

# PENSIONS SPECIAL ALERT

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## New investment and disclosure requirements for trustees from October 2019

Trustees will soon be subject to new duties in two important areas. Firstly, from 1 October 2019, new ESG-related investment disclosure requirements will apply to both defined benefit and defined contribution pension arrangements. Amongst other things, trustees will have to amend their Statement of Investment Principles (SIP). Secondly, from 10 December 2019, following an investigation by the Competition and Markets Authority (CMA), trustees using investment consultancy or fiduciary management services will have to comply with new requirements requiring them to set objectives for their investment consultants and undertake mandatory competitive tendering for fiduciary management services.

In this Special Alert, we summarise what is changing and recommend some compliance steps for trustees to take.

[Read more](#) about the new ESG-related investment and disclosure duties coming in from 1 October 2019.

[Read more](#) about the new requirements for trustees in relation to investment consultancy and fiduciary management services coming in from 10 December 2019.

If you wish to discuss any of these issues further, please contact us.

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## New ESG-related investment and disclosure requirements from 1 October 2019

From 1 October 2019 various new requirements will apply to trustees in relation to their investment and disclosure duties. Further requirements will apply in subsequent years, depending on whether the relevant pension arrangement is defined benefit or defined contribution (including defined contribution sections in hybrid pension schemes). The Government states that a principal aim of the new regulations is to clarify for trustees that they can consider environmental, social and governance (ESG) matters in their strategic and investment decisions.

Two sets of new regulations (*The Pension Protection Fund (Pensionable Service) and Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2018* and *The Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019*) will apply to both DB and DC schemes and will affect investment disclosure documents, most notably the SIP. The Pensions Regulator has updated both its [investment governance guide for DC schemes](#) and its [investment guidance for defined benefit pension schemes](#) to provide helpful practical advice for trustees.

### What's changing and when?

- **Taking into account "financially material considerations":** From **1 October 2019**, trustees of both **DB and DC arrangements** must state in their SIP their policies in relation to "*financially material considerations*". This is defined as including, but not being limited to, those considerations relating to environmental, social and governance (ESG) matters, including but not limited to climate change which the trustees consider financially material. The Regulator's DC guidance gives examples of considerations in each of these areas, noting that environmental considerations might include carbon emissions and water management, social considerations might include employee or local community relations and governance considerations might include matters such as board diversity and remuneration.
- **Policies on "non-financial matters":** Similarly, from **1 October 2019**, trustees of both **DB and DC arrangements** will have to state in their SIP their policies in relation to the extent to which (if at all) "*non-financial matters*" are taken into account in the selection, retention and realisation of investments. "Non-financial matters" means "*the views of scheme members and beneficiaries, including (but not limited to) their ethical views and their views in relation to the social and environmental impact and present and future quality of life of the members and beneficiaries of the scheme*". In practice, the Regulator has confirmed that trustees retain primary responsibility for investment decisions, and that they are not obliged to take into account members' views.
- **Policies on stewardship:** From **1 October 2019**, trustees of **both DB and DC arrangements** must state in their SIP their policies in relation to exercising voting rights and engaging and monitoring in respect of their investments on matters such as performance, strategy, and social and environmental impact. From **1 October 2020**, SIPs must also record how the trustees take into account the capital structure of investee entities and their management of actual or potential conflicts of interest.

- **Implementation statements:** From **1 October 2020**, trustees of **DC schemes only** will have to prepare a statement on the extent to which the SIP has been followed and describe any review of the SIP. These statements are commonly being called "implementation statements" (including by the Regulator) and they will have to be included in the annual benefit statement issued to members. From **1 October 2021**, the implementation statement will also have to include information on the trustees' voting behaviours.
- **Arrangements with asset managers:** From **1 October 2020**, for **both DB and DC schemes**, trustees will have to include information in their SIP on their arrangements with their asset managers. This will need address for example, how the scheme's arrangements incentivise the manager to align his strategy with the trustees' investment policies and to make decisions based on assessments about medium to long-term financial and non-financial performance of an issuer of debt or equity.
- **Publishing information for free on a searchable website:**

