



THE INSTITUTE
OF CHARTERED
ACCOUNTANTS
IN ENGLAND AND WALES

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Your ref:

Sean Scarle
Order and Rules Consultation
Enabling Retirement Savings Programme
Department for Work and Pensions
Adelphi (4th Floor)
1-11 John Adam Street
London WC2N 6HT

By email orderandrules.consultation@dwpgsi.gov.uk

Dear Mr Scarle

Pensions – Consultation on draft scheme order and rules

The Institute of Chartered Accountants in England and Wales (the ‘Institute’) welcomes the opportunity to comment on the consultation paper on the draft order and rules for the personal pension scheme published jointly by the Personal Accounts Delivery Authority and the Department for Work and Pensions in April 2009.

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 165 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 775,000 members worldwide.

Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.

General points

Financial governance: scheme accounts and audit or assurance

1. The proposed rules do not include provisions for financial governance and controls. Although the Trustee Corporation (the Trustees) is likely to have the same obligations in this respect as any pension scheme trustee body, the precise responsibilities will have to be thought through. Whilst there may be provision in the Pensions Act itself, it is not practical for administrators to have to refer to both principal and secondary legislation when carrying out their functions. If the provisions are not to be incorporated into a single piece of legislation, the Scheme Order should have a schedule to identify the provisions in the Act that are not reproduced in the Order. This would make it easier to update the Order if the Act were amended in the future.

2. The provisions need to take account of the fact that it will be practically impossible to treat the personal accounts scheme in the same way as the generality of pension schemes in relation to external review arrangements and financial statements. As the Institute explained in its briefing for the second reading of the Pensions Bill in the House of Lords¹:

“It is the view of the ICAEW that a national scheme such as the personal accounts scheme cannot be audited within the rules applying to occupational pension schemes. The main problem arises in relation to the audit of contributions. With thousands of small employers likely to participate, it will be impractical if not impossible to determine whether contributions have been paid within the appropriate level of materiality determined by the auditor. The problem is exacerbated by the statutory requirement for a pension scheme auditor to give a separate opinion on contributions which states whether or not, in the auditors’ opinion, contributions have been paid in all material respects at least in accordance with the payment schedule, an opinion which encompasses accuracy as well as timeliness. Whilst this is easy to establish in most occupational schemes where there are only a few employers, it is much more difficult and expensive where there are many.”

We do, however, believe the personal accounts scheme should prepare accounts that are independently scrutinised (audited), but there will need to be some departures and thus exemptions from the normal rules governing occupational trust-based schemes.

3. Firstly, the trustees should be required to prepare stewardship accounts, rather than general purpose financial statements. These accounts would depart from the SORP if our recommendation is accepted, that there should be no schedule of contributions (because this could be expensive to administer and monitor) and therefore no statement thereon by the auditors. We also do not support a compromised accruals basis for preparation of the accounts, as this would be subjective and again would involve additional costs. We suggest that the accounts be prepared based on the contributions received and invested by it in the scheme funds, and on any monies held or other current assets/liabilities. These accounts would be provided to the Secretary of State (but see our comments below regarding responsibility for the scheme) and we recommend that they be publicly available on the scheme’s website. There needs to be an

¹ ICAEW Pensions Bill 2007-08, House of Lords Second Reading Briefing 30th May 2008

audit or some other form of assurance engagement on the stewardship accounts: this could be undertaken by the National Audit Office or possibly a private firm.

4. The second aspect would be a governance statement to be provided by the Trustees on their administration of the scheme, for example a statement that the trustee corporation has satisfied itself that the administrator's and fund managers' processes are robust. This could form part of the trustee's annual report and would then be subject to review by the auditors that it was not a misleading statement. The Trustees would in turn require an AAF 01/06 or SAS 70 assurance report from any third party to whom administrative or fund management functions are outsourced, possibly joining in a tripartite engagement with the third party administrator and reporting accountant.
5. We should be pleased to meet representatives of the Department for Work and Pensions (the Department) and the Personal Accounts Delivery Authority (the Authority) later in the summer to discuss the questions of accounts and audit/assurance and how the Institute might help to answer them.

Ultimate responsibility for the scheme (scheme ownership)

6. Many of our criticisms of the proposed scheme rules arise from Government's apparent reluctance to take ownership of the scheme. This means that the proposals lay on the Trustees responsibilities, such as publicising the scheme to prospective members, that would be borne by the sponsoring employer in normal occupational schemes. Again, the sponsoring employer often underwrites scheme administration costs that cannot be allocated to members' funds and for which there are insufficient orphan assets from which payment can be made. There needs to be a principled decision as to who should take the role of the sponsoring employer, and this should underpin the provisions.

