



An tÚdarás Pinsean  
The Pensions Authority

# **SYNOPSIS OF RESPONSES TO THE PENSIONS AUTHORITY CONSULTATION ON DRAFT CODES OF GOVERNANCE FOR DC SCHEMES**

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## **Introduction**

The Pensions Authority published a consultation paper on draft codes of governance for DC schemes on 30 April 2015. The draft codes set out standards of conduct and practice which the Authority expects from all DC trustees. The improvement of trustee standards of governance forms part of the Authority's overall proposals for DC reform as indicated in its wider consultation on this matter in late 2013. The paper set out specific questions on the draft codes to which the Authority sought responses by 16 June 2015.

The Authority received a total of thirteen written submissions in response to the consultation, two of which came from individuals and eleven from organisations/professional advisers. The consultation paper posed four main questions and an invitation to offer other relevant comments. The responses summarised below reflect the main points made and a range of suggestions offered on how the draft codes could be improved.

This document is a synopsis of the responses received by the Authority and does not cover every point made. No definitive conclusions have been made at this point and the next stage of this process will involve a detailed consideration of all of the points made which will further inform the Authority's views on the appropriate revisions to be made to the codes.

## **Synopsis of responses**

### ***Question 1 – Are there any issues not covered in the codes at this point which you think should be?***

Many constructive comments and suggestions were offered in response to this question with some issues being mentioned repeatedly, most notably the following:

- *Contribution and benefit adequacy* – It was suggested that there should be more emphasis on this issue, most likely within the code on communications, and the implications of low contributions and small funds. It was considered that a key question for trustees should be whether all members are maximising the contributions available from employers and, if not, why not? Trustees should be encouraged to focus heavily on ensuring that members understand the direct link between their contribution levels and their benefit outcomes, and on explaining clearly to members that increased contributions are generally required to reach typical standard of living expectations in retirement.

- *Member support and financial advice* – This was considered to be an important issue. The point made was that trustees need guidance in relation to the provision of financial advice as trustees are reluctant to be seen to be involved in the advisory space. There is too much emphasis put on the provision by trustees of “neutral” information and not enough on member support. Trustees should therefore be encouraged to recommend (and, where possible, facilitate with employer support) the use of financial advice. This should be reflected in the codes, preferably in a separate code, and broadened to other situations where members need to make critical and complex decisions, especially at the point of retirement. This would involve details around communication to the individual members at appropriate intervals before retirement, providing access to independent financial advice or at least providing details of recommended financial advisers.
- *Member nominated trustees* – The issue of member nominated trustee regulations/informal arrangements in relation to appointment of member trustees should be covered in the codes. It was considered that a well-governed scheme should include a process whereby these issues can be monitored notwithstanding changing trustees, advisers and employers.
- *Trustee training* – It was suggested that guidance on a trustee’s duty to maintain their knowledge/skills and undergo trustee training would be useful for new trustees plus guidance for new trustees on how to get up to speed with their role.
- *Deferred member management* – This is an area which was merited to warrant a code in its own right in which the PA would clearly underline that trustees have continuing responsibilities to deferred members. The code could cover items such as:
  - Maintaining contact;
  - Whether different expense charges should apply;
  - Options for transferring out.
- *Data protection obligations* – While it was noted that this issue is covered somewhat in code 7 (record keeping) it does not address key data protection issues such as what the information can be used for or how consent to the use of the information might be obtained. It was suggested that trustees be directed to the Office of the Data Protection Commissioner (ODPC) for guidance on the data protection guidelines. It was also suggested that this issue might merit a code in its own right.
- *Impact on small schemes* – There were views expressed that for schemes with less than 100 members, who are typically small companies with limited

resources, the codes will place undue administrative burden and costs which will make small companies think twice about setting up a DC scheme. It was suggested that a less detailed and burdensome code for small companies would be desirable or that smaller schemes be given an option of delegating compliance with certain codes to a provider.

