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Consultants & Actuaries

16 July 2018

Sinead Donnelly and Vicky Bird
Department for Work and Pensions
Strategy Policy and Analysis Group
Private Pensions and Arm's Length Bodies Directorate
Ground Floor North
Quarry Road
Leeds
LS2 7UA

Dear Sinead and Vicky

CONSULTATION ON CLARIFYING AND STRENGTHENING TRUSTEES' INVESTMENT DUTIES

I am writing on behalf of BBS Consultants & Actuaries Ltd ('BBS') to provide our response to the consultation on the Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2018 ('the Regulations') dated June 2018.

BBS is an independent provider of administration, actuarial, investment and consultancy services to UK occupational defined benefit and defined contribution schemes, with over £4 billion in assets under advice.

Our responses to the questions are set out below. Given that we have broad concerns regarding the proposals, we have not commented on the extent to which the draft regulations meet the policy intent.

Q1: Proposal that the Regulations come into force approximately 1 year after laying

We think that any regulations should take effect for individual schemes within a reasonable period from the date due for the preparation of the next formal review of the Statement of Investment Principles (which is generally undertaken at least once every three years).

This will allow schemes to make changes in line with their existing governance cycle and will avoid the need to incur additional work and cost. Given that the ESG risks of principal concern are long-term in nature, such an additional period of grace (relative to the proposed timescales) does not seem unreasonable.

Q2: Proposal that all schemes required to produce a SIP state their policy in relation to financially materially considerations including, but not limited to, those resulting from ESG considerations, including climate change

SIPs are already required to include trustees' policies in relation to material risks and ESG factors. We do not see what the new regulations will really add in this regard. If a particular set of trustees regard climate change as a material risk, they already have the ability to comment on this in a SIP.

Whilst we recognise, based on the scientific case, that climate change is likely to be an important concern in future years, it is not clear that it is currently material in the context of risks relevant to many pension schemes. Even more problematic is how trustees can implement an investment strategy that mitigates the risk of climate change. We have a concern that the proposals to include climate change as a specific factor is driven by a political drive for pension schemes to become actors in changing corporate behaviour, but is being packaged as 'risk management'.

Q3: Proposal that trustees should be required to set out how they will take account of members' views

We do not think this is necessary and it should not be a mandatory requirement.

Our experience is that where it may be reasonable to assume that members of a scheme have a greater uniformity of views than the general population, members' views are often factored into investment strategy and confirmed in a SIP, provided that in doing so there is unlikely to be a material financial detriment to members. That is, the Law Commission's two-stage test is used in practice.

Examples of schemes where this approach might be taken include where the employer is a charitable organisation, religious group or political organisation.

Q4: Proposal that trustees should not be required to state a policy in relation to social impact investment

We agree with this proposal.

Q5: Proposal that trustees should be required to include their policy in relation to stewardship of the investments in the SIP

We do not have any in-principle objection to a requirement that SIPs should provide more detail on the stewardship of investments. However, detailed disclosure should only be required for the specific schemes where trustee action is likely to have a material impact on corporate behaviour.

This could be achieved via:

- A threshold of scheme assets below which the requirements would not apply, e.g. £1 billion.
- Simplified requirements where the responsibility for stewardship is, in practice, outsourced via the use of funds.

Q6: Proposal that when relevant schemes produce their annual report they should be required to prepare a statement setting out how they have implemented the policies in the SIP, explaining changes to the SIP, and include this and the latest statement outlining how trustees will take account of members' views in the annual report

Our experience is that SIPs of relevant schemes generally include detail on how the policies have been implemented via a practical strategy and, consequently, this proposal is unnecessary.

In addition, trustees often already explain their investment strategy and changes to it in the annual report, as well as via member newsletters, booklets and online communications.

Recent years have seen the implementation of a new Statement of Recommend Practice which has led to onerous additional disclosures in annual report and accounts. Annual reports are already very detailed, often duplicating other information that is freely available to members on request.

We do not agree that further additions to annual report and accounts should be required. This will avoid unnecessarily adding to the cost burden for schemes.

Q7: Proposal that, for relevant schemes, SIPs, implementation reports and statement setting out how trustees will take account of members' views should be published online and inform members of this in the annual benefits statement

We do not consider this to be an appropriate approach for all relevant schemes.

Many pension schemes already make the SIP available online through member portals. Furthermore, the SIP, annual report and other key documents are available on request to scheme members. We think it should be left to individual scheme trustees to determine how the SIP and related information is published, reflecting their own circumstances and cost constraints.

Again, a reasonable compromise may be to use an appropriate threshold for scheme assets in applying this proposal.

Q8 and Q9 – business burdens/benefits

We have commented on the potential additional burdens of the Regulations in our previous questions.

An additional point is that, whilst the aggregate cost determined in the impact analysis may appear to be relatively immaterial in the context of the size of UK pension assets, additional costs to individual schemes can be more important. In addition, the cumulative impact of yet another set of regulatory changes for pension schemes also needs to be considered before regulating; particularly where the case for making the changes is less convincing and where it will be difficult to measure the impact of the regulations in future years.

Q10 – Statutory Guidance

We have not made any specific comments on the revised Statutory Guidance at this stage, given our broader concerns regarding the Regulations.

Q11 – Comments on how well the requirements for preparing a SIP are working

Our role as advisers on pension schemes involves:

- The provision of advice to our investment consultancy clients on preparing SIPs.
- Provision of an oversight role to client who use a fiduciary manager that prepares the SIP.
- Working with other investment consultancies where we are not appointed for that role.

Consequently, we have a broad insight into the investment strategies and SIPs prepared by the trustees and advisors of a large number of schemes.

Our experience is that the process of reviewing a scheme's investment strategy, as ultimately formulated in a SIP, is not a 'box-ticking' exercise. Different advisory firms and trustee bodies use a variety of approaches, but these are typically undertaken via an appropriate process and documented accurately. Where we do come across cases where the process of preparing a SIP is weak, this is typically the result of poor overall scheme governance.

Some schemes may not have a strong focus on ESG considerations in their SIPs because the associated risks are much less material relative to other financial market risks and that of sponsor default. In addition, for many schemes, the practical mitigation of such ESG-related risks is either practically difficult and/or outsourced to professional fund managers.

Please let me know if you would like any clarification on our comments.

Yours sincerely

Jude Bennett FIA
Director of Investment Services