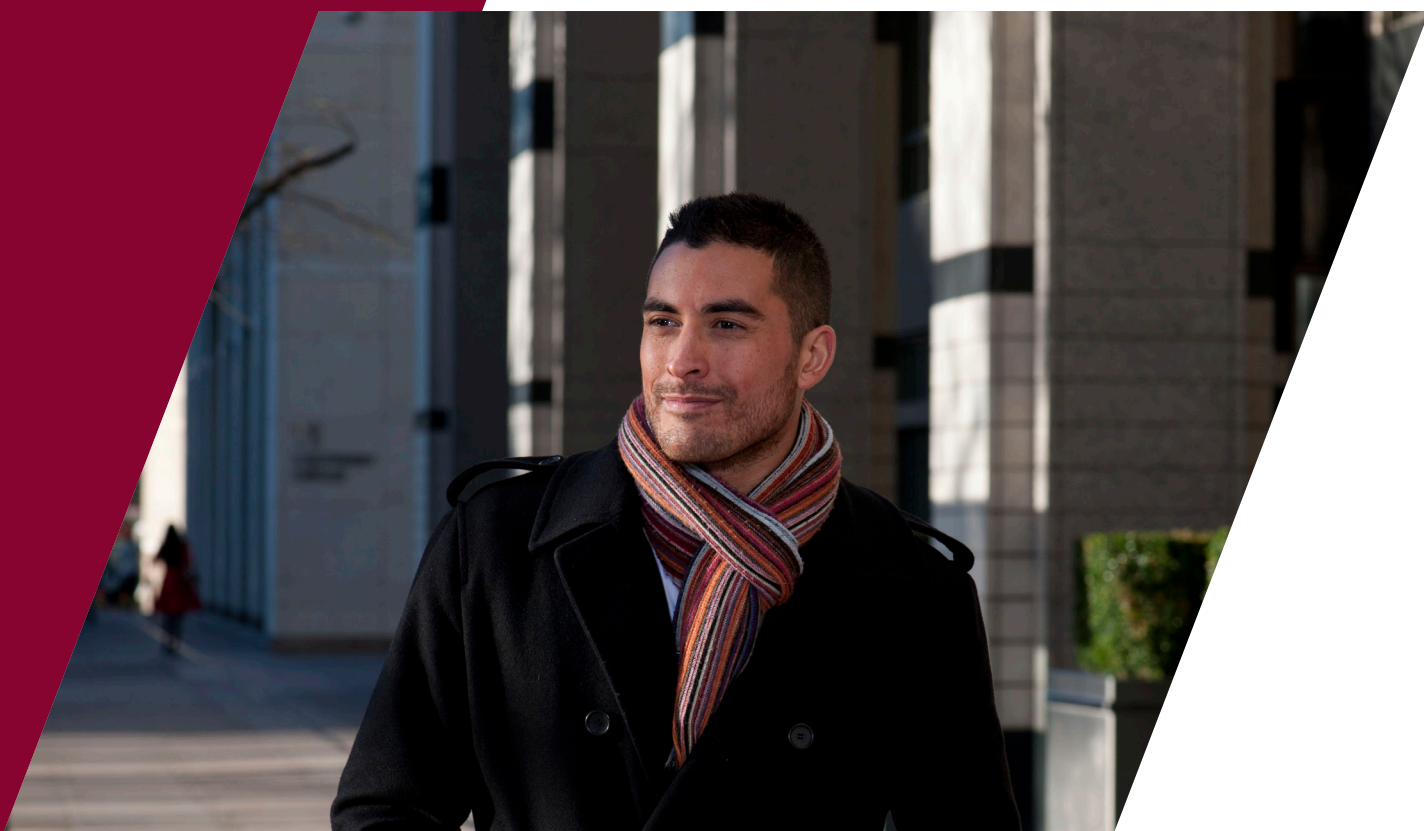


# Final rules for independent governance committees, including feedback on CP14/16

February 2015





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In this Policy Statement we report on the main issues arising from Consultation Paper CP14/16 *Proposed Rules for Independent Governance Committees* and publish the final rules.

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## Abbreviations used in this paper

<b>ABI</b>	Association of British Insurers
<b>CBA</b>	cost benefit analysis
<b>DC</b>	defined contribution
<b>DWP</b>	Department for Work and Pensions
<b>ESG</b>	environmental, social and governance
<b>FCA</b>	Financial Conduct Authority
<b>FSMA</b>	Financial Services and Markets Act 2000
<b>GAA</b>	governance advisory arrangement
<b>IGC</b>	independent governance committee
<b>IPB</b>	Independent Project Board
<b>MiFID II</b>	Markets in Financial Instruments Directive II
<b>NAPF</b>	National Association of Pension Funds
<b>NEST</b>	National Employment Savings Trust
<b>OFT</b>	Office of Fair Trading
<b>PQM</b>	Pension Quality Mark
<b>PRIIPs</b>	Packaged Retail and Insurance-based Investment Products Directive
<b>SIPP</b>	self-invested personal pension scheme
<b>TPR</b>	the Pensions Regulator
<b>WPC</b>	with-profits committee

# 1. Overview

## Introduction

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- 1.1** We are publishing rules to require the providers of workplace personal pension schemes to set up and maintain independent governance committees (IGCs). IGCs will have a duty to act in the interests of scheme members and will operate independently of the firm. They will assess and, where necessary, raise concerns about the value for money of workplace personal pension schemes.

## Who does this affect?

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- 1.2** This policy statement affects the providers of workplace personal pension schemes. Workplace personal pension schemes include personal pension schemes and stakeholder pension schemes which employers either use for automatic enrolment or make available to their employees.
- 1.3** In 2013, our data indicated that there were over 20 firms or groups that sold workplace personal pension schemes to employers in the UK. In addition, there are other firms or groups which operate group pension schemes which are no longer being actively marketed to employers. Our rules will affect these as well.
- 1.4** This policy statement is also likely to be of interest to:
- employers and their advisers, in relation to the selection and ongoing monitoring of workplace personal pension schemes, and
  - fund managers, administrators and other third parties providing services to firms operating workplace personal pension schemes.

## Is this of interest to consumers?

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- 1.5** IGCs will act in the interests of relevant scheme members by challenging firms on the value for money of workplace personal pension schemes. Therefore, this policy statement should be of interest to consumers who are members of workplace personal pension schemes, both employees actively contributing to a pension and deferred members. It is also likely to be of interest to consumer groups seeking better protection for consumers with workplace personal pensions.

## Context

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- 1.6** The UK has an aging society with many people not saving enough for their retirement. Automatic enrolment of employees into workplace pension schemes began in July 2012, as part of the government's policy response to this challenge. By 2018, when automatic enrolment applies to all companies, it is estimated that between eight and nine million people will be newly saving, or saving more, in a workplace pension scheme.<sup>1</sup> Many of these people will not have made any active choice about how their pension savings are invested and may be on low incomes.
- 1.7** Automatic enrolment means that it is even more important to ensure that workplace pension schemes deliver value for money. In 2013, an Office of Fair Trading (OFT) market study highlighted problems with the market, including a very weak buyer side and the potential for conflicts of interest. The study covered both trust and contract-based schemes, since employers can choose either type of scheme for their employees.
- 1.8** The OFT report<sup>2</sup>, published in September 2013, noted that the buyer side of the market was 'one of the weakest that the OFT has analysed in recent years'. Employers make most of the key decisions, but may lack the capability and/or the incentive to ensure that members of their schemes receive value for money in the long term. Many employees are not interested in their pension saving and, with the advent of automatic enrolment, may be enrolled into the default fund of their employer's scheme without making any active choice. Neither employers nor employees can be expected at this time to drive effective competition between firms.
- 1.9** On the contract side of the market, which we regulate, scheme members lack any direct agent to represent their interests. Most contract-based workplace pension schemes are provided by firms which are members of the Association of British Insurers (ABI). The OFT agreed with the ABI that ABI member firms operating workplace personal pension schemes would establish and maintain IGCs to assess and raise concerns about value for money on behalf of scheme members.<sup>3</sup>
- 1.10** The OFT also identified around £30 billion of saver's money in legacy defined contribution (DC) workplace pension schemes was considered at risk of being poor value for money, by modern standards, because of potentially high charges. The OFT agreed that the ABI and its members would undertake an audit of these legacy schemes, with an Independent Project Board (IPB) appointed to oversee the audit.
- 1.11** On 17 December 2014, the IPB issued its final report, which included the recommendation that IGCs agree remedial actions and an implementation plan with the providers of legacy schemes at risk of being poor value for money. An early priority for the IGCs of affected providers will be the implementation of the IPB's recommendations.<sup>4</sup>
- 1.12** As the regulator of personal pensions, we have been working with the Department for Work and Pensions (DWP) to both require the introduction of IGCs and to develop minimum quality standards, under which IGCs will provide governance oversight of workplace personal pension schemes. The FCA's principles and rules already place a number of requirements on the conduct of providers, including a requirement to treat customers fairly and to manage conflicts of interest between the provider and its customers.

<sup>1</sup> DWP *Transparency data – DWP business plan transparency measures* (July 2014)

<sup>2</sup> OFT *Defined contribution workplace pension market study* (September 2013) <http://webarchive.nationalarchives.gov.uk/20131101164215/http://www.of.gov.uk/OFTwork/markets-work/pensions/>

<sup>3</sup> While the OFT agreed with the ABI that ABI member firms operating workplace personal pension schemes would establish and maintain IGCs, our rules will apply to all providers of workplace personal pension schemes

<sup>4</sup> Further detail is provided under the section 'legacy workplace pension schemes' in Chapter 4

- 1.13** In our consultation paper, published on 6 August 2014,<sup>5</sup> we set out our proposed rules to require the providers of workplace personal pension schemes to establish and maintain IGCs.<sup>6</sup> Our consultation closed on 10 October 2014. We have considered comments and feedback received in finalising our new rules for IGCs.
- 1.14** This policy statement sets out our final rules for IGCs. We consider that our new rules will advance the following statutory objectives of the FCA:
- **securing an appropriate degree of protection for consumers:** IGCs will protect the interests of relevant policyholders by assessing the value for money of their schemes and raising concerns where necessary, and
  - **promoting effective competition in the interests of consumers:** IGCs will report on the value for money of their firm's schemes. This will increase the quality of information which employers and employees have access to and may improve competition between firms providing workplace personal pension schemes.
- 1.15** On the occupational pensions side of the market, which is regulated by the Pensions Regulator (TPR), the DWP will be introducing new regulations for minimum governance standards and to ensure the independence of the trustee boards of master trusts.
- 1.16** We have been working with the DWP and TPR on consistent minimum quality standards for workplace pension schemes. Our new rules and the DWP's proposed regulations are aligned, to ensure similar expectations for contract-based workplace pension schemes and occupational schemes.

### Summary of feedback and our response

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- 1.17** We received 67 responses to our consultation from a variety of stakeholders, including consumer groups, trade bodies, firms and political bodies. The National Association of Pension Funds' (NAPF) response was informed by a short survey of NAPF members and Pension Quality Mark (PQM) schemes. We received a further 180 responses from individuals, following a campaign by ShareAction. These individual responses conformed to a short template provided by ShareAction.<sup>7</sup>
- 1.18** We are grateful for the feedback received and want to take this opportunity to thank all those who responded to our consultation. We have considered carefully the responses that we received before deciding on our policy approach and final rules.
- 1.19** Respondents were generally positive about our proposals. IGCs were seen as an important step forward in improving the governance of contract-based workplace pension schemes.
- 1.20** The following table provides an overview of feedback received and our response to that feedback.

<sup>5</sup> FCA CP14/16 *Proposed rules for independent governance committees* (August 2014) <http://www.fca.org.uk/news/cp14-16>

<sup>6</sup> Not all providers of workplace personal pension schemes are ABI members. However, our rules will apply to all such providers.

<sup>7</sup> ShareAction campaigns for socially responsible investing by pension funds and fund managers. ShareAction called for measures to help ensure that IGCs are accountable to scheme members, such as holding an AGM and regularly surveying scheme members on their views and priorities.



Feedback received	Our response
<p>A few respondents called for a fiduciary duty to be placed directly on providers. In their view, this would best align the interests of pension schemes with those saving into them.</p>	<p>We believe that existing FCA rules and principles provide fiduciary-like protections and are confident that IGCs will be able to act independently and effectively in the interests of scheme members.</p>
<p>A small number of respondents commented that all members of IGCs ought to be independent of the provider, rather than the majority including the Chair.</p>	<p>We see value in allowing one or more provider employees on an IGC, provided they are in a minority and never the Chair. Provider employees bring in-depth knowledge about a provider's schemes and a mix of members helps ensure a balanced view in decision making. Any provider employees on an IGC would be contractually bound to act in the interests of scheme members in their capacity as IGC members. Moreover, we will require that an IGC quorum comprise a majority of independent members.</p>
<p>While most respondents thought that the FCA should not mandate a particular approach to assessing value for money, many thought that an FCA framework would be helpful to IGCs and would support a consistent approach.</p>	<p>We agree that there should be no mandatory approach to the assessment of value for money, given the very different characteristics of different providers' schemes. Nonetheless, we also see the value in supporting IGCs and providing guidance. We intend to start by holding a forum for IGC Chairs, around the time that our rules become effective, at which we will discuss how we can best help them assess value for money.</p>
<p>A number of respondents felt that IGCs had a role to play in assessing value for money for scheme members in decumulation.</p>	<p>We agree that IGCs may want in the future to consider value for money for scheme members in decumulation. We will consider making this a requirement once IGCs have their immediate priorities in hand. While the primary focus of IGCs will be on default strategies, there is no reason why this should not extend into consideration of decumulation and retirement income options.</p>

<p>Some respondents thought that the FCA should require providers to indemnify independent IGC members.</p>	<p>Our view remains that scheme members are more likely to pursue any legal action against the pension provider, rather than individual IGC members or the IGC collectively. The contracts are between the provider and individual policyholder; any changes to the scheme would be the responsibility of the provider. Therefore, we are not convinced of the need for an FCA rule, but will include guidance to the effect that firms should consider indemnifying members.</p>
<p>A number of respondents considered that our requirements would be unduly onerous for small providers.</p>	<p>Our rules will provide for an alternative approach for the providers of smaller and less complex schemes. We consider that this approach should provide equivalent protection for the members of such schemes. We do not propose any “lesser” solution for smaller providers since we believe that all members of workplace pension schemes should be assured the same minimum protection.</p>
<p>Some respondents suggested that the FCA should review the effectiveness of IGCs in a couple of years’ time.</p>	<p>IGCs will be new governance bodies and we will want to ensure that they are operating effectively. We intend to conduct a review of the effectiveness of IGCs in 2017. This could be in the context of a broader FCA/ DWP review of workplace pension reforms.</p>

### Equality and diversity considerations

- 1.21** In CP14/16, we said that we had assessed the likely equality and diversity impacts of the proposed rules for IGCs and did not think they give rise to any concerns. We considered that the proposed rules should ensure that the interests of potentially vulnerable members are represented and that concerns are raised on their behalf.

**Q1:** *We would welcome views on the likely equality and diversity impacts of the proposed rules.*

- 1.22** The majority of respondents agreed that our rules for IGCs apply equally to all scheme members and should not give rise to concern with regards to their likely equality and diversity impact.
- 1.23** A small number of respondents focused on the composition of the IGC itself. These respondents questioned whether there should be a requirement to ensure a diversity of members appointed to the IGC.

### Our response

We recognise the value in a diversity of viewpoints. We will expect the IGC to take into account the views of scheme members and will require the provider to ensure that member views are directly represented to the IGC. However, while supportive of a diversity of members on IGCs, we do not intend to make this a requirement in our rules.

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### Next steps

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- 1.24** The rules will come into force on 6 April 2015. Firms will be expected to comply from that date. Firms that already have IGCs in place will need to ensure that they meet the rules from 6 April 2015.

## 2. Requirement for an IGC

- 2.1** In this chapter, we summarise feedback received on the proposed scope of IGCs and on which firms will be required to operate an IGC. We provide our response to that feedback.

### Workplace personal pensions

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- 2.2** Workplace personal pensions are personal pension contracts between individual (including past) employees and the providers of personal pension schemes. When employees join a personal pension scheme through the workplace, a contractual agreement is established directly between the scheme provider and the employee. While the employer selects the pension provider and scheme, and possibly the default fund within the scheme, the employer is not party to this agreement. The agreements collectively within a workplace are commonly referred to as the employer's workplace personal pension scheme.
- 2.3** In CP14/16, we proposed that regulated firms operating workplace personal pension schemes should be required to establish and maintain an IGC.<sup>8</sup>
- 2.4** Overall, the response to our consultation was very positive. The large majority of respondents were in favour of our proposal to require firms operating workplace personal pension schemes to establish and maintain an IGC. This reflected a general view that something similar to trustee boards was needed for the contract-based side of the market, to represent the interests of often unengaged scheme members.
- 2.5** Nonetheless, the requirements for IGCs are not yet in place and the effectiveness of IGCs, including the extent to which providers listen and respond to their concerns, has yet to be demonstrated. Some respondents called for a formal review of the effectiveness IGCs in a couple of years' time. Comments included the suggestion that we are at the beginning of a journey with IGCs and that we may need to consider tightening its requirements in the future.