From 1 October 2019	From 1 October 2020	From 1 October 2021
<b>Trustees of DC schemes</b> - publish SIP	<b>Trustees of DC schemes</b> - publish implementation statement	<b>Trustees of DB schemes</b> - publish a statement, broadly on the extent to which the trustees' policy on the exercise of voting rights and stewardship has been followed during the year and describing the voting behaviour by the trustees
	<b>Trustees of DB schemes</b> - publish their SIP	<b>Trustees of DC schemes</b> - include further information in their implementation statement on the trustees' voting behaviour during the year and use of proxy voter services

The changes set out above apply only to trust-based occupational pension schemes. However, the FCA has recently consulted on introducing similar duties on Investment Governance Committees and pension providers in respect of contract-based schemes.

### A summary of the key changes

1 October 2019	1 October 2020	1 October 2021
<b>DB and DC schemes:</b> include policy on taking into account financially material considerations and include in SIP	<b>DC schemes:</b> prepare implementation statement, publish on website and sign-post in annual benefit statement	<b>DC schemes'</b> implementation statement requirements extended to cover matters such as trustee voting behaviours
<b>DB and DC schemes:</b> include policy on stewardship and include in SIP	<b>DB and DC schemes:</b> update stewardship policies to include relevant considerations of capital structure and management of conflicts	<b>DB schemes</b> to publish on website statement on trustees' compliance with stewardship policy and to describe trustee voting behaviour
<b>DC Schemes</b> publish SIP on website	<b>DB and DC schemes</b> to prepare policies in relation to asset manager arrangements and include in SIP	
	<b>DB schemes</b> to publish SIP on website	

### What actions should trustees be taking to address these changes?

It is likely that the Regulator will be closely examining trustee activities in the areas of ESG matters and stewardship once the changes come into force. Given that important requirements come into force from 1 October 2019, trustees need to act now. In practice, as well as carefully considering the Regulator's suggestions in its investment guidance papers, we recommend that trustees:

- liaise promptly with their investment consultants and asset managers to ensure that they have agreed policies in place in relation to their consideration of ESG factors and stewardship

activities for inclusion in their SIP;

- if trustees are thinking about adopting a particular ethical investment position, consider conducting a member survey to inform the trustees' decision about whether or not to adopt this;
- potentially agree specific voting criteria with their investment managers (as suggested by the Regulator) to ensure that trustee policies are followed; and
- make logistical arrangements to publish the scheme SIP on a website - in practice, this may have to be managed by an external provider and so relevant contractual arrangements should be put in place.

For those pension schemes that invest in pooled funds, the Regulator recognises that trustees' ESG considerations may be constrained by the funds on offer. However, the Regulator suggests that care should be taken by trustees to understand the ESG approach of the available funds.

To continue reading about the new requirements for trustees in relating to investment consultancy and fiduciary management, [click here](#).

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## **New requirements for trustees in relation to investment consultancy and fiduciary management services from 10 December 2019**

On June 10 2019, the CMA issued the *Investment Consultancy and Fiduciary Management Market Investigation Order 2019*. The Order implements the bulk of the CMA's remedies following its December 2018 findings that there are features of the investment and fiduciary management services market which adversely affect competition in the supply of those services to pension scheme trustees.

Whilst the majority of the new requirements under the Order fall on firms providing investment consultancy and fiduciary management services, a number of them will also be directly relevant to trustees of occupational pension schemes (both DB and DC) who use such services. In particular, **trustees who currently use investment consultancy services will need to take action ahead of 10 December 2019 when the new requirements come into force**. The aim of these new requirements is to encourage trustees to become more proactive in how they work with fiduciary managers and investment consultants.