- *1 member arrangements* – The practicality of the codes for these arrangements was questioned as it was considered that the interests of the trustees and member in such schemes are already well aligned with the member in the majority of cases being a trustee. Therefore, it was suggested that certain adjustments should be made for 1 member schemes to ensure the codes can be implemented in a more practical and workable manner for these arrangements.
- *Statement of Vision/Strategy* – It was suggested that the governance framework set out in the codes include a code requiring a Statement of Vision/Strategy for the scheme which would clearly state that the people making decisions for the scheme do so in order to serve the best interests of the members of the scheme. This positive statement would then provide an anchor/context for the rest of the codes.

***Question 2 – Does the level of guidance included in the codes provide sufficient details to assist trustees in the effective governance of their schemes?***

There was mixed responses in answer to this question varying from generally speaking “yes” subject to specific points of detail made, to “no” as it was considered that too many of the requirements are vague and it would be difficult for trustees to know how they can measure those. It was suggested that the codes would assist trustees more if they were more specific and that it would be useful, for example, if the Authority provided more detail, practical guidance and worked examples about how it envisages the codes working. Model documents corresponding to various aspects of the codes especially in relation to areas of risk management, conflicts of interest and value for money (where the underlying compliance requirements are not particularly well set out) would be much welcomed whether contained within the codes or separately published and cross-referred to in the codes.

### ***Question 3 – Do the codes contain enough practical guidance on the standards and competence that the Authority expects from DC trustees?***

Again, there was mixed responses to this question with a running theme concerning the need for more practical examples of how trustees can comply with the codes. There was a view that it may be preferable to have a modified compliance regime applying to smaller schemes. An alternative approach to a modified compliance regime (recognising that smaller entities should not have less governance/protection) is to provide ability for trustee groups to document why full compliance is not possible. In that regard, it was suggested that the Authority might consider “this sort of comply or explain” pragmatic approach when formulating its policy on the proposed “annual compliance return.”

There was a suggestion that each scheme should have terms of reference for its board which sets out (a) the minimum competencies and probity for individual trustees, and (b) the additional competencies which should be recognised for the trustee board as a whole. Coupled with this, there should be a requirement to assess board effectiveness on an annual basis and maintain a continuous training and improvement agenda.

Another view expressed was that until the codes are in place for a period of time it is not possible to fully ascertain if any further guidance is needed. Therefore, a review period of 1 year should be put in place with a feedback process to allow trustees to let the Authority know of any issues that have arisen with the practical implementation of the codes.

### ***Question 4 – Have you suggestions on how we could improve the codes?***

There were numerous comments on the various codes and how they could be improved with some suggestions concerning specific points of detail which can be synthesised as follows:

#### **In code 1 – Establish a governance plan of action**

- This code should be linked with establishing objectives for the scheme.
- Specify details of trustee training requirements and level of trustee knowledge required.
- The proposed action to document who is responsible for all elements of the scheme should be expanded further to require that a clear organisation structure, which specifies the roles and responsibilities of each of the individuals/service providers, be drawn up. This will ensure a system of accountability with appropriate oversight/feedback etc. Include as an action in

DC code 1 that trustees should establish a forward agenda of standing items and cyclical reviews, designed to ensure that all responsibilities are monitored at an appropriate frequency during the financial year.

- Trustees should be encouraged to establish and maintain a master file or repository of scheme documentation, policy documentation, meeting minutes and member booklets.

### **In code 2 – Risk Management**

- The introduction refers to “reasonable” level of member benefits without any reference to what could be considered reasonable – this needs clarification.
- Examples of actual risks should be included.
- Incorporate (a) a controls improvement agenda with clear deliverables and outcomes and (b) a controls effectiveness reporting process.
- A standard risk management document would be helpful to trustees in enabling them to ensure appropriate attention is paid to various areas of risk and mitigation processes are put in place.

