

## Introduction

Since April 2015, any provider of a contract-based pension scheme has been legally required to set up and maintain an Independent Governance Committee (IGC).<sup>1</sup>

IGCs are responsible for overseeing the governance of contract-based pension schemes and their remit is to:

- Ensure that such schemes act in the best interests of members; and
- Challenge providers, if they are not providing “value for money”.<sup>2</sup>

The committees are independent from the provider and assess and raise concerns on behalf of members. If the provider does not act on the concerns raised, the IGC has the power to escalate issues to the Financial Conduct Authority (FCA).

This Briefing Note provides a background to the development of IGCs and looks at the key themes emerging from their first 12 months of operation and what they expect may emerge during their 2nd year. Information was garnered from an on-line survey (Box 1).

For the purposes of this briefing note the term ‘workplace pension’ relates to contract-based pension schemes only.

## Why have IGCs been set up?

The process of automatic enrolment has brought 6 million workers into a workplace pension scheme.<sup>3</sup> Typically, the employer selects the provider of the workplace pension, with little or no involvement by the employee. As employers are also answerable to shareholders, there is a potential conflict of interest between offering value for money to their employees through the provision of a workplace pension and shareholder return.

Members are also likely to have relatively low levels of financial literacy, resulting in reduced judgement about whether they are receiving value for money.<sup>4</sup>

The majority of members in workplace DC schemes are investing into default funds (99% of master trust members and 85% of other workplace DC schemes).<sup>5</sup> This has led to the implementation of IGCs acting as a body to protect solely the members interest.<sup>6</sup>

## Role of IGCs

The IGCs role is to protect the member’s interest through effective governance and meeting minimum quality standards.<sup>7</sup>

IGCs were introduced by the FCA to assess the benefits, costs and professionalism of all contract based pension schemes.<sup>8</sup> The role requires them to act independently of the pension scheme provider and act upon any areas of concern, for example, protecting members against poor decisions.

IGCs need to:

- Consider whether the characteristics and net performance of investment strategies are regularly being reviewed by the provider, making sure that this is in line with the interest of members both deferred and active.<sup>9</sup>
- Produce an annual report, which will allow members to compare costs and charges against other schemes to ensure they are getting value for money. This is also aimed at improving the transparency of the scheme.

Scheme providers have a duty to ensure that the IGC is able to function effectively. This is done by providing committee members with the necessary resources to fulfil their duties in assessing value for money and in the production of the annual report. Similarly the providers must allow the IGC to interact with scheme members so that their views can be considered.<sup>10</sup>

### Box 1. Survey details

The PPI on-line survey was conducted with 15 IGC chairs during February 2016. All IGC chairs kindly completed the survey.

Questions covered various aspects of the IGC role and set-up, the challenges of the first year and investigated what additional issues will emerge or be actioned for the second year of operation.

The survey will be repeated at regular intervals to highlight any additional issues that may arise.

## IGC requirements

IGCs must have a minimum of 5 committee members, with one member who acts as a provider representative. Those who are not provider representatives must meet certain criteria; they must be independent and cannot have been employed by the provider in the last 5 years. In order to preserve the independence of the IGC, members will only be allowed to serve 10 cumulative years.<sup>11</sup>

## Findings from the survey

The survey looked at the dynamics of the IGCs, such as the frequency and duration of meetings, the number and type of members. There is consistency across all IGCs as shown in [Chart 1](#).

Establishing a governance framework and building relationships with the provider were challenges that IGCs faced in their first 12 months, as expected. In addition, the responses to the PPI survey highlighted three other main challenges:

- Value for money
- Transaction costs and charges
- Legacy schemes

The themes are summarised in [Chart 2](#).

### 1. Value for money

Despite different definitions of 'value for money' being available (such as the National Audit Office, the Pensions Regulator and the Office of Fair Trading)

all IGCs have developed their own definitions. Most say that they have been influenced by one or more of the existing definitions when deriving their own. However, a major challenge that they have all faced is; what actually constitutes value for money?

Without definitive regulatory guidance the IGCs have had to decide what the concept meant on behalf of their scheme members. With some committees, members appearing to have had different perceptions of what value for money meant, resulting in challenges to identify a single definition.

Investment defaults and charges were the two most important rated aspects included within the scope for value for money, followed by administration, governance and engagement.

There were also other challenging aspects around value for money, specifically:

- Determining how to assess value for money; and
- Developing principles for measuring value for money.

IGC chairs reported that they had undertaken detailed research into various aspects of the scheme (for example, investment strategies) in order to build their own tools (such as, a matrix) to assess value for money.

One of the most difficult aspects of measuring value for money, has been the lack of reliable industry benchmarking. This has made it

difficult for IGCs to compare their scheme(s) to others within the market.

Challenges around value for money are a 'work in progress' and IGCs continue to deliver an approach that fully reflects members interests.

### 2. Transaction costs and charges

The second most prominent challenge was around transaction costs and charges.

In the early stages the committees had to develop various relationships, particularly with the provider so that the committee could obtain the necessary resources for data and analysis to feed into the annual IGC Chair report.

IGCs reported that providers were helpful in their attitudes but there were issues for them in understanding the data for transaction costs and charges. Many IGCs reported that this has been on-going and that gaining a better, more detailed understanding about these costs and charges is an area that they will focus on over the next year.

### 3. Legacy Schemes

The third main challenge focused on those IGCs governing legacy schemes and identify whether such schemes were providing value for money. Some IGCs also commented that understanding the data for old schemes was an additional issue, making it increasingly complex to assess value for money.

