



Punter Southall
CONSULTING ACTUARIES



A framework for delivering your long-term strategy



Pension scheme governance

A guide for trustees



Contents

- **Developing a positive approach to governance**
- **Establishing controls**
- **Understanding your employer's covenant**
- **Governance of the pension scheme's assets**
- **Trustee Knowledge and Understanding**
- **Importance of good record-keeping**
- **Other important governance areas**
- **Developing a business plan**
- **Get in touch**

Importance of good governance for pension trustees

Pension trustees have a broad range of duties which are underpinned by a host of legal obligations and by copious guidance from the Pensions Regulator. Good governance helps trustees to carry out these duties efficiently and ensures that all key tasks required by law are carried out along the way.

Governance is all about putting a framework around the trustees' role and obligations so that they are better able to:

- identify and monitor the risks in the pension scheme;
- prioritise the issues they face, allowing them to focus on those that are most important; and
- make informed decisions based on the advice they receive from their appointed advisers.

This all helps trustees to:

- fulfil their fundamental role of ensuring that their scheme members' retirement benefits are looked after properly; and
- protect them from sanctions from the Pensions Regulator and legal challenges.

This guide sets out an approach to governance and the principal areas where trustees need to focus their attention.



How we can help you

We see our role as ensuring that the 'governance budget' set aside by trustees has a tangible impact on their scheme and goes significantly beyond just placing a tick in a box.

Developing a positive approach to governance

We strongly believe that governance can have a positive influence on the business of trustees and there is evidence to suggest that it can create tangible gains from improved performance of a scheme's investments.

For governance to be successful, it needs to be 'active' – not something you do once a year to tick a box but something that is integrated with the business of the trustees, driving the agenda and helping focus attention on what needs to get done.

From experience, trustee boards where governance works really well have following characteristics:

- the trustees recognised that putting the governance framework in place requires an initial investment of time and effort;
- there is an explicit ongoing 'governance budget' both in terms of trustee time and adviser fees; and
- the governance framework is used directly to develop a business plan that drives trustee business, which become more 'proactive' rather than 'reactive'.

The job of setting up and maintaining a good governance framework should be seen as an investment rather than purely as a cost.



How we can help you

Based on our experience in conducting risk assessments, we acknowledge that one type of review will not fit all schemes. We have therefore tailored our service to suit different types of schemes and the risks that are inherent in those schemes.

Establishing controls

Since 2005, trustees have been required to establish adequate controls for the operation of their pension scheme to help ensure that the scheme is being well run.

We have developed an online tool which looks at risks in five key areas – available at www.puntersouthall.com/riskevaluator. This has been designed to provide trustees with an initial 'high level' review of the issues and should help form a good starting point for a more detailed investigation of the risks.

A key part of this exercise is to establish the risks in the scheme which are then graded according to their likelihood of occurring and the impact on the scheme if they do occur. The depth to which the risks are assessed will depend on the size and complexity of the your scheme.

To make this process add real value to the business of the trustees, a risk register should be compiled that summarises each risk, procedures in place for monitoring and any follow-up actions required to mitigate either the likelihood or severity.

With a framework like this in place, trustees are able to focus on the areas of significant risk and establish an approach that aims to take appropriate action to help control the risk. The framework's 'ready-made' list of priorities also helps drive the trustees' agenda and business plan.



How we can help you

We use our experience of pension scheme funding and trustee funding issues to add real value to the assessment and monitoring process and produce useable information for the trustees on which they can make decisions.

Understanding your employer's covenant

The covenant of your employer refers to its legal obligation to fund your scheme now and in the future. The strength of the covenant is derived from a combination of the employer's willingness and ability to continue to support the scheme.

The Pensions Regulator expects trustees to assess the covenant objectively and regards ongoing monitoring of the covenant as a high priority. This is especially so in the context of:

- scheme funding, where views on the covenant will inform trustees' decisions on the assessed level of liabilities and any recovery plan needed; and
- corporate activity, where events may impact on the strength of the covenant and the trustees need to determine the extent of any mitigation that should be requested.

