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Conflicts of interest and actuaries:

A note for pension scheme trustees



Professional Regulation
Executive Committee

Version 1.1

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Introduction

As a trustee, you will want to be confident that the advice you receive from your actuary (and from other advisors) is not affected by conflicts of interest.

Indeed, in its guidance to trustees on conflicts of interest, the Pensions Regulator says that “trustees should actively manage their relations with advisors to ensure that advisors are able to provide independent advice”.

The Institute and Faculty of Actuaries (IFoA) recognises this, and we are keen to:

- provide assurance to trustees by making you aware of the professional obligations with which actuaries must comply; and
- help you to manage and get the best out of your actuary by being aware of the conflicts of interest sometimes faced by actuaries.

“trustees should actively manage their relations with advisors to ensure that advisors are able to provide independent advice”

Foreword and purpose of this note

This note is issued by the IFoA for the use and benefit of trustees and actuaries. It sets out the IFoA's view of good practice in relation to conflicts of interest that might arise for Scheme Actuaries and how Scheme Actuaries should manage those conflicts.

It is designed to assist trustee boards in exploring with their actuary the kinds of conflicts of interest which might arise in practice. In so doing, it may help inform trustees' thinking in relation to the issue of conflicts of interest which may be faced by them and their actuary. Trustee boards may also find that their actuary uses this note.

This note is not intended to be the only standard of good practice for actuaries and their employers to follow. The key consideration for an actuary is that, whatever means are employed, his or her obligations under the Actuaries' Code (and related standards), which is the set of ethical principles actuaries are expected to observe, are met.

This note does not constitute legal advice, nor does it necessarily provide a defence to allegations of misconduct. While care has been taken to ensure that it is accurate, up-to-date and useful, the IFoA will not accept any legal liability in relation to its contents.

Audience

This note mainly considers actuaries who are appointed by trustees of funded defined benefit pension schemes to act as Scheme Actuaries under the requirements of the Pensions Act 1995. However, much of it also applies in other situations where trustees take advice from actuaries.

1 November 2012

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1. Legal requirements and regulatory guidance

Your actuary, like some of the other professional advisors you appoint, is required by law to notify you immediately of any conflict of interest to which he or she is subject in relation to your scheme. However, as the Pensions Regulator points out, disclosure of a conflict of interest will not itself manage the conflict.

The Pensions Regulator's **regulatory guidance for trustees** on conflicts of interest provides many useful suggestions.¹

The Pensions Regulator has also issued **guidance to trustees on relations with their advisors**, including Scheme Actuaries, which also might be of assistance.²

1] www.thepensionsregulator.gov.uk/guidance/guidance-conflicts-of-interest.aspx

2] <http://www.thepensionsregulator.gov.uk/guidance/guidance-relations-with-advisors.aspx#s1683>

2. What to expect of your actuary

Your actuary will wish to support the role played by trustees in providing scheme members and the wider public with confidence in pension schemes. This is one of the reasons why actuaries aspire, and are held by the IFoA, to high standards of professional conduct.

Actuaries are expected to observe five principles set out in the Actuaries' Code: integrity, competence and care, impartiality, compliance and open communication. The particular principle that is relevant to conflicts of interest is impartiality:

Impartiality: members will not allow bias, conflict of interest, or the undue influence of others to override their professional judgement.

The Code amplifies this by, in effect, requiring actuaries to ensure that:

- advice to trustees is objective and cannot reasonably be seen to be compromised; and
- they do not provide advice where there is a conflict of interest that cannot be reconciled.

This means that there may be situations where an actuary will not be able to advise (or to continue to advise) you. And there may be other situations where an actuary can only advise (or continue to advise) you if certain steps are agreed with you.

The IFoA has also published specific actuarial ethical and conduct standards for pension scheme actuaries³. In particular, with effect from no later than 1 July 2013, there is a presumption that your Scheme Actuary cannot provide certain types of advice to any of the employers connected with your scheme.

This prohibition covers advice on scheme funding, actuarial factors, benefit changes and other matters which would directly affect scheme benefits.

Nevertheless, your Scheme Actuary may depart from this presumption in exceptional circumstances: for example, if your scheme's rules require your Scheme Actuary to provide advice to both you and the employers and it is not possible or appropriate to amend the scheme rules or if legislation prescribes that the Scheme Actuary must provide advice to both

you and the employers. Before doing so, however, your Scheme Actuary must have regard to all of the relevant circumstances, including public interest considerations.

Additionally, your Scheme Actuary must ensure that a written conflicts management plan is agreed with you as trustees and the employer if your Scheme Actuary, or anyone else in your Scheme Actuary's firm, is advising the employer in relation to the scheme. Furthermore, your Scheme Actuary must be reasonably satisfied that you, as trustees, in agreeing to the plan, are appropriately informed as to its implications. This requirement will normally be able to be met by your Scheme Actuary advising you to consider seeking independent legal advice in relation to the plan.

