

Understanding the General Code of Practice:

# *Guide to the ESOG*

January 2024

This guide provides a high-level summary of the new Effective System of Governance (ESOG) requirements being introduced by The Pensions Regulator's (TPR) General Code of Practice (the "Code"). We encourage trustees to read this guide alongside the Code which is available on **TPR's website**.



# Introduction to the ESOG

Pension schemes are required to establish and operate an effective system of governance otherwise known as an ESOG. An ESOG is essentially a collection of processes and policies that a scheme should have in place in order to operate effectively and efficiently.

An ESOG framework includes processes and procedures across various areas relating to management of activities, organisational structure, investment matters & communications and disclosure. It also includes internal controls.

Once an ESOG is established, each element should be reviewed at least every three years (or sooner if there is significant change to the scheme's governance or key risks) to see whether it is functioning as planned. Trustees should have policies in place for ESOG reviews, and these policies should also be reviewed every three years.

## Investment matters

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## Internal Controls

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- Data monitoring and improvement
- Receiving contributions
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## Management of activities

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- Conflicts of interest
- Managing advisers and service providers
- Risk management function



## *Why an ESOG matters*

Having a defined and robust governance framework for your scheme is fundamental to making good decisions and achieving better outcomes for your members. It puts your scheme ahead of the pack when it comes to dealing with the unexpected and taking advantage of market opportunities. We encourage governing bodies to embrace the new requirements proportionately and in a way that enhances how they operate.

Many pension schemes will already have robust governance frameworks in place and meet most of the requirements for an effective system of governance. However, it is likely that some changes to schemes' existing policies and processes will be required to meet new requirements.

## *The purpose of the Code*

TPR's codes of practice are not statements of law, except when set out in legislation. Codes of practice set out TPR's expectations on how it expects schemes to comply with the law in certain areas. The General Code distinguishes between legal duties and TPR's expectations. In this guide:

- Legal duties are shown by using the word **'must'**
- The Regulator's expectations use the word **'should'**

## *A note on proportionality*

Whilst TPR has broadly the same expectations for each type of scheme, the systems and controls put in place by a scheme should be proportionate to its size, scale, nature and complexity and the amount of resources and support available to the trustee to make changes. There is currently no guidance on how proportionality should be assessed and trustees may wish to discuss their approach with their legal advisers. In our view, it may be helpful for trustees to consider the following when addressing the new requirements:

- **Size** - there are some exemptions for schemes with fewer than 100 members
- **Scale** - larger schemes may have more involved governance frameworks and there might be a lighter touch approach for smaller schemes
- **Complexity** - there might be greater complexity where there are lots of employers or benefit categories, or for schemes with complex investment and funding strategies
- **Nature** - different approaches may be taken depending on the status of the scheme (open or closed to accrual) and where a scheme is relative to its derisking journey and some modules will not apply to DC schemes. Circumstances, such as a challenged covenant or funding position, may also require additional governance in order to support timely decision making.

## *ESOG Policies and procedures*

The rest of this document sets out a high-level summary of each of the areas included in the ESOG and the policies and procedures trustees need to consider and address.

