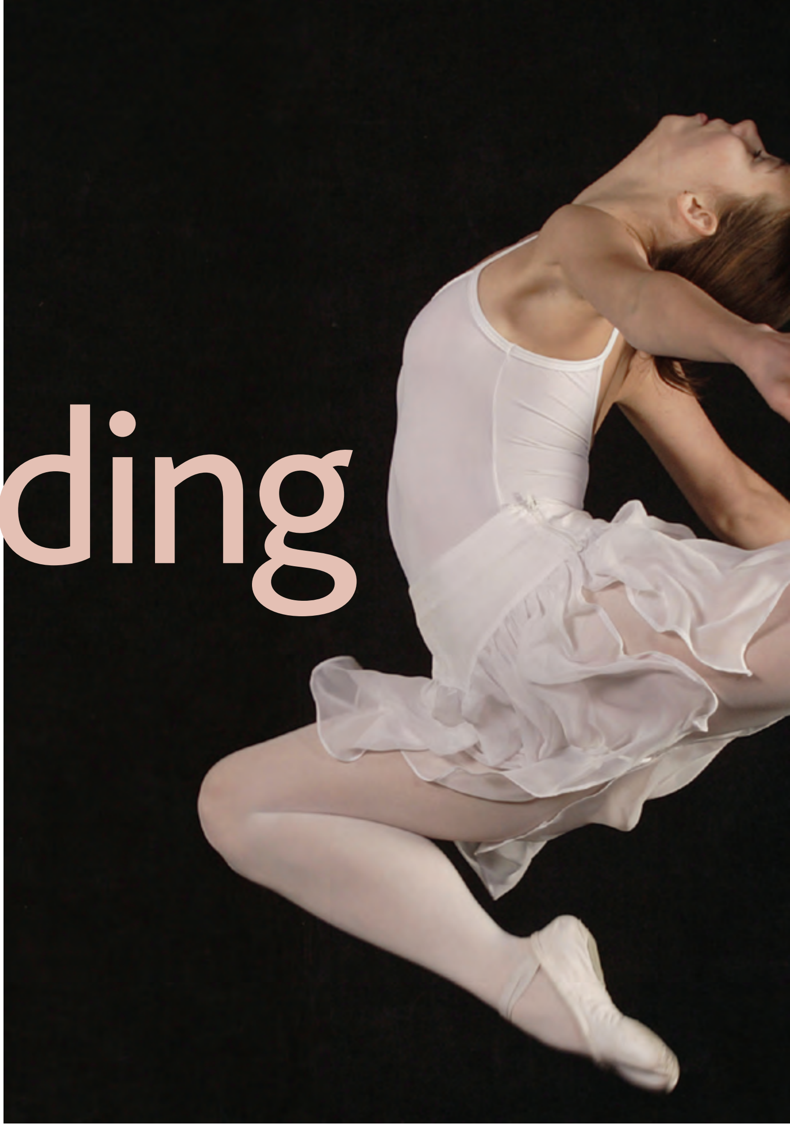
A demanding role



The amount and pace of change in the legislative and investment environments for pension schemes has highlighted the pressures on the role of trustee. So how should trustees be responding to the changes?

Peter Williams (PW): *Let's first clear up one question that troubles some people. What is the difference between an independent pension scheme trustee and a professional trustee?*
Roy Carr (RC): Historically, most trustees have been nominated by either the employer (in other words, the scheme's sponsoring company) from among its executives, or by its members, generally past or present employees. Legislation requires a minimum number of member-nominated trustees. For many years there have been instances of sponsors nominating 'independent' trustees and, at least in theory, employees could do the same, although usually only with the approval of the sponsor. There is some evidence that appointing independents is a growing trend, although it is not uncommon for them to have had some previous relationship to the sponsor.

PW: *And professional trustees?*
RC: There is no statutory qualification required to be a trustee. In practice, anyone who undertakes trustee work will pick up some relevant knowledge and many of those who do will undertake some form of training. At the most knowledgeable end are those who take on trustee appointments for a living, many of whom already have relevant experience in pensions and, often, an appropriate professional qualification. They are generally referred to as professional trustees and the Pensions Regulator places higher demands on their skills and actions than on a lay trustee.

PW: *So professional trustees are usually independent, but the reverse isn't always true?*
RC: Broadly, yes, but professionalism is at one end of a spectrum rather than a line on it, and legislation over recent years has forced all trustees to think much more seriously about their skills and responsibilities. Improving trustee knowledge and understanding is a key element of the Pensions Regulator's regime.