Nevertheless, trustee/employer relationships are not the only relationships which may lead to conflicts of interest for actuaries. Actuaries are expected to be continuously alert to other conflicts of interest and to consider whether there are specific features of a scheme or of the relationship between the scheme and their firm, which might increase the likelihood of a conflict of interest arising. The IFoA has published a guide for actuaries⁴ to help them identify and manage conflicts, which contains some specific questions for actuaries to consider in the pensions context.

The Actuaries' Code, along with other professional standards and information on the regulation of actuaries, may be found at

www.actuaries.org.uk/regulation/pages/regulation

3] In particular, see APS P1: Duties and Responsibilities of Members Undertaking Work In Relation To Pension Schemes: <http://www.actuaries.org.uk/regulation/pages/professional-standards-directory>

4] See: "Conflicts of Interest: A guide for actuaries" at: http://www.actuaries.org.uk/regulation/pages/conflicts_of_interest



3. Examples of what this might mean in practice

Some examples of real life scenarios which could be faced by your Scheme Actuary are given below, together with the steps, which are sometimes used to manage the conflicts of interest in these situations.

Note that the steps are only examples and may not be necessary or appropriate in all similar situations.

Example 1:

Duties to trustees and to sponsoring employer

A group of trustees has appointed Alan as their Scheme Actuary. He has recently also been asked to provide services to the scheme's sponsoring employer. These services were to provide information for publication in the employer's accounts and to assist the employer in agreeing the methodology to be used for an actuarial valuation.

Alan explained to the employer that he would not be able to advise it on the actuarial valuation methodology because the interests of the employer are likely to conflict with those of the trustees.

However, the scheme's trustees agreed that Alan and his team could provide advice to the employer in relation to accounting so long as Alan remains satisfied that the accounting assumptions are unlikely to have any material impact on the assumptions to be used for funding or for scheme factors.

These arrangements are set out in a conflicts management plan.

Example 2:

Duties to trustees and to sponsoring employer

Alan has another client in very similar circumstances to that in Example 1. However, in this case, the sponsoring employer has normally used its accounting assumptions as the basis for scheme funding negotiations.

Therefore, the trustees and Alan decided that he should not provide any advice to the employer in relation to accounting but that he can provide the results of calculations to the employer if the employer specifies the assumptions to be used.

Example 3:

Duties to trustees and to sponsoring employer

Brenda was in a similar situation to Alan in Example 1. Following discussion with the trustees, it was agreed that one of Brenda's colleagues, Colin, would provide all the services which the sponsoring employer is seeking.

The trustees and the employer have agreed a conflicts management plan, which sets out the extent to which Brenda and Colin are permitted to share information between themselves and with others in their organisation.

Example 4:

Duties to actuary's employer and to client

The trustees of the XYZ Pension Fund were encouraged by XYZ Corporation to appoint Debbie as their Scheme Actuary. Debbie's employer had just been awarded a large contract covering a variety of services to XYZ Corporation.

The trustees discussed this with Debbie, and they were both concerned that her ability to provide objective advice to the trustees could be seen to be compromised by the commercial relationship between her employer and XYZ. In the end the trustees decided to appoint a Scheme Actuary from another firm.

Example 5:

Duties to trustees of two schemes

The trustees of two pension schemes with the same sponsoring employer have both appointed Eleanor as their Scheme Actuary. Both schemes are currently undergoing actuarial valuations and the employer has told both sets of trustees that its long-term aim is to merge the schemes once their funding levels are more closely aligned.

Eleanor appreciated that she needed to exercise appropriate professional judgement and keep reviewing the potential for conflicts to arise during the course of her client engagements. She was also aware that in no way should she simply dismiss a potential conflict of interest simply because it had not yet practically arisen.

Accordingly, Eleanor discussed with both sets of trustees the conflict of interest she may face when she advised both sets of trustees if they were competing for a fixed amount of employer contributions, particularly if the employer wished to target its contributions at the less well-funded scheme.

The trustees agreed that Eleanor could remain as Scheme Actuary for both schemes. A conflicts management plan was put in place which included provisions that:

- permitted Eleanor to share information on both schemes with either set of trustees as she deemed appropriate; and
- provided for a review of the situation on an annual basis or earlier if Eleanor or any of the trustees so requested.

Example 6:

Duties to trustees of two schemes

One year after the situation described in Example 5, the employer covenant starts to deteriorate. Eleanor and the trustees become concerned that the employer may no longer be able to afford the contributions to both schemes which they feel are appropriate, and that the trustees need to consider all the options open to them.

Eleanor advises the trustees that she cannot continue to advise both schemes. The trustees agree that she is not in possession of information in relation to either scheme, which would require her to resign both appointments. They therefore agree that she will retain one appointment but that a different Scheme Actuary will be appointed for the other scheme.

4. Any comments?

The content of this guide will be kept under review and for that reason we would be pleased to receive any comments you may wish to offer on it. Any comments should be directed to:

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Or

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If you have any questions regarding the content of this note please email

conflicts@actuaries.org.uk for further information.