### Deferred members

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- 2.6** Deferred members are scheme members who no longer contribute to their pension savings in that scheme. In workplace personal pension schemes, individuals who are no longer employed by a particular employer are generally deferred members of the respective scheme.

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<sup>8</sup> Throughout this document, references to IGCs also apply to governance advisory arrangements (GAAs), which are the alternative arrangements to IGCs for providers with smaller and less complex schemes

- 2.7** Individual deferred members may have built up substantial pension assets, which may continue to grow through investment returns. Despite this, deferred members are often unengaged and poorly informed, with less interest in their pension because they are no longer actively contributing.
- 2.8** In CP14/16, we considered that IGCs should act in the interests of deferred members of workplace personal pension schemes as well as active members. Therefore, we proposed that deferred members be within the mandatory scope of IGCs

**Q2: *Do you agree that deferred members of workplace personal pension schemes should be within the mandatory scope of IGCs?***

- 2.9** Almost all respondents expressing an opinion agreed with the proposal and a number said they considered it essential. Some respondents observed that deferred members have a greater need of protection than active members, since they are likely to be even less engaged. One referred to deferred members as the 'poor relation' in both contract-based workplace pension schemes and occupational schemes.
- 2.10** A number of respondents commented that it would be difficult to identify deferred members. This was because the policies of deferred members may have no special marker to distinguish them as ex-workplace policies, appearing in provider records as individual personal pension policies.
- 2.11** Some respondents thought we should allow individual IGCs to determine the extent to which deferred members fall within their remit. Respondents noted that ABI members had already committed to a sampling exercise of individual personal pensions to identify those cases where savers were previously in a workplace pension.

**Our response:**

We have considered the feedback and remain of the view that deferred members should be within the mandatory scope of IGCs.

We acknowledge that some providers may find it difficult to identify deferred members. However, our rules will permit providers to extend the remit of their IGCs to include individual personal pension policyholders. The IGC would then act in the interests of those deferred members they are unable to distinguish from individual personal pension policyholders.

Some providers operate books in run-off and may have taken the active decision to stop further contributions into the scheme. All the members of such schemes may be deferred members. In this situation, we will still require the provider to establish an IGC to act in the interests of these deferred members.

### Individual personal pensions

- 2.12** Individuals may choose to invest in personal pension schemes as part of their financial planning. These individual customers generally receive advice and/or undertake research before selecting the pension provider and scheme that they want to join.

**2.13** Such customers can be expected to take more active interest in their pension scheme, including post-sale, and the value for money that it delivers. If not satisfied with the performance of the provider and/or scheme, they can transfer their savings, as with other forms of long-term saving product.

**2.14** In CP14/16, we did not propose including individual personal pensions within the mandatory remit of IGCs at this time. However, we noted that an IGC's terms of reference may be extended on a voluntary basis to include individual personal pensions, subject to the IGC being appropriately resourced and supported.

**Q3: *Do you agree that individual personal pensions, other than those that originated as workplace personal pensions, should not be in the mandatory scope of IGCs?***

**2.15** The substantial majority of respondents agreed that individual personal pensions, other than those that originated as workplace personal pensions, should not be in the mandatory scope of IGCs. Feedback recognised that individuals who have self-selected a personal pension product, generally with advice, are less in need of additional protections.

**2.16** Some comments reflected a concern that mandating inclusion of individual personal pensions would weaken the focus of IGCs on workplace pension schemes. Other comments suggested that the interests of individual personal pension policyholders may not be aligned with workplace personal pension policyholders.

**2.17** A small number of respondents disagreed with our proposal and considered that all personal pensions should be within the scope of IGCs. One respondent made the point that while advice may have been provided at point of sale, an individual may no longer be actively advised. Another respondent was concerned on behalf of self-employed people in the workforce, who might have individual personal pensions.

### **Our response**

We do not intend to include individual personal pensions, other than those that originated as workplace pension schemes, within the required scope of IGCs at this time. This is because – as with other long-term savings products – the individual made an active choice of both the provider and product and is therefore more likely to be engaged with their pension saving.

Nonetheless, we have sympathy with the concern expressed on behalf of self-employed people in the workforce, who may not have access to a workplace pension scheme. When individuals are not in a position to assess and monitor the value for money of the scheme that they choose, they may be at increased risk of a poor pension outcome in retirement.

The other side of issue is whether there should be any requirement for individual personal pensions, other than those that originated as workplace pension schemes, not to be in the scope of IGCs. Respondents did not explicitly comment on this, although some expressed concerns that including individual personal pensions would weaken the focus of IGCs on workplace schemes.

While we believe that at present the primary focus of IGCs should be on workplace personal pensions, due to the low levels of member engagement and potential lack of active choice, we do not propose to restrict, in FCA rules, the scope of IGCs to workplace personal pensions. Our rules will permit providers to extend the remit of their IGC to include individual personal pensions. Some providers finding it difficult to identify deferred members may choose to do this.

Where the remit of an IGC is extended to include individual personal pensions, the provider must ensure that the IGC is appropriately resourced and supported, such that the IGC's ability to act in the interests of workplace personal pension scheme members is in no way compromised.

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### Employer contributions to individual personal pensions

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- 2.18** Some employers may contribute to personal pensions arranged on an individual basis. These are accessible outside the workplace and without employer involvement in the original selection of the scheme. This includes situations where employers facilitate the payment of member contributions through payroll to such pensions.
- 2.19** In CP14/16, we considered that our new rules should not apply to firms operating schemes into which employers pay contributions but where the individual has made the final decision over the selection of their pension provider and scheme. For example, our rules would not apply to an executive's self-invested personal pension scheme (SIPP) or other personal pension arrangement, even where an employer has agreed to make or facilitate contributions into this.
- 2.20** However, we did propose that our rules apply to providers of group SIPPs used in the workplace and set up by employers for their employees. In this situation, the employer has selected the arrangement and the employees are less likely to be engaged with the administration and investment of their pension savings.

**Q4: *Do you agree that individual personal pensions should not be in the mandatory scope of IGCs, even where the employer contributes or facilitates payments?***

- 2.21** Respondents generally agreed that individual personal pensions should not be in the mandatory scope of IGCs, even where the employer contributes or facilitates payments. One respondent noted that the key point is that the individual has made an active choice in the selection of the pension provider and the scheme, and that whether or not the employer chooses to contribute is irrelevant. Other comments reflected this point.
- 2.22** One respondent agreed with our proposal but observed that it may be difficult, in practice, to distinguish these arrangements from workplace personal pension arrangements, since an employer will be contributing to the pension in both situations.
- 2.23** A few respondents questioned the extent to which SIPPs with employer contributions should be caught by our proposed rules. One respondent gave the example of group SIPPs, in which individuals may have actively chosen to invest outside the provider's long-term contracts of insurance. This respondent proposed that the IGC's protection should not extend to such individuals.

- 2.24** As before, a small number of respondents considered that all personal pensions, including all individual personal pensions, should be within the scope of IGCs.

#### Our response

We agree that the key point is that the individual has made an active choice in the selection of the pension provider and the scheme, and that whether or not the employer chooses to contribute is irrelevant. We remain of the view that individual personal pensions should not be in the mandatory scope of IGCs at this time, even where the employer contributes or facilitates payments.

For group SIPPs, the employer has selected the pension provider and the scheme. We consider that employees enrolled in group SIPPs should have the protection of IGCs.

Individual employees and deferred members who actively choose to invest outside the provider's long-term contracts of insurance are clearly more engaged in their pension saving. While the remit of IGCs will include such individuals, our rules allow IGCs to focus on those individuals who have not made any active choice.

#### Which firms will be required to establish an IGC

- 2.25** It is our intention that IGCs should represent the interests of active and deferred members of workplace personal pension schemes.
- 2.26** In CP14/16, we proposed that firms operating a personal pension scheme or stakeholder pension scheme will be required to establish and maintain an IGC if there are, or have been, direct payment arrangements to cover two or more employees of the same employer.
- 2.27** Direct payment arrangements are defined in the proposed rule as arrangements under which employers pay contributions directly to firms for the benefit of employees. This includes both employer and employee contributions.

#### **Q5: Do you agree with our proposals for which firms will be required to establish and maintain an IGC?**

- 2.28** The large majority of respondents agreed with our proposals for which firms will be required to establish and maintain IGCs. One respondent commented that the rules should be clear that firms operating legacy books of workplace personal pensions, including closed books, would also be required to establish and maintain an IGC, since the members of these schemes would need as much protection. Another respondent agreed but sought clarification on whether a provider of individual personal pensions operating a workplace scheme for its own staff only, and not workplace schemes commercially to the wider market, would be caught by our rules.
- 2.29** Some respondents agreed but were concerned about the costs of IGCs and the potential for overlap with existing, non-mandatory governance arrangements.



- 2.30** Some respondents disagreed with our proposals. A small number of respondents proposed that any firm operating a personal pension schemes, regardless of whether an employer was involved in selecting the provider and scheme, should be required to establish and maintain an IGC. These were the same respondents who considered that all personal pensions should be within the scope of IGCs.
- 2.31** Some other respondents were concerned about the cost for small providers of workplace personal pension schemes, and suggested a light touch approach or an exemption. In Chapter 6, we set out our intention for an alternative arrangement for the providers of smaller and less complex workplace personal pension schemes.

### Our response

We are pleased that respondents generally agreed with our proposals for which firms will be required to establish and maintain an IGC. Based on the responses received, we have decided to proceed with our rules as proposed.

In addition to their focus on the default funds of schemes used for automatic enrolment, we consider that IGCs will have an important role in ensuring the value for money of legacy workplace personal pensions, including closed books. Our proposed rules already encompass firms operating legacy books of workplace personal pensions, including closed books. We confirm that this is our intention and that we will proceed on this basis.

We have considered the situation where a provider of individual personal pensions operates a workplace scheme for its own staff only, and does not offer workplace schemes commercially to the wider market. We agree that such a provider has a vested interest in providing an appropriate arrangement for its own staff. We also note the proposed ban on differential charging between active and deferred members, which will help protect ex-employees.

On balance, we believe a requirement for an IGC or alternative arrangement in such a situation has the possibility of being disproportionate. In such circumstances, a provider operating a workplace scheme for its own staff only may apply for a waiver.<sup>9</sup> Such applications will be considered on a case-by-case basis. However, we would expect a provider granted a waiver to ensure that its scheme delivers value for money for all members.

We have also considered the arguments for extending the requirement for IGCs to any firm providing personal pension products, regardless of whether these are provided in the workplace. IGCs are intended as a means of enhancing the governance of contract-based schemes where an employer has selected the provider and the scheme, and where scheme members, as the ultimate beneficiaries, may be disengaged in their pension saving. At this time, we do not see the need to extend the remit of IGCs to all personal pension products or to other long-term saving products where the investor has made an active choice and has generally been advised.

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<sup>9</sup> under s.138A FSMA, and the guidance in SUP 8

### IGCs established at a group level

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- 2.32** Some corporate groups may include a number of different providers of workplace personal pension schemes. In such situations, the question arises as to whether each provider needs to establish its own IGC, or whether a group level IGC can operate across providers.
- 2.33** In CP14/16, we proposed that IGCs may be established at a group level for use by providers of workplace personal pensions under common ownership. We would expect the separate providers operating workplace personal pension schemes within the same corporate group each to ensure that all relevant scheme members have their interests represented by an IGC.

**Q6: *Do you agree that IGCs may be established at a group level?***

- 2.34** All respondents expressing an opinion agreed that IGCs should be permitted at a group level. Group IGCs were seen as an efficient and proportionate option.
- 2.35** Where there were concerns, these were mostly about the need to ensure that the IGC devoted sufficient time and resource to the schemes of each different provider within the group. There was recognition of the risk that the group level IGC might focus on the schemes of a particular provider and might not devote appropriate attention to all the schemes under its protection.

#### Our response

Based on the feedback received, we will proceed with our rules as proposed, allowing IGCs to be established at a group level. We note that if all the providers within a group were to merge into a single legal entity, there would only be a requirement for a single IGC anyway.

As with any IGC operating across multiple schemes, the interests of all relevant scheme members must be represented. We will expect the separate providers each to ensure that all relevant scheme members have their interests appropriately represented by an IGC, either at a group level or by an IGC that they set up.

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### Interaction with other committees and governance structures

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- 2.36** A number of providers operating workplace personal pension schemes already have investment committees and other governance structures, including committees that are intended to be independent of the provider. In addition, larger employers may have management and governance committees for the workplace personal pension schemes arranged for their workforce. TPR and the NAPF have encouraged the establishment of employer-level management and governance committees.
- 2.37** In CP14/16, we did not propose how IGCs should work with existing governance structures, either at the provider or employer level, where there might be overlap or duplication of activities relative to our proposals for IGCs.

- 2.38** Some respondents nonetheless commented or sought clarification on how IGCs would be expected to interact with other committees and governance structures. One respondent expressed the view that IGCs should be strongly encouraged to identify and make contact with all governance committees run by employers with schemes operated by the IGC's provider, and should set up a mechanism for listening to their views on the service being provided.
- 2.39** Another respondent asked whether an IGC would be required for group SIPPs under trust, where there is already a trustee.

### Our response

We recognise the role of such existing governance structures to provide oversight of the value delivered to workplace pension scheme members. We support employer-level management and governance committees as a way of engaging and looking after the interests of the employee scheme members. We see no reason why these existing structures should not work alongside IGCs.

Where the provider operates an existing governance committee that overlaps with an IGC in its duties, we will still expect the provider to establish and operate an IGC. It will be for the provider to determine whether the overlap is such that the IGC should replace the existing governance committee, rather than working alongside it, or whether the duties of the existing governance committee should be reconsidered in the light of the overlap.

We intend for our rules to apply to the providers of group SIPPs, including where group SIPPs are under trust. The responsibilities of the trustee are sometimes limited and may not extend to the minimum requirements of an IGC. We recognise that some trustees of group SIPPs, including corporate trustees, may be given wider responsibilities. We would expect governance bodies to coordinate their work and seek to avoid duplication of activities.

### Quality standards for occupational pension schemes

- 2.40** Occupational pension schemes are set up under trust, with trustees or managers appointed to run the scheme. Trustees are required to operate schemes in accordance with the scheme's trust deed and rules, and are also under a fiduciary duty to act in the best interests of members of the scheme. Trustees are responsible for appointing (in some cases) and holding to account (in all cases) those parties who are responsible for the day-to-day running of the scheme.
- 2.41** TPR is responsible for the regulation of occupational pension schemes. Our rules in this policy statement do not apply to occupational pension schemes.
- 2.42** Some respondents commented that it was important that the governance of occupational schemes and, in particular of master trusts, be improved through regulation. These respondents wanted to ensure that the requirements for master trusts would be aligned to our requirements for contract-based schemes used in the workplace, to ensure a level playing field.

## Our response

We have been working closely with the DWP and TPR to ensure that our proposed rules for IGCs and the proposed new requirements for occupational schemes are aligned, where appropriate. Our shared intent is to ensure that members of all workplace pension schemes, regardless of structure or type of scheme, can be confident of the same good governance.

In the DWP's paper *Better workplace pensions: Putting savers' interest first*<sup>10</sup>, published in October 2014, the government consulted on draft regulations on governance and charges in occupational pension schemes. These include requirements to ensure the independence of the trustee boards of master trusts, including a requirement for an independent Chair.

Subject to Parliamentary approval, the majority of this legislation will come into force from April 2015, alongside FCA rules in relation to workplace personal pension schemes, where appropriate.

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<sup>10</sup> CM 8929; [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/364567/better-workplace-pensions-putting-savers-interests-first.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/364567/better-workplace-pensions-putting-savers-interests-first.pdf)

## 3.

# Establishing and maintaining an IGC

- 3.1** This chapter summarises feedback received on our proposed requirements on firms for establishing and maintaining an IGC and provides our response to that feedback.

### Composition of an IGC

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- 3.2** An effective IGC needs members with the understanding and knowledge of workplace personal pensions to be able to assess and make judgements on value for money. Schemes may be complex, with differing benefits and services, and a variety of charges and costs that are often unclear. The IGC also needs to be independent of the firm, so that it can act solely in the interests of members in raising concerns about value for money.
- 3.3** In CP14/16, we proposed requiring firms to establish IGCs with sufficient collective expertise and experience so that they are competent to make judgements on the value for money of potentially complex schemes.
- 3.4** In addition, we proposed that an IGC must have a majority of members independent of the firm. Given the importance of the IGC Chair to the work of the IGC and in providing credible and effective challenge, we also proposed that the Chair must always be independent of the firm.

