Sackers

Finance & investment briefing

March 2023

Sackers finance and investment experts take a look at current issues of interest to pension scheme investors

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In this issue

Abbreviations

DB: Defined Benefit

DC: Defined Contribution

DWP: Department for Work and Pensions

ESG: Environmental, social and corporate governance

FCA: Financial Conduct Authority

IGC: Independent Governance Committee

LDI: Liability-driven investment

OTC: Over the counter

PLSA: Pensions and Lifetime Savings Association

TPR: The Pensions Regulator

Finance & investment focus

"Welcome to our first finance & investment briefing of 2023. We hope the new year has started well.

In this issue, we share our derisking team's highlights of 2022 in relation to risk transfer activity. Over the last year, we advised on 16 risk transfer transactions totalling over £4.2 billion. During the last five years we have consistently worked with all the major insurers and advised on over 63 transactions, totalling over £41.6 billion. We remain at the forefront of this work and last year were involved in one of the largest bulk annuity transactions in the market. We anticipate that 2023 will be another busy year.

On page 3, we summarise the recent guidance issued by TPR on maintaining LDI resilience. The guidance follows statements made by the Irish and Luxembourg regulators (which are the home regulators for most LDI pooled funds), and welcomed by the FCA, setting out expectations that LDI pooled funds maintain a specific level of liquidity buffer.

In previous years, we have published an annual ESG guide for trustees, covering the latest legal developments and thinking on this ever-expanding topic. This year we are planning a shorter publication to pull all the strands together and "take stock" of all the recent and forthcoming regulatory change. To assist trustees in navigating through all the areas of ESG we'll be providing links back to earlier publications where the reader may need more detail. Look out for this on our website.

If you have any questions about the issues raised in this briefing, please speak to your usual Sackers contact."

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For more information on our CSR policy, please visit our website at www.sackers.com/about/csr

TPR guidance on maintaining LDI resilience

Pooled funds expected to maintain a liquidity buffer

On 30 November 2022, TPR published guidance for DB schemes which aims to achieve and maintain an “appropriate level of resilience” in leveraged LDI funds and to improve schemes’ operational governance.

The guidance follows statements published by the Central Bank of Ireland and the Commission de Surveillance du Secteur Financier (collectively the “National Competent Authorities” or “NCAs”), setting out expectations that pooled funds maintain a specific level of liquidity buffer, and was “welcomed” by the FCA. Where the statements from the NCAs refer to pooled funds, TPR considers the “same level of resilience” should be maintained for segregated leveraged LDI mandates and single-client funds.

TPR recommends that trustees review their governance processes and consider the challenges that arose for their pension scheme “during the volatility in September and October 2022”. Trustees should test their liquidity buffer by following the recommended practical steps outlined in TPR’s guidance to ensure they are able to “react quickly in response to stress in the market”.

Recommended practical steps include, in summary:

- ✓ confirm authorised signatories are up to date and ensure governance is robust
- ✓ stress the non-leveraged LDI asset allocation using a yield shock
- ✓ stress the leveraged LDI pooled fund / segregated mandate using the same yield movement
- ✓ calculate the required collateral amount and the type of assets
- ✓ specify the dates when collateral / margin calls need to be made
- ✓ specify what assets would be sold on collateral / margin calls and the details and process for doing so
- ✓ document and regularly review arrangements

Detailed conversations with LDI managers on liquidity recommended

In addition, TPR recommends that trustees continue to have detailed conversations with LDI managers on liquidity including what the triggers for replenishment are, the process for meeting calls and providing visibility of liquidity.

If trustees depart from the NCAs’ liquidity buffer, TPR recommends that trustees should:

- work with their advisers to demonstrate the buffer the scheme has in place
- complete a risk assessment of how the scheme will respond to stressed market events
- prepare a plan for bringing the scheme to higher levels of resilience in the event of market volatility
- document and review these arrangements regularly

TPR has stated that the purpose of the guidance is to address immediate requirements on liquidity, adding that it is “alive to the constantly changing market conditions and the implications for the future”.

A further update is expected in TPR’s Annual Funding Statement in April 2023. TPR may also issue further statements and guidance, as necessary.