### **In code 3 – Conflicts of interest**

- Expand to provide an indication of how conflict could arise, and in particular, where there is a situation where trustee, administrator and advisor are owned/controlled by same entity.
- Include an action for trustees to take steps to ascertain whether their trust deed contains a provision permitting them to act notwithstanding a conflict of interest and understand how broadly applicable such a provision is to their circumstances. In addition, the code should expressly address the important related trustee obligation to disclose information to their co-trustees which is relevant to their decision-making.
- A conflicts register should be produced and any new conflicts declared at the beginning of each meeting.
- Where conflicts exist because trustees owe duties to two competing principals (e.g. to their employer or a trade union and beneficiaries), the other principal to whom they owe duties should be asked to expressly acknowledge that the individual’s duty as a trustee shall take precedence over any legal duties they owe to the other individual. This is deemed necessary for the protection of the individual in question and the beneficiaries under the scheme.
- Trustees should also be aware of and actively monitor any conflicts of interest their advisers may have and, where appropriate, ask to see a conflicts protocol.
- There is a risk that trustees might be given the impression that recording and monitoring the conflict is sufficient to discharge their legal duties when it may not be. Suggest additional guidance is included requiring individual trustees to subject to a conflict to assess if the conflict is such that they cannot in good faith

act independently in beneficiaries' best interests and this may require independent legal advice.

- It would be useful if a conflicts of interest policy standard could be made available.

#### **In code 4 – Trustee Meetings**

- Replace words “hear reports from investment managers” with recommendation “to review investment performance” as the focus should be effective oversight of the investment arrangements.
- Quarterly trustee meetings may be appropriate for larger schemes. However, this may not be the case for all schemes and perhaps certain operational matters could be better dealt with at sub-committee level, thus freeing up trustee meetings (held on a less frequent basis) to focus on more strategic matters. Smaller schemes could formally meet less frequently, but should receive quarterly administration and investment reports so they can convene “ad hoc” meetings if necessary.
- Code should specify number of trustee meetings based on scheme asset size.
- Code should reference the fact that corporate trustees will need to check their Memorandum of Association/Constitution to ensure trustee meetings are conducted in accordance with those requirements as well as what is set out in the their trust deed and rules.

#### **In code 5 – Collection and remittance of contributions**

- The suggestion “to prepare, maintain and revise if necessary a scheme payment schedule showing...” could be replaced with a broader recommendation to ensure that appropriate arrangements are put in place to ensure the timely remittance of contributions.
- The code places a lot of burden on the trustees who may not know in every instance that members' correct contribution rates and salaries have been applied to verify the correct contributions are paid on a monthly basis. It is suggested perhaps this burden should be placed on the employer to ensure that all contributions are paid across monthly within the statutory timescales.
- The question was raised whether trustees need to be provided with members individual investment strategies versus how the money was invested on a member level in order to ensure that contributions are being invested in the correct manner?
- Another question asked was where does the employers' role end and the trustees' role begin? Is it the trustees' role to ensure that the calculation of the employees' contributions has been performed correctly by the employers' payroll or simply for the trustees to accept what is remitted by the employer is correct? If the trustees are accountable for the calculation of the deductions, then how is this to be carried out?



- It was pointed out that many DC schemes have different levels of contributions where the employer's contribution can be increased if the members choose a higher member contribution. The need to ensure that the correct level of contributions has been recorded and are being paid should be in this code.
- This code should encourage periodic meetings between payroll administrators and scheme administrators to ensure alignment. In practice, this is where administrative issues can arise in terms of, for instance, scheme administrators operating off out-of-date payroll data or misunderstanding what salary basis is being used for death-in service-benefits.

### **In code 6 – Calculating and paying benefits**

- Trustees' attention should be drawn to the need to ensure appropriate insurance of life assurance benefits and robust processes in relation to medical underwriting where required.
- The code as currently worded is more relevant to DB than DC and that other types of benefits be included e.g. death-in-service where trustees can exercise their discretion.

### **In code 7 – Keeping records**

- It may be beneficial if actual provisions of the Pensions Act and data protection legislation were pinpointed, rather than a broad reference.
- This code should encourage trustees to remind members to keep "letters of wishes" up to date.
- As the trustees delegate this responsibility to the appointed administrator, it was questioned whether it would be appropriate/desirable for them to hold this information?
- It is important that there are records kept of the choices that members make such as the level of contributions and the funds in which they want their contributions invested and these should be specifically mentioned.
- Include a requirement to carry out some form of record validation. Expand to include engaging with a small number of individual members annually to check the veracity of the scheme records against the individual records.
- More detail should be provided on trustees' basic data protection obligations.