**Q7: *Do you agree that an IGC must have a majority of members independent of the firm and that the IGC Chair must always be independent?***

- 3.5** The large majority of respondents agreed with our proposal. Many stressed that the independence of the IGC is fundamental to its function. Some respondents noted that the IGC could not otherwise be expected to challenge the provider.
- 3.6** A number of respondents considered that all IGC members should be independent of the provider. One respondent thought that employees of the provider cannot be expected to challenge board decisions robustly and in the interests of scheme members.
- 3.7** Others thought that greater consideration should be given to mandating the inclusion of scheme members on IGCs. One respondent thought that scheme member and employer representatives should take the majority of positions on an IGC. In the view of this respondent, member and employer representatives should be either elected, or appointed by unions or appropriate employer associations.

## Our response

We have listened carefully to concerns about the independence of IGCs and have considered whether to require that all IGC members be independent of the provider.

We see value in allowing provider employees on the IGC, provided they are in a minority and never the Chair. In our view, a mix of members ensures a balanced view in decision making and provider employees will bring valuable, in-depth knowledge of the provider's schemes to the assessments of value for money. Provider employees may be able to answer the questions of independent IGC members before concerns are raised with the provider's board.

However, provider employees should be in no doubt that they are contractually bound to act in accordance with the terms of reference of the IGC, in their capacity as IGC members. These terms must include the duty to act solely in the interests of relevant scheme members. In other words, provider employees would be required to put aside the commercial interests of the firm and their duty to shareholders when acting as IGC members.

We would not expect the provider to appoint a provider employee to its IGC when the employee's day-to-day role and responsibilities are in direct conflict with the role and responsibilities of IGC members. For example, we would not expect to find the head of the provider's investment committee as an IGC member.

While provider employees must be contractually bound to act independently of the provider, we remain of the view that the majority of IGC members must be independent of the provider and that the Chair must always be independent. In CP14/16, we did not prescribe a quorum for IGCs. In the light of the feedback, we will require that a quorum must comprise a majority of independent members.

We remain supportive of scheme member representatives on IGC. We consider it vital that IGCs listen to the actual concerns of scheme members, rather than assuming they know their concerns. That is why we will require providers to have arrangements to ensure that the views of scheme members are directly represented to the IGC.

However, we do not consider it practical to require, in an FCA rule, the inclusion of scheme member representatives on IGCs. The scheme members most in need of protecting are those least likely to be engaged and willing to act as representatives. While we would encourage providers to find ways to include scheme member representatives on IGCs, we recognise that it may be difficult for providers to attract suitable candidates.

IGCs will not represent the particular concerns of individual scheme members against providers, but will rather represent the interests of relevant scheme members as a whole, or groups of relevant scheme members within the scheme. Individuals should, as before, take their concerns directly to the provider in the first instance and have the existing Financial Ombudsman Scheme or Pensions Ombudsman Scheme route if they are not satisfied with the provider's response.

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### IGC members

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- 3.8** In the DWP's March 2014 Command Paper, the government originally proposed that IGCs must have at least seven members.
- 3.9** We subsequently agreed with the DWP that this minimum requirement may be too high. While an IGC with seven members may be appropriate for large firms, the burden on other firms may be disproportionate to the benefit to members. Nonetheless, we considered that an IGC with too few members may not have the breadth of views to be effective, regardless of the expertise and experience of individual members.
- 3.10** In CP14/16, we proposed that that an IGC should have at least five members. We believed that this strikes the right balance between burden on the firm and benefit to members. Along with the earlier requirement for a majority of independent members, a five member IGC implies at least three independent members, including an independent Chair.

#### **Q8: Do you agree that an IGC should have at least five members?**

- 3.11** The majority of respondents agreed that an IGC should have at least five members. One respondent observed that with fewer than five members, firms would struggle to appoint an IGC with a sufficient diverse range of people and talents. Other respondents asked us to stress that five is a minimum number and that firms with larger and more complex schemes may need an IGC with seven or more members. A number of respondents were not convinced of the need to prescribe a minimum number and considered that any figure should be kept under review to see how IGCs work in practice.
- 3.12** Generally, respondents recognised the need to strike an appropriate balance between the cost of operating an IGC, which may ultimately be borne by policyholders, and having a range of views and expertise on the IGC.
- 3.13** A substantial minority of respondents disagreed with our proposal, but for different and opposing reasons. A small number of respondents preferred the original, higher minimum of seven members. Other respondents had concerns about the cost of IGCs and wanted a smaller minimum number. One respondent which is a mutual highlighted the fact that policyholders would be paying for the operation of the IGC. In this respondent's opinion, a three-member IGC would be sufficient where scheme assets are low or where it is difficult to cultivate employee and employer engagement, which means all the members may be paid professionals.
- 3.14** One respondent observed that it would be more appropriate to require a minimum number of members to form a quorum. Ultimately, any IGC must be judged on the outcomes for scheme members, not on the number of people that have contributed.

#### **Our response**

We acknowledge the range of views on this issue. We remain of the view that a minimum of five members strikes the right balance between the cost of operating an IGC and having a range of views and expertise on the IGC. We will proceed with our final rules on this basis but will keep this requirement under review.

We consider in Chapter 6 alternative arrangements for providers of smaller and less complex workplace personal pension schemes.

We note that some schemes may find it difficult to cultivate employee and employer engagement. In our view, that is exactly where a strong IGC is most needed.

We have considered whether there is a need to specify a minimum number of IGC members to form a quorum. We are concerned that, with some IGC members unavoidably absent, the independent members may no longer be in the majority for a particular IGC meeting. Therefore, we will require that a quorum comprise a minimum of two independent members and must have a majority of independent members.

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### Definition of independence

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- 3.15** The definition of ‘independence,’ for the purposes of determining which persons qualify as an independent IGC member, is relative of the person’s independence of the provider. The person must be free from any conflict of interest that might interfere with their capacity to act independently of the provider and in the interests of relevant scheme members.
- 3.16** The definition of ‘independence’ in the DWP’s Command Paper, published in March 2014, required that an independent IGC member must not:
- be an employee of the provider or scheme or paid by them for any role other than that which they fulfil on the trustee board/IGC
  - have been an employee of the provider or group within the last five years, and
  - have, or have had within the last three years, a material business relationship with the company.
- 3.17** A number of firms represented to us that these proposed requirements would be too restrictive, in the context of a limited pool of candidates with sufficient expertise and experience to be on an IGC.
- 3.18** In CP14/16, we proposed modifying the definition of independence in the DWP’s Command Paper to allow firms to appoint trustees of the firm’s master trust to the IGC as independent members.
- 3.19** We did not propose extending this to allow firms to appoint individuals to the IGC as independent members when they are also members of other committees within the firm, even if acting in a non-executive capacity on those other committees.
- 3.20** We clarified that, as proposed, the same person may serve on more than one IGC as an independent member. We considered that there may be valuable read across between IGCs operated by different firms. This would include the situation where firms within the same corporate group each have established an IGC, rather than using a group-level IGC.

**Q9: *Do you agree with our proposed definition of independence that would allow trustees of a firm’s master trust to be independent IGC members?***



- 3.21** The majority of respondents agreed with our proposed definition of independence and considered it a sensible compromise. Most felt that the trustees of a firm's master trust should be considered eligible for appointment to the IGC as independent members, provided that they otherwise meet our definition for independence. Respondents agreed that trustees of the firm's master trust may bring valuable read across to the IGC and vice versa.
- 3.22** A few respondents expressed concern about the potential for 'capture' by the provider of individuals with multiple independent roles. One respondent observed that a trustee could be chosen by the provider for their track record of acquiescence.
- 3.23** A number of firms responding to our proposal considered that our proposals were too restrictive and would limit the pool of expertise available for the independent members of IGCs. Some made the point that with-profit committees (WPCs) also consider value for money issues and that independent members of WPCs should be eligible as independent IGC members.
- 3.24** Our proposed guidance would preclude as independent IGC members those persons paid by the provider for any other role, or who had been so paid within the last three years. One respondent considered it unreasonable that providers with the foresight to have already set up independent governance structures, with independent members, should find those members excluded from being independent members of the IGC. This is because they would have been paid for their independent role on the other governance structure, despite otherwise being eligible for independent membership of the IGC.

### Our response

We continue to think that trustees of a firm's master trust should be eligible as independent members of the firm's IGC, provided that they meet our definition of independence. We note that to meet our definition, such trustees would in all probability be non-affiliated trustees. The DWP proposed regulations would mirror our definition and would allow independent IGC members to be considered for appointment as non-affiliated trustees.

While we acknowledge that independent members of WPCs and other governance committees may also bring valuable read across to a firm's IGC, and may face related challenges, we do not intend to widen our definition of independence. This is because of the potential of 'self review' and other conflicts between the roles.

We have sympathy with the provider that has already set up a committee that includes independent members and is similar in nature to an IGC. Our definition of independence is intended as guidance for providers and there may be situations where a provider is able to justify a different approach. It will be for the provider to determine whether such a member is independent in character and judgment and whether there are relationships or circumstances which are likely to affect, or could appear to affect, that member's judgement.

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### Fiduciary duty

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- 3.25** Our proposed rules require firms to establish committees to provide independent oversight of the firm's workplace personal pension schemes. While established as a committee of the firm, the IGC will have a clear duty to act independently of the firm.
- 3.26** Since we are not able to regulate IGCs directly, we propose requiring firms to make contractual arrangements for IGCs, with mandatory content to be included in the IGC's terms of reference. This content would include minimum duties on the IGC, with a duty to act in the interests of relevant scheme members and to assess the value for money of relevant schemes. The terms of reference for IGCs are covered in more detail in Chapter 4.
- 3.27** A small number of respondents proposed that a fiduciary duty be placed directly on providers. In their view, this would be the only way to align the interests of pension schemes with those saving into them. Pension providers would have a duty to prioritise the interests of savers above all others, with this duty policed by trustees.

#### Our response

The use of the term 'fiduciary duty' has caused difficulty, as it is often used in a manner inconsistent with the law. We believe that existing FCA rules and principles provide fiduciary-like protections, as noted in the recent Law Commission report on fiduciary duties on investment intermediaries.<sup>11</sup>

Our rules will provide regulatory force to the ability of IGCs to act independently and effectively in the interests of scheme members. Our regulatory grip is over the providers. Should we find that providers are not operating effective IGCs to improve the value for money of their schemes, we will consider further changes to our rules.

At this time, we will proceed with our proposed approach, whereby IGCs will be established by firms but with a contractual duty to act independently of the firm and in the interests of relevant scheme members.

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### Indemnification of IGC members

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- 3.28** We have previously considered whether there should be a requirement on firms to indemnify individuals against liabilities incurred in their capacity as IGC members. This followed a recommendation from the Law Commission that firms should be required to indemnify IGC members.
- 3.29** In our view, scheme members would appear more likely to pursue the firm than the IGC, since the firm remains responsible for any actions taken and changes made to schemes. Nonetheless, persons seeking appointment to an IGC may request such indemnification and firms may choose to offer it. We consider it likely that firms will choose to offer it, to provide all possible reassurance to IGC members and to widen the pool of candidates.

<sup>11</sup> [http://lawcommission.justice.gov.uk/docs/lc350\\_fiduciary\\_duties.pdf](http://lawcommission.justice.gov.uk/docs/lc350_fiduciary_duties.pdf)

- 3.30** In CP14/16, we proposed guidance that firms should consider indemnifying IGC members against any liabilities incurred while fulfilling their duties as IGC members. However, we did not believe it necessary to make this a requirement under our rules.

**Q10: Do you agree that we should not require firms to indemnify IGC members?**

- 3.31** There was a roughly even split of respondents between those who agreed that there was no need to make indemnification a requirement and those who thought that we should. A number of respondents noted that providers would be likely to offer indemnification to those candidates requesting it and that some candidates may carry their own indemnity insurance.
- 3.32** A number of respondents felt strongly that we should require providers to indemnify IGC members. The main reason given was that a lack of protection could leave IGC members financially vulnerable on a personal basis, which could deter credible candidates from coming forward and might cramp existing IGC members in their willingness to take decisive action in the interests of scheme members as a whole.

### Our response

We have considered carefully the arguments for and against a requirement on firms to indemnify IGC members.

We note that the Law Commission's recommendation was alongside a recommendation that a statutory duty be placed on IGC members to act in scheme member interests. If under a statutory duty to scheme members, IGC members might be liable to action from scheme members. However, under our rules, the duty to act in the interests of scheme members will be contractual and between the IGC member and the provider. Further, IGCs will be raising concerns and making recommendations to the boards of providers, and will be unable to take direct action since the pension contracts exist between the provider and the individual policyholders.

Our view remains that scheme members would seem more likely to pursue the provider rather than individual IGC members or the IGC collectively. We find it difficult to see a basis on which a personal liability for IGC members would arise, unless it was specifically written into their contract. There would not be a common law duty of care or contractual relationship between an IGC member and a pension scheme member; nor would a breach of the rules, which apply to the firm, create a private law remedy under the Financial Services and Markets Act 2000 (FSMA) as against individual IGC members.

Therefore, we are not convinced of the need to require providers in an FCA rule to indemnify IGC members. We agree that providers are likely to indemnify anyway, if they need to do so to appoint credible candidates. Moreover, some individuals will already carry their own indemnity insurance or will be indemnified through their employment, eg, as a professional trustee.

We acknowledge that the lack of indemnification may nonetheless deter some candidates from coming forward. We will include guidance to the effect that firms should consider offering indemnification or insurance against personal liabilities arising from IGC membership.

### Approved persons

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- 3.33** We previously considered whether one or more of the members of the IGC should be approved persons, to increase our regulatory control over IGCs. If one or more roles on the IGC were controlled functions, this would allow us to determine whether a candidate is a fit and proper person to carry out the function for which they are proposed. In addition, it would give us increased powers to intervene, where an IGC is not acting in line with our rules or its terms of reference.
- 3.34** However, we took on board stakeholder concerns that making the IGC Chair and/or other IGC members approved persons might deter potential candidates from seeking appointment, because of the additional responsibilities. Further, the cost to firms may be higher because the compensation of IGC members may need to reflect their additional responsibilities.
- 3.35** In CP14/16, we did not propose making any role on the IGC a controlled function at this time. We said that if, in the future, we believed that IGC members, and in particular IGC Chairs, are not suitably qualified or performing their duties correctly, we may consider requiring that one or more members of IGCs be approved persons.

**Q11: Do you agree that members of the IGC, including the IGC Chair, should not be approved persons at this time?**

- 3.36** Most respondents agreed that making the Chair or other roles on the IGC controlled functions (ie, the holder would be an approved person) would further reduce the pool of eligible candidates for appointment to IGCs. A number of respondents thought that we should keep this under review.
- 3.37** Some respondents disagreed, on the grounds that approved person status would help ensure that candidates have the expertise and understanding to tackle complex issues in the assessment of value for money. One respondent commented that being an approved person focuses the mind.

#### Our response

We remain of the view that members of the IGC, including the IGC Chair, do not need to be approved persons at this time. If, in the future, we find that IGC members are not suitably qualified or performing their duties correctly, we may reconsider our position.

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### Appointment of IGC members

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- 3.38** An IGC's independence is crucial to its ability to challenge the firm effectively on value for money issues. We recognise the potential for conflicts of interest in the appointment process; for example, firms might seek to appoint 'independent' members who may not put the interests of scheme members first.
- 3.39** In CP14/16, we proposed making it a requirement on firms to ensure an open and transparent appointment process of independent IGC members. We proposed guidance that firms can meet this requirement through the use of an external search consultancy or open advertising. We also said that we would expect firms to involve the IGC Chair in the appointment of other IGC members, both independent members and employees of the firm.

**Q12: Do you agree that we should require firms to recruit independent IGC members through an open and transparent recruitment process?**

- 3.40** There was close to unanimous agreement that we should require an open and transparent recruitment process of independent IGC members. One respondent observed that this is preferable to an 'unworkable' election process. Another took the view that the most open and transparent process would be an election process. There were strong concerns that a 'private' or 'closed' appointment process would result in the appointment of members with personal ties or obligations to those making the appointments.
- 3.41** A number of respondents agreed, but wanted to see the recruitment of independent members from employees and employers contributing to the scheme.
- 3.42** Some smaller providers responding to the consultation had concerns about the cost of the use of an external search agency or open advertising. Some agreed with the proposals for IGCs, but contingent on there being sufficient opportunity for smaller providers to use governance advisory arrangements (GAAs), which are an alternative arrangement for the providers of smaller and less complex workplace personal pension schemes. We consider GAAs in Chapter 6.

### Our response

We continue to believe that an open and transparent recruitment process is fundamental to the credibility and independence of IGCs. Scheme members must have visibility of the process and confidence in the appointments.

