SLAUGHTER AND MAY/

BULLETIN

OCTOBER 2021

PENSIONS BULLETIN

QUICK LINKS

One Bunhill Row
London EC1Y 8YY
United Kingdom
T: +44 (0)20 7600 1200

In this month’s Pensions Bulletin we cover:

1. Trustees of £5 billion+ pension schemes should note the Government is consulting to require using a fourth metric to measure climate risk - from October 2022.
2. The Government is consulting on DWP guidance on stewardship that trustees will have need to take into account in preparing investment Implementation Statements.
3. The Treasury has published a paper on mandatory “Sustainability Disclosure Requirements”.
4. Introduction of simpler annual benefit statements for DC auto-enrolment schemes has been postponed to October 2022.
5. The Pension Protection Fund’s consultation, suggesting a risk-based levy reduction for 2022/23, will close on 9 November 2021.
6. Trustees should consider new Pensions Ombudsman guidance on dealing with complaints and communicating with members.
7. Our Watch List: the introduction of simpler annual benefit statements is the only change this month.

GOVERNMENT CONSULTATION ON CLIMATE RISK AND STEWARDSHIP REPORTING

Trustees of schemes of £5billion+, which now have to comply with Taskforce on Climate-related Financial Disclosures (TCFD) governance and disclosure requirements, will have to adopt a fourth metric for measuring climate risk from October 2022.

New draft guidance for all size schemes from the Department of Work and Pensions (DWP) on reporting of stewardship and voting reflects a marked change in approach for trustees. There will be increasing pressure on trustees to "up their game" on the level of detail and analysis in Implementation Statements.

The DWP consultation issued on 21 October 2021 and closing on 6 January 2022 covers two different areas:

- Proposed amendments to the Climate Change Governance and Reporting Regulations 2021 to add a new (fourth) metric. This requires trustees to measure and report from 1 October 2022 on a portfolio alignment metric, describing the extent to which their investments are aligned with the Paris Agreement goal.
- Draft Guidance on trustees' reporting of stewardship and voting in Statements of Investment Principles (SIPs) and Implementation Statements (ISs). The part on SIPs will be non-statutory best practice but the guidance for ISs will be statutory guidance.

Measuring and reporting Paris alignment

Under the 2021 Regulations, broadly, schemes with net assets of £5 billion or more are required to disclose annually in line with TCFD disclosure requirements, and have climate governance arrangements in place by October 2021. The equivalent requirements will apply to schemes with at least £1 billion assets in 2022.

One of the governance requirements is for trustees to select and ("as far as they are able") calculate an absolute emissions and an emissions intensity metric for scheme assets, both measuring greenhouse gas emissions (GHG). Trustees must also select one additional climate change metric, not directly related to GHG.

Following recommendations from the TCFD, the DWP proposes that, from 1 October 2022, the 2021 Regulations are amended to require pension schemes to report on a fourth metric - a portfolio alignment metric - setting out the extent to which their investments are aligned with the Paris Agreement goal of pursuing efforts to limit the global average temperature increase to 1.5 degrees Celsius above pre-industrial levels.

Trustees would be able to use three main types of portfolio alignment metrics: binary target measurements, benchmark divergence models and implied temperature rise models. As with the existing metrics requirements, the "as far as they are able" principle would apply, which means trustees should request data from their asset managers and make reasonable and proportionate efforts to obtain the data, but would not be expected to pay disproportionate sums for access to the data.

Two timing points are raised in the consultation:

- Trustees already in scope may have selected a portfolio alignment metric as their "additional climate change metric" for the part of the scheme year that falls before 1 October 2022. However, from 1 October 2022 onwards, trustees would need to select a further additional climate change metric to remain compliant with the Regulations (since the portfolio alignment metric would no longer be regarded as an additional climate change metric). Trustees in this position would need to undertake a review of their current metrics.
- The amendment will not be phased in; the requirement to select a portfolio alignment metric would apply in the part scheme-year that runs from 1 October 2022. In other words, trustees in scope will have to report against the metric within seven months of end of the scheme year which is underway on 1 October 2022. There would be no requirement to report on the fourth metric for scheme years ending before 1 October 2022.

Next steps for trustees: The Paris Agreement goal has been interpreted as requiring emissions to meet "net zero" by 2050. For investors such as pension schemes to achieve the Paris Agreement goal, emissions attributable to scheme assets must reach net zero by that date. Although there is no requirement to do so, many large occupational pension schemes are voluntarily targeting net zero. The new metric will require schemes to assess the risks of transitioning to net zero: the DWP says this will highlight schemes that are furthest from alignment with the Paris Agreement goal.

Stewardship and Implementation Statements

The DWP's proposed guidance - a combination of statutory and non-statutory guidance - is intended to develop best practice for SIP and IS reporting. The consultation sets out the Government's expectations in a variety of stewardship matters, set out in the table below.

