Sackers

Finance & investment briefing

September 2019

Sackers finance & investment group takes a look at current issues of interest to pension scheme investors

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In this issue

Abbreviations

BEIS: the Department for Business, Energy and Industrial Strategy

CMA: Competition and Markets Authority

DB: Defined benefit

DC: Defined contribution

ESG: Environmental, social and governance

FCA: Financial Conduct Authority

LDI: Liability-driven investment

OTC: Over-the-counter

SIP: Statement of Investment Principles

TCFD: Task Force on Climate-related Financial Disclosures

TPR: The Pension Regulator

Finance & investment focus

"Welcome to the September issue of our finance & investment briefing.

Trustees will have spent recent months updating their SIPs to set out their policies on ESG and stewardship. The 1 October 2019 deadline was brought in by changes in the Investment Regulations published at the end of 2018. However, further recent changes to the regulations (made in June 2019 to implement the Shareholders Rights Directive II) will require more updates to SIPs over the following 12 months, including additional detail on stewardship policies and investment disclosure obligations. One of the biggest challenges is likely to be the requirement on all schemes to provide annual reporting to their members on how they have implemented their policies. The precise timings for compliance have been made mind-bendingly complicated under the regulations, so in this briefing we try to take a step back and set out an indicative timetable. We illustrate this for DB and DC schemes with a typical scheme year of 1 January to 31 December but schemes with other scheme years (eg 1 April to 31 March) will need to take advice.

Those wanting to get ahead of the latest changes may wish to attend our next seminar "Documenting your investment policies – tips and traps", on 1 October 2019, in which we will look at what investment practices and policies schemes have in place. For details and to sign up, please see our website.

Finally, in our legal update we focus on the CMA investment consultants and market investigation order, the revised TPR guidance for DC trustees and the launch of the new Government Green Finance Strategy.

If you would like discuss any of the matters covered in this briefing please speak to your usual Sackers contact."

Stuart O'Brien
Partner

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Environment

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ESG and Extended Stewardship regulatory timetable

This timeline is based on a scheme year of 1 January to 31 December

Schemes with a different scheme year to the above will require a specifically tailored timeline – please speak to your usual Sackers contact to discuss further.

DB schemes

Update **SIP** to set out policies in relation to:

- "financially material considerations" (including ESG considerations and climate change)
- the extent to which "non-financial matters" are taken into account
- undertaking engagement activities in respect of investments (stewardship).

Extended Stewardship

Further details required in **SIP**:

- provide additional information in stewardship policy (ie how investee company is monitored on capital structure and how actual and potential conflicts of interest in relation to their engagement are managed)
- set out policy in relation to arrangements with asset managers (including information on how the trustees incentivise managers to align their investment strategy with the trustees' own; how they incentivise the manager to assess investee companies' medium-to-long-term financial and non-financial performance, and engage accordingly; how the method and time horizon for evaluating the manager's performance, and the basis of its remuneration, are aligned with the trustees' other investment policies; and how trustees monitor portfolio turnover costs incurred by the asset manager).

Publish **SIP** on website

Produce an **implementation statement**:

- explaining how and the extent to which policies on exercising rights and undertaking engagement in respect of the scheme's investments have been followed during the preceding scheme year[1]
- describing voting behaviours by and on behalf of trustees, including most significant votes cast by trustees or on their behalf during the preceding scheme year.

Include **implementation statement** in the annual report[2] for the 2020 scheme year.

NB: This will require relevant information to be gathered during 2020

Publish **implementation statement** on website

01 OCTOBER 2019

1 January 2020

2020 Scheme Year

01 OCTOBER 2020

31 December 2020

31 July 2021

01 OCTOBER 2021

DC schemes

Update **SIP** to set out policies in relation to:

- "financially material considerations" (including ESG considerations and climate change)
- the extent to which "non-financial matters" are taken into account
- undertaking engagement activities in respect of investments (stewardship).

Publish **SIP** on website and inform members of its availability via annual benefit statement

Extended Stewardship

Further details required in **SIP**:

- provide additional information in stewardship policy (ie how investee company is monitored on capital structure and how actual and potential conflicts of interest in relation to their engagement are managed)
- set out policy in relation to arrangements with asset managers (including information on how the trustees incentivise managers to align their investment strategy with the trustees' own; how they incentivise the manager to assess investee companies' medium-to-long-term financial and non-financial performance, and engage accordingly; how the method and time horizon for evaluating the manager's performance, and the basis of its remuneration, are aligned with the trustees' other investment policies; and how trustees monitor portfolio turnover costs incurred by the asset manager).

