

CONFLICTS PENSIONS CASE STUDIES

Case Study A: Trustee/Employer conflict

You are a Scheme Actuary and you have just carried out a scheme funding valuation on assumptions agreed by the Trustees and presented initial results, which the company are copied in on. The company then asks you to use those same assumptions to calculate the impact on future service costs if the benefits are changed in some way.

This request was made without the company telling the Trustees that it was asking you to carry out this work.

Case Study A: Discussion Points and Suggested Answers

1. Who is your client? To whom do you owe duties of confidentiality and disclosure?

As the Scheme Actuary, your client is, and your statutory responsibility lies with, the Trustees. Within the context of this case study and in relation to the specific request mentioned, your client (or your firm's client) appears also to be the company, although this is not entirely clear on the facts presented.

In this scenario, if you take on the request from the company without telling the Trustees, you're in breach of your disclosure obligations to the Trustees as your client, because the request is almost certainly relevant to them and to your role in advising them as Scheme Actuary. However, if the company is also a client then informing the Trustees would be a breach of your duty of confidentiality to that client, unless you have agreed with the company a waiver of that duty. This dilemma goes to the heart of the problem of a 'conflict of interests' between two clients, and the difficulties of working for them both.

A related question to consider, even if you decline the request to act, is whether you still have to make it known to the Trustees that you have been approached by the company? The very asking of this question of you makes it clear what the company is considering, thus giving you a potential problem as regards disclosure and confidentiality. This is one of the purposes of a conflicts management plan, to make it clear at the outset that you will have a duty to share such information with the Trustees.

Please also consider the generic conflicts provisions of the Actuaries' Code, section 3: "Impartiality" and paragraphs 3.3 and 3.4 of the Institute and Faculty of Actuaries' (*IFoA*) Conflicts of Interest Guide for Actuaries (*Guide*), which reinforce and discuss the concepts of the duty to disclose relevant information to your client(s) and the relationship between the duties of confidentiality and disclosure.

2. What sections of APS P1 v 2 might be relevant here?

Section 5 and (in relation to other members of the Trustee advisory team) paragraphs 6.4 to 6.7. In particular, consider paragraph 5.3 of APS P1 v2.0 and whether this is a situation in which the presumption of an irreconcilable conflict applies. This will be so if the work falls within the definition of 'client advice' (and relates to funding or has a direct bearing on the benefits payable). On the assumption that the company is a 'client' (see 1 above), the question boils down to whether the work involves "a material element of judgement or analysis". As a general rule, the intention in drafting APS P1 was that non-trivial actuarial calculations would always involve (at least) some analysis, but it is possible that some actuaries will conclude that pure 'number-crunching' (if that is all this request amounts to) does not. If the work is considered to be 'client advice', then the Scheme Actuary may only undertake it if he or she believes that the specific circumstances, "exceptionally", warrant rebuttal of the general presumption under the provisions of 5.4 of the APS.

The requirement under paragraph 5.6 for a conflicts management plan (where anyone in the Scheme Actuary's firm is contracted to provide 'client advice' to the company in relation to the scheme) may also be relevant, with the plan specifying the work for the company that may be done and by whom it may be done, albeit that if/where work is not considered to be 'client advice' there is no explicit need for it to be covered by such a plan.

It should be noted that even if it is concluded that a course of action is not prohibited by APS P1, it may still be inappropriate to undertake it. For example, even if a request from the company is for purely arithmetical calculations to be performed, the actuary responsible may still be concerned that the provision of these numbers carries an implication that the basis on which they have been determined is or remains appropriate, and as soon as that kind of judgement is inferred any assumption that the work can be considered to be purely arithmetical becomes questionable.

3. Would your answer be different if your number 2 or a member of your team had been asked to undertake the calculation instead?