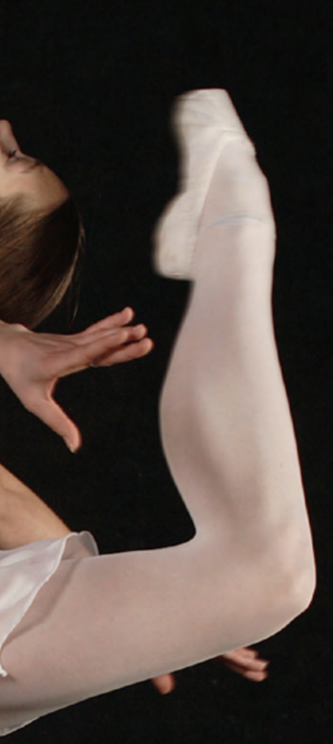
PW: *So how do trustees go about this?*
RC: Getting started is fairly easy, as long the trustee concerned has plenty of time available. The Pensions Regulator's Trustee Toolkit is available online and for the trustee with little or limited experience it imparts some important basic concepts. Various professional bodies provide training and qualifications, such as the Pensions Management Institute. Of course, the ACT's Certificate in Risk Management for Pensions would also be a valuable qualification for trustees.

Executive summary

- **All trustees – professional, member-nominated and independent – have to be up to speed with developments in the fast-changing world of pensions. Those who act as professional trustees have the additional pressure of ensuring they build the appropriate infrastructure and support, such as continuous professional development and peer review.**

PW: *You imply that getting started is easier than making progress and keeping going.*
RC: You are right. It is the sheer quantity and pace of change in the legislative and investment environments that lies at the heart of the problem. The Pensions Act 2004 changed almost everything to do with pension regulation. Accounting and other changes have dramatically altered the way that sponsors and trustees look at investments: five years ago the concept of liability-driven investment didn't exist, a tiny minority of schemes utilised derivatives and the buy-out market was considered the Boot Hill of pensions. A typical lay trustee, one who attends only half a dozen or so trustee meetings a year, has no realistic chance of keeping on top of developments.

PW: *So what's the answer?*
RC: The answer is no different to what it would be in any other



PETER WILLIAMS INTERVIEWS ROY CARR, CHAIRMAN OF FORESIGHT TRUSTEES, WHICH PROVIDES INDEPENDENT SERVICES TO PENSION FUNDS, ON THE INCREASED DEMANDS PLACED ON PENSION SCHEME TRUSTEES.

financial services business, such as a life assurance company. Not all of the scheme trustees can be lay people; some of them have to be professionals. The thought of a life company having no professionals on its board of directors would never be taken seriously and the same should be true of pension schemes.

PW: *So having one or two professional trustees usually solves the problem?*
RC: Not necessarily. To function effectively, a professional trustee needs a certain amount of infrastructure and support as well as an appropriate background. Two of the fundamental ingredients are continuous professional development (CPD) and peer review. CPD will be familiar to members of the ACT and other professional bodies and requires a major ongoing time commitment, especially in pension work. Peer review is an essential discipline, because even the most experienced professional trustees will come across issues with which they have no recent personal familiarity.

PW: *How do you and other professional trustees organise this?*
RC: Not all professional trustees do. Historically, professional trusteeship is something taken up by a variety of practitioners, either by design or through circumstances. Some have joined one of the established trustee firms, where infrastructure may be available to a greater or lesser extent. Others have become sole practitioners, where it can be much harder to find the time for CPD. Sole practitioners will also by definition find peer review more difficult and may therefore have to rely to a greater extent on paid advisers of one sort or another, which can have adverse implications for cost and the timeliness of decision-making. It can also be difficult for sole practitioners to find alternates if unavoidably absent from meetings.

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PW: *Is it the job of employer-nominated trustees to represent the interests of the scheme members and member-nominated trustees to represent the employees?*
RC: Far from it. Trust law is very clear that trustees have the responsibility to represent the interests of the beneficiaries of the trust. These beneficiaries are generally present and past employees (including pensioners) and, in some cases, their dependents. Once a trustee has accepted that appointment, it is quite inappropriate for him or her to carry out their trustee duties with a view to promoting the interests of the employer or employees. Their duty is to the members, which is, of course, obvious in the case of an independent professional trustee.

PW: *So it is quite possible to find that an employer/member-nominated trustee has a conflict of interest in carrying out their duty?*
RC: Indeed. Treasurers and chief financial officers in particular might find occasions when their duties as a company executive are diametrically opposed to their duties as trustees. Of course, this is a great pity, since these are the very people most likely to aid the trustee board in asset-liability management issues.

PW: *Is there a way round this?*
RC: Some trustees in this position simply absent themselves from meetings when serious conflicts arise, which can be the very time a cohesive board at full strength is required. A better long-term solution may be for senior financial executives to make themselves available to the appropriate subcommittees that form an integral part of most scheme governance arrangements. This might involve co-opted membership of investment or asset-liability management subcommittees and frequent attendance at whichever subcommittee has the task of monitoring the sponsor covenant.