We consider that two good ways of fulfilling our requirement for an open and transparent recruitment process will be through the use of an external search agency or open advertising. However, these two ways will remain as guidance, rather than a rule. We do not see the need to be overly prescriptive in how firms should achieve the good outcome that we seek.

We support the recruitment of independent members from employees and employers contributing to the scheme, as well as from deferred members, but we are conscious of the practical difficulties in attracting suitable candidates and/or organising elections. As such, we do not intend to make this a requirement at this time.

We have considered the risk that IGC members are appointed as independent members, but subsequently take on other responsibilities with the provider that may compromise their independence. Therefore, we will include guidance that the firm should review on a regular basis whether its independent IGC members continue to be independent and take appropriate action if it considers that they are not.

### Duration of appointment

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- 3.43** There is a risk that, without any restriction on the duration of appointment, independent IGC members become too 'close' to the firm that appointed them. We considered that there would be merit in capping the overall duration of appointment, with a limit to each term of appointment.
- 3.44** In CP 14/16, we proposed that independent IGC members be appointed for fixed terms of no longer than five years, with a cumulative maximum duration of ten years, unless that member is a corporate person. Individual independent IGC members would not be eligible for reappointment to the IGC until five years have elapsed, after having served on the firm's IGC for the cumulative maximum duration of ten years.
- 3.45** We also proposed that firms manage appointments to maintain the continuity of the IGC's expertise and experience, for example through staggered terms of appointment. We said that we would expect firms to replace any vacancies that arise within IGCs as soon as possible and, in any event, within six months.

**Q13: *We would welcome views on the proposed duration of appointment of IGC members.***

- 3.46** Almost all respondents agreed that the overall duration of appointments should be capped and that terms should be limited. The majority of respondents considered that our proposals for a cumulative maximum duration of ten years, and fixed terms of no more than five years, seemed to strike the right balance between a member becoming effective in the role and continuing to challenge the firm.
- 3.47** A few respondents considered a maximum term of five years too long and preferred the original proposal in the DWP's March 2014 Command Paper, with terms of no more than three years and members eligible for reappointment twice (in other words, a cumulative maximum duration of nine years). This is in line with the UK Corporate Governance Code. Others commented that three years would be too short, since members need enough time to make a difference.
- 3.48** One respondent made a strong argument for not allowing reappointments, on the basis that the member would have an incentive to seek favour from those deciding on his or her reappointment. That incentive might compromise their effective challenge of the provider on behalf of members. The respondent also made the point that provider employees on the IGC would be in a position to monitor the behaviour of non-independent members and report this to the provider's board and those with influence over the reappointment process.
- 3.49** A small number of respondents felt that providers would still have too much control over IGC appointments. Particular concerns on this and the previous question were that the final selection and appointment would be up to the provider, and that the possibility of reappointment gives members the incentive to seek favour from those deciding their reappointment.
- 3.50** One respondent commented that they would like to see a requirement that the IGC Chair be involved in the selection of IGC members, including those members representing the firm. Another respondent commented that they would expect the board's nomination committee to monitor the performance and effectiveness of IGC members.

### Our response

We are pleased that respondents generally agreed with the principle of a cap on the duration of appointment.

We acknowledge the concern that the possibility of reappointment may result in a member seeking favour from those who decide on his or her reappointment. However, we consider a single fixed term of more than five years too long, since there is also a risk that individuals become 'comfortable' in the role and cease to challenge effectively. We note that the reappointment process would also be open and transparent, and subject to scrutiny.

Having not been convinced to the contrary, we will proceed with our proposals for fixed terms of no longer than five years, with a cumulative maximum duration of ten years, unless that member is a corporate person.

We consider that the appointment of the Chair is particularly important for the IGC to be able to raise effective challenge to the provider's board. There may be ways to take the appointment (and removal) of the Chair out of the control of the provider's executives. For instance, the non-executives of the provider's board, or the board's nomination committee, could be given oversight of the process. However, we do not intend to prescribe the appointment process at this time.

On removing the possibility of reappointment, we think it unlikely that individuals would want to commit to unduly long terms upfront and long terms may result in provider 'capture' of individuals in any event. In our view, an open and transparent reappointment process will mitigate the incentive for members to seek favour from those deciding their reappointment. Therefore, we do not intend to rule out the possibility of reappointment of IGC members at this time.

### Corporate persons as IGC members

- 3.51** There are a number of potential benefits to allowing corporate persons, such as firms providing trustee services, as IGC members. These include:
- **high levels of professionalism and consistency**, where corporate persons provide similar services in their normal course of business
  - **improved access to research and insights** from across the pensions market, where corporate persons have central resources, and
  - **individuals representing a corporate person can be more readily replaced** if they are no longer able to be the representative on an IGC.
- 3.52** However, we recognised that some corporate persons may have, or have had, other business relationships with the appointing firm. Therefore, there would be the potential for a conflict of interest that might affect the independence of the corporate person.

- 3.53** In CP14/16, we proposed that firms should be allowed to appoint corporate persons to an IGC, including as Chair, provided that the corporate person is independent of the firm. We said that we would expect the firm to consider the circumstances of the corporate person and ensure that any potential conflicts of interests are managed effectively and do not affect the corporate person's ability to represent the interests of scheme members.
- 3.54** We did not consider that there should be an overall cap to the duration of a corporate appointment, because the named individual can be changed. Further, we did not want to prevent firms from accessing a limited pool of organisations capable of acting as IGC members by being overly restrictive on their reappointments.
- 3.55** Therefore, we proposed that, where a corporate person is appointed as an IGC member, the firm should ensure that the corporate person's representative is named and is rotated at least as frequently as would be required for an independent individual IGC member, but with no restriction on the duration of the corporate appointment.

**Q14:** *Do you agree that we should permit the appointment of corporate persons to IGCs, including as the IGC Chair?*

**Q15:** *Do you agree that there should be no restriction on the duration of a corporate appointment?*

- 3.56** Of those who responded to these questions, the majority agreed with our proposals for corporate persons as IGC members. Respondents felt that there were substantial benefits in having professional trustee bodies as corporate persons on IGCs. Some respondents sought clarification as to whether or not a corporate person could fill more than one position on the IGC.
- 3.57** While in favour of our proposals, a number of respondents were concerned about the faceless nature of a corporate entity. Comments included 'people should be represented by people.' These respondents sought individual accountability, with a named individual representing the corporate person and identified to scheme members.
- 3.58** A minority of respondents felt that corporate persons should not be permitted on IGCs because of a perceived lack of individual accountability and/or the potential for conflicts of interest. One respondent considered that any third party supplying services to the firm should not be considered for appointment as an independent member of the firm's IGC. In this respondent's view, providers should not be relied upon to police 'Chinese walls' that the third party might have in place to manage any conflict of interest, because the provider itself might benefit from any breach of the wall, in that its IGC may be less willing to raise effective challenge.
- 3.59** Most respondents were satisfied with an unlimited duration of corporate appointments, provided that the individual representing the corporate person is rotated as proposed. However, a number considered that the corporate person should be subject to periodic review and a re-tender process. One respondent argued for a single term for both corporate and individual members, on the grounds that the potential for reappointment would skew their incentives away from effective challenge on behalf of scheme members.



## Our response

We have considered the responses for and against the use of corporate persons as independent IGC members. We continue to believe that corporate persons can bring substantial benefits to an IGC.

We agree that there is a risk that a corporate person is perceived as ‘faceless’ by scheme members and may deter them from engaging with their IGC. We will expect the provider to ensure that any corporate person nominates an individual to represent them on the IGC. A named individual will also provide continuity and allow for the accumulation of firm-specific experience.

We share the concern expressed by some respondents that a third party doing other business with the provider may face a potential conflict of interest. We are aware of a situation where a third party has ruled themselves out of a possible IGC position as an independent member because of the potential perception of a conflict of interest.

We intend to focus on the outcome we seek, which is that any corporate person must act independently of the provider in representing the interests of scheme members. Therefore, we will expect the provider either to appoint a corporate person free from potential conflict or to ensure that any potential conflicts are managed effectively. To the extent that the provider is in doubt of the third party’s ability to do this, the provider should not make the appointment.

As to whether or not a corporate person may fill more than one role on the IGC, we proposed in our consultation paper that the appointment of a corporate person to an IGC should count as a single appointment. We do not intend for the same corporate person to be appointed multiple times to the same IGC. This is because we seek a diversity of viewpoints on an IGC and the named individuals from the same corporate person may share the same corporate view.

We can see the argument for a periodic review of a corporate appointment and a re-tender process. Providers may wish to consider this, in the context of their responsibility to ensure the effective functioning of their IGC. However, we recognise that there may be a limited pool of organisations capable of acting as IGC members and do not intend to limit the duration of a corporate appointment in our rules at this time.

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## 4.

# Terms of reference for IGCs

- 4.1** This chapter summarises feedback received on our proposed minimum terms of reference for IGCs and provides our response to that feedback.

### Duty to act in member interests

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- 4.2** We continue to recommend a requirement for minimum terms of reference for IGCs. These would impose a duty on IGCs to act in the interests of scheme members and challenge providers on the value for money of their workplace pension schemes.
- 4.3** Whereas under FCA rules the provider already has a duty, in relation to investment business carried on for its client, to act honestly, fairly and professionally in accordance with the best interests of its client, it also has a duty to its shareholders to act commercially. We intend that the duty on the IGC will be to act solely in the interests of scheme members.
- 4.4** In CP14/16, we recognised that there may be situations where conflicts of interest exist across different groups of scheme members. Rather than prescribing how an IGC should address conflicts of interest, we will expect the IGC to manage any conflicts that arise. This will include how the IGC prioritises its work across potentially many schemes and diverse groups of members.

### Duty to assess value for money on an ongoing basis

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- 4.5** The primary purpose of an IGC is to act in the interests of scheme members in assessing and raising concerns about the value for money of the provider's workplace personal pension schemes.
- 4.6** In CP14/16, we said that we would expect IGCs to consider, in particular, the value for money received by individuals enrolled in default strategies.<sup>12</sup> This is because consumers not making any active choice will be automatically enrolled into the default. These disengaged consumers will be in the greatest need of protection. Moreover, the default will be likely to contain the most scheme members.
- 4.7** Nonetheless, we considered that IGCs should have a wide remit to consider all the choices available to scheme members, to help protect against the possibility of members making poor decisions. Non-default funds have the potential to be poor value relative to the default, since they may have high fund-management charges and transaction costs, in particular where actively managed, and the proposed charge cap relates to default funds only.

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<sup>12</sup> both value for money of the default fund and of scheme administration

- 4.8** We proposed that, at a minimum, IGCs must assess whether the characteristics and net performance of all investment strategies (including non-default investment strategies) are regularly reviewed by the firm, to ensure alignment with the interests of scheme members. Beyond this minimum requirement, we thought that IGCs should determine their own priorities, subject to their terms of reference and having regard to the interests of workplace personal pension scheme members.
- 4.9** We recognised that it may not be practical or cost effective for the IGC to assess the value for money of each employer's scheme individually. An IGC may want to consider grouping schemes with similar characteristics and assess value for money at the level of groups of similar schemes together. The IGC would still be able to drill down to the level of individual schemes.
- 4.10** We did not seek to prescribe in rules how IGCs should go about assessing value for money. Firms will have schemes with different characteristics and it will be for each IGC to determine how best to undertake its assessment.
- Q16:** *Do you agree that IGCs should consider, in particular, the value for money received by individuals enrolled in default funds?*
- Q17:** *Do you agree that, at a minimum, IGCs must assess whether the characteristics and net performance of all investment strategies are regularly reviewed by the firm?*
- Q18:** *Do you agree that, rather than mandating a particular approach, we should allow individual IGCs to determine how best to assess value for money?*
- 4.11** Respondents were close to unanimous in agreeing that IGCs should consider, in particular, the value for money received by individuals enrolled in default funds. One respondent commented that they very much liked this simple formulation, focused on the outcome for the scheme member and without prescribing detailed characteristics for schemes. Another commented that, with over 90 per cent of scheme members invested in the default for the duration of their membership, this should be the focus for IGCs.
- 4.12** A number of respondents noted that vertically-integrated providers may use internal funds when designing a default strategy and that IGCs should be aware of the conflict of interest. Some respondents sought clarification on whether the focus should be on provider-specified default strategies only or whether it should also include default strategies specified by investment consultants or other advisers to employers.
- 4.13** While the majority agreed that, at a minimum, IGCs must assess whether the characteristics and net performance of all investment strategies are regularly reviewed by the firm, there was a focus on the words 'at a minimum'. A number of respondents thought that IGCs should do more than ensure that the provider conducts regular reviews. These respondents thought that the IGCs should itself oversee the reviews to ensure that they are done objectively.
- 4.14** Other respondents did not think it realistic that the IGC should be expected to review the many funds that the members of different schemes might have access to. One made the point that an investment strategy is different from the component funds, which are building blocks for the strategy. Where a provider offers a wide choice of funds that simply provide investment exposure of different kinds, this respondent questioned whether significant scrutiny of the funds would be good use of an IGC's time.

- 4.15** A theme emerging from the responses was that we should develop guidance for IGCs on assessing value for money. While most respondents agreed that we should not mandate a particular approach, many felt that an FCA framework would help with consistency. A few respondents observed that it would be better for us, rather than providers, to take the lead in developing guidance for IGCs on assessing value for money.
- 4.16** One respondent was concerned that IGCs would find it extremely difficult to manage conflicts of interest between members of different schemes and within schemes. Each IGC would need to explain how it managed such conflicts and have a strategy for doing so. The respondent thought that FCA guidance on this issue would be needed.

### Our response

We are pleased that respondents agree that the value for money of default strategies should be a focus for IGCs. We consider that this is vital, given the characteristics of scheme members enrolled in default strategies. We intend to proceed with the proposed policy approach.

We will require that the minimum terms of reference for an IGC include a requirement to assess whether default investment strategies are designed in the interests of policyholders. Previously, we had referred in the proposed rules to '*the firm's* default investment strategies'. However, we did not intend to exclude those default strategies specified by investment consultants or other advisers to employers. We believe that these also should be subject to the IGC's scrutiny. Therefore, we will remove the qualifier '*the firm's*' and refer to 'default investment strategies' in the final rules.

We have considered carefully whether to require the IGC to review all investment strategies, rather than requiring that the IGC ensure that all investment strategies are regularly reviewed by the firm. Given the other calls on an IGC's time, and the focus on default strategies, we have decided not to require the IGC to review all investment strategies, since such a requirement would apply to every IGC. Nonetheless, an IGC may recommend to the provider that the IGC should review all investment strategies, in the interests of relevant scheme members, and, if the provider refuses to support this, may escalate that refusal to us.

Value for money means different things to different people. While there is a substantial body of literature on the subject, there is no clear framework for how to go about assessing the value for money of workplace pension schemes. We intend to hold a forum for IGC Chairs at around the time that our rules become effective in April 2015, when we will start discussions about how to assess value for money.

We will seek a consistent approach across trust and contract-based schemes in the assessment of value for money and we will be working closely with the DWP and TPR in the support that we provide.

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### Scheme quality and minimum governance standards

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- 4.17** An assessment of value for money involves weighing up the quality of the scheme, by which we mean the benefits and services it provides, against what it costs scheme members. The assessment also needs to consider whether the members of a particular scheme need and want each of the different benefits and services provided. If scheme members do not need or want a particular benefit or service, it is hard to see how that benefit or service can deliver value to them, regardless of what it costs them.
- 4.18** There are some aspects of scheme quality which we believe are fundamental to members receiving adequate protection. Based on our experience of supervising firms, and our work with the DWP, we believe that good governance must include an assessment of whether:
- default investment strategies are designed in the interests of scheme members, with a clear statement of aims, objectives and structure appropriate for scheme members
  - the characteristics and net performance of investment strategies (including non-default strategies and/or funds made available to scheme members) are regularly reviewed by the firm to ensure alignment with the interests of scheme members, and action taken to make any necessary changes, and
  - core scheme financial transactions are processed promptly and accurately.
- 4.19** In CP14/16, we proposed that that the terms of reference must require IGCs, as a minimum, to assess these three aspects of the services provided to members of workplace personal pension schemes.
- 4.20** We recognise that providers may include additional services, guarantees, bonus payments or other benefits, to differentiate their proposition to employers and scheme members. Further, the various schemes of an individual provider may differ in the terms and conditions of services offered to the workforces of different employers.
- 4.21** Since IGCs should be able to assess the overall value for money of services provided to members of workplace personal pension schemes, we did not believe that they should be restricted in the range of services they review. Instead, we proposed that IGCs should be able to determine which other services they consider.
- Q19: *Do you agree that IGCs should be required, at a minimum, to review the three aspects of scheme quality proposed, and should consider other aspects as appropriate?***
- 4.22** Respondents generally agreed that IGCs should be required to review the three aspects of scheme quality proposed and most considered this critical to any assessment of value for money. Respondents also agreed that IGCs should not be limited to these three aspects and should consider other aspects, as appropriate.
- 4.23** A theme running through the more detailed responses was the need for IGCs to look at the quality of member communications. Some respondents also commented that IGCs should consider compliance with relevant regulation and legislation, and the impact of changes to legislation. There was a consensus that IGCs would need to look more broadly than the design and performance of investment strategies.