Communications

7. We are concerned that communications with employers and members are planned to be carried out mainly, if not exclusively, in electronic form, with paper copies not being an option. We disagree strongly in relation to scheme members. It needs to be recognised that many scheme members may not have access to email or the Internet and so should be able to opt for paper communications.
8. Paper communications should also be considered for employers. Many employers, especially the smaller ones that are likely to be the employers of the majority of scheme members, may not be e-enabled when the scheme comes into operation, despite government attempts to force all employers to submit tax forms online, which will mean that such employers will have to incur the additional expense and inconvenience of either paying an agent to complete and submit forms and communicate with the relevant arm of government, or buying a computer and software, learning how to use it and subscribing to broadband or using an internet café or library with inherent security problems. However, we appreciate that paper communications with employers might be expensive to administer, and so might be restricted in the interests of keeping scheme costs to a minimum.

Consequential amendments

9. Legislation containing provisions affecting retirement provision, such as the Finance Act 2004, will need to be checked and amended as necessary to allow for the implementation and operation of the proposed Order, Regulations and Rules.

Representative panels

10. We are not convinced that the proposed member and employer panels will serve any useful purpose, and may not be worth the time and expense that would be involved in establishing them and the resulting consultation procedures. We appreciate the will to consult and involve members and employers, but given the numbers involved and the profile of members identified in the Authority's discussion paper on an investment strategy for the scheme, there would seem to be little point. We consider that it is the duty of the Secretary of State to appoint Trustees whose key responsibility is to consider and safeguard the interests of scheme members. The Trustees in turn may wish to have a single panel that they can consult, the members of which come from a number of representative bodies, such as the TUC, CBI, and NAPF. We expand on this view in our answers to questions 1 to 3 below.

Costs of administration

11. The only reference to the cost of administering the scheme is in question 8, which refers to the setting of a minimum level of contributions in relation to workers without qualifying earnings. The question of costs is central, given the likely size of fund accumulated by members, and the lack of consideration on this point is disappointing. We recommend that the provisions be kept as simple as possible, in order to minimise the administrative costs of the Scheme. This is consistent with our views on the proposals for employer and member panels.
12. Given the need to minimise costs, we do not consider that the trustee corporation should spend a considerable amount on raising awareness of the scheme among employers and prospective members. Raising awareness is not a part of trustee responsibilities in relation to conventional occupational schemes and we do not see that it is a fair expectation of the trustees of the personal accounts scheme. We therefore recommend that the fullest possible use be made of existing lines of communication with employers and prospective members, such as those established by the Department for Business, Innovation and Skills, H M Revenue and Customs, and of course the Department itself.

Answers to specific questions

Question 1, Article 7: Are the following aspects of the members' panel the right model for ensuring that members' interests and perspectives influence the day to day running of the scheme? • The role of the members' panel; • The members' panel involvement in the recruitment and selection process for all members of the trustee corporation; • The members' panel remit to produce a report on whether the trustee considers members' interests in its decision making process.

Question 2, Article 7: Are there ways in which the panel can be constituted or its functions defined that would maximise its effectiveness?

Question 3, Article 7: Is it appropriate to allow representative bodies in the members' and employers' panels?

13. We are concerned that the proposals for the panels make over-complicated what is supposed to be a simple investment scheme. We do not see any practical way of filling the panels with people who are genuinely representative of the constituencies. We question whether there is any need for the equivalent of member nominated trustees: the scheme needs to minimise costs, but to be effective, panel members will need to have knowledge, understanding, and training.
14. Similarly, we recommend that the proposal for an employers' panel be dropped. Given that most, if not all, large employers have their own occupational schemes, it may be difficult to find individual employers that are representative of the constituency, so that the panel would need to be populated by delegates from employer organisations.
15. In the case of both member and employer panels, there is likely to be circularity in appointment of members, in that potential candidates/representative bodies will have to be identified by someone: there is not a natural pool from which suitable people can volunteer or be selected.
16. As we have stated in our paragraph 10 above, we believe that it is the Trustees' duty to have regard to the needs of scheme members, but that it may be useful to the Trustees in identifying and responding to those needs to have a single panel drawn from a number of bodies that represent employees, employers and pension funds. The Trustees should therefore be able to set up a panel that they can consult on any proposals that would affect members' interests but this should not be a requirement.

Question 4, Article 14: Are the provisions in the scheme order providing indemnity and insurance appropriate to this scheme?

17. There needs to be extra wording or clarification in this Article to make it clear that the Trustees can use scheme assets to indemnify themselves, otherwise cover would be very expensive, if indeed it were possible to arrange cover at all. The alternative would be for the Secretary of State to indemnify the trustees. The latter course will be necessary in any case in the early years of the scheme, when there will not be a sufficient accumulation of orphan assets. There is, therefore, a case for saying that the Secretary of State should indemnify members of the trustee corporation from liability for all losses arising from the discharge of their fiduciary duties.