Legal update

TPR publishes consultation on DB funding code

On 16 December 2022, TPR published a package of scheme funding documents, including a consultation on its draft Code of Practice ("the draft Code"), a consultation on its "twin track" regulatory approach, and a response to its first funding code consultation. This follows the DWP consultation on draft funding and investment regulations back in July 2022 (see our Alert).

Regulations expected to come into force October 2023 at the earliest

The draft Code is intended to replace the current Code, introduced in 2014, with effect from October 2023, when the funding and investment regulations are expected to come into force. Unusually, the draft Code is based on the draft regulations in the form consulted on by the DWP, as the regulations have not yet been finalised.

The consultation will run until 24 March 2023. The new regime is expected to come into force for actuarial valuations with effective dates on or after 1 October 2023 at the earliest. To meet this timescale, the final Code is expected to be laid before Parliament in mid-June 2023, alongside the DWP's final regulations.

See our Alert for further details.

PLSA publishes guidance on good workforce reporting

On 16 December 2022, the PLSA published guidance for companies and investors on workforce disclosures, providing good practice examples of workforce reporting. The guidance aims to improve reporting to help "deliver more effective workforce engagement and, in turn, improved outcomes for companies, investors and workers".

Guidance sets out good practice examples of workforce reporting

Among other things, investors are encouraged to support companies to produce meaningful reporting by ensuring they are targeted in their requests, focusing on key metrics that are most material to a specific company.

Productive Finance Working Group publishes guides on key considerations for DC investment in illiquid assets

New guides on DC investment in illiquid assets

The Productive Finance Working Group published new guides on 24 November 2022, intended to help give DC scheme trustees, sponsoring employers and investment consultants "the tools to consider investing in [less liquid assets] such as venture capital, private equity, private credit, real estate, and infrastructure, where appropriate and in scheme members' best interests". Key issues discussed by the guides include value for money, performance fees, and liquidity management.

DWP responds to consultation on broadening the investment opportunities of DC schemes

On 30 January 2023, the DWP published a response to its consultation on broadening the investment opportunities of DC schemes. The consultation sought views on draft regulations and guidance to:

Regulations intended to be in force by the spring

- require schemes to disclose and explain their policies on illiquid investment and their asset allocations, and
- introduce an exemption for performance-based fees from the charge cap that applies to default funds (see our Alert for more details).

Following "broad support" in the consultation feedback, the DWP is proceeding with its proposals with relatively minor amendments, and intends to bring regulations (accompanied by statutory guidance) into force "by the spring".

Risk transfer highlights 2022

Our specialist derisking team is delighted to share highlights of our 2022 risk transfer activity and anticipates another busy year in 2023.

£4.2bn+

Total risk transfer transactions for 2022

One of the largest bulk annuity transactions in the market in 2022

We advised on 16 risk transfer transactions, six over £350m

£600m
ITV Pension Scheme,
April 2022,
Buy-out

£545m
Undisclosed,
October 2022,
Buy-out

£1.1bn
Electronic Data Systems 1994 Pension Scheme,
July 2022,
Buy-in to buy-out

£461m
Undisclosed,
April 2022,
Buy-in

£530m
Undisclosed,
August 2022,
Buy-in

£350m
Coats UK Pension Scheme,
December 2022,
Buy-in

£41.6bn+ | 63 | 5yrs

In the last five years, we have worked on risk transfer transactions totalling over £41.6bn across 63 transactions

£1bn+

We are currently advising trustees and employers on two significant longevity transactions and over 40 risk transfer transactions, with at least five transactions anticipated to be £1bn+

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We act for 36 of the top 200 pension funds in the UK (source: Pension Funds Online)

Sackers

Contact

Sackers is the UK's leading commercial law firm for pension scheme trustees, employers and providers. 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 on all aspects of pension scheme finance and investment.

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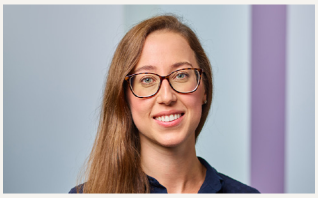

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