

The Pensions Research Accountants Group is grateful for the opportunity to respond to the Review of Pensions Institutions consultation paper "Emerging Issues" issued on 7 March 2007. A brief statement of the purpose and history of PRAG is appended to help set the context in which our response is made. The short period available for consultation means that PRAG, as an entirely volunteer member-based organisation, is not in a position to submit a comprehensive response, but we trust our brief comments will nevertheless be useful.

First of all, we need to make it clear that PRAG's attempts to consult with its members on this topic did not generate a huge volume of responses. Conversations with individual members lead us to conclude that this is not a sign of lack of interest, rather a sign that there is no urgent recognition of any need for significant change in the structure of pensions institutions - at least, not at the present moment when the two main institutions created by the Pensions Act 2004, that is, the Pensions Regulator and the Pension Protection Fund, are only 2 years old and just now moving into a more mature phase of operation. tPR has had the advantage of building on the foundations of its predecessor, OPRA, but PRAG's clear view is that radical change to the structure of the Pension Protection Fund at this early point in its development can only present risks to the achievement of the vitally important functions delegated to it by the Pensions Act 2004. Some members expressed puzzlement as to why a structure created in 2004, which is generally agreed to be fit for purpose in terms of its clear segregation of duties between tPR and PPF, should be subject to such an early review. Even OPRA was allowed 5 years of full operation before a quinquennial review was carried out.

There did seem to be consensus among PRAG members that the structure set up under the Pensions Act 2004 was inherently robust. There was a recognition that most mature financial services industries have developed 3 distinct areas of responsibility in the space between providers and consumers:

Regulation - to mitigate the risk of things going wrong

Dispute resolution - to find out whether things really have gone wrong, and decide what to do about it

Compensation - to put things right when they really have gone wrong

In the pensions savings environment, there may well be the opportunity to consider some vertical integration within those three functions - for example, it is worth examining whether the differences between personal and work-based savings, or trust-based and contract-based savings, are crucial to the regulatory function, where the product (a money-purchase arrangement that delivers a fund with which to buy an annuity, for example) is essentially identical. Similarly, one could see the regulatory processes of assessing the solvency of insurance companies as not radically different from those of assessing the solvency of occupational pension schemes. It might therefore be cost-effective to contain these similar functions within one regulatory body.

Members saw however little justification for considering horizontal integration between the three areas of responsibility. Some cost savings may be achieved, but at what price? The need for compensation can be attributed at least in part or in some instances to regulatory failure; a regulator that controls the compensation function is at the very least open to the charge of being able to cover up its own failures. Where a regulator controls a compensation fund, it gains direct and

potentially market-moving power over investment markets, and through its own investment strategy, indirectly influence the strategy of other market participants. This appears inherently incompatible with a regulatory function which is independent and transparent - at the extreme, if a pension scheme fails and has followed the regulator's investment strategy for its own compensation fund, the moral pressure on the body that set up the regulator in that way (i.e. the Government!) to bail the scheme out of its investment failure would be intense.

Members agreed that the idea of reviewing the boundaries between institutions and agencies involved in the pensions industry must be a good one - ensuring there are no yawning gaps or expensive overlaps between the institutions is just part of responsible governance. However, the effectiveness of the institutions should not be sacrificed simply for organisational convenience or minor cost savings - and "effectiveness" has to include maintaining independence, supporting fairness and transparency, mitigating conflicts of interest in managing the relationships between providers and consumers. It is at the present moment far too early to conclude that the structure established in 2004 is in any way ineffective - in fact, all the early evidence is completely in the other direction, that the transparent segregation of duties between tPR, PPF and the dispute resolution functions is a source of strength. Removing this source of assurance to scheme trustees and scheme beneficiaries for the sake of having to process one levy invoice instead of two seems fundamentally misguided.

#### Appendix:

The Group was formed in 1976 by a group of professionals with an interest in the preparation and communication of financial information relating to pension schemes with the objectives of "carrying out research into and encouraging the advancement of knowledge and the development of best practice relating to pension schemes and in particular the reporting and accounting by such schemes." It was involved in the publication in 1986 by the Accounting Standards Committee of the first Statement of Recommended Practice No. 1 for pension scheme financial statements, and has been continuously active in issuing a significant number of publications on many aspects of pension scheme accounting, financial operations, investment management, tax, internal audit and internal control.

In 1996, PRAG was recognised by the Accounting Standards Board as the SORP-making body for the financial statements of pension schemes. In recognition of this responsibility, the Group (formerly constituted as a "Club or Society") incorporated as a company limited by guarantee. This change of legal form has had little impact on PRAG's character or working practices however, and it remains a member-oriented organisation and carrying out all of its work on a volunteer basis. PRAG issued its first SORP in 1996 and a revision in 2002. A second revision is currently being consulted on using the Exposure Draft process required under the ASB's Code of Conduct for SORP making bodies. The SORP has what is sometimes described as quasi-legal status, as it is referred to in the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 (generally referred to as the Audited Accounts Regulations). These

regulations require schemes to comply with the SORP when preparing their accounts or describe and justify non-compliance. PRAG also makes annual public awards for scheme Summary Reports, recognising that this is the most frequent way that trustees communicate financial information to their members.

PRAG currently has around 400 members drawn from professionals working in pension scheme management, accounting, audit, trusteeship, investment management, pensions law, actuarial science and scheme administration. It holds two general meetings a year and operates a range of other member services, largely now through its website. The Group generally uses the "working party" method of working, for example to develop new publications, and has no full-time secretariat or technical drafting resources to contribute to this work. PRAG raises its income largely from member subscriptions, which are traditionally set at a very low level (currently £30 per annum); membership is personal to the member - PRAG has never had any corporate members nor any other corporate sources of income through sponsorships or similar arrangements.