Professional qualifications

One way in which trustees can improve their effectiveness is to study for the ACT's Certificate in Risk Management for Pensions (CertRMP). The qualification is for financial managers and covers the legislative and financial framework surrounding pensions, including the role of trustees, risk management implications and associated governance issues.

The CertRMP is designed to enable individuals to understand, analyse and manage the risks associated with company pension funds. It explores the impact of the pension fund on the cost of capital, helping individuals manage the financial assets of the business and address funding requirements.

Topics covered include the UK pensions framework, types of company pension and pension risk exposures. For more information, go to: **www.treasurers.org/qualifications/certrmp**

IF ANYONE HAS A WIDE RANGE OF TECHNICAL SKILLS RELATED TO PENSIONS, IT IS LIKELY TO BE THE PROFESSIONAL TRUSTEE.

PW: *Do professional trustees invariably become the chairs of trustee boards?*
RC: There are certainly many cases where they do not, although it does seem to be a trend. Chairmanship skills may or may not be present in someone who can add value to a trustee board through their knowledge of pensions. The important thing is that the sponsor understands whether one or both skill sets is required and recruits accordingly. In the cases where a professional trustee is not the chairperson an important part of their brief will normally be to provide strong technical support to the chair. In these situations there may be some analogy with the role of a senior non-executive director on a company board.

PW: *Can the analogy of non-executive directors and professional trustees be taken further?*
RC: Probably not. The irony is that on most company boards the executive directors are expected to have strong technical skills and the non-executive directors are not. The reverse is the case on most trustee boards. If anyone has a wide range of technical skills related to pensions, it is likely to be the professional trustee.

PW: *Can professional trustees actually add value?*
RC: If they can't they shouldn't be doing the job. I can think of at least one recent case where a professional trustee made the difference between a scheme being able to take advantage of a significant market opportunity to the benefit of the members and the sponsor, which may well not have been the case had that person not been on the trustee board. The system probably shouldn't have to depend on individuals in situations like this, but in practice it does. Speeding up 'pension time', which is a much slower version of normal business time, is one of the less frequently discussed skills of the professional trustee.

PW: *Do professional advisers such as actuaries and investment managers tend to resent professional trustees?*
RC: There is no reason why they should resent them as a class, although in any profession there will be the odd individual who can have this effect. In practice, most advisers welcome being given clear instructions and a clear timetable for providing deliverables, both of which tend to be more likely when a professional trustee is involved. Likewise, intelligent questioning of advice given should be welcome.

PW: *There seems to be general agreement that defined benefit pension arrangements are heading towards extinction. Is there still a place for the professional trustee?*
RC: Yes, there is, for at least two reasons. First, even fully closed defined benefit schemes are likely to remain in existence for many years, unless they are wound up. Even then, the wind-up itself can be a long, drawn-out process. Second, although alternative structures are available, many defined contribution and risk-sharing pension arrangements are still provided through trust structures, which still require trustees. Incidentally, it is a common misconception that sponsors and trustees do not have to worry about defined contribution schemes: the problems are different, but still present. In particular, the trustees are responsible for the investment choices made available to the members and the way in which they are communicated.

PW: *You mentioned that the Pensions Regulator placed higher demands on professional trustees. Does this bring with it any risks?*
RC: Taking on any fiduciary role carries with it risks, whether it is a company directorship, charity trusteeship or pension scheme trusteeship. For trustees, seeking to reduce these risks generally goes hand in hand with reducing the risks for beneficiaries of the trust. The techniques used will be common to other business activities, such as proper governance arrangements, risk control procedures, external audit and so on. Most trustees, whether professional or not, will benefit from limited indemnity arrangements granted to them by the scheme and/or its employer and many schemes also arrange trustee liability insurance, either as part of or in parallel to directors and officers liability insurance for the sponsor. In some cases sponsors leave it to trustees to arrange their own liability insurance.

PW: *Will the market for professional trustees grow?*
RC: My colleagues and I certainly believe so. Two factors in particular will contribute to the rate of growth. It is pretty clear that the Pensions Regulator would ideally like a higher proportion of professional trustees, but at the same time the mass resignation of thousands of lay trustees would not be in the best interest of schemes. Gentle encouragement is therefore required without lay trustees feeling that they are under pressure to stand down. Over time it would not be surprising if the Pensions Regulator placed a greater emphasis on trustee professionalism.

The other factor is the attitude of sponsors. It is entirely natural that companies feel more comfortable with a trustee whose interests coincide with those of the company, particularly where the trustee serves as chairperson. However, dealing with the increasing incidence of perceived and actual conflicts of interest means that experienced senior company trustees now need to stand down in many situations. Their replacement by professionals with the necessary skills and knowledge to address the complex issues involved in running the pension scheme, with due regard for the sponsor's role, looks to be a solution which will increasingly be adopted. Trustee boards without a good professional trustee sometimes wonder why they need one; trustee boards which appoint one wonder how on earth they ever managed beforehand.

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