PENSIONS IN 30 PODCASTS

29 Conflicts of interest and pension scheme trustees

Key points

- Trustees cannot act lawfully when unduly influenced by a conflict of interest;
- A conflict of interest can impact on the validity of a trustee decision and on the management of the pension scheme;
- The Pensions Regulator has issued guidance around conflicts of interest;
- Trustees need to understand, identify and manage conflicts of interest including adviser conflicts;
- Trustees should adopt a conflicts of interest policy;
- A conflict can arise in relation to confidential information; and
- Separate Companies Act 2006 requirements apply to trustee directors.

Main sources

- The Pensions Regulator Guidance "Conflicts of Interest" issued October 2008.
- The Pensions Regulator Code of Practice "Trustee knowledge and understanding" in force November 2009.

General Principle

Trustees of pension schemes cannot act lawfully when unduly influenced by a conflict of interest. There are some inherent conflicts in being a trustee which can be managed as long as they do not infect the decision making process. Conflicts of interest are likely to be of two main types:

- Conflicts between the personal interests of a trustee, director or staff member and his duty to the beneficiaries of the pension scheme (for example, the possibility of financial gain); or
- Conflicts between the duty owed by the trustee, director or staff member to the beneficiaries of the scheme and his fiduciary duty owed to other persons (for example, as an officer of the employer or as a trustee of another trust).

Conflicts of interest may be classified as either real conflicts or potential conflicts.

Impact of conflict of interests

The impact of conflict of interests can be considered as follows:

- **Decision** - A decision which is infected with an actual conflict of interest has serious legal consequences. The decision may be invalidated (or restrained) without any proof that a trustee has been (or will be) swayed by improper or irrelevant considerations as a result of the conflict. This may have a serious impact in terms of costs and administrative work, for example, if the decision is part of a high value transaction. In certain situations acting in conflict could result in the personal liability of the trustee in question;

- **Scheme management** – acting in conflict of interest impacts on the way in which the pension scheme is managed. This could result in a practice of poor governance such as inhibited discussions amongst the trustees and/or employer. It could lead to a breach of duty to act in the best interests of the scheme beneficiaries, or in a trustee failing to properly consider a decision; and

- **Perception** – where there is no actual conflict but there is a perception that trustees have not acted properly can be damaging to a scheme. The membership may lose confidence in the trustees and their ability to run the scheme. There may be wider reputational damage (to both the pension scheme and the employer) even if the trustees have not done anything wrong.

Considering Conflicts of Interest

The Pensions Regulator has issued Guidance to provide educational support to trustees with a view to sharing good practice and raising standards around conflicts of interest. The Pensions Regulator Guidance sets out the key principles which govern sound conflict management and governance. The key principles are:

- Understanding the importance of conflicts of interest;
- Identifying conflicts of interest;
- Management or avoidance of conflicts;
- Managing adviser conflicts; and
- Conflicts of interest policy.

Understanding the importance of conflicts of interest

Trustees must:

- be aware of their fiduciary obligations to beneficiaries, the requirement to exercise independent judgement and be perceived as doing so;
- have a clear understanding of the circumstances in which they may find themselves in a position of conflict;
- recognise that there are legal complexities in the area of conflicts of interest and should seek legal advice as necessary.

Identifying Conflicts of Interest

It is the trustee or trustee director's responsibility to:

- identify and consider any conflicts that may arise in the future and notify the other trustees as soon as practicably possible; and
- identify and consider any conflicts which have arisen and notify the other trustees as soon as practicably possible.

Introducing a process for identifying conflicts is pivotal to the management process. For example by maintaining an up to date register of each trustee's interests and have a means of recording conflicts that have arisen or are likely to arise.

Trustees who take the time to identify any conflicts are better placed to manage conflict situations that arise.

Management or avoidance of conflicts

When a conflict has been identified, trustees should manage the conflict of interest by:

- implementing procedures for managing conflicts that have been identified: this could include the withdrawal of the conflicted trustee from discussions and the decision making process, establishing a sub-committee (this is particularly common in relation to scheme funding decisions), appointing an independent trustee. In the case of an acute conflict which cannot be managed the trustee could resign.

- detailing in the minutes of the meeting conflicts which may arise during a decision making process and record the action to manage the conflict – it is important that this is a recurring item at every trustee meeting as standard. Where a particular agenda item gives rise to a higher risk conflict more detail should be set out in the minutes as to how this will be managed. The methods of managing the conflict should be checked to see that it is consistent with the current conflicts policy (see below), if not, reasons need to be given and if necessary the conflicts policy should be updated. It is important that there is detailed paper trail in place so that if a decision is ever challenged in the future on the grounds of a conflict, the decision making process is properly documented;

- obtaining legal advice for non-trivial conflicts – where the conflict is identified as being potentially detrimental to the decision making process, legal advice will assist the trustees in identifying how the decisions could be impacted by conflicts and finding appropriate ways to manage them.

Managing Adviser Conflicts

Trustees need to ensure that adviser conflicts are managed. Trustees should:

- actively manage their relations with advisers to ensure advisers are able to provide independent advice;

- require advisers to declare any conflicts that may arise; and

- evaluate the conflict if one arises and determine a course of action.

Conflicts policy

It is good practice for trustees to adopt a conflicts of interest policy for identifying, monitoring and managing all conflicts of interest. The Pensions Regulator now expects to see a conflicts policy in place and any trustees without one in place would potentially find themselves in difficulty with The Pensions Regulator if this were to ever be investigated.

A conflicts policy assists trustees so that when a conflict potentially or actually does arise there is an agreed set of procedures in place to manage them.

The conflicts policy needs to be regularly updated and monitored. It needs to be considered and reviewed to ensure that it is still relevant to the circumstances of the trustees. The trustees must ensure they are conversant with the procedures it contains.

Confidential Information

A conflict of interest can arise when a trustee has information relevant to the pension scheme that conflicts with his duty to share the information with his fellow trustees because of a duty of confidentiality to somebody else. This is typically seen when a trustee is also an employee of the employer and owes a confidentiality duty to the employer. For example, confidentiality issues may arise in relation to a corporate transaction or a proposal to close the pension scheme.

Confidentiality conflicts are particularly difficult to manage. This is because withdrawing from discussions and decision making does not necessarily absolve the trustee from their duty to disclose information to their fellow trustees.

The easiest method to address a confidentiality conflict is for the employer to waiver the confidentiality requirement, although the employer may not always be willing to do so. Alternatively the trustees may be able to enter into a deed of amendment to waive the trustee from their duty to disclose information to the rest of the trustees. In other circumstances a confidentiality agreement may be appropriate.

As this is notoriously a difficult area, trustees should seek legal advice to ensure confidentiality issues are appropriately managed.

Companies Act 2006 Requirements

The Companies Act 2006 has separate additional requirements for directors of corporate trustees. This is set out in section 175 Companies Act 2006 which requires directors of a company to:

"avoid a situation in which they have, or can have a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company".

Any director of a corporate trustee needs to consider the Companies Act 2006 requirements together with the obligations set out in this note.

More information

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