Linklaters

Memorandum

24 April 2015

To Department for Work and Pensions

From Richard Kandler

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Consultation on changes to the Investment Regulations following the Law Commission's report "Fiduciary Duties of Investment Intermediaries"

I refer to the consultation document of 26 February 2015 on possible changes to the Occupational Pension Schemes (Investment) Regulations 2005. Linklaters is an international law firm that advises many employers and trustees on the full range of occupational pension schemes.

The fact that the Government is reviewing these regulations provides a good opportunity also to revisit the restrictions that they set out on employer-related investments. It is 25 years since these restrictions were first introduced, and the changes in UK pensions during that time suggest that a reconsideration of the principles is long overdue.

The current restrictions on employer-related investment contain anomalies that we suggest should be reviewed. In particular:

(a) The regulations allow trustees to invest up to 5% of the fund in shares in the sponsoring employer, but impose an absolute ban on loans. The fact that on insolvency creditors are paid ahead of shareholders suggests employer loans might be the safer of the two investments.

(b) The 5% restriction on investments in the employer’s shares also applies to investments in property occupied by or leased to the employer. Yet land has its own intrinsic value independently of the employer, which the employer’s shares do not.

(c) The legislation recognises no distinction between secured and unsecured loans. However, the latter clearly places the lender at a far greater risk than the former. The PPF and the Pensions Regulator both encourage trustees to seek security over assets. It seems odd to prohibit schemes from investing in assets that would be welcomed as security.

Some of these issues have led employers and trustees to devise funding structures which are considerably more complicated than might otherwise be necessary. The work involved in devising these tends to be time-consuming and can be expensive for both employers and trustees, to the potential detriment of the scheme’s funding position. The Pensions Regulator and the PPF also have to devote time, effort and costs into reviewing these arrangements.

Please do not hesitate to contact me if you would like to discuss these issues further.