

Getting ready for the Code: reviewing the ESOG

What makes for a good ESOG review?

Welcome back to the Muse series **Getting ready for the Code**, where we are sharing tips and tools to help you navigate the Code. Get in touch to find out more at governanceservices@museadvisory.com.

This article in the series is a short practical look at **how to get the most out of your ESOG review** – the review of your Effective System of Governance that will inform your initial Own Risk Assessment (ORA).

TPR say in the introduction to the Draft Code and have stressed consistently since: “Governing bodies need to use their judgement as to what is a reasonable and proportionate method of ensuring compliance for their scheme.”






This article aims to help you make practical sense of what’s reasonable and proportionate for your ESOG.

The Final Code is coming soon, to apply proportionately

TPR have been clear that a first iteration of the Final Code which they expect to be in force by ‘late Autumn’ will be a tidied up version of the draft, with the Own Risk Assessment (ORA) more proportionate.

Many Trustees are planning to carry out an ESOG gap analysis to review their governance and documentation against Code requirements.

What does a good ESOG review look like for us?

-  *Our ESOG review starts with the end in mind*
-  *We evidence compliance in a proportionate way*
-  *We rebadge and group related items where we can*
-  *We prioritise changes that help us move the dial*
-  *We embed our ESOG and ORA processes into BAU*

June 2022



The ESOG review informs actions you decide to take on compliance, to improving your governance and strengthening the way you manage risk. Progress can be reflected in your initial ORA. The Final Code will confirm the grace period for the ORA - it may be more than a year.

Smaller, less well-resourced schemes will have simpler ESOG reviews and ORAs, proportionate to needs.

Faced with a lengthy and detailed Code with many of the modules forming part of the ESOG, where do you start your review and what is your benchmark?

Starting with the end in mind

Starting with the end in mind enables you to get value from the review, and judge what is proportionate. Considering these main questions gives you a top-down perspective on what you need to have in place:

What MUST we do for compliance
What, for our situation, is a proportionate response?



Governance design needs to stay in step with what you are seeking to achieve, mitigating risk and helping you cope well with change, whilst building in contingencies so as to keep your scheme and outcomes on track.

Where are we going? The more you can focus on articulating and regularly checking in on your Trustee objectives for the scheme, the better. Not only your financial objectives (for DB these are around funding, covenant and investment, for DC around member outcomes, member value), also think about your non-financial objectives relating to administration, clean data, operations and member engagement. These all need to align with a financial journey plan and with your objective for scheme governance – is it best practice or something more proportionate, for compliance?

What could knock us off course? This question helps you work out what the most significant risks are to achieving objectives, and how these may impact an overall journey plan. What events could knock you off course, slow you down or speed things up? How well could you tolerate and/ or cost effectively control them? These are the key risks and key control needs which your policies, processes and risk management framework need to address.

You may find it helpful to take a look at earlier articles in this series on risk and controls, assurance and reporting at www.museadvisory.com/viewpoints.

What resources have we got? What resources can you call on to deliver what you are aiming to do and where are the gaps, risks in this. Typically examples might be key person or succession issues, gaps in advisory needs, a lack of critical project resource, some notably conflicted roles? How clear are your delegations to all concerned? Is everyone pulling towards the same objectives? If you need different resources, what are the cost/ value benefits to progress objectives or mitigate risk? Some changes can often be valuable, reducing timelines in important work, saving wider cost, better allocating resource.

Governance priorities for the ORA: Over and above being compliant, looking through the lens of objectives, key risks and resources will help you see where any important governance gaps lie, and the extent to which your policies, processes and procedures fit with what you need.

Using the ESOG review and ORA process to embed this way of working – top-down for governance design and risk scanning and bottom up for scheme compliance and effectiveness of controls – is a good way to drive value from your governance, adopting the Code in a proportionate way. Your ORA report is then also meaningful and supports ways you engage with the sponsor and with members on outcomes.

We have shared this thinking with TPR who are supportive of this approach.

Evidencing compliance in a proportionate way

In reviewing your system of governance against the Code there are these elements to consider:

1. Legal duties, where the Code says 'must' – to be checked and confirmed in your review
2. TPR expectations where the Code says 'should' – these are for your judgement on how they apply
3. Necessary to operate a scheme where TPR says 'need' – a well-run scheme has these in place
4. Good and evolving 'best practice' that TPR points to – for you to be aware of and apply as suits.

If an aspect of Code compliance does not have a bearing on your objectives, main risks and journey, you will allocate less time and resource to it – serving to keep your approach reasonable and proportionate.

This may be the case for many of the 'should' and 'best practice' categories above, peppered throughout the Code and ESOG modules, including aspects of the newer requirements stemming from IORP II.

For example, a Trustee Remuneration policy is a 'must' – both for trustee director and for adviser and service provider 'remuneration' arrangements paid by the Trustee or Company. But what the policy covers in its detail and scope is up to the Trustee to determine, and practice here will obviously evolve.

Your own policy might reasonably stick to some core principles, with a process to apply those principles, so that your ORA check can review if any change is needed e.g. in light of wider trends.

Looking to rebadge and group related items in the documentation review

Continuing on that theme, many Trustees will have a raft of good policy documents which are not necessarily organised neatly into Code modules or called the same things, but which are fit for purpose.

You won't need to spend time perfecting these if it's not going to help you do things materially better. Pointing to where the Code requirement is covered is going to be sufficient, and you could have a simple table on the front of a policy to help keep tabs on its links to the Code and what you call things.

Several clients are using our 'master' documents list which shows what is needed for the Code and within this what is needed for ESOG and ORA compliance. We will be updating this to a final version when the final Code is available. We are also templating policy documents in a proportionate way for areas that may typically be newer or missing, with hints and tips for using them.

Let us know if you would like to use these or talk to us about your approach to documentation review.

You are likely to have a logical way of grouping items. For example, your adviser and service provider policy work might sit together to cover selection and appointment, with remuneration, contract management and review. It may make more sense to look at how these vital Trustee areas join up.



The governance benefits: Final thoughts to help you pull the ESOG review together

The ORA is an assessment of your system of governance – helping you determine whether you have the right controls in place and that they are effective in managing your risks.

A few thoughts stemming from what we've said above:

- In making any changes to your governance as a result of your ESOG review, aim to focus on what is going to help the Trustee move the dial on its objectives, key risks and how well you use resource.
- Notice areas where you may be doing more than needed – can you use resource/ budget better?
- Compare notes with your advisers and other schemes, there will be useful Code learnings to share.
- Aim to embed your ESOG review via the ORA process into your BAU business plan from 2023.



Muse Advisory's 'Getting Ready for the Code' series

Contact Rosanne, Jo, Julia or Barry for practical help and independent advice at governanceservices@museadvisory.com

Our next article will look at the [Risk Management and Internal Audit Functions](#).