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Dear Sir/Madam

RESPONSE TO CONSULTATION ON CLARIFYING AND STRENGTHENING TRUSTEES' INVESTMENT DUTIES

We welcome the opportunity to comment on these draft regulations.

Introduction to Pinsent Masons LLP

Pinsent Masons LLP is an international law firm. We have one of the strongest pensions teams in the UK. Spanning our UK offices, the team has around 80 specialist lawyers, paralegals and independent trustee administrators dealing with pensions. We are dedicated to providing clear, practical, cost-effective advice for our clients. We advise trustees, sponsoring employers and providers on the full range of pensions issues and are the only law firm to have generated significant thought leadership around the topic of trustees' fiduciary duties in the context of sustainable investments.¹

Our comments

We have responded only to those questions where we disagree with the proposals or have something further to add.

Q2. We propose to require all trustees of all schemes which are obliged to produce a SIP to state their policy in relation to financially material considerations including, but not limited to, those resulting from environmental, social and governance considerations, including climate change. a) Do you agree with the policy proposal? b) Do the draft Regulations meet the policy intent?

¹ Pinsent Masons commissioned a report to help trustees understand the practical steps they can take to engage with climate risk - see <https://www.pinsentmasons.com/en/media/publications/pension-investors-having-a-positive-impact-on-climate-change/>

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Trustees have a fiduciary duty to take account of financially material considerations in any event. However, we understand that many do not do this in the context of sustainable investing – often because of confusion about their duties and because they conflate the concepts of sustainable investing and ethics. The proposal should have the welcome effect of improving trustees' understanding of their duties in this area.

Comments on proposed wording

The new wording of regulation 2(3)(b)(vi) will read "financially material considerations including how those considerations are taken into account in the selection, retention and realisation of investments". We think the word "other" should be inserted at the start of that wording, since the other factors listed in regulation 2(3)(b) (such as "the expected return on investments") are also "financially material considerations". We assume that regulation 2(3)(b)(vi) is intended to be a separate, additional policy requirement for the SIP.

The definition of "financially material considerations" needs amending. The current wording suggests that *all* environmental, social and governance considerations are financially material. We propose the following wording: "means such considerations (including but not limited to environmental, social and governance considerations, such as climate change) as are financially material".

Q3. When trustees prepare or revise a SIP, we propose that they should be required to prepare a statement, setting out how they will take account of scheme members' views. a) Do you agree with the policy proposal? b) Do the draft Regulations meet the policy intent?

We do not agree with this policy proposal for the following reasons:

- this proposal forces trustees to decide whether or not to take account of members' views. This of itself puts trustees in the difficult position of needing to exercise that decision properly and on an informed basis. Trustees who eventually decide not to take account of members' views will still need to think about this carefully (following advice);
- for most schemes, the practical difficulties and cost of surveying members' views outweighs any benefits;
- it would be difficult to frame survey questions in a neutral way that does not lead members to respond in a certain way;
- responses to any survey are likely to come mainly from a small number of vocal activists;
- once trustees have sifted through members' responses, they will still have a difficult task in deciding how to act. In most cases, there will be no clear majority view from members (although this proposal may make more sense in relation to DC rather than DB schemes since DC schemes could decide to introduce an ethical fund on the basis of members' views);
- this proposal could perpetuate some trustees' current confusion. The key objective of this legislation ought to be to ensure that trustees properly understand their duties in relation to financially material risks. If there is a chance that this could be compromised by proposals relating to members' ethical views, those proposals should be delayed or abandoned.

Q4. Do you agree with our proposal not to require trustees to state a policy in relation to social impact investment? If not, what change in legislation would you propose, and how would you address this risk of trustee confusion on this point?



We agree. Trustees need to be aware of the need to take account of financially material factors. And trustees should be aware of the circumstances in which members' views can be taken into account. To introduce a third category of social impact investment that does not correspond with any particular aspect of trustees' fiduciary duties could cause confusion.

Q5. We propose that trustees should be required to include their policy in relation to stewardship of the investments, (including monitoring, engagement and voting) in the SIP. a) Do you agree with this proposal? b) Do the draft Regulations meet the policy intent?

We agree with this proposal. Pension schemes range in sophistication and size, and only the larger schemes are likely to take an active role in this area. The draft Regulations work to give trustees a wide discretion, and do not prevent trustees delegating stewardship to their investment consultants, which is what happens in practice in the majority of schemes. It would be useful if The Pensions Regulator produced guidance on how trustees could be more rigorous in holding their investment consultants and asset managers to account in this area.

Q6. When trustees of relevant schemes produce their annual report, we propose that they should be required to: prepare a statement setting out how they have implemented the policies in the SIP, and explaining and giving reasons for any change made to the SIP, and include this implementation statement and the latest statement outlining how trustees will take account of members' views in the annual report. a) Do you agree with the policy proposal? b) Do the draft Regulations meet the policy intent?

We do not agree with this proposal.

You state that these additional requirements are not required for DB schemes since it is "in the interest of the sponsoring employer to ensure that the investment strategies of the scheme are as effective as possible". However, employers' level of engagement varies from DB scheme to DB scheme. In practice, many employers with DB schemes fail to engage in any depth with scheme investments, never mind environmental, social and governance considerations. Therefore, the logic for drawing a distinction between DB schemes and DC schemes falls away.

Trustees are already required to take account of the SIP in choosing investments (section 26(3) of the Pensions Act 1995), and to report any breach in their annual report (paragraph 30 of schedule 3 to the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013). Members will be more interested, in any event, with the trustees' report on investment performance, rather than the technicalities of how the SIP has been implemented. We believe that existing requirements alone, taken together with guidance from TPR, are sufficient to ensure trustees of all schemes take their SIP seriously.

Q7: We propose that trustees of relevant schemes should be required to publish the SIP, the implementation report and the statement setting out how they will take account of members' views online and inform members of this in the annual benefits statement. a) Do you agree with the policy proposal? b) Do the draft Regulations meet the policy intent?

We do not agree with this proposal. For the reasons stated above, no scheme should be required to produce an implementation report or a statement in relation to members' views. In particular, the problems we have already identified regarding the statement in relation to members' views would be exacerbated if published online.

Comments on proposed wording

If the government disagrees with us, then the proposed new regulation 12(5) of the Disclosure Regulations should be amended by the addition of the words "and is one to which section 35 of the 1995 Act applies" after the words "the Occupational Pension Schemes (Scheme Administration) Regulations". Otherwise, regulation 12(5) could be read as a free-standing



requirement to publish the specific information cross-referred to online, even where the relevant scheme is exempt from the requirement to produce a SIP (because it has fewer than 100 members). Similar amendments need to be made in regulation 29A of the Disclosure Regulations and paragraph 5B of schedule 6 to those regulations.

Q10. Do you agree that the revised Statutory Guidance clearly explains what is expected of trustees in meeting their duty to publish the SIP, implementation statement, and statement of members' views?

Paragraph 14 of the Statutory Guidance incorrectly states that these new requirements apply to the same schemes as are affected by the Occupational Pension Schemes (Administration and Disclosure)(Amendment) Regulations 2018. This is wrong because the new requirements apply only to those relevant schemes that need to produce a SIP under section 35 of the Pensions Act 1995.

Please contact Simon Tyler (simon.tyler@pinsentmasons.com) if you have any questions about this response.

Yours faithfully

Pinsent Masons LLP