10 January 2014

Our ref: ICAEW Rep 04/14

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Dear Ruth

Private Pensions: Miscellaneous Amendment Consultation November 2013

ICAEW welcomes the opportunity to comment on the Consultation – *Private Pensions: Miscellaneous Amendment* published by Department for Work and Pensions in November 2013, a copy of which is available from this link.

ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter, working in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 140,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.

ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

This response reflects consultation with the ICAEW Pensions Subcommittee of the Business Law Committee, which includes representatives from public practice and the business community. The Committee is responsible for ICAEW policy on business law issues and related submissions to legislators, regulators and other external bodies.

Main Points

1. We are responding only in relation to the questions on Regulation 4(2) of the Occupational Pension Schemes (Scheme Administration) Regulations 1996.

2. We welcome the efforts of DWP to address this issue which we think will give rise to real difficulties in the pensions industry if not addressed as master trusts grow in size.

3. The approach of defining ‘very large’ master trusts by reference to the number of employers as proposed has the advantage of simplicity but, whatever number is used, is somewhat arbitrary in effect, because number of employers alone does not necessarily determine what influence any one employer may have over a scheme. We have considered other measures such as relative size of scheme funds attributable to a particular employer or relative size by reference to number of employees, but the same concern, in theory at least, might apply to those sorts of measure to some degree (along with additional unwarranted complications to assess).

4. Auditors are subject to overarching requirements on independence. In particular, the Companies Act 2006 requires an auditor to be a member of a recognised supervisory body which is required to have rules designed to ensure that statutory audit work is conducted properly and with integrity and that persons are not appointed in circumstances in which they have an interest likely to conflict with the proper conduct of the audit. Rules applicable to the UK accountancy profession (including those of ICAEW) implement these requirements. This is an important consideration when it comes to considering the detail of the proposed solution because, even absent any statutory prohibition covering particular circumstances, an auditor must always consider whether or not he has the requisite degree of independence in respect of any appointment and, if not, must decline the appointment (and is subject to a regulatory regime with powers of sanction for breach).

5. In our view, it would be sufficient for the Department to rely upon these general requirements for auditor independence in this context so that the statutory restriction could be removed entirely for all scheme audits. In meeting its regulatory obligations, the auditor would then need to consider all relevant factors in determining whether or not there is a conflict (including, potentially, number of employers, size and other relevant factors). This approach would also meet the government objective of cutting red tape.

Q1.1 Do you think the proposed solution is sufficient to address this problem? If you do not think it would be sufficient please state why not.

6. Notwithstanding the above comments and with one exception, we believe that the proposal would, in practice, largely overcome the concern in relation to the current restrictions (that they will adversely restrict the number of appropriately skilled audit practices available to the largest master trusts).

7. The exception relates to the requirement for at least two thirds of the employers not to be associated or connected (which we take to mean associated or connected with each other). We do not believe that it will be practicable for either trustees or auditors to satisfy themselves on whether or not this threshold is met where there are numerous employers.

8. The definitions of ‘associate’ and ‘connected’ are drawn from the Insolvency Act and are extremely broad. For instance, they may include (and this is selective) employees, husbands/wives/civil partners, relatives (including brothers, sisters, uncles, aunts, nephews, nieces, lineal ancestors or lineal descendants), directors (of companies) and partners (of partnerships) and where one person is an associate of another they are each to be taken as associates of each other.

9. These definitions are workable in the context of the Insolvency Act where the relevant tests need to be applied only in narrow circumstances, such as whether a person to whom a payment is made is associated with another person. In those cases enquiry can be made of specific individuals or entities at the relevant time to establish the position. This is very different from the context in question where it would be necessary for every conceivable defined association or connection that might exist between the numerous employers to be ascertained before the exemption could be relied upon. This would require information that none of the scheme trustee, the auditor or in many cases, the employer, would otherwise have reason to hold and which it would be laborious to obtain.

10. Applying these definitions even to a small master trust (where employers might include individuals, partnerships and companies), would be problematic and would be practically impossible for large master trusts. Numerous 'connections' might well arise (to the extent that the two thirds test might actually be met more often that might be thought likely or appropriate), but they would have little if any significance in terms of auditor independence.

11. We assume that the two thirds test was included in case one employer might control or have material influence over others to the extent that it might be appropriate for them to be considered as one person in this context. We have considered whether there is an alternative narrower definition which could be used for that purpose but have concluded that any provision that would require the trustee or auditor to assess connections between 500 or more employers would be problematic. Whether or not a person is controlled by another is not necessarily determined solely by information in the public domain so that enquiry would need to be made. Even if the test were limited to matters in the public domain, we consider that the work involved in checking the relationships between so many entities would be disproportionate in the context. At a practical level, the concern would only be a legitimate one were a group of employers to be coordinated in a way that would bring into question the independence of the audit of the pension scheme. In the case of a master trust with 500 or more employers, the circumstances where this could arise would need to be extraordinary and we believe that the generally applicable audit regulations noted above would be sufficient to address concerns that might arise in such exceptional cases.

12. We would note that the amount of work required to assess associations or connections of the kind outlined above is very different from the work already undertaken by auditors to assess eligibility for company or pension scheme audits under current legislation. In the latter case, the auditor is aware of its connection with any given company (eg, if a partner is acting on a pro bono basis for a charitable company) and checks can be appropriately focused.

13. In conclusion on this point, we agree that 'very large' multi-employer schemes should be exempted but do not think that it is necessary to have a carve-out from the exemption by reference to connected or associated employers, at least where the test of 'very large' involves numerous employers as proposed. Even without a connected person test, significant practical issues could arise where the test for disapplication is linked to a number of employers of the magnitude proposed.

Q1.2 Are there any other types of scheme affected that we have not considered?

14. We are not aware of any.

Q1.3 As a minimum, how many employers should be involved in a scheme before this disapplication should apply, and why?

15. As noted above, we believe that the statutory restriction could be removed entirely in view of existing general auditor regulation without any adverse impact on audit independence. If, however, a limit on employer numbers is to be set for disapplication, the administrative burden (and related cost which will ultimately be borne by the schemes) should be taken into account in determining the number.

16. In our view, 500 is a sufficiently large number to make any concern about an employer having undue influence over an audit extremely remote without the need for any connected or associated person or other additional test (and should an exceptional case arise where there might be a concern, general auditor regulation could be relied upon). We therefore see no reason for the number to be higher and believe that it could be much lower (if the statutory restriction is not to be

removed). We think that a combination of a number anywhere near as large as 500 with additional associated person (or other) tests, will be unworkable in practice.

Yours sincerely

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