Publish **SIP** on website and inform members of its availability via annual benefit statement

Produce an **implementation statement**:

- setting out how the principles set out in the SIP have been followed during the preceding scheme year[1]
- describing voting behaviours by and on behalf of trustees, including most significant votes cast by trustees or on their behalf during the preceding scheme year.

Include **implementation statement** in the annual report for the previous scheme year.

Publish **implementation statement** on website and inform members of its availability via annual benefit statement

The requirement to publish the description of voting behaviours element of the implementation statement applies from 1 October 2021.

1 For scheme years ending 31 December 2020, the implementation statement is required to report against Extended Stewardship in place from 1 October 2020 to the end of the scheme year – as indicated by ////.

To the extent that schemes have adopted Extended Stewardship ahead of 1 October 2020, schemes should report on such policies in the implementation statement for the period from such adoption to the end of the scheme year.

2 Legislation permits a period of up to 7 months following the end of a scheme year to produce the annual report. In practice, a scheme may take less time than this and so may produce a report in the summer each year.

This timeline assumes that the first annual report falling after 1 October 2020 will be the annual report for the 2020-2021 scheme year, produced in summer 2021.

Legal update

CMA: Investment consultants market investigation – Order published

On 10 June 2019, the CMA published the Investment Consultancy and Fiduciary Management Market Investigation Order 2019 ("the Order"). The Order gives effect to the remedies suggested in the CMA's final report following its Investment Consultants Market Investigation in December 2018.

Amongst other things, the Order requires:

- pension scheme trustees who wish to delegate investment decisions for 20% or more of their scheme assets to run a competitive tender when first purchasing fiduciary management services
- pension scheme trustees who have already appointed a fiduciary manager for 20% or more of their scheme assets without a tender, to put the service out to tender within five years of the appointment
- fiduciary management firms to provide potential new customers with more information on their fees and performance, so they can compare service providers with ease.

Please see our March 2019 briefing for more information

Of note, the Order now requires trustees:

- to enter into a contract with an investment consultant or to continue to obtain their services only if they have set out "Strategic Objectives". This requirement comes into force on **10 December 2019**. The expectation is that such objectives will be closely linked to the scheme's investment objectives (and that they will be reviewed every three years and after any significant change to strategy) and trustees will ask their investment consultants to report periodically on their performance in meeting the Strategic Objectives. The Strategic Objectives should include a clear definition of the outcome expected to be delivered and the timescale over which it should be delivered
- to send the CMA a compliance statement confirming the above point (the text and the format of which are set out in the Order). The first notice must be sent by **January 2021** and annually thereafter.

Trustees now have six months to ensure their practices are in line with the Order's requirements. Those found not to be complying may be taken to court by the CMA.

Revised investment guidance for DC investments

Guidance published

On 27 June 2019, TPR published revised investment guidance for DC trustees. The guidance has been updated to reflect recent changes to legislation for DC schemes (see the regulatory timeline on pages 3-4 and our recent Alert).

The guidance is intended to provide further clarity around what is meant by "financially material considerations" and stewardship, and more information about preparing an implementation statement.

Government launches Green Finance Strategy

On 2 July 2019, BEIS published the Government's Green Finance Strategy, Transforming finance for a greener future, in response to the Green Finance Taskforce's March 2018 report. The strategy aims to:

Government to develop TCFD guidance for pension schemes

- ensure that current and future financial risks and opportunities from climate and environmental factors are integrated into mainstream financial decision-making, and that markets for green financial products are robust – referred to as "greening finance". It includes a Government expectation that all listed companies and large asset owners will disclose in line with the Financial Stability Board's TCFD recommendations by 2022. Together with TPR, the Government has established an industry group to develop TCFD guidance for pension schemes and a consultation is expected in late 2019
- accelerate finance to support the delivery of the UK's carbon targets and clean growth, resilience and environmental ambitions, and international objectives
- ensure that UK financial services capture the domestic and international commercial opportunities arising from "greening finance", such as climate-related data and analytics, and from new green financial products and services.

Sackers

Contact

Sackers is the UK's leading commercial law firm for pension scheme trustees and employers. Over sixty lawyers focus on pensions and its related areas, including Sackers' finance and investment group, a team of lawyers who provide cutting edge advice to trustees, employers, corporate investors and providers on all aspects of pension scheme finance and investment.

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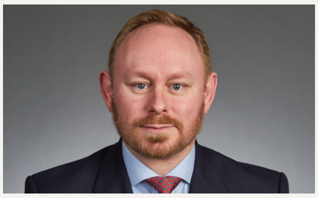

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