### **In code 9 – Investment**

- Two additional sources relevant to this code are Revenue Rules and Trust Law. It would be worth noting in this code that different types of schemes are subject to different regulations in relation to investment of scheme assets. In particular, one man arrangements and SSAS might be noted as being special cases. This code should also reference scheme borrowing and the purpose for which schemes are entitled to borrow.

- Agree the DIS needs to be accepted by the trustees. However, it is reasonable for the trustees to delegate the formulation of DIS to the provider who will base their advice on verifiable analysis of inputs such as time to retirement, members' attitudes to risk and the form and amounts of the benefit decision. Such analysis will be based on studies of the provider's client bank of similar type schemes and industry research.
- Refers to "membership" throughout code. Suggest change to "majority of membership" as trustees are unlikely to be able to cater for every individual member's specific needs. Could more clarity be provided on how frequently investment options should be reviewed? (Code says on "an ongoing basis"). How frequently do we recommend that "principles governing how decisions about investment" must be made? On "member communications" are we recommending member presentations and one-to-one sessions throughout membership and especially near retirement? If so, how do trustees draw a line between providing information/giving advice? In the action grid what does "members' capacity for liabilities" mean? Identify the correct entity, which SLAs are agreed – investment managers, administrator or investment adviser? In the monitoring grid – agree performance for benchmarks for what exactly e.g. funds, managers, advisers? Provide more clarity in relation to frequency of when "periodically review" are required. How frequent should DIS and SIPP be reviewed? How should trustees deal with/manage transition of assets where required i.e. managing out of market exposure and transaction costs where members are forced to switch? Phrases like "appropriate to the members/suitable for needs of members" set a very high bar and are very subjective – perhaps use phrase like "reasonably likely to reflect the assessed needs of the members taken as a whole" would be more appropriate?
- Include a paragraph to encourage trustees to seek appropriate advice if they are not satisfied that they understand their investment manager's charging structures, or are unsure how they compare against the market.

### **In code 10 – Member Communications**

- This code needs to be much more robust. It would be preferable to see a headline statement of principle along the lines that members or deferreds are entitled to clear and timely info on the state of the fund in which their savings repose. The proposed wording makes communications seem like a box-ticking exercise.
- Expand code to include scheme promotion of membership, adequate contribution level and rational investment decision making behaviours.
- The introduction should say that communications "are capable of being understood or understandable". It would be impossible for the trustees to check they are understood by each member. While agreeing with comments on user friendliness etc, it has to be recognised that the trustees must comply with disclosure regulations and there is additional costs in producing further

communications. The requirement for adequacy level of contributions to be flagged up is difficult for trustees as they will not know what is adequate for individual members without knowledge of other savings and benefits. The requirement should be that “Members can understand their investment strategy ...” as trustees cannot ensure that all members understand it. Of the actions required, members should be reminded of their contribution levels as well as their investment choices.

- Second bullet – how are trustees supposed to report “adequacy” to members when it is the members’ decision? Perhaps say “Members can understand whether their contribution levels are likely to provide an income in retirement that will meet their needs” and something similar for third bullet.
- Should this be a joint responsibility between employer and the trustees as employer will ultimately pay for any communications strategy and deliverables?

### **In code 11 – Communicating costs**

- There should be recognition that in many DC schemes the employer will bear a lot of the costs and that the trustees might not have a role in reviewing or monitoring these.
- In terms of asset-based fees, trustees should be encouraged to focus on total expense ratios as well as headline annual management charges. In general, provided that charges are clearly and regularly communicated there should be no need to “develop a communications plan on pension charges”.

### **In code 12 – Value for money**

- Expand criteria – how are trustees supposed to compare against other similar schemes?
- Pension schemes are contracts set up by employers for benefit of employees. The trustee is part of the delivery of those benefits and will either be a professional paid for service or be an employer/employee representative effectively giving the service as part of their job. The VFM of the service that the trustee provides is part of the VFM proposition and it’s difficult to see how their determination of VFM can be sensible. The major beneficiary of VFM is the employee and the employer who provides the benefits and it should be up to them to establish VFM.
- The costs borne by the employer might impact the level of monitoring the trustees can do in this area. This is an example of an area where it is very difficult to see how trustees could confirm they are abiding by the code as it is particularly vague in nature.
- Suggest including sample questions that trustees should ask various scheme providers to assist them in assessing whether they are getting VFM.

