking a consistency check on the material published alongside the accounts. It is unlikely that auditors will be willing to provide a separate report giving positive assurance on the chair of trustee’s annual statement. The mistakes in terminology suggest a lack of understanding of assurance engagements and a lack of clarity as to what the requirement for an audited annual statement is designed to achieve. The material in Audit Practice Note 15 (Revised): The Audit of Occupational Pension Schemes in the UK sets out, on pages 108 and 109, the auditor’s responsibilities to other information in documents containing audited financial statements.
- The terms ‘quality standards’ and ‘governance standards’ appear to be used interchangeably and this makes what is being proposed here even less clear.

The requirement for an audited annual statement needs to be reconsidered. The pension auditors on the ICAS Pensions Committee would be willing to discuss this issue with the DWP.

Question 8. Should trust-based schemes be required to have a chair of trustees?

Answer 8. We agree that trust-based schemes should have a chair of trustees and we believe that this is already the case for most schemes. However, we do not believe that it is sufficient to bring this requirement into regulation without setting out comprehensively what additional responsibilities a chair would have.

There are higher legal duties placed on trustees who have a professional role and we believe that placing additional responsibilities on the chair could result in a higher duty of care. If this is the impact of any additional responsibilities, this could impact on the cost of trustee liability insurance.

Chapter 1, paragraph 5 of the Command Paper states that the “chair of the governing body must produce an annual report explaining how the scheme has performed against quality standards”. This could be interpreted in two ways: first, that the chair is responsible for preparing the report and is therefore solely responsible for its content; and second, that the report is signed by the chair on behalf of the board. The former scenario would give rise to a higher duty of care while the latter would fall within the scope of collective board responsibility. The wording in paragraph 7 alludes to collective responsibility on this point.

We recommend that careful consideration is given to setting out the envisaged responsibilities of the chair. If there is no intention to place a higher duty of care on the chair in this regard and this would be our preferred approach, then the additional responsibilities should be developed with this in mind.

Question 9. Will the new reporting requirements help drive compliance with the standards and regulation of these?

Answer 9. We do not believe that the new reporting requirements are sufficiently well thought out.
Transparency

Question 10. We would welcome views on how these transparency requirements could be made to work effectively in unbundled trust-based arrangements (including mastertrusts).

Answer 10: We are generally supportive of measures to increase transparency. However, we do have some comments with regard to contract-based DC and DC generally in the context of auto-enrolment.

There is often a knowledge gap at employer level around their ability to assess the quality of a scheme at the point of selection and on an on-going basis. The implementation of auto-enrolment increases the number of employers caught by this knowledge gap and, as smaller employers are now reaching their staging dates, we have become aware that scheme selection is becoming a compliance exercise and for most of these small employers choice may be limited to NEST and one or two other mastertrusts. ICAS members in practice are beginning to bring their concerns about auto-enrolment implementation to us with particular concerns about the ability of the payroll products they use to deliver a sufficient choice of auto-enrolment solutions.

In summary, constraints in scheme selection appear to be due to a combination of the cost of compliance (set up costs and recurrent costs), difficulties accessing professional advice due to the cost of advice and high-levels of demand and the need to ensure that an auto-enrolment solution is compatible with the employer’s payroll arrangements. We do not have a comprehensive picture of the extent to which payroll solutions may be unduly limiting the selection of an auto-enrolment solution by employers and we would welcome more visible engagement between DWP and TPR with payroll providers on this issue.

We are concerned therefore that scheme quality in some circumstances is no longer a consideration.

We believe that the introduction of ICGs provides an opportunity for employers and employer-established internal governance committees to assess more effectively the quality of default funds offered by providers of contract-based DC arrangements. Also, we would welcome any developments which would enable employers to compare the performance of default funds offered by a range of providers and the development of benchmarking data on mastertrusts.

Question 11. We would welcome views on whether the transparency we propose for DC schemes should, in future, be extended to DB schemes, to enable sponsoring employers to further scrutinise the costs of such schemes.

Answer 11. We believe that transparent reporting by DC schemes and DB schemes to employers and members requires different approaches. However, we would prefer to comment on proposals specifically tailored to DB schemes than to form our comments around proposals for DC schemes. We would expect the issue of transparency to be revisited as a topic in respect of any products which would fall within the category of defined ambition in due course.