ALLEN & OVERY

10 June 2019

Pensions: what's new this week

Welcome to your weekly update from the Allen & Overy Pensions team, bringing you up-to-speed on all the latest legal and regulatory developments in the world of occupational pensions.

Further SIP requirements from October 2020 | New PASA guidance: cyber security | Stewardship: new rules for life insurers, asset managers | FRC leaves SMPI standard unchanged

Further SIP requirements from October 2020

The government has published new regulations setting additional requirements for the content of a scheme's statement of investment principles, and expanding trustees' duties to prepare and disclose information about pension scheme investments – other changes are already due to come into effect on 1 October 2019. The new developments are relevant to both DB and DC schemes.

Expanding the scope of the statement of investment principles (SIP)

For trust-based schemes with 100 or more members:

- The SIP will need to state the trustees' policy in relation to their arrangement with an asset manager, setting out specified matters (or explaining why these have not been set out). The issues include how their arrangement incentivises the asset manager to: (a) align its investment strategy and decisions with the trustees' policy on various investment considerations (including risk/return and financially material factors); and (b) make decisions/engage with investee companies based on an assessment of their medium to long-term performance. Other matters such as asset manager performance, remuneration and turnover costs are also included.
- The regulations also extend the requirement (which comes into effect on 1 October 2019) to state the trustees' policy on stewardship and engagement. The requirement refers to how trustees engage with 'relevant persons' on 'relevant matters'; the new regulations broaden the definition of 'relevant persons' to include any person with an interest in the issuer, and the 'relevant matters' will include the capital structure of an investee company, and management of conflicts of interest – but the deadline for the first policies in relation to these extended elements is 1 October 2020.

Relevant DC schemes (not AVC-only schemes) with 100 or more members will also need to comply with these requirements in relation to the SIP for default arrangement(s). The deadline for first preparing a SIP which meets these new requirements is 1 October 2020.

Extending the obligation to publish the SIP free online

Rules are already due to come into force on 1 October 2019 which will require some DC schemes to make the SIP publicly available free of charge online. Under the changes, the obligation to publish the SIP free online is extended to all schemes with 100 or more members which are required to prepare a SIP – this means a DB scheme with 100 or more members will be required to publish their SIP online. The deadline for compliance is 1 October 2020.

Annual report and implementation statement

Schemes will be required to update their annual reports in connection with the changes to the content of the SIP, including explaining how their policy on voting and other rights and engagement activities has been followed during the year, and noting the voting behaviour by or on behalf of the trustees (including the use of a proxy voter).

The obligation to publish an implementation statement has been extended as follows:

- All schemes that are required to prepare a SIP (other than a relevant DC scheme) will need to publish an 'engagement policy' implementation statement explaining how their policy on voting and other rights and engagement activities has been followed during the year. This includes describing the voting behaviour by or on behalf of the trustees (including the use of a proxy voter). This statement must be published free online by 1 October 2021.
- A relevant DC scheme with 100 or more members is already required to publish an implementation statement by 1 October 2020 – this implementation statement is more detailed than the above requirement. By 1 October 2021, this implementation statement must also cover the expanded matters in relation to the SIP (see above) as well as describing the voting behaviour by or on behalf of the trustees (including the use of a proxy voter).

Our briefing Pension scheme investing: keeping members informed covers the changes that had previously been announced and which come into effect on 1 October 2019. We will provide an updated and integrated guide to the new requirements shortly.

New PASA guidance: cyber security

PASA has published guidance on cyber security in the context of pension schemes. The guidance covers areas including: conducting a risk assessment; types of cyber risk; governance issues; and risk and incident management. It also identifies some key risks (such as device use and human error), and suggests some organisational controls that may be used to mitigate cyber security risks.

Stewardship: new rules for life insurers, asset managers

The Financial Conduct Authority (FCA) has published new rules aimed at improving shareholder engagement and transparency on stewardship. The changes come into force on 10 June 2019 as part of the implementation of the revised Shareholder Rights Directive (see also the measures affecting pension scheme trustees discussed above).

Engagement policies

In relation to investments in shares traded on a regulated market, life insurers and asset managers will be required to:

- develop and publicly disclose an engagement policy that meets requirements set out by the FCA (see below), and then explain annually how this has been implemented; or

- publicly disclose ‘a clear and reasoned explanation of why it has chosen not to comply’ with those requirements.

The FCA Rules set out a list of matters to be covered in the engagement policy, including how shareholder engagement is integrated into the investment strategy, how voting and other rights are exercised, and how investee companies are monitored on issues including financial and non-financial performance and risk, and social and environmental impact and corporate governance. The FCA has said that, for an initial period, asset managers and life insurers can comply with the requirement by explaining what they are doing to develop an engagement policy.

Greater transparency for institutional investors

The FCA is also introducing changes to increase transparency and make it easier for an institutional investor (such as a pension scheme) to assess a manager’s performance. Life insurers will be required to make disclosures about their arrangements with asset managers, and both life insurers and asset managers will be required to make disclosures about how their strategies contribute to the medium to long-term performance of the assets of the asset owner or fund.

The FCA Rules set out matters that must be reported on, including key material medium to long-term risks, portfolio composition, conflicts of interest in relation to engagement activities and whether/how investment decisions are made based on the medium to long-term performance of an investee company. Unlike the new rules on engagement policies, this obligation does not apply on a ‘comply or explain’ basis, but it may be complied with by making the information publicly available.

FRC leaves SMPI standard unchanged

The Financial Reporting Council has announced that there will be no changes to actuarial standard TM1 at the present time. The standard is used when producing statutory money purchase illustrations.

Contact information

Helen Powell — 0203 088 4827
PSL Counsel, London — helen.powell@allenovery.com

Ruth Emsden — 0203 088 4507
PSL (Australian lawyer), London — ruth.emsden@allenovery.com