

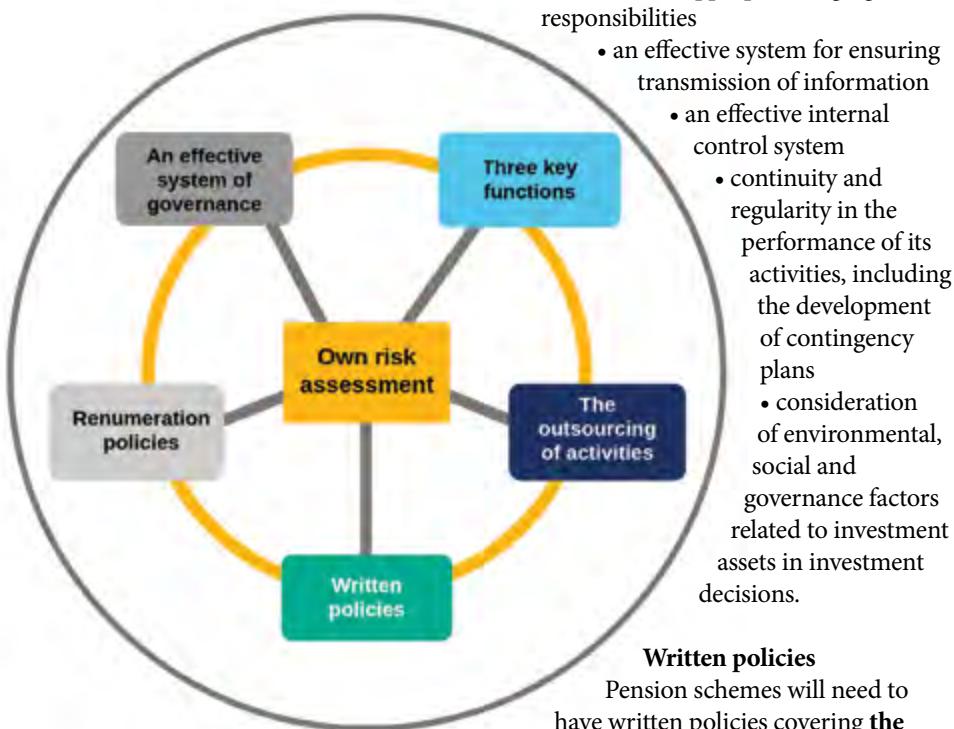
# Setting standards

► Judith Hetherington looks at the upcoming pension scheme governance guidelines for trustees

In January 2019, the Pensions Act 2004 was amended to require trustees to 'operate an effective system of governance including internal controls'. The Pensions Regulator is currently preparing a code of practice that will set out how it expects trustees to do this.

## Overview

New regulations require the code of practice to cover the following areas:



**Three key functions** of risk management, actuarial and evaluation of the system of governance will be covered by the code of practice.

Most trustees already have these covered, but the new challenge will be

how trustees **evaluate their system of governance**, including internal controls and documentation of policies.

**The effective system of governance must be subject to regular review, covering:**

- sound and prudent management of activities
- an adequate and transparent organisational structure with a clear allocation and appropriate segregation of responsibilities
- an effective system for ensuring transmission of information
- an effective internal control system
  - continuity and regularity in the performance of its activities, including the development of contingency plans
  - consideration of environmental, social and governance factors related to investment assets in investment decisions.

## Written policies

Pension schemes will need to have written policies covering **the three key functions, outsourcing of activities and a remuneration policy**. We expect the code of practice to provide guidance as to what these policies should cover – examples might be delegation authorities, managing conflicts of interest, whistle blowing,

supplier selection and monitoring, payment authorities and data security.

An **own risk assessment** will need to be carried out and documented covering how the trustees or pension managers:

- integrate the own-risk assessment into the occupational pension scheme's management and decision-making processes
- assess the effectiveness of the risk-management system
- prevent conflicts of interest with the employer, where the occupational pension scheme outsources key functions to the same person as the employer, or to any person employed by the employer
- assess the occupational pension scheme's funding needs, with reference to the recovery plan where applicable
- assess the risk to members and beneficiaries relating to the paying out of their benefits and the effectiveness of any remedial action taking into account
- assess the mechanisms protecting retirement benefits, including, as applicable, guarantees, covenants or any other type of financial support by the employer, insurance or reinsurance, or coverage by a pension protection scheme
- assess the operational risks
- assess new or emerging risks in relation to where environmental, social and governance factors are considered in investment decisions.

## Considerations for scheme trustees

Trustees need to think about how they evaluate their systems of governance and internal controls, when they will carry out the evaluation and how they document it. If they do not already have an evaluation system in place, then it will need to be built into their business plan. Consideration will need to be given as to what help is needed in order to undertake this assessment.

Many trustees will already have a risk register that measures the impact and likelihood of key risks and measures

the effectiveness of mitigating actions. If done properly, this can be a very effective tool for scoring risk exposures and comparing to risk appetite, allowing trustees to focus resources on those risks where more work needs to be done.

Trustees might consider appointing an internal auditor or specialist adviser, to help them assess key controls and

policies and provide assurance that they are suitable and operating effectively. The scheme administrator, investment manager and custodian may provide assurance reports that can help with the assessment of internal controls.

Delegation of these activities to a sub-committee of the trustee board can be an effective way of ensuring

adequate time and resources is given to these activities, drawing on specialist knowledge of the trustees and advisers.

While these new requirements may seem onerous for some schemes, the regulations acknowledge that the system of governance must be proportionate to the size, nature, scale and complexity of the activities of the occupational pension scheme.

Schemes of all sizes are required to operate an effective system of governance, but some of the above requirements will not apply to schemes of fewer than 100 members.

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