## Chart 1: Independent Governance Committees

PENSIONS POLICY INSTITUTE

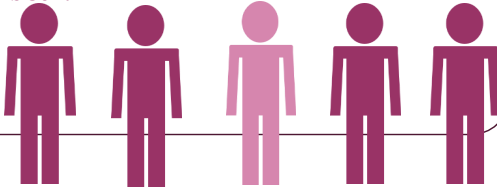
PPI

The majority of IGCs have 5 members and a couple have 6.

All with one provider representative.

Most consider this to be the correct balance of independent members vs. representatives.

Although there are some IGCs who govern only a closed or open scheme, there are more who have a mixture of both.



IGCs hold 4-8 meetings per year lasting between 3 to 4 hours

## Chart 2: Summary of main themes emerging from the survey results

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- **Value for money**

There were issues around defining, assessing and measuring the concept. This was the main challenge IGCs have been facing over the past 12 months much of their future work is likely to be around developing a measure that fully reflects member views.

- **Transaction costs and charges**

There were issues around understanding the transaction costs and charges. Many IGCs struggled to understand in depth the transaction costs and charges which is key to performing their role fully.

- **Legacy schemes**

There were issues around value for money in legacy schemes and understanding old data. Many IGCs expressed concerns over understanding legacy scheme data and getting members on to more modern platforms due to not receiving value for money in historic policies.

The IGCs stated that future work to overcome these challenges would revolve around:

- Overseeing the implementation of further changes to legacy schemes that the IGC have suggested following the independent project board recommendations;
- Considering transferring some members on to more modern platforms. However, there are transitional issues that need serious deliberation.

**Other findings from the research** The survey looked at various aspects of the role as an IGC, including the relationship between it and the scheme members, the scheme's quality and the writing of the Chair's Annual Report.

The majority of chairs reported that members had had an opportunity to interact with the IGC; many committees have implemented a number of methods for doing so. However, some have yet to put theirs into place.

Those that have been interacting have been doing so in various ways:

- Through direct email links;
- Focus groups and member forums;
- Surveying members;
- Reviewing complaints.

Some IGCs need to determine how these channels help inform them in terms of member opinions.

The chairs also responded that they felt more member communication was required and the cur-

## Chart 3: Main challenges when writing the Annual Reports

### Audience

Many of the IGCs found the audience the main challenge when writing the annual report. As the target audience (members) are more likely to be less engaged, the report needs to be written so that it is accessible and easy to understand. However, the annual report is aimed at both members and stakeholders therefore writing to suit both these audiences proved difficult.

### Content/Format

The content and format of the report was another challenge. There was a lack of guidance around what was expected and many of the IGCs had to decide what issues were the most important and need to be included within the report.

### Value for money

Some of the IGCs found 'value for money' a challenge when writing the annual report. Obstacles that arose were addressing value for money in an objective way and avoiding being premature in deciding what value for money is to members within the report.

### Transparency vs. Confidentiality

When writing the annual report some IGC chairs stated that reporting on commercially sensitive data and being transparent proved difficult as it required getting a balance between transparency and confidentiality.

rent methods of interaction needed improving; for example, although a direct email link was offered, very few members had utilised it.

A majority of chairs felt the scheme quality was good. However, the response was more positive for open schemes compared to legacy ones.

The main aspects considered as good quality were investments, charges, administration and member engagement. The general sentiment is that the cur-

rent provider offering is of a good standard.

The writing of the IGC Chair annual report produced a number of challenges, specifically:

- Writing for multiple audiences;
- Making sure it was accessible for all;
- Approaching value for money objectively; and
- How to achieve the correct balance between transparency and confidentiality over sensitive data.

Chart 3 gives further details about the annual report challenges.

### The Future of the IGCs

The Chairs were asked about the challenges over the next 12 months, in addition to the three themes previously identified. The majority responded with concerns around improving the clarity and understanding of transaction costs and value for money and legacy schemes (Chart 4).

## Chart 4: Challenges over the next 12 months

### What are the key challenges for the next 12 months?

- Overseeing the implementation of the changes that have been agreed with the provider for example, independent project board recommendations or agreed legacy scheme changes.
- Achieving an approach to value for money that fully reflects members interests
- Improving member communications
- Working through the consequences of any new exit charge regulation
- Developing industry wide benchmarks
- Publishing the annual report
- Reviewing old investment strategies

Some IGCs suggested areas of development in the future, such as increasing digital access and negotiating pricing with providers (Chart 5).

### Conclusion

The PPI survey identifies a consistent picture of the process details and make-up of IGCs. The main challenges include:

- Definition, assessment and measurement of value for money;

- Understanding transaction costs and charges; and
- Legacy schemes.

These themes set out much of the agenda for the next twelve months especially achieving an approach to value for money that suits all members.

### References:

1. DWP 2014 "Better workplace pensions: Putting savers' interests first"
2. FCA 2014 "Proposed rules for independent governance committees"
3. TPR 2016 "Declaration of compliance report"

4. PPI 2014 "Transitions to retirement: How complex are the decisions that pension savers need to make at retirement?"
5. PPI 2015 "The Future Book: Unravelling workplace pensions"
6. FCA 2014 "Proposed rules for independent governance committees"
7. DWP 2014 "Better workplace pensions: Putting savers' interests first"
8. FCA 2014 "Proposed rules for independent governance committees"
9. DWP 2014 "Better workplace pensions: further measures for savers"
10. FCA 2014 "Proposed rules for independent governance committees"
11. FCA 2014 "Proposed rules for independent governance committees"

## Chart 5: Future work

- What more can be done by the IGCs?
- Further oversight into value for money and appropriate benchmarking across the market place
- Better understanding of transaction costs
- More interaction between the IGC and members
- Transfer those who are in older schemes on to more modern platforms
- Continue pressing the provider on pricing and digital access for members
- In due course cover the retirement processes and outcomes for members