

# Lay trustees in the 21st Century



## The 21st Century Trustee

Since the publication of Pensions Regulator research in October last year highlighting gaps in trustee knowledge and understanding (TKU)<sup>1</sup> the regulator has made it a priority to raise trustee standards.

Lesley Titcomb, Chief Executive of the regulator, announced the need for “more capable, competent 21st century trustees”. While the term “21st century trustee” has quickly entered the pensions lexicon, its meaning is still evolving.

Initially there was some speculation that the regulator was questioning the continued appropriateness of the concept of member-nominated trustees (MNTs). This suggestion was quickly dispelled, with Titcomb correctly pointing out that the MNT regime is enshrined in primary legislation, and not a policy matter for the regulator. The regulator’s aim is to ensure that all trustees are better equipped for their role.

The requirement that trustees should, by a combination of their own skill and experience and the skill and experience of their professional advisers, be fit to undertake their duties appropriately is not a 21st century idea. What has changed are the demands placed on pension scheme trustees: longevity hedging transactions, technically challenging investment strategies, and high pressure pre-pack insolvencies, to name but a few.

Hetal Kotecha, a professional trustee and a director at Independent Trustee Services, believes the regulator is right to address these skill and training issues, but is quick to point out that suitability for trusteeship is not the preserve of professional trustees:

“The regulator is rightly focused on the challenge of 21st century trusteeship. Governing and managing a pension scheme in 2016 is a complex business requiring increasingly sophisticated boardroom skills on the part of trustees, but these skills are not possessed exclusively by professional trustees.”

## The value of lay trustees

It is clearly important that scheme members feel that their interests are being represented, that they trust those in charge of doing so, and that the process of managing their pension scheme is transparent. According to Kotecha, this is an important function of lay trustees, but is by no means the only benefit that lay trustees bring to trustee boards:

“The role of lay trustees is often defended on the grounds that they bring a connection to the membership and are closer to their needs, and I think this is perfectly true. It is really only employed trustees who can bring and embed something of the scheme sponsor’s organisational culture into the heart of the running of what, after all, is the

sponsor’s pension scheme. However, this point around representation is too often focused on the benefits brought to member communication, but the influence of effective lay trustees spans a wider range of areas, contributing to the overall effectiveness of the trustee board.”

Kotecha makes a valuable point; to conclude that MNTs serve principally to give members a sense of representation would be reductive: they can also provide valuable experience and knowledge of the employer and the employer covenant; they have an existing relationship with the employer that can prove beneficial during negotiations; and they are often able to provide a much-needed ‘common sense’ approach to trustee decision-making, or an approach to trusteeship that benefits from skills and experience gained in the ‘day job’.

## Creeping towards professionalisation?

Despite the regulator’s support for MNTs, current legislation requiring their appointment, and our perception that MNTs retain widespread support within the pensions industry, is their role under threat in the longer term? Is there likely to be tension between the MNT requirements and other legal developments? Or will the regulator’s push to improve standards of governance mean that it becomes increasingly likely that those trustees making the grade (in the regulator’s mind) will be professional trustees? More prosaically, will commercial pressures lead to the increasing use of a sole professional trustee or fully professional trustee boards?

## Legal developments

The original text of the IORP II Directive proposed by the European Commission would have required all trustees to have adequate professional qualifications. However, with both the European Council and the Committee on Economic and Monetary Affairs of the European Parliament favouring amendments removing the need for professional qualifications, allowing the trustees of a scheme to demonstrate that collectively they have appropriate qualifications, the threat initially posed to the UK system of trusteeship by IORP II appears to be receding.