- 4.24** Some respondents pointed to the performance of third-party service providers as an area for IGC investigation. Performance against service level agreements should be considered and third-party agreements assessed for value for money. One respondent considered that IGCs need to consider environmental, social and governance (ESG) factors on behalf of scheme members.
- 4.25** A number of respondents thought that value for money in decumulation should be a mandatory focus for IGCs, in particular the information and support that scheme members receive at retirement.

### Our response

We are satisfied that the three aspects of scheme quality proposed are important to an assessment of the value for money of workplace pension schemes. We confirm our intention to require IGCs to review at least these three aspects of scheme quality in their assessments of value for money.

The effectiveness of member communications, including member support beyond mandatory disclosure requirements, is clearly important to improving scheme member engagement and pension outcomes. To the extent that the costs of communications are borne by the scheme member, this must be part of the IGC's assessment of value for money. Where the employer pays, we see this as a type of employee benefit and not necessarily within scope for an IGC.

In assessing value for money, we would expect IGCs to consider all the benefits and services that scheme members pay for in costs and charges, either directly or indirectly. The three aspects of scheme quality that we identify should not be considered the only aspects that an IGC will need to assess. An IGC will need to weigh up all the benefits and services delivered relative to their cost to scheme members, in the context of an assessment of whether members need and value each benefit or service.

We observe that many legacy schemes have complex charging structures which may benefit some pension savers while others may lose out. Further, different employers have workforces with various characteristics and pension-saving needs. IGCs will need to consider carefully a variety of factors in assessing value for money and calibrating recommendations to the profile of a scheme's membership.

We welcome the feedback on other aspects of scheme quality that IGCs may consider in assessing value for money. We recognise, in particular, the importance of decumulation strategies and retirement income options, as well as the behaviour of the provider around and in advance of retirement, to pension outcomes for scheme members. We consider these issues later in this chapter when discussing priorities for IGCs.

A theme for our policy statement is that IGC members should not assume that they know what scheme members need and want. In this context, we would emphasise the importance of assessing member views on ESG factors and on the availability and use in the default of ethical and long-term social investments, while at the same time considering the risks and potential impact on pension outcomes. In Chapter 5, we discuss our proposed requirement that the firm must make arrangements for the views of members to be directly represented to the IGC.

### Costs and charges

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- 4.26** To assess overall value for money, IGCs will need to obtain from firms the costs and charges associated with the workplace personal pension schemes that they operate.
- 4.27** The government's proposed 75 basis point charge cap will help protect scheme members invested in default funds of qualifying schemes.<sup>13</sup> However, the cap is not intended to set a market price and we expect many schemes will charge at levels beneath the cap. IGCs will need to consider whether charges are appropriate for the services provided to scheme members.
- 4.28** When a member chooses a non-default investment strategy, or is invested in a scheme which is not used as a qualifying scheme by their employer, higher costs and charges may apply. We would expect IGCs also to ask firms to provide them with details of relevant costs and charges of these funds and schemes.
- 4.29** All funds, including default funds, are subject to varying levels of explicit and implicit transaction costs. These are considered later in this chapter, under the heading 'improving transparency of all costs and charges'.
- 4.30** In CP14/16, we proposed that IGCs must assess the level of charges borne by scheme members and all costs (direct and indirect) incurred in relation to transactions and other activities in managing and investing the pension assets of scheme members.

***Q20: Do you agree that IGCs should consider all costs and charges, as proposed? If not, what would you suggest?***

- 4.31** Respondents providing feedback were unanimous in agreeing that IGCs should be required to consider all costs and charges, including transaction costs.
- 4.32** Many respondents recognised the difficulty in obtaining all relevant transaction costs from investment managers. One respondent observed that 'while, on the face of it, it seems conceptually simple to identify all transaction costs, it is in fact notoriously difficult.' Another respondent noted that the disclosure of investment management charges and transaction costs must be meaningful and helpful for IGC members in their decision making.
- 4.33** A number of respondents made the point that both contract-based workplace pension schemes and occupational schemes face this difficulty and that we will have an important role in making sure that transaction-cost information is provided in contract-based schemes.
- 4.34** Some respondents highlighted the need to weigh costs and charges against the level and quality of services being provided. Others pointed to the need to consider all benefits attaching to some legacy schemes, such as guaranteed annuities. One respondent observed that the costs of IGCs need to be included in the measurement.

<sup>13</sup> Better workplace pensions: a consultation on charging CM8737, published March 2014 [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/254332/cm8737-pension-charges.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/254332/cm8737-pension-charges.pdf)

### Our response

We consider it vital that IGCs should be able to assess value for money in the light of all the costs and charges that may impact on a scheme member's pension outcome. We will require IGCs to assess the level of charges borne by scheme members and all costs (direct and indirect) incurred in relation to transactions and other activities in managing and investing the pension assets of scheme members.

We acknowledge there may currently be difficulties in identifying and obtaining information about transaction costs. However, that must not prevent IGCs and trustee boards from pursuing this information which will enable a comprehensive assessment of value for money for pension savers.

There is a distinction to be made between the costs and charges that impact on a scheme member's pension outcome and the costs that the provider or third-party provider may incur in supplying services. The latter costs are borne by the providers. IGCs should be primarily concerned with the costs and charges that impact on the scheme member's pension outcome. The level of detail of costs and charges that impact on the scheme member's pension outcome, rather than being borne by the provider or third party provider, will depend on the particular charging arrangements.

In assessing value for money, IGCs should consider whether costs and charges borne by scheme members pay for services that deliver value to scheme members. The IGC will need to take into account the characteristics of scheme members enrolled in a default strategy to determine whether a particular service is likely to deliver value for them.

We agree that the emphasis should be on obtaining an appropriate balance between quality and cost, rather than simply the lowest cost.

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### With-profits funds and legacy schemes

- 4.35** We already require firms managing with-profits funds to establish a with-profits committee (WPC) or, where appropriate, an alternative advisory arrangement to represent the interests of all with-profits policyholders. As part of their remit, WPCs should assess the charges incurred by the with-profits fund. We expect an IGC to work with the arrangements already in place for with-profits funds, and make use of information from and/or provided to the IPC, to minimise overlap and duplication of activities.
- 4.36** In CP14/16, we proposed that IGCs should have the flexibility to decide how to work alongside existing arrangements for with-profits funds. The characteristics and cost allocations of with-profits funds will differ between firms. Therefore, individual IGCs are best placed to decide how to assess the costs and charges of the funds for which they provide oversight, on behalf of pension scheme members.
- 4.37** While we did not ask a specific question on with-profits funds and legacy schemes, one respondent asked for clarification on whether a WPC could be combined with an IGC.



### Our response

The remit of a WPC is focussed on the provider's with-profits funds and, in particular, on ensuring that the provider manages effectively the conflicting rights and interests of with-profits policyholders and other policyholders or stakeholders, including, if applicable, shareholders. An IGC, on the other hand, has a remit centred on the value for money of the provider's workplace personal pension schemes and has a duty to act solely in the interests of scheme members. While we would expect a provider to facilitate the sharing of information, to avoid duplication of activities, we do not consider that a WPC can be combined with an IGC.

### Improving transparency of all costs and charges

- 4.38** Because of their impact on the returns delivered to investors, it is important that all costs and charges are identified and quantified so the full costs of investment services can be made clear. In the DWP's March 2014 Command Paper, the government outlined a vision for workplace pension schemes that will involve full transparency of all costs and charges throughout the value chain in a way that enables pension scheme managers, and IGCs or trustees, to compare value across the market and identify the best deal for scheme members.
- 4.39** The Pensions Bill 2014 places a duty on the Secretary of State and FCA to require the disclosure of information about transaction costs and administration charges of workplace pensions. Although some costs will be predictable, many costs are expected to vary, especially costs incurred for transactions and other activities in managing and investing pension assets.
- 4.40** If pension scheme operators are not aware of all the costs, including transaction costs, they will be required, wherever possible, to obtain the information from the other suppliers in the value chain for the assets in which pension scheme monies are invested.
- 4.41** In CP14/16, we proposed rules that will require public disclosure by firms of their IGC's assessments in the IGC Chair's annual report, to enable IGCs to compare their assessments with those of other IGCs. We outlined our proposed approach to improving the way cost information is disclosed by firms.

**Q21: *We would welcome views on how best to improve the disclosure of all costs and charges, and how we could transpose the industry standards for authorised funds to pensions.***

- 4.42** Respondent views reflected the complex and technical nature of the challenge. A number of respondents made the point that life funds may be organised as funds of funds, with multiple layers, and with costs allocated algorithmically. Authorised funds tend to be simpler. It may be difficult to transpose the industry standards for authorised funds to life funds in which pension assets are held.
- 4.43** Some respondents considered that the government or the FCA needs to mandate disclosure by the fund management industry. This would complement the requirement on IGCs and providers to obtain the information and help ensure that it is supplied on a consistent basis.

- 4.44** A number of respondents, while in favour of disclosure, had concerns that a narrow focus on transaction costs might drive behaviour that is not in the best interests of scheme members. For example, a cash equivalent fund with very low transaction funds might be perceived as best value, whereas transaction costs need to be considered in the context of the investment strategy and target returns. One respondent commented that the vast majority of scheme members will not understand transaction cost information.
- 4.45** One respondent considered that the UK should take the lead on transparency and set the template for Europe, rather than waiting for European agreement on transparency of general fund disclosures.

### Our response

We recognise the complex challenge in requiring the disclosure of all costs and charges in a way that is meaningful and useful.

We have work underway on this issue and have commissioned independent research to investigate the various transaction costs that arise when investors invest in pension scheme assets and funds. This work will also look at options for measuring and disclosing these costs.

In our view, the complexity of life funds and how they are structured should not act to prevent full transparency of costs.

We are working closely with the DWP. The timetable set by the government requires us to consult on draft rules by autumn 2015, but we will engage with stakeholders before then.

We are mindful of the need to take into account European-level initiatives. Both the Packaged Retail and Insurance based Investment Products (PRIIPs) Regulation and re-cast Markets in Financial Instruments Directive (MiFID II) will require, from December 2016 and January 2017 respectively, all costs and charges to be disclosed to retail investors at product and distribution level before an investment product is purchased.

### Raising and escalating concerns

- 4.46** IGCs must present a credible challenge to firms on value for money issues. Where they identify poor value for money, IGCs must be able to raise concerns and make recommendations as they see fit.
- 4.47** In CP14/16, we proposed that the terms of reference should require the IGC to raise its concerns with the firm's governing body, typically its board. The firm's board must be given a right to respond before the IGC takes its concerns further.
- 4.48** We also proposed a duty on firms to take reasonable steps to address any concerns raised by the IGC. If the firm does not follow any recommendations made by the IGC to address the concerns raised, the firm must give written reasons to the IGC. We consider this 'comply or explain' duty on the provider further in Chapter 5.

- 4.49** Where an IGC has raised concerns to the firm's board which, in the IGC's opinion, have not been addressed satisfactorily, we proposed that the IGC must be able to escalate its concerns to the FCA. Where appropriate, we may require the firm to take action. We also proposed that the IGC may alert relevant scheme members and employers, where the IGC sees fit, and make its concerns public.

**Q22: *Do you agree that IGCs should be able to escalate concerns directly to the FCA, alert relevant scheme members and employers, and make their concerns public?***

- 4.50** Almost all respondents expressing an opinion supported this proposal requiring that the IGC be able to escalate concerns.
- 4.51** A number of respondents considered that escalation should be a last resort. The provider should make every effort to remedy the situation first and the IGC should allow the provider to make this attempt before escalating.
- 4.52** Some respondents felt strongly that IGCs should be required to escalate any concerns to us first, before alerting relevant scheme members and employers and making concerns public. Respondents noted the potential reputational damage to the provider if the claims were without foundation. Other concerns related to the release of potentially confidential or commercially sensitive information and the wider impact on confidence in pension saving.
- 4.53** One respondent suggested that we should give guidance about the sort of concerns that would merit escalation. Similar suggestions were made by other respondents. These comments were not just about limiting the nature of concerns being escalated but about ensuring that IGCs feel empowered to escalate where appropriate.

### Our response

We consider that the force of regulation behind the escalation route will give IGC's 'teeth.' This, in turn, should result in providers being more willing to engage and respond to the IGC's concerns in the first place.

We expect the provider to take action on an IGC's recommendations and, where there is disagreement, to explain in the first instance to the IGC why it disagrees.

If an IGC is not satisfied with the provider's explanation, the IGC should be able to make material concerns public and/or escalate its concerns to the FCA, as it sees fit. We would expect an effective IGC to make robust recommendations and take appropriate action should the provider not take the necessary steps necessary to rectify the IGC's concerns.

An IGC will be required to notify us<sup>14</sup> in advance of making concerns public, including when it proposes to alert relevant scheme members and employers. This will enable us to provide guidance to IGCs on whether and how to make the concerns public. Where material concerns have been raised, we would also expect the firm (under their Principle 11 obligations) to have raised the issue with us in the course of the firm's regular engagement with us.

<sup>14</sup> Under Principle 11 of the FCA handbook, 'Relations with Regulators' <http://www.fshandbook.info/FS/html/FCA/PRIN/2/1>

As outlined earlier, we intend to hold a forum for IGC Chairs around the time that our rules become effective in April 2015. At this forum, we intend also to discuss the process for escalating concerns to us and the extent of our remit in responding to escalated concerns.

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### Requirement to produce an annual report

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- 4.54** The publication of IGC annual reports should increase transparency and encourage comparison between schemes provided by different firms. In addition, it will enable interested scheme members, employers and consumer groups to scrutinise an IGC's work and the provider's response to any concerns raised or recommendations made.
- 4.55** In CP14/16, we proposed that the terms of reference for an IGC must require the IGC Chair to produce an annual report on the IGC's work. The firm would be required to make this annual report publicly available.
- 4.56** We would expect the report to include information on the level of direct and indirect costs incurred for transactions and other activities in managing and investing the pension assets of scheme members. Where the IGC has not been able to obtain the information it needs, we would expect the report to include an explanation as to why, as well as the steps that will be taken to give it access to the information in the future.

**Q23: *Do you agree that the IGC Chair should be required to produce an annual report and that the firm should be required to make this report publicly available?***

- 4.57** Respondents generally agreed with the requirement for an annual report. Feedback included comments to the effect that this would allow scrutiny and accountability of the IGC, as well as of the provider. However, a number of respondents considered that the production of the report should not be the sole responsibility of the IGC Chair.
- 4.58** Some respondents questioned whether the annual reports should contain commercially sensitive information. One respondent suggested that only a summary of the annual report should be made public.
- 4.59** There were mixed views as to whether we should further prescribe the content of the annual report. Some respondents thought that this would aid consistency and comparability. One respondent also asked for clarification regarding the reporting period.

#### Our response

We will require the production of an annual report and will require the firm to make this report publicly available.

We do not intend for the annual report to be produced solely by the IGC Chair. The report should reflect the opinions and the findings of the IGC as a whole. Our rules will make the IGC Chair responsible for ensuring that an annual report is produced.

We acknowledge the tension between publication of useful information on the value for money of schemes and the concern of providers about the release of potentially confidential and commercially sensitive information. We expect the charges borne by scheme members to be transparent to scheme members in any case. We do not intend to further prescribe the content of annual reports at this time.

With regard to reporting period, we have considered whether this should be annual from the date of inception of the IGC or in line with the scheme year. While we can see some advantages to all IGCs reporting on the same period, we do not intend to be prescriptive at this time. We would expect an IGC annual report to be produced on or before 5 April 2016 even where this is a partial year report.

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### Legacy workplace pension schemes

- 4.60** In its report<sup>15</sup>, published in September 2013, the OFT found that the buyer side of the market was ‘one of the weakest that the OFT has analysed in recent years’. The OFT also identified around £30 billion of saver’s money in legacy defined contribution (DC) workplace pension schemes at risk of being poor value for money, because of historically high charges.
- 4.61** Most contract-based workplace pensions are provided by firms which are members of the ABI. The OFT agreed that the ABI and its members would undertake an audit of these legacy schemes.<sup>16</sup> An Independent Project Board (IPB) was appointed to oversee the audit.
- 4.62** On 17 December 2014, the IPB issued its final report, in which it found that up to £26 billion of in-scope pension assets in legacy contract and bundled trust-based DC schemes was potentially exposed to a reduction in yield of more than one per cent due to charges.<sup>17</sup> Around half of this amount (up to £13.4 billion) was potentially exposed to a reduction in yield of more than 1.5 per cent.
- 4.63** The IPB recommended that affected providers should identify remedial actions for legacy schemes at risk of being poor value for money. The IPB further recommended that IGCs and trustee boards should agree actions and an implementation plan with their provider by end December 2015. An early priority for the IGCs of affected providers will be the implementation of the IPB’s recommendations.