The sections on SIPs are "best practice" not statutory guidance. However, guidance in relation to ISs would be statutory guidance, to which trustees must have regard when complying with the IS requirements in the Disclosure Regulations.

Common themes that emerge are:

- SIPs and ISs should be written for members and should be trustees' statements, not those of their consultants.
- Trustees should explain how the policies in the SIP are in members' interests.
- Trustees should be able to include material from voluntary disclosures, such as Stewardship Code reporting, as long as they meet the requirements in the Investment and Disclosure Regulations.

	SIP (non-statutory)	Implementation Statement or IS (statutory)
Stewardship: engagement and significant votes	Trustees should not simply report that they have delegated stewardship to their asset managers. They should identify what the schemes' stewardship priorities are and set out their own stewardship policy in relation to those priorities if they have one, or that of their managers if they do not. The stewardship policy must cover both voting and engagement. **There are reported problems with splitting the vote in pooled funds, including legal barriers in terms of ownership, IT and operational problems, a weakening of the asset manager's voice and regulatory barriers. However, the DWP believes that trustees have a number of options to be actively engaged and advocate for the scheme's policies, even when invested in pooled funds, whether directly or via fund platforms. This includes at the selection phase, and in setting an expression of wish, collective voting, asset manager engagement and monitoring, and collaborative investor initiatives.**	Trustees should report on how and the extent to which voting carried out on behalf of the scheme reflects the policies they have adopted. Where trustees have their own policy but voting is exercised on their behalf by another person, they should explain whether that person has agreed to follow it. Trustees must report all of the most significant votes within the IS itself, and should also report the considerations by which the trustees selected significant votes. If asset managers are unable to give them details of significant votes in time for the publication, trustees should include as much detail as possible, including what information is missing and why the information is missing.

Choosing investments		*(For DC schemes only)* This should include a statement as to whether the investments were chosen in line with Section 36 Pensions Act 1995.
Review of the SIP		*(For DC schemes only)* The information need only include key points on any review which has taken place in the past year. It is sufficient to describe that the review took place, when the review took place and the most significant changes, including brief reasons for any change.
Investment strategy	Substantive policies should be provided and trustees should not simply report delegation to asset managers.	*(For DC schemes only)* Trustees should state whether the SIP policies have been adhered to and, where this is not the case, the reasons why, including explaining what action, if any, it is proposed to take or has already been taken to remedy the position. Trustees have to explain how the policies have been followed and are expected to explain the extent to which this is in members' interests.
Financially material considerations	Processes should be in place for ESG issues to be integrated into trustees' investment decisions. This may include that tenders and mandates contain requirements to integrate ESG into investment decisions, minimum standards for tendering firms and trustee commitments on monitoring and reviews.	*(For DC schemes only)* Trustees should not report simply the delegation of all these matters to asset managers. The IS should explain any outcomes of work relating to ESG carried out by the trustees or others on their behalf. Trustees are expected to explain how this is in members' interests.
Non-financial matters	Trustees are encouraged to explain how they consider member views. Trustees of DC and hybrid schemes may find it helpful to have a mechanism by which members and beneficiaries of DC sections can express their view on investments made, including both self-select options and any default arrangements.	*(For DC schemes only)* Trustees should explain what actions, if any, they have taken as a result of views expressed by members and beneficiaries of DC and hybrid schemes. Trustees are expected to explain how this is in the members' interest.
Arrangements with asset managers	Trustees must explain: • any arrangements they have for incentivising the asset manager to align its investment strategy and decisions with the trustees' policies - this can include monitoring and review, as well as financial incentives • how the trustees monitor transaction costs and, if they have	Trustees of DC and hybrid schemes should confirm whether they followed the policies set out in the SIP - if not, trustees should state the reasons why and explain what action, if any, it is proposed to take or has already been taken to remedy the position. Trustees should explain very briefly how, if at all, they have ensured the design and award of mandates include requirements to integrate stewardship and investment to align with the investment time horizons of clients and beneficiaries and how they have

	a targeted portfolio turnover, what that is. Trustees are encouraged to explain any policies on retention and replacement of asset managers.	monitored asset managers to ensure that assets have been managed in line with their policies. Trustees are expected to explain how these arrangements were in members' interests.

Next steps for trustees: Although there is no indication of when the new guidance will take effect, trustees should check that, in preparing their SIPs and ISs, they are complying with their ESG and stewardship duties. The Government is taking a strong line that these documents should be trustees' statements, not those of their consultants and that boilerplate statements and tick-box compliance will not suffice.

FURTHER ESG DISCLOSURES ON THE HORIZON FOR PENSION SCHEMES

Mandatory "Sustainability Disclosure Requirements" (SDR) for pension schemes could be in place by 2022 and apply to funds of £5 billion or more two to three years after, with funds of £1 billion+ in 2023.