It is therefore important for trustees to develop a proportionate approach to capturing information about the employer covenant on a regular basis.

The level of detail and regularity of this information will depend largely on the particular circumstances of the employer and the funding level of the scheme.

We have developed a pragmatic approach to the ongoing assessment of the employer covenant that provides more than just a regurgitation of the figures contained in published accounts or provided by the company.



How we can help you

We recognise that the investment governance needs of trustees vary greatly depending on the nature of a scheme and the complexity of its chosen investment strategy. We have worked with trustees from a broad spectrum of schemes to create pragmatic governance structures that meet their specific requirements.

Governance of the pension scheme's assets

The most fundamental scheme risk is that it has insufficient money to provide the benefits that have been promised to the members. Arguably then, some of the biggest decisions trustees make are on the investment of the assets that have been provided to pay those benefits.

It is essential therefore that one of the primary focuses of any governance structure should be to establish appropriate mechanisms and procedures to ensure the proper implementation and ongoing monitoring of the trustees' chosen investment strategy.

The Myners review from the early part of the last decade introduced a series of principles (reviewed by the NAPF in 2007) and these have become the fundamentals for investment governance.

In brief, it's about:

- **Strategy**
 - which includes the periodic review of a scheme's allocation to the various asset classes, how to access and implement the chosen investments, and how the chosen strategy should evolve over time as a scheme matures and/or its objectives change;

- **Measuring performance**
 - which includes the setting of appropriate and specific targets for the investment funds;
- **Risk management**
 - which includes setting up controls around a wide range of issues to minimise risks that may emerge from time to time; and
- **Organisation of the investment function**
 - which includes how the trustees engage with their service providers and how the trustee board itself deals with investment issues.



How we can help you

We have a wide range of training resources, which will enable you to receive the level of training you need.

Trustee Knowledge and Understanding

To carry out their duties properly, trustees must ensure they develop and maintain the right skills to run their scheme.

This does not mean they need to become pensions experts! The key is that they should have sufficient knowledge to:

- understand the advice given to them by their professional advisers;
- have the confidence to challenge that advice constructively where appropriate; and then
- feel able to make informed decisions.

The Trustee Knowledge and Understanding requirements were introduced in 2005 and set out what trustees are expected to know. Broadly speaking, the requirements focus on a working knowledge of the scheme's documents (including the scheme's trust deed and rules), an understanding of pensions and trust law, and the principles of scheme funding and investment issues.

The Pensions Regulator expects trustees to look at each area, determine which part applies to their scheme and what degree of knowledge is required for each item, and then identify gaps in their knowledge which should then be addressed through a training plan.

A first port of call for most pension trustees, especially those new to the role, is the e-learning modules produced by the Pensions Regulator and which are available at www.trusteetoolkit.com.

We have a range of training courses that aim to provide:

- basic grounding in the core areas of the Trustee Knowledge and Understanding requirements – ideal for new trustees, although more experienced trustees have welcomed these courses as a good 'refresher';
- more specific training targeted at particular times in the life cycle of the scheme – for example, trustees have found it very useful to attend a course on pension scheme valuations just prior to carrying out a valuation for their scheme; and
- advanced training for those trustees that require more detailed knowledge – for example, members of an investment subcommittee generally require higher levels of investment knowledge to carry out their role effectively.



How we can help you

We can provide reports on the quality of your data and develop plans to address any problem areas.

Importance of good record-keeping

Recent guidance from the Pensions Regulator gives pension scheme trustees 18 months to assess their membership data and take action to correct any deficiencies. We strongly recommend that action is taken now to identify any issues.

Poor record-keeping can have a significant impact on your pension scheme. Inaccurate, out-of-date and/or missing data about the pension scheme members can lead to a variety of problems in the day-to-day administration of the scheme, and uncertainty about data quality can add significant costs and delays to the scheme's triennial valuation, and any de-risking exercises that are carried out (such as closures to future accrual or buy-outs).

Regular reviews of the accuracy of membership data should be an integral part of a scheme's risk management plan.