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### Priorities for IGCs

- 4.64** In CP14/16, we outlined what we consider to be priorities for IGCs. As noted above, an early priority for IGCs will be the implementation of the IPB’s recommendations following the audit of legacy schemes.
- 4.65** Other potential priorities included the following:
- oversight of a sampling exercise of individual personal pensions to identify deferred members

<sup>15</sup> OFT *Defined contribution workplace pension market study* (September 2013) <http://webarchive.nationalarchives.gov.uk/20131101164215/http://www.of.gov.uk/OFTwork/markets-work/pensions/>

<sup>16</sup> An audit of pre-2001 contract based and bundled trust-based DC schemes and such schemes established since then with multiple charging structures or with charges greater than one per cent of assets under management.

<sup>17</sup> <http://www.fca.org.uk/static/documents/defined-contribution-workplace-pensions-ipb.pdf>

- ensuring that providers comply with a proposed ban on differential charging and consideration of whether deferred members are getting value for money
- ensuring that firms comply with the proposed charge cap on default funds and proposed bans on adviser commission and consultancy charging, and
- challenging firms on the value for money offered by fund managers, brokers, and other third-party providers.

**4.66** We acknowledged that some problems will be particularly difficult for providers to address. These include where schemes are sub-scale and where IT platforms are out of date. We said that, regardless of the difficulty for providers, we would still expect IGCs to challenge providers where they see poor value for money for scheme members.

**4.67** The priorities of IGCs are likely to change over time. In CP14/16, we did not propose to mandate what individual IGCs should prioritise.

***Q24: We would welcome views on where IGCs should focus their attention.***

**4.68** A number of respondents commented specifically that they agreed we should not mandate the priorities of individual IGCs. An appropriate prioritisation will depend on the schemes of the particular provider. No respondent disagreed with this.

**4.69** Some respondents called for us to prioritise recommendations for IGCs and for providers coming out of the legacy audit. One respondent referenced the OFT's finding that £30 billion of pension savers' money may be trapped in legacy schemes at risk of offering poor value for money, and expressed concern that the review may not result in the action needed to improve standards. Another respondent made the point that firms should be addressing the issues raised by the IPB as a result of the legacy audit and that IGCs should provide oversight.

**4.70** Other areas highlighted by respondents included the following:

- the treatment of deferred members and oversight of the sampling exercise
- governance around decumulation
- the effectiveness of communications to scheme members, and
- the need to challenge providers to negotiate better deals from fund managers.

**4.71** A number of respondents felt strongly that IGCs had a role to play in decumulation, given the blurring of the boundary between accumulation and decumulation, and concerns about provider behaviour. Some thought that IGCs should be required to consider decumulation. One respondent noted that the risks of detriment to pension savers will increase with the introduction of the new pension flexibilities. Another suggested that IGCs should review default fund strategies around retirement, as a de-risking mandate may no longer be appropriate.

**4.72** Some concerns were expressed that IGCs would be over-burdened and might neglect disengaged scheme members enrolled into default funds without making any active choice. A number of respondents reiterated that the primary focus of IGCs should be on default funds, with one commenting that IGCs should consider default fund suitability as well as pricing. There was also concern that defaults not specified by the provider might be overlooked.

## Our response

In our view, these are all important areas. We would expect IGCs initially to take up the challenges coming out of the audit of legacy workplace pension schemes and to provide oversight of the sampling exercise. We consider that these will give IGCs an opportunity to get to grips with complex charging arrangements and ensure that scheme members receive value for money, weighing benefits and services received against the cost to scheme members.

Exit fees can be one element of a charging structure in legacy schemes, as are fixed fees and contribution charges. We expect IGCs to review exit fees as part of their general review of charging structures and levels of charges, and make recommendations where they consider that charges are too high.

We agree that IGCs will want in the future to consider value for money for scheme members in decumulation. We will consider making this a requirement once IGCs have their immediate priorities in hand. While the primary focus of IGCs will be on default strategies, there is no reason why this should not extend into consideration of decumulation and retirement income options.

An IGC may recommend to the provider that the IGC should consider decumulation and retirement income options, in the interests of relevant scheme members, and, if the provider refuses to support this, may escalate that refusal to us.

In our view, the IGC should prioritise in accordance with the interests of scheme members and, if pension outcomes are at risk because of poor decisions or support at retirement, IGCs should engage with providers on these issues.

As noted earlier in this chapter, effective member communications are clearly important to improving scheme member engagement and pension outcomes. Where the costs of communications are borne by scheme members, the IGC will consider the value to scheme members and may challenge the provider. Where the costs are borne by employers, the IGC may provide useful advice, but this is not its primary role.

Over time, and with potential benefits for all scheme members, we expect improved competition between providers as a result of the operation of IGCs. IGCs will act in the stead of informed and engaged scheme members in focusing providers on good pension outcomes and promoting the transparency of costs and charges. Providers will need to understand where transactions deliver value in the context of an investment strategy and where the volume and/or costs of transactions may be excessive. We expect IGCs to challenge providers to negotiate better deals with fund managers and other third party providers, on behalf of scheme members.

We remain of the view that we should give individual IGCs the ability to prioritise their work, given the particular schemes operated by their provider and the attributes and needs of their scheme members. We see no reason to change our position at this time.

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## 5. Ensuring the effectiveness of IGCs

- 5.1** This chapter summarises feedback received on our proposed requirements on what firms must do to ensure that IGCs/GAAs<sup>18</sup> are effective and our response to that feedback.

### **Duty to provide all information reasonably requested**

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- 5.2** For a comprehensive assessment of value for money, IGCs will need detailed information about the benefits and services of a firm's workplace personal pension schemes and about the costs and charges borne by scheme members. We expect IGCs to consider what they need to assess value for money, whether particular schemes or aspects of schemes may be poor value for money and request the information they need from firms.
- 5.3** We recognise that there may be a tension between what an IGC wants and what a firm may be willing to provide. There is a cost to the firm in obtaining data and carrying out analyses on the IGC's behalf. Ultimately, there is a risk that this cost may be passed on to scheme members or that firms may withdraw schemes from the market.
- 5.4** In CP14/16, we proposed that the firm must provide all information 'reasonably requested' by the IGC for the purposes of carrying out its role. The firm and the IGC will need to agree what constitutes a reasonable request, having regard to proportionality and the interests of scheme members. We also expect firms to ensure the quality of the information.
- 5.5** If the firm cannot agree with the IGC what constitutes a reasonable request, we expect the IGC Chair to raise a concern with the firm's board. If the IGC Chair is not satisfied with the response of the firm's board, the IGC Chair should escalate the concern to us.
- 5.6** We consider that IGCs are likely to need information that may be confidential and/or commercially sensitive to carry out their duties. We proposed that a firm should ensure that arrangements are in place for sharing confidential and commercially sensitive information with the IGC.
- 5.7** When a corporate group chooses to have a single IGC at the group level, we said that the corporate group should ensure that this does not lead to restrictions on the sharing of information which would not otherwise be in place if there were firm-level IGCs.

***Q25: Do you agree that we should place a duty on the firm to provide the IGC with all information that it reasonably requests for the purposes of carrying out its duties?***

<sup>18</sup> References to IGCs throughout this chapter also apply to Governance Advisory Arrangements (GAAs), which are an alternative arrangement for the providers of smaller and less complex workplace personal pension schemes. We consider GAAs in Chapter 6.



- 5.8** The majority of respondents agreed that this requirement on firms is necessary to ensure that IGCs get the information they need to assess value for money properly. One respondent commented that supply of information to the IGC should become part of the firm's standard process and any unreasonable withholding information should be regarded as a cause for concern.
- 5.9** Respondents also considered that it would be reasonable for the IGC to request confidential and commercially sensitive information. Some respondents sought restrictions on how this information would be used by the IGC to ensure that it would not become public.
- 5.10** A number of respondents commented that, transaction costs aside, it should not be unduly onerous for providers to supply the information that an IGC needs. One respondent said that the information should be readily available and come from existing systems.

### Our response

In our view, an effective IGC depends not just on its ability to challenge and defend, but also on a strong and clear working relationship with the provider.

We expect the provider to be proactive and to supply relevant information and analysis to its IGC. We note the IPB's recommendation that affected providers take responsibility for providing their IGCs with analyses and proposed actions to improve outcomes for members of legacy schemes, where members are potentially exposed to high charges. Conversely, we expect the IGC to recognise that its requests for further information come with a cost and that cost may ultimately be borne by the scheme members it is intended to protect.

With regard to confidential and commercially sensitive information, we agree that IGCs will need access to this information. As proposed, we will expect the firm to ensure that arrangements are in place for the sharing and use/disclosure of confidential and commercially sensitive information with the IGC.

### Duty to provide sufficient resources

- 5.11** In addition to information, an IGC is likely to need administrative and analytical support from the firm to fulfil its duties effectively. Where schemes are large and/or complex, considerable data processing and analysis may be needed before information can be provided to the IGC in a form that is useful.
- 5.12** The IGC will also require other support to carry out its duties effectively. This might include independent advice, funded by the firm, to the extent necessary and proportionate and not inconsistent with the firm's duty to act in members' interests. For instance, funds should be available to engage advisers who are independent of the firm, such as an independent investment adviser or lawyer, where specialist or legal input is required.
- 5.13** In CP14/16, we proposed that a firm must provide the IGC with sufficient resources as are reasonably necessary for the purposes of carrying out its role independently. The firm and the IGC will need to agree what constitutes 'sufficient resources as are reasonably necessary', having regard to proportionality and the interests of scheme members.

- 5.14** We also proposed that the firm should agree arrangements for the IGC secretariat and other administrative support with the IGC Chair. As with information requests, if the IGC has concerns about the resources offered or provided by the firm, we expect the IGC Chair to raise the concerns with the firm's board. If the IGC Chair is not satisfied with the response of the firm's board, the IGC Chair should escalate the concerns to us.
- 5.15** Some firms may want to extend the scope of their IGC beyond its mandatory minimum duties, for example, to include oversight of individual personal pensions set up outside the workplace. We considered that this would be for the firm to agree with the IGC. If the scope is extended, we would expect the firm to provide additional resources and support, so that the IGC's ability to fulfil its minimum duties is not compromised.

**Q26: *Do you agree that we should place a duty on the firm to provide sufficient resources to the IGC as are reasonably necessary for it to carry out its duties?***

- 5.16** As with the previous requirement on information, the majority of respondents agreed with our proposal. A number of respondents commented that IGCs would need independent advice, including investment and legal advice, and that this would come at a cost. One respondent observed that the ability to appoint investment advisors and legal advisors would put them on an equal footing with trustee boards.
- 5.17** Some respondents questioned what we mean by 'sufficient' and by 'reasonably necessary'. These respondents anticipated that there would be disagreements from time to time over these terms.

### Our response

IGCs will depend on providers for the resources and support they need to operate effectively. As well as analytical support, this will include secretariat and administrative support. It may also include funding for external advice, such as independent investment or legal advice.

We recognise that 'sufficient' and 'reasonably necessary' are open to interpretation. We would expect the provider to make resources and support available so that the IGC can operate effectively. Conversely, we would expect the IGC to consider whether the anticipated benefits of its requests are proportionate to the cost.

We anticipate that there may be instances when the provider does not meet the IGC's request for information or for additional resources or support, when the IGC considers the request reasonable. If the IGC is not satisfied with the provider's explanation, we intend that the IGC will be able to escalate its concerns to us and make its concerns public. This power will operate in the same way as the IGC's ability to escalate any concerns about value for money.

### **Duty to ensure that member views are directly represented to the IGC**

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**5.18** IGCs have the challenge of representing scheme members who may not be interested in the management and administration of their pension assets, especially members who have been automatically enrolled into the default fund of their employer's scheme. Nonetheless, IGCs have the potential to be more effective if there are arrangements in place for interested members to make their views known.

**5.19** In CP14/16, while not seeking to prescribe the mechanism, we proposed that firms must make arrangements to ensure that relevant scheme member views can be directly represented to IGCs. We clarified that by 'directly', we meant without intervention by the firm as to which views are put forward.

**Q27: *We would welcome views on possible arrangements to ensure that member views are directly represented to the IGC.***

**5.20** Respondents were agreed that member views should be directly represented to the IGC. However, some respondents considered it unlikely that members would want to engage to the extent that they would offer their views to IGCs.

**5.21** Respondents suggested a wide range of possible arrangements, which we summarise for providers to consider:

- member panels and research of member views, with the National Employment Savings Trust (NEST) suggested as an example of good practice
- offering sessions to groups of scheme members around the UK, to engage and get direct feedback
- webinars and other online sessions for members
- an online facility for members to raise concerns directly with the IGC, with this referenced in the IGC's annual report
- an invitation in the annual report for written or emailed reports, with an IGC address for this, in other words, by-passing the provider
- the circulation of questionnaires to members in pension statements, with an explanation of what the IGC is about
- a named IGC member identified as the main contact for scheme members with issues or concerns
- an IGC annual general meeting for scheme members, with modern technology to maximise access, and
- a members' committee to feed views into the IGC.

**5.22** There was a mix of views on whether we should go further and require that one or more independent IGC members be scheme members.

- 5.23** A few respondents considered that we should require at least some scheme members on the IGC. One respondent went further and made a strong case for direct election by scheme members of the majority of IGC members.
- 5.24** Other respondents considered that it would not be practical to require this. One respondent noted a number of reasons why it would not be practical, including:
- the much greater demands on time relative to a single employer trust
  - the difficulty of achieving adequate and fair representation across various employers participating in a provider's schemes, and
  - the specialist knowledge required of workplace personal pensions.

### Our response

We welcome the variety of suggestions for how providers can facilitate the direct representation of member views to IGCs. Given the diversity of providers and schemes, we intend to leave it to the provider and the IGC to decide how best to make such arrangements. However, we stress the need for direct representation of views, without the possibility of filtering by the provider, and would encourage the provider to discuss possible arrangements with the IGC.

We strongly support the appointment of scheme members as IGC members, provided they are considered able to represent all relevant scheme members effectively. We consider that some allowance should be made for a possible lack of expertise and experience, since scheme members may bring a valuable viewpoint into IGC discussions. However, this should not be considered to weaken our requirement on providers to ensure that the IGC has sufficient collective expertise and experience to be able to make judgements on the value for money of relevant schemes.

We have considered carefully whether to require direct election by scheme members. This would be a democratic ideal. However we have concerns about the feasibility of direct elections in practice, given the widespread lack of engagement of scheme members – the very reason why we see the need for IGCs. Therefore, we do not intend to require direct elections of IGC members at this time, but would remind providers and IGCs of the need to seek member views by direct representation or some other means.

### Duty to make annual report and terms of reference publicly available

- 5.25** In CP14/16, we proposed that the firm should be responsible for making publicly available both the annual reports of the IGC Chair and the IGC's terms of reference. The firm could do this by placing the documents on its website and providing them on request to scheme members and employers.

**Q28:** *Do you agree that the firm should make the IGC's annual report and terms of reference publicly available?*

- 5.26** We asked earlier in the consultation about our proposal that the terms of reference for an IGC must require the IGC to produce an annual report. The responses to the earlier question and to the question above overlapped substantially.
- 5.27** The large majority of respondents agreed or strongly agreed that we should require firms to make the IGC's annual report and terms of reference publicly available. Comments included that making these documents publicly available would help ensure the IGC's accountability to members and potential members of the pension schemes in question.
- 5.28** Some respondents sought clarification on whether a summary version of the annual report would be acceptable, due to concerns about publication of potentially confidential and commercially sensitive information.
- 5.29** Respondents expressing an opinion generally endorsed our proposed guidance that a firm may comply with the requirement by making the documents available on request and on its website.

### Our response

We will proceed as proposed with a requirement that providers must make the IGC's annual report and terms of reference publicly available.<sup>19</sup> Providers may do this by making the documents available on request and on their websites. We would also expect providers to make employers and scheme members aware of the availability of the annual report and terms of reference, as part of their communications with them.

We consider that the primary purpose of the annual report should be as a public document making the IGC's work transparent to scheme members and other stakeholders, as well as to other IGCs and trustee boards. We are not convinced of the need for a summary report in addition to the annual report. Any summary report would still need to comply fully with our requirements for the contents of the annual report, as outlined in the minimum terms of reference.

We acknowledge the concerns about publication of potentially confidential and commercially sensitive information. It will be for the IGC and the provider to manage how they address these concerns, in the context of our requirements for the content of the annual report.