# Management of activities

Module references	Summary of requirements	Policies and procedures required
Role of the governing body	<ul style="list-style-type: none"><li>Those responsible for appointing members to the governing body need to do so using the principles of proportionality, fairness and transparency, while also considering the mix of skills and experience needed by the governing body.</li><li>As far as possible, the governing body should be well-balanced and diverse, with its members demonstrating varied skills, knowledge and experience.</li><li>Governing bodies <b>should</b> meet TPR’s expectations on how trustees of trust-based schemes should act as set out on page 10 of the Code. These include behaviours such as acting honestly and with integrity, meeting legal obligations and acting in the interests of all scheme members and beneficiaries. Those acting as professional trustees should comply with TPR’s professional trustee standards and guidance, and professional codes of conduct and trustee accreditation.</li></ul>	<ul style="list-style-type: none"><li>Appointment and induction processes for new Trustees</li></ul>
Meetings and decision making	<ul style="list-style-type: none"><li>Governing bodies <b>must</b> include certain items in their written meeting records as set out on page 20 of the Code, such as the meeting’s details, attendees and decisions made.</li><li>Governing bodies <b>should</b> also establish processes for planning and running meetings and making robust decisions, as set out on page 21 of the Code.</li></ul>	<ul style="list-style-type: none"><li>Terms of reference for any sub-committees</li><li>Meeting minutes</li><li>Records of decisions taken</li></ul>
Remuneration and fee policy	<ul style="list-style-type: none"><li>The requirement for a remuneration policy only applies to schemes with 100 or more members.</li><li>As set out on page 23 of the Code, governing bodies <b>should</b> establish a proportionate written remuneration policy that sets out the basis and means for paying those undertaking activities in relation to the scheme that are paid for by the governing body. It applies to all persons or corporate bodies who run the scheme, carry out key functions or whose activities materially impact the scheme’s risk profile and any outsourced service providers. The policy should support the effective management of the scheme and include measures to mitigate against potential conflicts of interest and an explanation of the decision-making process for the levels of remuneration and why these are considered appropriate.</li><li>The policy <b>should</b> be reviewed every three years. It is not necessary to publish the remuneration policy online or otherwise made available to members.</li></ul>	<ul style="list-style-type: none"><li>Remuneration policy</li></ul>



# Management of activities

Module references	Summary of requirements	Policies and procedures required
Knowledge and understanding  Governance of knowledge and understanding	<ul style="list-style-type: none"><li>Governing bodies <b>should</b> maintain a list of all items that they should be familiar with, and review this regularly. The items that TPR considers to be key are set out on pages 26 to 30 of the Code. The list is not exhaustive and covers areas such as pensions law, scheme specific information, scheme funding and investments, risk management, administration and communications.</li><li>The governing body as a whole <b>should</b> demonstrate they jointly possess the skills, knowledge and experience to run the scheme effectively by meeting the requirements set out on page 32 of the Code. This, for example, includes having sufficient skills to question advice.</li><li>Members of a governing body <b>should</b> invest sufficient time in their learning and development in order to ensure their knowledge and understanding is maintained. Members of a governing body should meet the requirements set out on page 33 of the Code. This includes, for example, identifying gaps in knowledge and understanding at least annually.</li></ul>	<ul style="list-style-type: none"><li>List of items trustees should be familiar with (as per the guidance given in the Code)</li><li>Training plan for the ongoing maintenance and development of knowledge</li><li>Records of learning activities (training logs)</li><li>Approach to reviewing knowledge and understanding and addressing any gaps</li></ul>
Dispute resolution procedures	<ul style="list-style-type: none"><li>Governing bodies <b>must</b> put in place formal procedures and processes to investigate and decide upon pension scheme disputes quickly and effectively.</li><li>In particular, governing bodies <b>must</b> ensure their scheme’s procedures allow a reasonable period, which should be at least six months beginning on the date their interest in the scheme stopped, for people or their representatives to make their applications.</li><li>The full requirements for resolution procedures are set out on pages and 152 and 153 of the Code. We would anticipate most up to date IDRPs to meet these requirements.</li></ul>	<ul style="list-style-type: none"><li>Internal Dispute Resolution Procedure</li></ul>
Scheme continuity planning	<ul style="list-style-type: none"><li>Governing bodies <b>should</b> develop and implement continuity plans to ensure that the operations of their scheme can be maintained in the event of a disruption to the activities of the scheme. Such events could include disruption to the scheme’s general administration, the service provided by advisers and trustee decision making.</li><li>TPR’s expectations of governing bodies are set out on page 54 of the Code.</li></ul>	<ul style="list-style-type: none"><li>Scheme continuity plan covering all trustee business</li></ul>

