



13 February 2009

Our ref: ICAEW Rep 16/09

Carl Davey
The Pensions Regulator
Napier House
Trafalgar Place
Brighton BN1 4DW

By email materialdetrimentcode@thepensionsregulator.gov.uk

Dear Carl,

CODE OF PRACTICE 12: APPLICATION OF THE MATERIAL DETRIMENT TEST

The Institute of Chartered Accountants in England and Wales (the Institute) welcomes the opportunity to comment on the consultation paper *Code of practice 12: Application of the material detriment test* published by the Pensions Regulator (tPR) in December 2008.

The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 132,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 700,000 members worldwide.

GENERAL COMMENTS

We support the introduction of these new powers for the Regulator. We believe these new powers will be beneficial as they will allow the Regulator to consider the actual outcome/effect of the employer action/transfer, rather than being restricted to the supposed intention (which can be difficult to demonstrate). We also believe that an additional benefit will be a strengthening of the position of trustees when dealing with the sponsoring employer in advance of proposed transactions. However, would be interested to know whether tPR has considered a more mathematical (definitive) approach, and we believe that (in the absence of such an approach), more detailed guidance will be needed to avoid the potential for an unreasonable increase in administrative burden or increase in defensive or over cautious clearance applications where there is no material detriment to the scheme.

RESPONSES TO SPECIFIC QUESTIONS

i) Does this draft code meet the requirements of the Act?

In our view it covers appropriate material but it is for tPR to satisfy itself that the proposed Code discharges their legal obligation. We also note that some of the requirements of the Act relate to the process of approving the draft of the Code - Secretary of State sign off, for instance.

ii) Does the code identify correctly those circumstances where the regulator should consider the use of the material detriment test?

Yes, although a number of our members have suggested a mathematical (more definitive) approach (such as 'any action that would reduce the support for the scheme by an amount greater than a certain percentage of scheme obligations'), and we would be interested to know whether tPR had considered a more mathematical formula/approach. It would be helpful for us to understand why tPR decided instead on the (more subjective) proposals in the consultation document. In the absence of such a mathematical approach, the criteria set out in this consultation would appear to us to provide a system to match the objectives that tPR has been trying to achieve since the moral hazards regime was introduced, and it does appear to us to include appropriate safeguards, including the statutory defence described in the consultation document that applies to directors who can demonstrate that it was reasonable for them to have concluded that their action or inaction was not materially detrimental to the likelihood that the scheme members would receive their benefits.

We note the burden will be on the directors to demonstrate that they have given proper consideration to the potential implications for the scheme's ability to provide benefits. However, see (iii) below for our suggestions for how to minimise the amount and cost of such administrative burden. We also believe that tPR now has a track record demonstrating that these moral hazards powers will be used only where appropriate, which we hope will promote trust and confidence amongst the regulated community that the Regulator will not bring inappropriate action against them. This would mean that these new powers would not lead to an increase in clearance applications for transactions that are clearly not of material detriment to the pension scheme.

We also hope that these new powers will strengthen trustee position because, under the current regime, the prospect of a Contribution Notice is a relatively hollow threat.

iii) Do you think the circumstances described include any areas where the regulator should not be considering use of the material detriment test, and if so how should the circumstances be narrowed?

We support all 5 categories, but think that (iv) and (v) should be fleshed out in supporting guidance. We believe that, rather than being limited to containing specific scenarios, this guidance could include example factors that would point towards:

- a 'green' scenario - where clearance should not be necessary, although legal advice might be appropriate, and care would need to be taken that directors can demonstrate they gave proper consideration to implications for the scheme,
- an amber scenarios – marginal situations where seeking clearance likely to be appropriate; and
- a red scenario - inappropriate transaction which would likely result in action by the Regulator.

We hope that including such factors in the supporting guidance will minimise the cost of obtaining specific legal advice in advance of a transaction (where clearance is not sought), and facilitate the preparation of appropriate documentation to demonstrate that proper consideration was given to the potential implications for the scheme's ability to provide benefits.

As we mentioned above, a number of our members suggested a mathematical (more definitive) approach, and the supporting guidance might be the place to address this point. It is also important that this code properly dovetails with the other moral hazards powers, and that the code and/or supporting guidance makes reference to the other relevant guidance on, for example, Type A events.

We also note that OPRA used to publicise anonymised details of cases brought in their Bulletins, and we think it would be helpful for tPR to do this, to give a better understanding of when action is likely to be taken.

iv) Are there any further circumstances which you think may present unacceptable risks to members' benefits or the PPF where the regulator should consider the material detriment test?

We are not aware of other categories that should be included, and we believe this is sufficiently comprehensive to cover relevant scenarios.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

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