Question 5, Article 15: Does the wording of Article 15 adequately cover the activity that the trustees will need to undertake to raise awareness of the scheme to employees and prospective members?

18. We consider that this is primarily the role of Government as the quasi sponsor of the scheme: to impose the duty on the Trustees means that they will have to fund their awareness raising activity from the assets of the scheme, which in turn means that the cost will fall on scheme members. The Pensions Regulator also has a role, under the Pensions Act 2004, to promote, and to improve understanding of, the good administration of work-based pension schemes. Representative bodies and organisations can help in raising awareness, and the

Institute is planning to cover the personal accounts scheme in a series of roadshows to take place in Spring 2010.

Question 6, Article 17: What remedies would be useful for the trustee corporation to have available in order to deal with employers who persistently fail to meet the agreed terms and conditions of the scheme?

19. It is hard to see how employer compliance can be enforced without considerable additional costs involved in monitoring the receipt of contributions and sending out reminders, etc., let alone enforcing payment of any fines levied for non compliance. We recommend that, even if the scheme will not use the PAYE/NI deductions system for policy or practical reasons, the Department and Authority discuss enforcement issues with H M Revenue and Customs to see if the latter have any practical tips to offer.
20. To make compliance easier, there should be clear rules and guidance explaining the rules which is easy for employers to follow, for example as to due dates for payment, and other requirements. It might help if there were a register of members so that employees could check whether they had been enrolled on the scheme. It would also be useful for members to have online or ready access to their own benefit statement so that they could check monies paid over and query apparent under- or non-payments.

Question 7, Articles 18 and 19: Are there any issues arising out of the proposal to operate one membership category and not to differentiate between “active” and “deferred” members?

21. We do not see any difficulties and therefore agree with the proposal.

Question 8: In order to avoid disproportionate administrative costs should the scheme set a minimum level of contributions in relation to workers without qualifying earnings?

22. Yes, we think there should be a minimum level of contributions. This could be set at £20 per month, as in the current stakeholder scheme.

Question 9, Article 25: Should there be a specific provision to require the trustee corporation to make the level and method of deductions transparent, and if so, how can this be achieved?

23. A balance needs to be struck between transparency and the amount of information given. It is possible that, the more information that is provided, the greater will be the volume of questions from members. The costs of the scheme will comprise investment manager charges for running the funds and administrative costs that we assume will include the following:

- Set up costs
- Database administration
- Cost of investing member and employer contributions received with an investment manager
- Establishing a sinking fund for one-off or long-term expenses
- On-line/IT costs
- Cost of trustee indemnity insurance (if cover can be obtained) unless or until there are orphan assets available to pay for this
- Administration of orphan assets.

We recommend that members be told what the investment and administrative costs are, and the method by which the costs are allocated, i.e. deducted from the fund. It will be for the Department to decide whether allocation is on a per member basis, or on the size of each member's 'pot'.

24. The charging structure will need to be announced soon: as we have argued in the general points above, the system should be kept as simple as possible, in order to keep costs to a minimum. Transparency and reliability would be enhanced if the allocation of costs by the trustee corporation were covered by the assurance report recommended in our paragraph 4 above.

Question 10: should the trustee have the power to change the scheme rules without the agreement of the Secretary of State? If not, what are the circumstances where you feel that the trustee should not be able to make changes?

25. The answer to this question depends on who has ownership of the scheme. To suggest that the Trustees should have power to change the scheme rules without the agreement of the Secretary of State, suggests that the Government is passing ownership of the scheme to the Trustees. This will become increasingly burdensome as the scheme grows, and we are very concerned that the responsibility will make trusteeship risky and therefore unattractive to most people. We appreciate that the trustee corporation needs to have flexibility in the longer term, subject to the overriding duty to uphold the interests of scheme members, but there needs to be a balance, as is the case in normal occupational schemes, between the sponsoring employer and the trustees.
26. The converse of this question is whether the Secretary of State should be able to change the rules without consulting the trustee. In a normal pension scheme the sponsoring employer does not have this power, and we consider that the Secretary of State should consult the trustee on any changes.

Other points

27. So far as rules on ill health and retirement benefits are concerned, these need to be kept simple and clear. On retirement, the member should be entitled to a lump sum payment and annuity purchased with the remainder of the pot. The test for incapacity benefit should be strictly applied, requiring the member to be unfit for any form of work, rather than just unfit for their current employment. There also needs to be provision for members who are unemployed or between jobs and seeking employment, for example contributions paid by the state.
28. There is a question of how to pay benefits where a member dies intestate and not having nominated a person to whom any death benefits should be paid. As it can be very difficult to determine next of kin, it would be helpful to give the Trustees discretion as to where to pay the benefit and to indemnify them against any resulting claims.

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

Yours sincerely

Liz Cole
Manager, Business Law
T +44 (0)20 7920 8746
F +44 (0)20 7638 6009
E liz.cole@icaew.com