The Treasury has published a policy paper, Greening Finance: A Roadmap to Sustainable Investing which sets out the Government's plans for sustainability-related disclosures. (Sustainability is defined as encompassing the three ESG factors.) It is intended to build on the Green Finance Strategy, published in 2019. According to the section of the forward from the Secretary of State for Work and Pensions, it will "*empower pension schemes … to weigh these [sustainability] factors in all their financial decisions*".

The Government is looking to require asset managers and asset owners (including occupational pension schemes) to disclose how they take sustainability into account. The disclosures would be combined with Taskforce on Climate-related Financial Disclosures (TCFD) climate risk reporting (see above) and presented in a sustainability report referenced within the annual report. Disclosure would be in the same format as existing TCFD climate risk disclosures, based on the four pillars of strategy, governance, risk management and metrics/targets.

The scope and timing, and the reporting detail, will be determined following consultation. The roadmap suggests that the regulations for mandatory SDR for pension schemes would be in place "by 2022" and that, for funds with at least £5 billion of assets, the requirement would take effect within two to three years of the regulations coming into force, with funds of £1 billion or more coming into scope a year later.

The paper contains a strong endorsement of **stewardship**, encouraging schemes to sign up to the Stewardship Code and to encourage or require their service providers to do so. The Government expects the pensions sector to use the information generated by SDR to fulfil their stewardship role by integrating ESG considerations into their investment decision-making, monitoring and engagement strategies, collaboration with other investors and voting practices. The Government will assess progress on stewardship at the end of 2023.

The Pensions and Lifetime Savings Association (PLSA) has published a series of case studies - *Towards a Greener Future: Case Studies from the Pension Sector* - showcasing the climate policies of workplace pension schemes. The publication is presented as a series of essays authored by experts from a variety of pension schemes. A recurring theme is a belief that selling and re-investing in "greener" companies will not be an effective strategy; active engagement with high emitting companies through investor collaboration is preferred to disinvestment.

SIMPLER ANNUAL BENEFIT STATEMENTS TO BE INTRODUCED FROM OCTOBER 2022

The Government has postponed introduction of simpler annual benefit statements for DC auto-enrolment schemes until October 2022.

The Government has published finalised regulations, statutory guidance and illustrative template for the introduction of simpler annual benefit statements for members (not in receipt of pension benefits) of auto-enrolment DC schemes. The regulations will come into force on 1 October 2022, the DWP responding to concerns about schemes' abilities to make the changes required for the regulations to come into force in April 2022, as was initially proposed.

Trustees will be required to provide annual statements that do not exceed a maximum of one double-sided sheet of A4 paper when printed. The illustrative template of the two-page statement is divided into five sections:

1. The member's personal (and scheme) details.
2. How much they already have in their pension plan, with signposting to other information: on costs and charges (although the DWP response encourages trustees to provide costs and charges information on the face of their statements); how money goes in and out of the plan; how to transfer money in from another scheme; and investment (including pooled funds and, where applicable, reference to the TCFD report).
3. How much they could have when they retire.
4. What they could do to increase this.
5. Contact details for further information or to update member details.

As proposed in the consultation, trustees will be able to provide material to members to supplement the required information. However, the final statutory guidance continues to make clear that information must be provided in a separate document(s) to the one double-sided sheet of size A4 paper statement itself, either in physical form or through signposting to digital content. The statement must be the first substantive document presented in any pack of material sent to the member if a covering letter is not included. If a covering letter is included, then the statement should immediately follow. Trustees should “take a proportionate approach” to the provision of any additional documentation and ensure that it is short, simple and accessible.

A number of responses suggested that the regulations should be broadened to include all DC schemes. The Government will consider how applicable the regulations are to other kinds of scheme in its review of the roll out. It will publish a report of the review before 1 October 2027. Meanwhile, the DWP “strongly encourages” trustees of schemes not in scope to apply the same principles of brevity and simplicity set out in the statutory guidance and illustrative template.

Next steps for trustees: Trustees of those DC schemes within scope should plan ahead to comply with the new requirements. Whilst most would be supportive of producing a simpler statement for members to read, this may prove a challenge in the light of the increased disclosure burden placed on trustees. Trustees may want to consider the use of “layering”: items highlighted in the statement with links to other documents for further information. The Government strongly encourages trustees of schemes not in scope to use the discretion that they already have when designing their statements to apply the same principles set out in the statutory guidance and illustrative template.

PPF CONSULTATION ON 2022/23 LEVY

The annual Pension Protection Fund (PPF) consultation suggests a slight reduction to the risk-based levy.