But the initial Commission proposal may represent the long-term direction of EU thinking. The European Insurance and Occupational Pensions Authority (EIOPA) recommended to the Commission that the fit and proper requirements applying to those running insurance and reinsurance undertakings, which include requirements for professional qualifications, are suitable for application to IORPs, and so it would not be surprising if this idea is resurrected in the future. ►



Dan Naylor  
Partner  
Travers Smith LLP



Alex White  
Associate  
Travers Smith LLP

---

<sup>1</sup> Research published in October 2015 revealed that 51% of schemes which had non-professional trustees believed that not all trustees met the standards in the regulator’s trustee knowledge and understanding code, and 5% of schemes admitted that none of their trustees met these standards

Further reservation of specific roles for trustee chairs could start to generate the sense of a two-tier system of trusteeship, and arguably start to erode a fundamental principle of the MNT legislation, which is that MNTs should not be excluded from functions exercisable by the other trustees

Domestically, the Occupational Pension Schemes (Charges and Governance) Regulations 2015 recently introduced a requirement for an annual governance statement signed by the chair of trustees of schemes with defined contribution (DC) benefits. In a potentially interesting development for pension scheme trusteeship, a specific trustee – rather than the board as a whole – has been required to take responsibility for a particular task. The Government's thinking seems to have been that requiring a named trustee to sign the governance statement would ensure that at least one member of the board is sufficiently focused on DC governance; the perception of policymakers appearing to be that trustees, in particular trustees of hybrid schemes, do not give DC issues the time and energy they deserve.

It will be interesting to see if this idea of trustee chair responsibility finds its way into more pensions legislation. Not all trustee chairs are professional trustees, of course, but on those boards that do have a professional trustee, that person is, in our experience, far more likely than not to be the chair of trustees. Further reservation of specific roles for trustee chairs could start to generate the sense of a two-tier system of trusteeship, and arguably start to erode a fundamental principle of the MNT legislation, which is that MNTs should not be excluded from functions exercisable by the other trustees.

### Training

The regulator has recently revamped its 'Trustee Toolkit' training software by introducing a function which assists trustees with identifying gaps in their knowledge, and has also published for consultation user-friendly DC 'how-to' guides. For the time being there is still no suggestion that the regulator would like to impose objective standards on trustees, and we believe this maintains the right balance. Training requirements should not be allowed to become so onerous as to require trustees to become experts – this has never been a legal requirement of trusteeship; trustees need sufficient knowledge to understand when and where to seek professional advice.

### Commercial pressures

In our experience there is an ongoing trend for reducing the numbers serving on trustee boards. Sometimes this is for perceived governance advantages, but often the reason is more pragmatic; either the employer or membership cannot provide the requisite number of willing trustees. On the employer side, if a scheme is closed to new entrants

and accrual the employer might simply want to minimise management time committed to the scheme – but will often want to maintain a particular ratio of employer trustees to MNTs. The use of professional trustees is often seen as a potential solution to these sorts of pressures, with the added advantages of addressing conflict issues more commonly faced by employer trustees.

### Closing observations

We hope that policymakers take care to ensure that legislation does not unduly increase the pressures on lay trustees; the duties of trusteeship are inherently onerous without additional prescription. It is also hoped that care is taken to ensure that future legislation does not inadvertently lead to the development of a two-tier trustee system that could have the effect of devaluing the contribution made by MNTs. If there are concerns about trustee standards, amongst MNTs or more generally, then educational support is the answer, and not the replacement of, or marginalisation of, lay trustees.

It is our view that MNTs (and other lay trustees) can bring a huge amount to trustee boards and the trustee decision-making process, and that with appropriate support and professional advice the majority of lay trustees are capable of exercising their duties properly in even the most complex or stressful situations. But there will be some schemes where the appointment of a professional trustee to act alongside lay trustees is critical to a board's effectiveness, and other circumstances where a sole professional trustee or entirely professional trustee board would be appropriate. The key consideration should always be whether or not a scheme's trusteeship arrangements are effective to safeguard members interests. ■

### KEY MESSAGES

- MNTs can be '21st century trustees'
- There may be pressure in the future for trustees to have professional qualifications
- New regulations set a potentially unhelpful precedent for chair specific trustee tasks
- New training resources are welcome provided they do not in themselves represent a barrier to lay trustees
- Policy makers should take care not to marginalise lay trustees
- The key consideration should always be trustee effectiveness