There might be a little bit more scope for the Scheme Actuary's number 2 to act. The number 2 may be able to do mechanical calculations which the Scheme Actuary would generally be banned from doing by APS P1 v2.0 (unless rebuttal of the presumption applies). Actuaries should be aware of the extension of obligations to other members of the Scheme Actuary's Trustee advisory team in section 6 of the APS. In particular, those actuaries should consider paragraphs 6.5 - 6.7, whether there is the presumption of an irreconcilable conflict and, if so, whether the circumstances might, "exceptionally", justify a rebuttal of that presumption.

The reason why APS P1 might allow more scope to the number 2 is that, under paragraph 6.5, the presumption of an irreconcilable conflict applies only where the work involves "a material element of judgement" (by that actuary) and not just "analysis". However, as under 2 above, not being prohibited by APS P1 is not necessarily the same as it being appropriate to act. Note also that the same issues about the duty of disclosure to one client and the duty of confidentiality to another client arise as for the Scheme Actuary under 1 above.

4. How would you respond to the request being made without the company telling the Trustees that you were being asked to carry out this work?

See 1 above. The Trustees, as your client, have a right to know about these requests. Tell the company that you are obliged to tell the Trustees.

5. What would your response have been as the Scheme Actuary if the company had informed the Trustees of the request and you had been asked to copy your reply to the Trustees?

This would probably address the problems about disclosure and confidentiality discussed in 1 and 4 above. However, you would still need to be satisfied that the Trustees are happy for you to provide this information (the conflicts management plan under 5.6 of APS P1 being a way of setting out pre-agreed criteria as to what the Trustees will permit you and others in your firm to do for the company). But transparency and consent do not necessarily rectify conflicts of interest and if an APS (such as 5.3 or 6.5 of APS P1) or statutory/regulatory requirement indicate that you cannot act, then you cannot act for the second party even if you have consent from the first party.

6. What would your response have been if the request had been made a year after the previous Scheme Funding valuation had been completed so that you were required to use some of your professional judgement in relation to the assumptions to be used?

In this case, the work clearly falls within the definition of 'client advice' in APS P1 (even if it had been considered that an 'immediately after the valuation' request as in the original question would not) and is therefore also a presumed irreconcilable conflict under paragraphs 5.3 and 6.5 – as such, the work could only be undertaken by the Scheme Actuary or within the Trustee advisory

team if the presumption could (“exceptionally”) be rebutted under paragraph 5.4 or 6.6. Also, as ‘client advice’, the conflicts management plan provisions of 5.6 explicitly apply.

7. Would your response be any different if the company had asked the Trustees to make the request to you, so that you respond to the Trustees and copy your reply to the company?

This procedure seems to result in reporting to your ‘Scheme Actuary’ client, i.e. the Trustees, so you can appreciate how this might be seen to make reporting easier. However, it would need to be realised that, as the Trustees are the client, your ‘best interests’ duty is to them and not to the company, which might not be readily apparent if the Trustees are just being seen as a ‘postbox’. The extent, if any, to which the company may (as a ‘non-client’) ‘rely’ on the advice should be made clear.

Case Study B: Professional and Personal Conflicts

You recently replaced a retiring colleague as Scheme Actuary to Scheme Bond. Scheme Bond is one of your firm's clients and you have worked on it for many years. Your firm also provides:

- advice to the Employer (from another office of your firm) on accounting under FRS17/IAS19. With the Employer's and Trustees' knowledge, the actual calculations are done by your team under instruction from the actuary advising the Employer. Over the last 3 years, you have signed off the calculations as consistent with the assumptions and methods specified by the Employer, making clear that you are not giving advice on the actuarial assumptions.
- administration services to the Trustees. The head of the administration division is an actuary, but does not hold a Scheme Actuary certificate.

The pension scheme is complex and it has been many years since the Trust Deed and Scheme Rules were consolidated. There are old Amending Deeds, one of which appears to require that the benefits should mirror an earlier scheme for one participating employer. During the previous actuarial valuation, you had found that in one respect administration was inconsistent with this, having not been "mirror image", and actuarial valuations have been carried out in accordance with the way the Scheme is administered.