This part of our update summarises the main points for trustees coming out of the Order and provides an overview of the new duties that apply to investment consultants and fiduciary managers. While the Order will come into force first, the requirements on trustees will be replaced with equivalent obligations within the main body of pensions legislation. Based on draft legislation published on 29 July 2019, we are expecting that to happen in April 2020. It is unlikely, however, that the new regulations will result in any significant changes to the headline requirements on trustees covered in this alert.

### **New requirements for trustees**

New provisions requiring trustees to undertake competitive tendering in relation to fiduciary management services will come into force from 10 December 2019. Trustees will be required to use "reasonable endeavours" to obtain bids from three or more unrelated providers when tendering for fiduciary management services. The new rules will apply broadly as follows:

- **New mandates:** trustees must run a competitive tender for any new FMA(s) which would result in 20% or more of scheme assets being delegated
- **Existing mandates covering 20% of more of scheme assets:** trustees must run a competitive tender within five years from the date of the commencement of the original FMA if the original FMA was not subject to a competitive tender process (a shorter two year deadline applies in some cases)
- **Existing mandates covering less than 20% scheme assets:** trustees must run a competitive tender at the point the assets covered by an existing FMA (or FMA(s)) increase to 20% or over

In most cases, trustees will have to confirm to the selected provider that they have been selected as a result of a competitive tender process.

The Regulator has published [draft guidance](#) for trustees on tendering for fiduciary management services as part of a suite of new guidance on investment governance.

- **Objective setting for investment consultants** - from 10 December 2019, trustees will be prohibited from receiving investment consultancy services under existing contracts, or entering new contracts for such services, unless they have first set strategic objectives for the provider. The Pensions Regulator has issued [draft guidance](#) for trustees which, although not yet in final form, provides an indication of what the Regulator will expect in this area.
- **Reporting** - in principle, trustees will be required to submit annual compliance statements to the CMA. However, if, as expected, the reporting requirement for trustees under the Order becomes incorporated into pensions legislation, this is likely to be replaced with a different process and deadline (currently expected to involve submitting information to the Regulator via Exchange) before trustees are required to take action under the Order.

## Enforcement

The CMA is responsible for enforcing the provisions of the Order, including, in principle, in relation to the new requirements on trustees. At the point the new requirements on trustees are incorporated into pensions legislation, regulatory oversight will pass to the Regulator. Under draft legislation, the Regulator would have the power to impose financial penalties for non-compliance up to a level not exceeding £5,000 (in the case of individual trustees) and not exceeding £50,000 in all other cases.

## New requirements for Investment Consultants and Fiduciary Managers

These are summarised as follows:

- To separate advice in respect of investment consulting or fiduciary management services from marketing material in respect of fiduciary management services and to label such marketing material clearly.
- To provide disaggregated fee information in respect of fiduciary management services to existing trustee clients regularly.
- To disclose and itemise all costs and related charges to all potential trustee clients when involved in a tender process.
- To provide potential trustee clients with information on the past performance of fiduciary management services using a standardised methodology and template (based on a standard to be approved by the CMA).
- To provide potential trustee clients with information on past performance of recommended products or funds using a basic minimum standard.

## Getting ready for the new regime

Based on the provisions of the Order and on the draft guidance from the Regulator, trustees should consider taking the following action:

- Review contractual documentation under which any current investment consultancy and fiduciary management services are provided in order to establish which requirements will apply and when. Trustees will need to establish, in conjunction with legal advisers where necessary, whether the particular arrangements are caught within the relevant definitions. This will require an assessment of the underlying nature of the services, which can be complex - trustees should not rely on how services have been labelled.
- Start considering what strategic objectives might be appropriate in relation to any existing contracts for investment consultancy services in order to have these in place from 10 December 2019. In due course, update processes to ensure that objective setting is incorporated into any new contract for investment consultancy.
- In due course, update policies and procedures to ensure that necessary compliance statements are made by the required deadlines, reviewing, as necessary to take into account further developments.

To read about the new ESG-related investment and disclosure requirements, [click here](#).

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