# Organisational structure

Module references	Summary of requirements	Policies and procedures required
Appointment and role of the chair	<ul style="list-style-type: none"><li>Governing bodies of occupational pension schemes need to have someone who fulfils the role of chair as a matter of best practice. The role of the chair is set out on page 19 of the Code, and includes skills such as communication, debating, challenging, negotiating and the ability to gather and understand diverse views.</li><li>TPR expects the appointment of a chair to be set out in a robust and documented process.</li></ul>	<ul style="list-style-type: none"><li>Policy on the process for appointing a chair</li></ul>
Conflicts of interest	<ul style="list-style-type: none"><li>Governing bodies <b>should</b> meet TPR’s expectations for identifying and recording conflicts of interest as set out on page 56 of the Code. In particular, governing bodies should be mindful of any conflicts of interest arising from advisers and service providers both at the time of their appointment and as any conflicts arise.</li><li>Governing <b>should</b> have processes in place to ensure that their decision-making is not compromised by actual or potential conflicts as set out on page 57 of the Code. As part of this, governing bodies should consider the different options for dealing with conflicts, which may include taking independent advice, withdrawal from discussions and the decision-making process and in some cases resignation.</li></ul>	<ul style="list-style-type: none"><li>Conflicts of interest policies for trustees and advisers</li><li>Conflicts of interest register</li></ul>
Managing advisers and service providers	<ul style="list-style-type: none"><li>Governing bodies <b>should</b> follow TPR’s expectations in relation to the selection, appointment, management and replacement of professional advisers and service providers, as set out on pages 38 to 41 of the Code. We anticipate that whilst most schemes will have tested frameworks in place, many will need to consider how best to document their approach as part of the ESOG.</li><li>The requirements for selecting, appointing, managing, and replacing professional advisers and service providers as detailed on pages 39-41 only apply to schemes with 100 or more members.</li></ul>	<ul style="list-style-type: none"><li>Policy for appointing and managing advisers and providers, including addressing poor service</li><li>Delegation schedule(s)</li><li>Performance indicators (KPIs, SLAs, objectives)</li><li>Records of assessment of advisers and progress</li><li>Procedure for replacing or changing advisers or providers</li></ul>
Risk management function	<ul style="list-style-type: none"><li>Governing bodies of schemes with 100 or more members or more <b>should</b> have in place a proportionate risk management function.</li><li>The risk management function is responsible for supporting the governing body to identify, evaluate and record risks, and monitor and manage risks.</li><li>The risk management function is in addition to the requirement to prepare an own risk assessment.</li></ul>	<ul style="list-style-type: none"><li>Written policy regarding the operation of the risk management function</li></ul>

# Investment matters

Module references	Summary of requirements	Policies and procedures required
Investment governance	<ul style="list-style-type: none"><li>The term ‘investment governance’ refers to the policies and procedures that ensure a governing body complies with any obligations it has in relation to investment. The obligations of governing bodies of DC and DB schemes is set out on page 73 of the Code and includes, for example, having a good working knowledge of investment matters and investment powers and duties in the scheme and producing a SIP and annual implementation report.</li><li>Governing bodies with investment responsibilities <b>should</b> also have certain measures in place, for example around clarity of roles and responsibilities and investment decision making, as set out on pages 74 and 75 of the code.</li></ul>	<ul style="list-style-type: none"><li>Statement of Investment Principles (for schemes with 100 or more members)</li><li>Documentation of the objectives, roles, responsibilities and reporting relationships of all parties involved in making investment decisions</li><li>Terms of reference for any investment sub-committee</li><li>Policies on the use of investment advisers</li><li>Procedure for considering the performance of investment managers and advisers</li></ul>
Investment decision making	<ul style="list-style-type: none"><li>Governing bodies of trust-based pension schemes with 100 or more members <b>must</b> invest in a way that ensures security, quality, reasonable liquidity and profitability for the scheme’s portfolio as a whole; invest mainly in regulated markets; and make sure scheme assets are properly diversified.</li><li>Governing bodies <b>should</b> have processes in place to ensure the prudent management of investments as set out on page 77 of the Code. This includes, for example, processes around investment decision making, clarity around roles, responsibility and accountability and the management of conflicts of interest.</li></ul>	<ul style="list-style-type: none"><li>Process to ensure investment decisions are made in an effective and timely manner</li><li>Regularly assess the effectiveness of decision making</li><li>Document objectives, strategies and changes to investments or investment strategy</li><li>Have clear terms of reference for any sub-committees</li><li>Document reasons for any investment in non-regulated markets</li></ul>
Investment monitoring	<ul style="list-style-type: none"><li>Governing bodies <b>should</b> have systems in place to review the performance of their investments as set out on pages 79 and 80 of the code. This includes, for example, procedures to review and negotiate the terms of contractual arrangements, regularly monitoring the performance of the scheme’s investment advisers and setting expectations for their investment managers in relation to investment performance, returns and risk.</li><li>To govern effectively and meet the Regulator’s expectations, governing bodies <b>should</b> set clear expectations for their investment managers where relevant.</li></ul>	<ul style="list-style-type: none"><li>Procedure to review and negotiate the terms of contractual arrangements and fund documents with managers and advisers</li><li>Procedures to monitor investments and performance</li><li>Policy on whether and how to report on investment performance to interested parties (members, employers)</li></ul>