The participating employer is large, and there would be a material impact on the actuarial valuation if the Scheme had to be administered/valued in accordance with the "mirror image" formula (to say nothing of the immense task of revisiting previous benefits paid or communicated).

During the previous valuation you had raised the issue with your predecessor Scheme Actuary and had then discussed it with senior colleagues. You had not been party to the subsequent discussion but had been told that the issue had been satisfactorily resolved without remedial action being required, after the head of the administration division had presented a paper on it to the Trustees. Although relieved, you had several residual concerns:

- the matter had not been flagged to your Legal and Compliance department as a potential claim;
- although you had seen the Trustee Minute that benefits should continue to be administered as per the prevailing practice, you had not seen the paper to the Trustees, and the Trustee Minute of the matter was short on detail;
- so far as you know, the Trustees took no legal advice. They rely heavily on your firm, and would almost certainly have been swayed by the way in which your colleague had presented the issue; and
- the matter had not been raised with the Employer nor brought to the attention of your colleagues who advise the Principal Employer in connection with FRS17/IAS19 and other matters.

However, due to pressures of work you had not pursued any of these points at that time. An actuarial valuation has fallen due; the first you will be carrying out as Scheme Actuary for Scheme Bond.

Case Study B: Discussion Points and Suggested Answers

1. What areas of APS P1 v2 and the Actuaries' Code are relevant?

Just about every section of both the Code and the APS is potentially relevant.

Principle 3 of the Code, "Impartiality" is clearly relevant. Members must always look to the conflicts provisions in the Code first before looking at the more specific guidance in Actuarial Profession Standards. In this scenario there are potential conflicts between the actuary himself and both his client and his employer as well as potentially between clients. Principle 1 "Integrity" will also be relevant to how the actuary deals with the challenges of the situation.

Principle 4 "Compliance" becomes relevant if the new Scheme Actuary uncovers what appears to be unprofessional behaviour by other actuaries.

Principles 2 and 5, "Competence and Care" and "Open Communication", may also be relevant: you need to be proactive and discuss matters which might affect your advice with the Trustees, rather than just waiting for them to come to you with concerns.

As for APS P1 v2.0, sections 1 and 2 are of course always relevant to Scheme Actuary appointments and section 3 (handover of Scheme Actuary appointment provisions), paragraphs 4.1 to 4.3 (Scheme Actuary informing the Trustees on becoming aware of matters which might lead to the Trustees needing to request advice, and Scheme Actuary raising concerns and taking appropriate action if trustees fail to act on advice or otherwise appear to be acting inappropriately), and section 5 (potential conflicts between Trustees and Employer as clients) are also relevant.

2. What issues arise for you as the Scheme Actuary given your previous work on the calculations for the Employer?

Regardless of the possible historical problem with benefit calculations, you would need to consider whether your previous involvement in work for the employer might affect your ability to take on the Scheme Actuary role without giving rise to some irreconcilable conflict. In principle, in the circumstances described, accepting this appointment would probably be ok but you would need to be clear as regards the information you possess from the role you played with the employer previously and how that might impact on this new appointment.

If you are personally continuing to do any work for the employer, for example still preparing the accounting numbers, it needs to be clear that the Trustees are now your principal client and that you cannot provide numbers to the employer without their consent. Your own involvement with the employer, along with the nature of all 'client advice' in relation to the scheme provided to the employer by other members in your firm, would need to be disclosed and documented in your Conflicts Management Plan, including the procedures to be followed in the event of an actual conflict of interest arising. (Any Conflicts Management Plan drawn up by the previous Scheme Actuary would need to be suitably amended and in effect replaced by your Plan.)