The PPF has published a consultation on the 2022/23 levy rules for the issue of invoices in Autumn 2022. The consultation closes on 9 November 2021 and the final rules are expected to be published at the end of December 2021. The PPF notes that the full impact of the pandemic is yet to be known but its strong funding position means that it has decided to reduce the 2022/23 levy by £105 million from its 2021/22 level, to £415 million. The PPF estimates that this will mean that approximately 82% of schemes will see a reduced risk-based levy.

The levy scaling factor, the scheme-based multiplier and the risk-based levy cap will remain the same. The PPF has also confirmed it will continue to allow levy payers to apply for an extension of payment terms for the 2021/22 levy where they have been adversely affected by the pandemic. (The concession was introduced for the 2020/21 levy in June 2020.) The levy is normally payable within 28 days of receipt, with interest being incurred for late payment. The concession gives levy payers up to 90 days to pay without incurring interest. Schemes and sponsoring employers can apply online for the payment extension within 28 days of receiving their levy invoice. The application must include details of how the levy payer continues to be affected by the pandemic.

No changes are proposed to the employer-scoring model used by Dun & Bradstreet. As a result of previously announced changes to assumptions, updated mortality assumptions and adjustment to discount rates and wind-up expenses apply to valuations with an effective date on or after 1 May 2021.

PENSIONS OMBUDSMAN GUIDANCE ON COMMUNICATING WITH MEMBERS

New useful guidance from the Pensions Ombudsman (TPO) on best practice for dealing with complaints.

TPO has published a guidance note on best practice for communicating with pension scheme members. The two-page note uses feedback from enquiries and complaints up to 2020/21 to produce a list of top tips. Some of the less obvious are:

- Make sure there is a shared understanding of the complaint.
- In explaining what has/should have happened to the member, include legislation, policies, or procedures.
- Clarify the outcome the member desires.
- Make sure administrators are aware of all scheme changes.

The guidance note includes a link to a new section on TPO's website, "*How to avoid the Ombudsman*". This includes guidance, case studies and links to key determinations in the following areas:

- Communication (providing information to members)
- Distress and inconvenience awards
- Early Resolution Service
- Ill health pensions
- Unpaid pension contributions
- Death benefits.

PENSION LEGISLATION AND REGULATION WATCH LIST

No	Topic	Expected effective date	Further information/action
1	Annual statement on compliance with policy on stewardship and engagement activities, and voting behaviour on website	1 October 2021	DB schemes only. The requirements for DC schemes applied to annual reports signed off on or after 1 October 2020.
2	Climate risk governance and reporting requirements	1 October 2021	For all authorised master trusts and schemes with £5 billion or more in net assets on the first scheme year end date on or after 1 March 2020. Governance to be in place for the scheme year underway and the first annual report to be published within seven months of the end of the scheme year.
3	Changes to DC scheme governance and disclosure, including the annual Chair's statement and charge cap	First scheme year ending after 1 October 2021 (changes to Chair's statement); 5 October 2021 (changes to annual scheme return); first scheme year ending after 31 December 2021 (detailed value for money assessments for schemes with assets below £100m) April 2022: introduction of £100 de minimis pot size below which flat fees cannot be charged	DC schemes only. DWP to confirm whether look-through mechanism for charge cap compliance will be amended or removed. DWP to review whether fines for non-compliance with Chair's statement requirements should be mandatory (DWP review of Charges and Governance Regulations April 2021).
4	Restrictions on transfers of a member's cash equivalent transfer value by trustees/managers of occupational or personal pension schemes unless prescribed conditions are met	Autumn 2021	Awaiting final regulations.

No	Topic	Expected effective date	Further information/action
5	Trustee oversight of fiduciary managers and investment consultants	Under the Investment Consultancy and Fiduciary Management Market Investigation Order 2019, compliance statements, confirming the extent to which requirements have been met, had to be provided to CMA by 7 January 2021	Consultation response and new DWP regulations have been delayed until June 2022.
6	DB superfunds	Regulatory regime expected Autumn/Winter 2021	Interim regulatory regime in place from October 2020.
7	Refer members to guidance before processing application to access or transfer flexible benefits	April 2022	For DC schemes only. Consultation on draft regulations closed 3 September 2021.
8	Register certain trusts with the Trust Registration Service	Registration by 1 September 2022	Applies to some trusts relating to pension and life assurance benefits where no exemption applies (e.g. bare trusts set up on distribution of a lump sum).
9	Simpler annual benefit statements	1 October 2022	DC schemes used for auto-enrolment.

London
T +44 (0)20 7600 1200
F +44 (0)20 7090 5000

Brussels
T +32 (0)2 737 94 00
F +32 (0)2 737 94 01

Hong Kong
T +852 2521 0551
F +852 2845 2125

Beijing
T +86 10 5965 0600
F +86 10 5965 0650