# Investment matters

Module references	Summary of requirements	Policies and procedures required
Stewardship	<ul style="list-style-type: none"><li>• Effective stewardship includes, but is not limited to, the consideration of environmental, social and governance factors (ESG) in investment decision-making and how those factors might impact the balance of risks/returns over the longer term.</li><li>• Unless exempt, the SIP <b>must</b> include the governing body’s policies in relation to financially material ESG considerations and the exercise of voting rights attaching to investments.</li><li>• Governing bodies that are required to produce a SIP, <b>must</b> also produce an Implementation Statement (IS) setting out how they acted on stewardship policies set out in the SIP. The IS must be included in the scheme’s annual report and made publicly available, free of charge, on a website. More details on the IS can be found on page 82 of the Code.</li><li>• Page 83 of the code sets out the Regulator’s expectations of governing bodies with investment responsibilities.</li></ul>	<ul style="list-style-type: none"><li>• Process for exercising the rights and responsibilities relating to the investment held</li><li>• Statement of investment principals</li><li>• Policy on monitoring and regular review of investment managers’ stewardship practices</li><li>• Identify and account for the systemic risk of climate change in decisions made about investment and funding and engage with stakeholders to mitigate these risks</li><li>• Implementation statement</li></ul>



# Investment matters

Module references	Summary of requirements	Policies and procedures required
Climate change	<ul style="list-style-type: none"><li>Governing bodies <b>should</b> ensure that consideration of environmental factors is part of its investment decision-making. TPR expects governing bodies to:<ul style="list-style-type: none"><li>understand from their advisers and asset managers how short and long-term climate change risks and opportunities are built into their recommendations; and</li><li>understand what measures are being taken to reflect climate change risk within investment portfolios.</li></ul></li><li>Governing bodies are not currently required to align their investment and funding plans with the objectives of the Paris Agreement and other climate change goals, such as the UK’s own target of net zero emissions by 2050. However, they may wish to examine how their governance practices and investment decision-making take into account global progress towards those goals.</li><li>Governing bodies <b>should</b>, as part of their internal controls risk assessment, assess the risks and opportunities associated with climate change.</li><li>Governing bodies of certain schemes <b>must</b> meet the governance and reporting requirements set out in regulations under the Pension Schemes Act 2021, relating to climate-related risks and opportunities. For schemes in scope, governing bodies <b>must</b> take steps to identify, assess and manage climate-related risks and opportunities and report on what they have done. These reporting requirements align with the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD).</li></ul>	<ul style="list-style-type: none"><li>Maintain and document processes for identifying and assessing climate related risks and opportunities</li><li>Document the management of climate related risks in the risk register</li></ul>
Statement of Investment Principles	<ul style="list-style-type: none"><li>The purpose of a SIP is to set out the governing body’s investment strategy, including the investment objectives and investment policies they adopt.</li><li>Schemes with 100 or more members <b>must</b> prepare a SIP and review it at least every three years.</li><li>Details of what a SIP must contain are set out on pages 88 and 89 of the Code. Governing bodies <b>should</b> also consider the Regulator’s expectations when preparing and maintaining their SIP as set out on pages 90 and 100 of the Code.</li></ul>	<ul style="list-style-type: none"><li>Statement of investment principles</li></ul>