Special issues could also arise in this case as a result of the possible historical problem with benefit calculations. You have clearly had some involvement in the past and may now be worried about issues concerning "numbers" that you have previously signed off on. As the new Scheme Actuary, you will be in a heightened position of responsibility to your client and this may create a conflict with your own interests regarding that previous involvement. Concerns in this area may be increased by a feeling that you were remiss in not taking your earlier concerns further at the time (or before agreeing to take on the Scheme Actuary appointment now).

3. What issues arise in relation to the other two actuaries identified above i.e. the:

- a. The previous Scheme Actuary**
- b. The Head of the Administration Division**

While it might originally have been acceptable for you to accept the assurances given by or on behalf of the previous Scheme Actuary and the Head of the Administration Division that the benefit uncertainty issue had been satisfactorily resolved, as the new Scheme Actuary you now are under a heightened duty to be satisfied that the scheme is being properly run in accordance with its rules and if you continue to have doubts in this regard you will need to ask further probing questions about the decisions made by the previous Scheme Actuary and the Head of the Administration Division. Ultimately, if after these investigations you believe that either of these two actuaries has covered up (whether deliberately or inadvertently) potential problem issues relating to the scheme benefits in an unprofessional manner, then you have a duty under 4.4 of the Actuaries' Code to report the matter for consideration under the relevant disciplinary scheme of the IFoA.

4. What action should you take as the Scheme Actuary and why?

You are very likely to need additional information: perhaps obtain some relevant minutes/look at the audit trail/any other relevant documents which your colleagues might have and which might shed some light on matters.

You could talk to your compliance team, to any in-house legal team or senior colleagues who might be able to assist first rather than setting hares running with the Trustees without collating the relevant background and evidence first. Perhaps you have a colleague who you feel has a great deal of integrity: maybe you could ask their advice?

Is there a handling issue here too? You may have a personal conflict here: you don't want to upset your boss unnecessarily so perhaps you could consider whether you have any internal mechanisms within your firm to raise your concerns or whether you might seek guidance from the IFoA's confidential Professional Support Service. You may also be in the position of having to challenge your own client, the Trustees, if you do not think they have taken the correct course of action.

You could also consider taking independent legal advice, recognising that you might have a conflict with members of your own firm. It is your independent, professional judgement which is relevant here and you should be prepared to stand your ground with your firm and seek independent advice.

Perhaps you could also consider the issue in some other ways to try and look at it more objectively:

- (a) If your predecessor was from another firm, what would you do?
- (b) How would it look if you proceeded with your chosen course of action if it ended up on the front page of a national tabloid?
- (c) Look at the engagement as if you were coming to it afresh and without the background history?

Ultimately, you have a professional responsibility not to turn a blind eye and will need to carry out some investigations and if necessary take some further action.

5. Is there a way forward which is consistent with the Actuaries' Code which could minimise any adverse consequences to you and your firm?

This clearly depends on the circumstances, but the key here is to try to do as much information-gathering as possible without setting unnecessary hares running. Your firm is likely to have policies regarding how potential claims are handled and you should adhere to these unless there is a conflict with your professional or legal responsibilities (and if you think there is, you would be well-advised to seek independent advice before deciding what to do). Ultimately, however, your responsibilities to your firm will not be able to take precedence over your responsibilities to the Trustees and to act professionally.

6. If you did decide you could not proceed with the actuarial valuation without raising your concerns about the interpretation of the Amending Deed, how would you present the issue to the Trustees?

Again, this will depend on the precise circumstances but the key is likely to be disclosure – being upfront about matters and discussing the available ways of managing the problem with the Trustees.

You will need to be mindful of the possibility that the Trustees may not want to re-open the issue, whether because they are fully convinced that there is no problem or because they are concerned at the potential costs involved in addressing any problem.

You will want to listen to any reasons the Trustees may have for wanting to take no further action (these may even include having obtained legal advice on the matter of which you were previously unaware!) but you will need to remain mindful of your obligations to speak up to them where necessary under section 4 of APS P1.