### 'Comply or explain' duty

- 5.30** For IGCs to be effective, firms must listen and respond to their concerns. IGCs are not able to make changes directly to pension schemes to improve value for money, since the firm remains responsible for any changes to its schemes.

<sup>19</sup> Similarly, providers of smaller and less complex schemes using GAAs, under which the equivalent of an IGC is provided by a third party, must make the annual report provided under the GAA and terms of reference of the GAA publicly available. We consider GAAs further in chapter 6.

- 5.31** In CP14/16, we proposed that a duty be placed on the firm to take reasonable steps to address concerns raised by an IGC under its terms of reference, or to explain in writing to the IGC why it does not intend to do so. To ensure that concerns are given due weight and attention, we proposed that IGCs raise their concerns directly with the boards of firms.
- 5.32** We said that while the IGC would raise their concerns directly with the boards of firms, we would expect the firm's executive management to consider the IGC's concerns and inform their board on proposed actions to address the IGC's concerns. Where the IGC is at group level and the concerns relate to pension schemes of a subsidiary of the group, the executive management of the subsidiary may be best placed to consider the IGC's concerns and propose actions to address them.
- 5.33** Where an IGC seeks to escalate its concerns, we proposed requiring the firm to take all necessary steps to facilitate the escalation of the concerns raised by the IGC under its terms of reference. This duty on the firm operates alongside the ability of IGCs to escalate concerns to us, to alert relevant scheme members and employers, and to make concerns public more widely where the IGC sees fit.

**Q29: *Do you agree that we should place a duty on the firm to address concerns raised by the IGC or explain to the IGC why it does not intend to do so?***

- 5.34** All respondents expressing an opinion agreed with the need for a 'comply or explain' duty on firms. A number of respondents considered this essential.

#### Our response

We agree that a 'comply or explain' duty is essential.

In our final rules, we require the firm to take reasonable steps to address any concerns raised by the IGC under its terms of reference. We also require the firm to provide written reasons to the IGC as to why it has decided to depart in any material way from any advice or recommendations made by the IGC.

The firm must take all necessary steps to facilitate the escalation of the concerns raised by the IGC under its terms of reference.

#### Our supervisory approach

- 5.35** Our supervisory approach comprises three 'pillars,' which take into account the scope of our remit and are designed to support our statutory objectives. These pillars are as follows:
- **Pillar 1: proactive firm supervision**, assessing whether the firm is run in a way that results in the fair treatment of customers, through identifying and addressing the drivers of conduct risk at the firm level
  - **Pillar 2: event supervision**, addressing significant crystallising or crystallised conduct risks at the firm level that occur outside the firm assessment cycle

- **Pillar 3: issues-based supervision**, addressing specific conduct risks across a sector and, as such, will be the main way we address our conduct priorities.

- 5.36** In CP14/16, we proposed that IGCs are captured within our existing supervisory three pillar framework while we monitor their set up and implementation. We said that we will use our full range of supervisory tools; for example, we may take firm-specific action on concerns escalated to us or a thematic review of IGCs to assess their effectiveness. We would expect IGC Chairs to escalate concerns to the firm's usual supervisory contact.
- 5.37** We said that our supervisory approach to IGCs will be kept under review to ensure that concerns are dealt with consistently and, where appropriate, acted upon.
- 5.38** While we did not ask for comments on our supervisory approach, respondents asked for further clarification on our supervisory approach. A number of respondents called for us to review the effectiveness of IGCs in a couple of years' time.

### Our response

We have developed our supervisory approach to IGCs. Matters relating to the effectiveness of IGCs will be considered and prioritised alongside other risks and issues faced by the firm, and the wider supervisory strategy for the firm. We will use supervisory judgement to include elements of our proactive firm supervision strategy, which may include meetings to investigate further any concerns raised by an IGC, or requests for further information where relevant details of a commercially sensitive nature are excluded from an IGC's annual report.

We expect providers to appoint an individual to take responsibility for managing the relationship between the provider and its IGC. This will enable us to direct any challenges at a particular individual where concerns arise and specific remedial action is expected. We would expect providers to consider appointing an FCA significant-influence holder as the individual responsible. However, it will be for the provider to determine the most appropriate individual.

Our supervisory approach will include a risk-based assessment of concerns escalated to us. Before any concerns are escalated to us, we will expect the firm to use its best endeavours to answer an IGC's concerns. Concerns escalated to us may include concerns about the firm's response to requests for information or resources, as well as concerns raised with the provider's board about the value for money of the provider's workplace personal pension schemes.

We will expect the IGC to notify us<sup>20</sup> of any concerns before a decision to alert relevant employers and scheme members, and before a decision to make its concerns public more widely. We will then be in position to help the IGC understand whether or not the firm is in breach of FCA rules or principles.

The provider would be expected to facilitate escalation to the relevant supervisory contact within the FCA. For large providers, the relevant supervisory team would be the first point of contact for IGCs. For other firms, our firm contact centre would be the first point of contact. We will have a procedure

<sup>20</sup> Under Principle 11 of the FCA handbook, 'Relations with Regulators' <http://www.fshandbook.info/FS/html/FCA/PRIN/2/1>

in place to ensure that IGC concerns received by our firm contact centre are directed to the appropriate supervisory team.

When the firm is in breach, we will consider taking action against the firm. When the firm is not in breach, we will consider the issue in conjunction with information from other firms and IGCs. We have a range of regulatory actions available to us to address issues that we prioritise.

As outlined earlier, we intend to start with a forum for IGC Chairs around the time that our rules become effective in April 2015. We will use this as an opportunity to clarify our expectations of IGCs and GAAs, identify relevant contact points and outline the process for escalation of issues. We will also begin discussions about how best to support IGCs in their assessments of value for money.

We acknowledge calls for an FCA review of the effectiveness of IGCs in a couple of years' time. IGCs are new governance bodies and we will want to ensure that they are operating effectively. We intend to conduct a review of the effectiveness of IGCs in 2017. This review would take into account the planned review in 2016 of progress against the IPB's recommendations and could be in the context of a broader FCA/DWP review of workplace pension reforms.

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## 6. Alternative arrangements to IGCs

- 6.1** This chapter summarises feedback received on our proposals for alternative arrangements to IGCs and provides our response to that feedback.

### Governance advisory arrangements

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- 6.2** An IGC may not be a proportionate approach for firms with smaller and less complex workplace personal pension schemes.
- 6.3** In CP14/16, we proposed that firms with smaller and less complex workplace personal pension schemes should be able to appoint another firm, as an independent third party, to take on their IGC responsibilities. The third party would provide a committee of individuals (including individuals independent of the third party and the firm) to carry out these responsibilities. This committee would be equivalent to an IGC, but would be able to serve multiple firms, with the potential for economies of scale and resulting lower cost solutions for smaller firms.
- 6.4** We referred to this as a governance advisory arrangement (GAA). We proposed that firms seeking to establish GAAs must ensure that their GAA performs the same functions that an IGC would have done. In particular, firms will be required to ensure that the mandatory requirements in the terms of reference for an IGC also apply to the GAA. We would expect a third party seeking to provide GAA services to take these requirements on firms into account in designing the service.
- 6.5** We also proposed requiring that firms seeking to establish GAAs do this on terms that secure the independence of the GAA committee and its Chair from the appointing firm. We said that we would expect the majority (or all) of the members of the GAA committee, including the Chair, to be independent of the firm(s) using its services.

**Q30: *Do you agree that GAAs should be allowed as an alternative to IGCs for firms with smaller and less complex workplace personal pension schemes?***

- 6.6** The majority of respondents agreed with our proposals as a proportionate approach for the providers of smaller and less complex schemes. One respondent observed that GAAs would be similar to professional trustees, the use of which is considered best practice by TPR. A couple of respondents commented that GAAs should be permitted to all providers, regardless of scheme size or complexity.
- 6.7** Some respondents, while agreeing with our proposals, made the point that GAAs would be contingent on third-party providers entering the market and offering a GAA service at reasonable cost.

- 6.8** Respondents disagreeing with our proposals had concerns that GAAs might be a weaker form of governance and might be, or be seen as, a ‘soft touch’ relative to IGCs. These respondents considered that IGCs should be required of all firms operating workplace personal pension schemes. One respondent commented that GAAs would encourage the continuation of sub-scale providers. Some others said that providers unable to afford the cost of GAAs should not be operating workplace pension schemes.
- 6.9** A number of respondents observed that GAAs, in being equivalent to an IGC, might be prohibitively expensive for small providers, despite the potential scale economies of multiple providers contracting with the same third party. Some mutual respondents observed that the cost of GAAs would be borne by their members.

### Our response

Our proposals for GAAs are intended to ensure that GAAs can be as effective as IGCs in acting for the providers of smaller and less complex schemes. We intend that GAAs will be established along similar lines to IGCs but that the same third party committee will be shared by multiple providers. This should lower the cost of governance, which may ultimately be borne by scheme members.

We have considered the concerns of smaller providers about the cost of GAAs as proposed. However, we do not propose any ‘lesser’ solution than GAAs, such as an audit-style arrangement or GAAs that do not conform to our requirements for IGCs. We note that, where schemes are very small and simple, less GAA time may be required and the cost of a GAA may reflect this.

The same individual may serve on both GAAs and IGCs. However, in establishing a GAA, a provider should have regard to its obligation to ensure the independence of the GAA and its chair from the firm.

As yet, there is no market for GAA services. If no third party provider of GAA services emerges, or if we have concern about the cost or quality of GAA services offered, we will reconsider our rules on a proportionate approach for the providers of smaller and less complex schemes.

### Threshold for use of a GAA

- 6.10** We had previously considered whether we should determine a threshold below which a GAA will be allowed as an alternative to an IGC. However, we believed that setting a threshold based simply on number of members, or funds under management, would not be appropriate, because different firms may have schemes with very different characteristics. For example, firms may have closed and open schemes, different types of legacy scheme, workforces with different characteristics, or schemes with additional benefits or services.
- 6.11** In CP14/16, we proposed allowing firms to determine whether or not it would be appropriate for them to establish a GAA rather than an IGC. In making this assessment, we would expect firms to consider:

- their market share of workplace personal pensions, and
- the complexity of their workplace personal pension schemes.

**6.12** While we do not seek to prescribe a threshold, we recognise that firms will receive comfort from having guidance on the level of market share below which a GAA may be considered appropriate. We proposed that, for firms with less than a five per cent market share of two or more of the following measures, a GAA may be considered appropriate:

- funds under management in relevant schemes
- number of relevant scheme members, and
- number of employers contributing to relevant schemes.

**6.13** We also expect firms to consider the complexity of their schemes in determining whether a GAA would be appropriate, since the more complex a firm's schemes, the greater the need for the in-depth and firm-specific knowledge that an IGC can provide. One or more of the following features of schemes might indicate complex arrangements:

- schemes operated on multiple IT systems
- multiple charging structures
- schemes offering with-profits funds, where costs are allocated to members and conflicts of interest may arise, and/or
- schemes offering funds managed by firms within the same group, in other words, the fund management is vertically integrated.

**6.14** The large majority of members of workplace personal pension schemes are concentrated within a small number of providers. We said that, if firms adopt the above guidance about when a GAA may be considered appropriate, we believed that the large majority of members of workplace personal pension schemes will be represented by an IGC.

***Q31: Do you agree with our proposals for the types of firm that can use GAAs?***

**6.15** A minority of respondents did not agree that we should allow any alternative arrangement to IGCs, for the reasons given earlier. Some of these respondents still commented on GAAs.

**6.16** Of those respondents expressing an opinion, the majority agreed with our proposed guidance for firms in determining whether a GAA would be appropriate. A few respondents considered that the use of a GAA should be at the discretion of the FCA.

**6.17** One respondent felt that we should set a threshold for the type of scheme permitted to use GAAs. This respondent considered it essential that providers understand whether they are required to set up an IGC or whether they qualify for an alternative arrangement. However, other respondents thought that it was important not to be too prescriptive, since there are too many variables to be considered for any form of threshold to be applied.

- 6.18** Some respondents suggested that all providers should be permitted to use GAAs. One respondent considered that GAAs are similar to professional trustees, the use of which is considered best practice by TPR.

#### Our response

We do not consider that we should be overly prescriptive on the type of firms that can use a GAA at this time. We remain of the view that guidance for firms on the use of GAAs is the best approach. However, we will follow closely how the market for GAA services develops.

That said, we do not consider GAAs to be appropriate for providers with larger and more complex schemes. This is because we consider an IGC better placed to acquire the in-depth knowledge of the provider's schemes and to challenge the provider on value for money issues.

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## 7. Cost benefit analysis and next steps

- 7.1** This chapter summarises feedback received on our cost benefit analysis, provides our response to that feedback and sets out next steps.

### Cost benefit analysis

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- 7.2** In CP14/16, we provided estimates of the costs and benefits of our proposals. Based on input from providers, we estimated that one-off incremental costs to firms would be within the wide range of £0.8m to £10.8m. We estimated that ongoing costs to firms would be within the range of £5m to £13.8m. Our central estimates were for one-off incremental costs of around £2m and ongoing costs of around £8.5m.
- 7.3** A robust estimate of benefits was hard to provide. To illustrate the scale of the benefits, we observed that if charges reduced by as little as one basis point as a result of the IGCs, averaged across all assets held (where total charges on default funds will be capped at 75 basis points), the potential cost savings to scheme members could be around £10m per year, based on currently affected assets under management.<sup>21</sup> A 1.5 basis point reduction would deliver savings of £15m per year.
- 7.4** Going forward, with forecast growth in assets under management (AUM) of 11.6 per cent per annum,<sup>22</sup> and assuming an average one basis point reduction in charges across all assets held, we estimated that this could result in annual savings to scheme members of as much as £50m per annum. We included these figures to illustrate the relatively small change in charges needed, as a result of IGCs, to generate significant benefits from charges alone.
- 7.5** Given the range of wider benefits expected from IGCs, we considered that actual benefits will be substantially higher, further strengthening the case for the introduction of IGCs. We did not consider it proportionate to provide an estimate of the other benefits, since the estimated benefits exceeded our expected incremental compliance costs to firms.
- 7.6** A number of respondents observed that the cost of IGCs and GAAs may ultimately be borne by customers, including the scheme members they are intended to protect. One respondent observed that the incremental costs per firm are not insignificant and there is the potential for higher provider costs leading to higher charges for scheme members.
- 7.7** A few respondents considered that we had underestimated the number of smaller providers<sup>23</sup>, since firms may have historic arrangements that would be caught even though they are no longer active in the market.

<sup>21</sup> Based on £100bn funds under management (a cautious assumption given IGCs will commence in 2015)

<sup>22</sup> Spence Johnson, Broad Brush, Number 14, December 2012

<sup>23</sup> For the purposes of our cost benefit analysis, we assumed that 15 smaller providers would establish GAAs

## Our response

Governance comes at a cost and – as with all value for money assessments – there is a balance to be struck between cost and quality. We have sought in our proposals to take a proportionate approach and not to be too prescriptive. Our proposals will ensure that workplace personal pension schemes meet, at a minimum, the governance standards sought by government

We believe that IGCs will improve pension outcomes for scheme members. IGCs will result in providers more focused on what matters to pension outcomes, particularly for those consumers in default investment strategies. This focus, together with improvements to the transparency of costs and charges, including transactions costs, will support and promote competition between providers on value for money, including the value for money delivered by asset managers.

We have no better information on the number of smaller providers affected by our rules. It may be that firms have historic arrangements that would be caught even though they are no longer active in the market. However, we do not believe that the number of smaller providers would be so much larger as to change the result of our cost benefit analysis.

As outlined in the previous chapter, we believe that all scheme members of workplace personal pension schemes should benefit from good governance, regardless of the size of scheme or provider, and regardless of whether the scheme is open or closed to new members. If a provider has a particular concern about the impact of our proposals on scheme members, the provider may consider applying for a waiver.<sup>24</sup> Such applications will be considered on a case-by-case basis.

## Next steps

- 7.8** A number of providers have already set up an IGC and others are in the process of recruiting IGC Chairs or have been waiting for our final rules. We would expect providers to have established an IGC or GAA by the 6 April 2015 deadline, in line with the government's timetable.
- 7.9** We intend to hold a forum for IGC Chairs around the time that our rules become effective. We will use this forum as an opportunity to clarify our expectations of IGCs and GAAs, identify relevant contact points and outline the process for escalation of issues. We will also begin discussions about how best to support IGCs in their assessments of value for money and consider whether further guidance would be helpful for them.
- 7.10** An early priority for the IGCs of affected providers will be to take forward the recommendations of the IPB, following its audit of charges and benefits in legacy DC workplace schemes. On 17 December 2014, the IPB issued its final report, in which it found that up to £26 billion of in-scope pension assets in legacy contract and bundled trust-based DC schemes was potentially exposed to a reduction in yield of more than one per cent due to charges.<sup>25</sup> The IPB recommended that affected providers should identify remedial actions for legacy schemes at risk of being poor

<sup>24</sup> under s.138A FSMA, and the guidance in SUP 8

<sup>25</sup> <http://www.fca.org.uk/static/documents/defined-contribution-workplace-pensions-ipb.pdf>

value for money. The IPB further recommended that IGCs and trustee boards should agree actions and an implementation plan with their provider by end December 2015.