The Pensions Regulator has recently published revised guidance on record-keeping. This guidance set out a methodology for the measurement and reporting of:

- 'common data', which is basic information such as name, date of birth and membership status and will be applicable to all the members of a scheme; and

- 'conditional data', which is the more detailed information required for the proper administration of a scheme and is expected to differ from scheme to scheme.

The Pension Regulator wants pension scheme trustees to measure their data to identify where gaps and/or inconsistencies exist, and then put in place improvement plans that seek to rectify any problems by the end of 2012.

We are actively helping trustees with:

- tailored reports that give an overall rating of their scheme's data quality and which identify the presence of common and conditional data;
- developing plans to fill any data gaps identified; and
- tracing members through the DWP tracing service and other specialist tracing companies.



How we can help you

We have a range of different pro-forma IDRPs and Conflicts of Interest Policy formats that can be adapted quickly to reflect your policy for dealing with any complaints and conflicts.

Other important governance areas

There are a number of important governance areas where we would normally work with trustees and, where appropriate, their legal advisers to develop appropriate procedures. These areas include:

Internal Disputes Resolution Procedures

Pension scheme trustees are required to have a formal complaint procedure, known as the Internal Disputes Resolution Procedure (IDRP). This gives any interested parties the opportunity to formalise any complaints they have regarding any aspect of their membership of the scheme.

An IDRPs provides a structure for all parties during the complaint process, helps manage the expectations of both sides and means that, overall, the process runs much more smoothly.

Conflicts of Interest Policy

Pension scheme trustees have a strict duty to act in the best interest of the scheme's beneficiaries, but this does not mean that a trustee will not have other roles or responsibilities which may result in a conflict of interest. For example, you may also be a beneficiary of the scheme for which you are a trustee.

The Pensions Regulator has provided some guidance for trustees and one of its clear recommendations is the establishment of a Conflicts of Interest Policy. This will help trustees identify conflicts, establish procedures to manage them and document how they will act in the best interest of the scheme's members.

Ultimately, you may need to be able to demonstrate to the Pensions Regulator, scheme members or other parties how you have identified and dealt with any conflicts.

Member Nominated Trustee arrangements

Legislation requires that at least one-third of a scheme's trustees are member-nominated. Member-nominated trustees ('MNTs') can be drawn from active members and current pensioners, as well as deferred pensioners. Regulations do not specify a minimum or maximum period of office for an MNT, but it is normally between three and six years.

Your first priorities are to determine the number of MNTs needed for your scheme and then to ensure arrangements are in place for their nomination or selection within a reasonable period. The Pensions Regulator usually defines a reasonable period as six months, depending on the size of the scheme.



How we can help you

We have worked with many sets of trustees to put this final piece of the 'governance jigsaw' in place and they find this output from the governance process a very valuable tool in the ongoing management of their many duties and obligations.

Developing a business plan

A forward-looking business plan is essential for trustees as it should effectively underpin their whole approach to governance and bring an element of planning to the issues that they consider. Agreeing a strategic direction for the pension scheme over a given timeframe will help trustees to identify which areas of governance are most important. This will help with setting the governance budget of time and cost.

It also introduces a robust framework around all aspects of the business of the trustees, including:

- monitoring and reviewing key risks to the scheme, including investment strategy, employer covenant, and internal controls;
- trustee training requirements;
- key communication exercises with the members;
- expiry of trustee periods of office and MNT nomination and selection dates; and
- key statutory reporting dates and exercises with compliance deadlines.

Business plans are particularly useful for schemes looking for a managed wind-up process, so that progress against the long-term plan can be monitored by putting in place appropriate milestones. The milestones can then be integrated into the scheme's annual events planner. Bringing all of this together means that both long and short term goals are met.



Get in touch

For further information on any of the areas covered by this governance guide, copies of Punter Southall's governance documents, or to set up an initial meeting to discuss how we might help you in developing an effective governance strategy, please contact our Trustee Governance team.

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Punter Southall Group operates from the following locations:

Aberdeen, Birmingham, Bolton, Bristol, Cardiff, Edinburgh, Guildford, London, Maidstone, Redhill and Wokingham. We also have a sister business in Boston, USA.

For further information, visit our website at www.puntersouthall.com