Proposed rules for independent governance committees

RESPONSE FROM ICAS TO THE FINANCIAL CONDUCT AUTHORITY

10 October 2014
Introduction

The ICAS Pensions Committee welcomes the opportunity to comment on the FCA’s proposed rules for independent governance committees (IGCs).

Our CA qualification is internationally recognised and respected. We are a professional body for over 20,000 members who work in the UK and in more than 100 countries around the world. Our members represent different sizes of accountancy practice, financial services, industry, the investment community and the public and charity sectors.

Our Charter requires ICAS committees to act primarily in the public interest and our responses to consultations are therefore intended to place the public interest first. Our Charter also requires us to represent our members’ views and to protect their interests, but in the rare cases where these are at odds with the public interest, it is the public interest which must be paramount.

Key points

We have not responded to the individual consultation questions but rather our comments on various aspects of the proposals are set out below.

Our main concerns about the proposals arise from the following two themes:

• How independent would IGC members actually be or be perceived to be? and
• How likely are IGCs to fulfil their duty to assess value for money?

The independence of IGC members

We are concerned that the independence of IGC members will be compromised from the outset through all members being paid directly by the provider. Being paid by the provider could stifle the type of challenge IGCs are expected to give or could give scheme members the impression that challenge is not being made. Representatives of corporate trustee firms sitting on IGCs could be doubly conflicted through being remunerated by their firm which in turn may receive a good income stream from the provider through a trusteeship on the provider’s master trust.

If the FCA had the power to appoint a nominee to each IGC, this could guarantee a degree of independence. However, it may be preferable to levy the providers to cover payments to IGC members and for the FCA to be involved in the appointment of the majority of those members. If this approach was taken, we would encourage the FCA to take a broad and considered approach to these appointments. We would favour personal appointments to IGCs rather than corporate appointments to minimise the potential for conflicts of interest to arise.

In summary, we do not believe that the duty of IGC members to act in the interests of scheme members and the proposals for managing conflicts of interest will be sufficiently effective.

IGC duty to assess value for money

Annex 1 of the consultation paper ‘market failure and cost benefit analysis’ gives a flavour of the scale of the task which could conceivably sit with a relatively small number of people. Table 2, of Annex 1, estimates that the proposals will require 16 large providers to introduce IGCs and 15 small providers to introduce governance advisory arrangements (GAAs). Therefore, there will be approximately 31 new governance arrangements implemented to cover £336 billion of assets or 19% of all UK pension assets belonging to 8.6 million members. A large proportion of these assets will fall within the scope of the 16 IGCs – a group of as few as 80 people, assuming each ICG has no more than the five members required.

How would value for money be defined and assessed from the perspective of the ‘patient investor’? While we believe that having a small number of IGC members across the country makes an FCA levy viable, we question whether it is feasible for such a small group of people to assess value for money on an on-going basis without unintended consequences. This could limit the choice of arrangements available during the pension accumulation phase with the effect that investment strategies could become more passive in the pursuit of facilitating a more definitive assessment of value for money.

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1 Current UK pensions market (figures 2012, ONS)
Providers operate multiple schemes and it is difficult to envisage how 80 people will be able to gather and analyse sufficient relevant information on the schemes offered by a provider and compare these to the offerings of other providers in a meaningful way. It may be more realistic to IGCs to consider instead the overall control environment, for example, by reviewing reports prepared by internal and external auditors (including AAF 01/06 assurance reports on internal controls) and to ensure that recommendations made are responded to and agreed actions delivered.

The cost of contract-based schemes should be less than trust-based schemes, with the additional governance arrangements operated by trust-based schemes contributing to the cost differential. If an employer places greater emphasis on governance than cost when it is selecting a scheme then the legal form of the scheme could be the defining factor and it would select a trust-based scheme. Therefore, we question whether strengthening the governance arrangements of contract-based schemes in a manner which could be viewed as replicating trust-based style governance arrangements is the correct approach.

In summary, we believe that the proposals would be workable if oversight committees with a more realistic and proportionate role were established rather than governance committees as currently envisaged. The extent of the FCA levy on providers would provide a budget for such oversight committees and the budget would be a factor in influencing the scope of their activities.

We have the following additional observations and comments:

The indemnification of IGC members by providers
We agree that the indemnification of ICG members by providers should not be mandatory on the grounds that indemnification could provide a further disincentive to challenge the provider and therefore impact negatively on the performance of ICG members and the overall effectiveness of the IGC. Perversely, this could encourage providers to indemnify IGC members.

Member (consumer) representation
As a general principle, we believe that consumer representation within the governance arrangements for pensions is valuable. However, the appointment of member nominated trustees in trust based arrangements provides a challenge around knowledge and training and we believe IGC membership would provide a bigger challenge to scheme members. Therefore, we agree that member representation on IGCs should not be mandatory. Instead, we would welcome a requirement for scheme members to be involved in the appointment of IGC members.

FCA approved ICG members
While we do not oppose the proposals around FCA approved members, we are not convinced that it will be possible to construct a list and for appointments to be made from that list in time for the April 2015 deadline for the establishment of IGCs.

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