## Additional comments

There were a number of additional comments and suggestions concerning the development of the codes. Issues mentioned were:

- **Taking advice:** Some of the codes might benefit from trustees being directed to specific types of third parties who can assist them to comply with a code and better govern their scheme e.g. the experience of insurers, administrators and consultants should be availed of in relation to drafting communications to members and maintaining records but also in ascertaining what represents best practice in schemes which they work with in complying with the codes. If legal issues arise, e.g. those related to conflicts of interest, trustees should be encouraged to take legal advice if they are in doubt as to what they should do.
- **The role of the employer:** This also needs to be considered particularly where the employer is responsible for the appointment of trustees, deciding on the objectives, contribution levels and the payment of the costs of the scheme.
- **Additional costs:** There also needs to be a balance between the introduction of the codes and the additional costs that may result in complying with these, particularly where the trustees of DC schemes do not necessarily have a budget for such costs.
- **Service Level Agreements (SLAs):** Encouraging trustees to establish SLAs with their investment manager and administrator is a positive development from a governance perspective. However, in practice SLAs are drafted by providers or their advisers and, as such, typically contain provisions which are not provider-friendly. It's important that trustees ensure that SLAs are independently reviewed so that they are not fast-tracked in to agreements/contracts which are weighted in favour of the provider. There is too much emphasis throughout on the need to have all processes formally documented in a SLA – which for smaller schemes in particular may add significantly to the governance burden without necessarily improving the quality of governance to a material degree. The danger is that while a scheme may be functioning very well on short term operational matters, it may be weak or lack focus relative to more strategic longer term objectives – essentially the trustees should be asking themselves whether they understand their members' expectations at retirement, whether those expectations are reasonable and whether their contribution and investment choices are consistent with delivery of those objectives.
- **Legal status of the codes:** There were some concerns about the legal status of the codes which are intended to be voluntary initially with legislation being

introduced at a later stage to require trustees to submit an annual compliance return to confirm they are “abiding” by the codes. The ability to give such a confirmation would be difficult in practice as some of what the codes require is quite non-specific, for instance, “internal audit of risk management process”.

- **Reduction of lay trustees:** There was also a concern that imposition of higher standards might lead to the reduction in lay or member and employer nominated trustees and an increase in the appointment of independent professional trustees. Lay trustees add value to trustee boards, and they help ensure that members’ views are known. They also have a role in conveying historical/cultural understanding. Trustee boards which include member/employer nominated trustees strengthen good scheme governance and gives members a greater sense of engagement with their schemes.
- **Large number of small schemes:** The primary problem with the large number of small DC schemes is whether such schemes are viable in the first place. Ideally these small schemes should be encouraged to consolidate into purpose-built large group vehicles (master trusts or industry collective schemes) where good governance can be better exercised, more professionally and at scale. It must be recognised that increasing the governance burden on smaller schemes may result in governance requirements becoming disproportionate from a cost perspective. In more mature DC markets, master trusts have proved to be a successful solution to governance challenges and typically much more effective at delivering quality outcomes for members than contract based approaches.
- **Access to reference data:** To assist trustees with complying with the codes for which they must retain full responsibility, trustees will need access to easily understandable reference data. Investment performance statistics are readily available while total expense ratios, encompassing headline annual management costs (AMC) and other investment related costs must be made available from investment managers.
- **Running costs of schemes:** Where RA costs are passed through to members by deduction from retirement accounts, guidance as to market averages by scheme size (members and assets) needs to be available: this is not necessarily an issue where the sponsor meets costs directly. However, on a related point, as highlighted in the DB Financial Guidelines, where the employer bears some or all of the costs of running of the scheme, there should be a written agreement between the trustees and the sponsoring employer(s) setting out the terms, including any restrictions on the freedom of trustees to incur costs.