- 7.11** IGCs will be new governance bodies and we will want to ensure that they are operating effectively. We intend to conduct a review of the effectiveness of IGCs in 2017. Following this review, we intend to consider extending the required remit of IGCs to scheme members in decumulation.

# Annex 1

## List of non-confidential respondents

### Companies and organisations

Admin Re

Aegon

Age UK

Ashurst LLP

Association of British Insurers

Association of Member Nominated Trustees

Association of Member-Directed Pension Schemes

Association of Pension Lawyers

Association of Professional Pension Trustees

B&CE, The People's Pension

BlackRock

Brian Shearing & Partners

Charlton Frank Ltd

Chartered Insurance Institute

City of London Investment Group

Complyport Ltd

Crowe Clark Whitehill

Equitable Life Assurance Society

Eversheds LLP

Fidelity Worldwide Investment

Fidelus Ltd



Financial Services Consumer Panel

First Actuarial

Friends Life Group

Greg McClymont MP, Shadow Pension Minister

Hargreaves Lansdown

Hymans Robertson LLP

Independent Trustee Services Limited

Institute & Faculty of Actuaries

Institute of Chartered Accountants Scotland

Integrated Financial Arrangements Group

International Financial Data Services (UK) Ltd

Investment Association

KPMG LLP

Legal & General Assurance Society Ltd

Marine & General Mutual

Mercer Limited

National Association of Pension Funds

Novia Financial plc

Occupational Pensions Defence Union Limited

Pension Play Pen

Pensions Management Institute

Phoenix Group

Prospect

Prudential plc

PTL

Royal London Group

Sacker & Partners LLP

Scottish Friendly Assurance Society Ltd

Scottish Widows

ShareAction

Society of Pension Professionals

St. James's Place Group

Standard Life Plc

Towers Watson Limited

Trades Union Congress

UK Sustainable Investment and Finance Association

Zurich

### **Individuals**

Barry Dixon

Ben Grimwood

Dominic Lindley

Matthew Speck

Timothy Morris

We received a further 180 individual responses that conformed to a short template provided by ShareAction.

Four confidential responses were also received.

# Appendix 1

## Made rules (legal instrument)

**PERSONAL PENSION SCHEMES (INDEPENDENT GOVERNANCE  
COMMITTEES) INSTRUMENT 2015**

**Powers exercised**

- A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137A (General rule-making power);
  - (2) section 137T (General supplementary powers); and
  - (3) section 139A (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 138G (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 6 April 2015.

**Amendments to the FCA Handbook**

- D. The Glossary is amended in accordance with Annex A to this instrument.
- E. The Conduct of Business sourcebook (COBS) is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Personal Pension Schemes (Independent Governance Committees) Instrument 2015.

By order of the Board of the Financial Conduct Authority  
29 January 2015

## Annex A

### Amendments to the Glossary of definitions

In this annex, underlining indicates new text, unless otherwise stated.

Insert the following new definitions in the appropriate alphabetical place. The text is not underlined.

*governance advisory arrangement* (in COBS 19.5) an arrangement between a *firm* and a third party under which the third party establishes a committee to represent the interests of *relevant policyholders* in the *firm's relevant schemes*.

*IGC* (in COBS 19.5) an independent governance committee established by a *firm* with terms of reference which satisfy COBS 19.5.5R with the purpose, in summary, to represent the interests of *relevant policyholders* in the *firm's relevant schemes*.

*relevant policyholder* (in COBS 19.5) a member of a *relevant scheme* who is or has been a worker entitled to have contributions paid by or on behalf of his employer in respect of that *relevant scheme*.

‘Worker’ has the same meaning as in section 88 of the Pensions Act 2008, that is, in summary, an individual who has entered into or works under (a) a contract of employment, or (b) any other contract by which the individual undertakes to do work or perform services personally for another party to the contract.

Amend the following as shown.

*relevant scheme* ...

(3) (in COBS 19.5) a *personal pension scheme* or *stakeholder pension scheme* for which direct payment arrangements are, or have been, in place, and under which contributions have been paid for two or more *employees* of the same employer.

‘Direct payment arrangements’ has the same meaning as in section 111A of the Pension Schemes Act 1993, that is, arrangements under which contributions fall to be paid by or on behalf of the employer towards the scheme (a) on the employer’s own account (but in respect of the employee); or (b) on behalf of the employee out of deductions from the employee’s earnings.

## Annex B

### Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, all the text is new and is not underlined

In COBS 19 (Pensions supplementary provisions) insert the following new section after COBS 19.4.

#### 19.5 Independent governance committees (IGCs)

##### Application

- 19.5.1 R This section applies to a *firm* which operates a *relevant scheme* in which there are at least two *relevant policyholders*.

##### Requirement to establish an IGC

- 19.5.2 R (1) Subject to *COBS 19.5.3R*, a *firm* must establish an *IGC*.
- (2) This *rule* does not apply to a *firm* ('Firm A') if another *firm* in Firm A's *group* has made arrangements under this section for an *IGC* to cover *relevant schemes* operated by Firm A.

##### Governance advisory arrangements

- 19.5.3 R (1) If a *firm* considers it appropriate, having regard to the size, nature and complexity of the *relevant schemes* it operates, it may establish a *governance advisory arrangement* instead of an *IGC*.
- (2) If a *firm* has decided to establish a *governance advisory arrangement* rather than an *IGC*, this section (other than *COBS 19.5.9R(2)*, *COBS 19.5.9R(3)*, *COBS 19.5.10G*, *COBS 19.5.11R* and *COBS 19.5.12G*) apply to the *firm* by reading references to the *IGC* as references to the *governance advisory arrangement*.
- (3) A *firm* must establish a *governance advisory arrangement* on terms that secure the independence of the *governance advisory arrangement* and its Chair from the *firm*.
- 19.5.4 G (1) *Firms* with large or complex *relevant schemes* should establish an *IGC*. For the purposes of this section, a *firm* may determine whether it has large *relevant schemes* by reference to:
- (a) the number of *relevant policyholders* in *relevant schemes*;
- (b) the funds under management in *relevant schemes*; and
- (c) the number of employers contributing to *relevant schemes*.
- (2) Examples of features that might indicate complex schemes include:

- (a) schemes that are operated on multiple information technology systems;
- (b) schemes that have multiple charging structures;
- (c) schemes that offer a *with-profits fund*; and
- (d) the *firm* offers *relevant policyholders* access to investment funds it operates or which are operated by an entity with the same ownership.

Terms of reference for an IGC

- 19.5.5 R A *firm* must include, as a minimum, the following requirements in its terms of reference for an *IGC*:
- (1) the *IGC* will act solely in the interests of *relevant policyholders*;
  - (2) the *IGC* will assess the ongoing value for money for *relevant policyholders* delivered by *relevant schemes* particularly, though not exclusively, through assessing:
    - (a) whether default investment strategies within those schemes:
      - (i) are designed and executed in the interests of *relevant policyholders*;
      - (ii) have clear statements of aims and objectives;
    - (b) whether the characteristics and net performance of investment strategies are regularly reviewed by the *firm* to ensure alignment with the interests of *relevant policyholders* and that the *firm* takes action to make any necessary changes;
    - (c) whether core scheme financial transactions are processed promptly and accurately;
    - (d) the levels of charges borne by *relevant policyholders*; and
    - (e) the direct and indirect costs incurred as a result of managing and investing, and activities in connection with the managing and investing of, the pension savings of *relevant policyholders*, including transaction costs;
  - (3) the *IGC* will raise with the *firm's governing body* any concerns it may have in relation to the value for money for *relevant policyholders* delivered by a *relevant scheme*;
  - (4) the *IGC* will escalate concerns as appropriate where the *firm* has not, in the *IGC's* opinion, addressed those concerns satisfactorily or at all;

- (5) the *IGC* will meet, or otherwise make decisions to discharge its duties, using a quorum of at least three members, with the majority of the quorum being independent;
- (6) the Chair of the *IGC* will be responsible for the production of an annual report setting out:
  - (a) the *IGC's* opinion on the value for money delivered by *relevant schemes*, particularly against the matters listed under (2);
  - (b) how the *IGC* has considered *relevant policyholders'* interests;
  - (c) any concerns raised by the *IGC* with the *firm's governing body* and the response received to those concerns;
  - (d) how the *IGC* has sufficient expertise, experience and independence to act in *relevant policyholders'* interests;
  - (e) how each independent member of the *IGC*, together with confirmation that the *IGC* considers these members to be independent, has taken into account *COBS 19.5.12G*;
  - (f) the arrangements put in place by the *firm* to ensure that the views of *relevant policyholders* are directly represented to the *IGC*.

- 19.5.6 G
- (1) An *IGC* is expected to act in the interests of *relevant policyholders* both individually and collectively. Where there is the potential for conflict between individual and collective interests, the *IGC* should manage this conflict effectively. An *IGC* is not expected to deal directly with complaints from individual policyholders.
  - (2) The primary focus of an *IGC* should be the interests of *relevant policyholders*. Should a *firm* ask an *IGC* to consider the interests of other members, the *firm* should provide additional resources and support to the *IGC* such that the *IGC's* ability to act in the interests of *relevant policyholders* is not compromised.
  - (3) An *IGC* should assess whether all the investment choices available to *relevant policyholders*, including default options, are regularly reviewed to ensure alignment with the interests of *relevant policyholders*.
  - (4) Where an *IGC* is unable to obtain from a *firm*, and ultimately from any other person providing relevant services, the information it requires to assess the matters in *COBS 19.5.5R(2)*, the *IGC* should explain in the annual report why it has been unable to obtain the information and how it will take steps to be granted access to that information in the future.



- (5) If, having raised concerns with the firm's *governing body* about the value for money offered to *relevant policyholders* by a *relevant scheme*, the *IGC* is not satisfied with the response of the firm's *governing body*, the *IGC* Chair may escalate concerns to the *FCA* if the *IGC* thinks that would be appropriate. The *IGC* may also alert *relevant policyholders* and employers and make its concerns public.
- (6) The *IGC* Chair should raise with the firm's *governing body* any concerns that the *IGC* has about the information or resources that the firm provides, or arrangements that the firm puts in place to ensure that the views of *relevant policyholders* are directly represented to the *IGC*. If the *IGC* is not satisfied with the response of the firm's *governing body*, the *IGC* Chair may escalate its concerns to the *FCA*, if appropriate. The *IGC* may also make its concerns public.
- (7) The *IGC* should make public the names of those members who are *employees* of the provider firm, unless there are compelling reasons not to do so. The *IGC* should consult *employee* members as to whether there are such reasons.

#### Duties of firms in relation to an IGC

- 19.5.7 R A firm must:
- (1) take reasonable steps to ensure that the *IGC* acts and continues to act in accordance with its terms of reference;
  - (2) take reasonable steps to provide the *IGC* with all information reasonably requested by the *IGC* for the purposes of carrying out its role;
  - (3) provide the *IGC* with sufficient resources as are reasonably necessary to allow it to carry out its role independently;
  - (4) have arrangements to ensure that the views of *relevant policyholders* can be directly represented to the *IGC*;
  - (5) take reasonable steps to address any concerns raised by the *IGC* under its terms of reference;
  - (6) provide written reasons to the *IGC* as to why it has decided to depart in any material way from any advice or recommendations made by the *IGC* to address any concerns it has raised;
  - (7) take all necessary steps to facilitate the escalation of concerns by the *IGC* under *COBS* 19.5.5R(4) and *COBS* 19.5.6G(5); and
  - (8) make the terms of reference and the annual report of the *IGC* publicly available.
- 19.5.8 G (1) A firm should consider allocating responsibility for the management

of the relationship between the *firm* and its *IGC* to a person at the *firm* holding an FCA *significant-influence function*.

- (2) A *firm* should fund independent advice for the *IGC* if this is necessary and proportionate.
- (3) A *firm* should not unreasonably withhold from the *IGC* information that would enable the *IGC* to carry out a comprehensive assessment of value for money.
- (4) A *firm* should have arrangements for sharing confidential and commercially sensitive information with the *IGC*.
- (5) A *firm* should use best endeavours to obtain, and should provide the *IGC* with, information on the costs incurred as a result of managing and investing, and activities in connection with the managing and investing of, the assets of *relevant schemes*, including transaction costs. Information about costs and charges more broadly should also be provided, so that the *IGC* can properly assess the value for money of *relevant schemes* and the funds held within these.
- (6) If a *firm* asks an *IGC* to take on responsibilities in addition to those in *COBS 19.5.5R*, the *firm* should provide additional resources and support to the *IGC* such that its ability to act within its terms of reference in *COBS 19.5.5R* is not compromised.
- (7) A *firm* should provide secretarial and other administrative support to the *IGC*. The nature of the support, including how it is provided and by whom, should not conflict with the *IGC's* ability to act independently of the *firm*.
- (8) A *firm* can make the terms of reference for the *IGC* and the annual report of the *IGC* publicly available by placing them on its website and by providing them on request to *relevant policyholders* and their employers.

#### Appointment of IGC members

- 19.5.9 R
- (1) A *firm* must take reasonable steps to ensure that the *IGC* has sufficient collective expertise and experience to be able to make judgements on the value for money of *relevant schemes*.
  - (2) A *firm* must recruit independent *IGC* members through an open and transparent recruitment process.
  - (3) A *firm* must appoint members to the *IGC* so that:
    - (a) the *IGC* consists of at least five members, including an independent Chair and a majority of independent members;
    - (b) *IGC* members are bound by appropriate contracts which reflect the terms of reference in *COBS 19.5.5R*, and on such

terms as to secure the independence of independent members;

- (c) independent *IGC* members who are individuals are appointed for fixed terms of no longer than five years, with a cumulative maximum duration of ten years;
- (d) individuals acting as the representative of an independent corporate member are appointed to the *IGC* for a maximum duration of ten years;
- (e) independent *IGC* members who are individuals, including those representing independent corporate members, are not eligible for reappointment to the *IGC* until five years have elapsed, after having served on the *firm's IGC* for the maximum duration of ten years;
- (f) appointments to the *IGC* are managed to maintain continuity in terms of expertise and experience of the *IGC*.

- 19.5.10 G (1) The effect of *COBS* 19.5.9R(3)(b) is that *employees* of the *firm* who serve on an *IGC* should be subject to appropriate contractual terms so that, when acting in the capacity of an *IGC* member, they are free to act within the terms of reference of the *IGC* without conflict with other terms of their employment. In particular, when acting as an *IGC* member, an *employee* will be expected to act solely in the interests of *relevant policyholders* and should be able to do so without breaching any terms of his employment contract.
- (2) An individual may serve on more than one *IGC*.
- (3) A *firm* should replace any vacancies that arise within *IGCs* as soon as possible and, in any event, within six months.
- (4) A *firm* should involve the *IGC* Chair in the appointment and removal of other members, both independent members and *employees* of the *firm*.
- (5) A *firm* should consider indemnifying *IGC* members against any liabilities incurred while fulfilling their duties as *IGC* members.

#### IGC members who are independent

- 19.5.11 R The *firm*, in appointing independent *IGC* members, must determine whether such a member is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, that member's judgement.
- 19.5.12 G (1) An *IGC* member is unlikely to be considered independent if any of the following circumstances exist:
- (a) the individual is an *employee* of the *firm* or of a company within the *firm's group* or paid by them for any role other

than as an *IGC* member, including participating in the *firm's* share option or performance-related pay scheme;

- (b) the individual has been an *employee* of the *firm* or of another company within the *firm's group* within the five years preceding his appointment to the *IGC*;
  - (c) the individual has, or had within the three years preceding his appointment, a material business relationship of any description with the *firm* or with another company within the *firm's group*, either directly or indirectly.
- (2) A *firm* may appoint a *body corporate* to an *IGC*, including as Chair. The corporate member should notify the *firm* of the individual who will act as the member's representative on the *IGC*. A *firm* should consider the circumstances of a corporate *IGC* member and any representative of the corporate member with the objective of ensuring that any potential conflicts of interest are managed effectively so that they do not affect the corporate *IGC* member's ability to represent the interests of *relevant policyholders*.
- (3) Should the *firm*, or another company within the *firm's group*, operate a mastertrust, there may be benefits in a trustee of such a mastertrust also being an *IGC* member. If such circumstances exist, an individual or a corporate trustee may be suitable to be an independent *IGC* member, notwithstanding the relationship with the *firm*.
- (4) A *firm* should review on a regular basis whether its independent *IGC* members continue to be independent and take appropriate action if it considers that they are not.

**Financial Conduct Authority**



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