# Communication and disclosure

Module references	Summary of requirements	Policies and procedures required
General principles for member communications	<ul style="list-style-type: none"><li>When preparing communications to members, the governing body <b>should</b> meet the general principles set out by TPR on page 130 of the Code. These principles include ensuring communications are accurate, clear, concise, relevant and in plain English and considering the use of technology and producing accessible content such as Braille or large font.</li></ul>	<ul style="list-style-type: none"><li>Meet TPR's general principles when communicating with members</li></ul>

# Internal Controls

Module references	Summary of requirements	Policies and procedures required
Identifying, evaluating and recording risks	<ul style="list-style-type: none"><li>Governing bodies <b>must</b> establish and operate internal controls which are adequate for the purpose of securing that the scheme is administered and managed in accordance with the scheme rules and with the requirements of the law.</li><li>Governing bodies <b>should</b> ensure that their internal controls are proportionately documented and reviewed at least annually or sooner if substantial changes take place.</li><li>TPR expects that the process for monitoring, recording and mitigating risk is closely integrated with the operation of internal controls.</li><li>Governing bodies <b>should</b> also have in place the systems, arrangements and procedures in the modules listed in first column of this table.</li></ul>	<ul style="list-style-type: none"><li>Risk register</li><li>Procedures to ensure financial transactions are processed promptly and accurately</li><li>Record keeping processes</li><li>Data monitoring processes, including data reviews and data protection</li><li>Payment schedule (DC schemes) or schedule of contribution (DB Schemes)</li><li>Procedure for monitoring contributions (if any)</li><li>An IT Policy covering maintaining, upgrading, and replacing hardware and software</li><li>Performance indicators (KPIs, SLAs, objectives)</li><li>Procedures in place to reconcile employer data and scheme data, if appropriate</li><li>Procedures in place to address when an sponsor fails to meet their legal duties to the scheme, in relation to scheme data and record keeping</li><li>Cyber security procedures</li></ul>
Internal controls		
Financial transactions		
Record-keeping		
Data monitoring and improvement		
Receiving contributions		
Monitoring contributions		
Maintenance of IT systems		



# How we can help

LCP’s Pensions Management Consulting team of governance consultants and scheme managers, along with other specialists at LCP, are well placed to help you meet the new requirements in the General Code.

## Our services

- Governance Healthcheck**

- Review your existing governance framework against the effective system of governance requirements of the General Code.
  - Identify any governance gaps for the trustees or in-house team to address.
- Governance Healthcheck Plus**

- In addition to the Governance Healthcheck services: drafting and implementing any new policies and procedures that have been identified to meet ESOG requirements.
- LCP’s own risk assessment (ORA) service**

- Specialist own risk assessment in line with TPR guidelines.
  - Identification of any areas that require further focus.
  - Presentation of findings to the board and assistance with agreeing next steps.

We take a tailored approach to consulting and if you prefer, we can deliver a bespoke service to meet your needs.

## How our approach benefits you

- ✓ Specialist support provides comfort of good governance.
- ✓ Professional support introduces independence.
- ✓ Gives the trustees a clear plan of action of what areas need more focus.
- ✓ Trustees benefit from our deep understanding of governance best practice and our experience of working with many different schemes.
- ✓ Relieves the extra governance burden that might otherwise fall to the in-house pensions team or the trustees themselves.
- ✓ Allows trustees to focus on high-level and strategic issues, leaving the detail to us.
- ✓ Our support is tailored to meet your needs and the approach taken will be proportionate to your scheme’s size, nature, scale and complexity.



# Contact us

If you'd like further information, please contact your regular LCP adviser or one of our specialists for more support.



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*At LCP, our experts help to power possibility by navigating you through complexity to make decisions that matter to your business and to our wider society. We are powered by our desire to solve important problems to shape a more positive future. We have market leading capabilities across pensions and financial services, insurance, energy, health and analytics.*

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