Necessary overload

The Pensions Regulator's (TPR) new trustee requirements came into force at the beginning of this month to ensure that trustees disclose how they are integrating sustainable investment principles into their strategies. Jack Gray investigates what this means for trustees, the challenges it presents and whether this is one regulation too far

Since 1 October 2019, trustees have had to abide by new pension scheme investment guidelines, which changed the way they must present their statement of investment principles (Sip). The Pensions Regulator (TPR) has said that the Sip must now include details of trustees' policies on several aspects of their investment strategy, including environmental, social and governance (ESG) factors and stewardship of investments. Trustees are now also obligated to disclose the extent to which members' views are considered when planning scheme investments and the details of arrangements with asset managers. The industry is somewhat split on the guidelines, with some believing it is a necessary step for pensions to keep up with other financial markets, while others think that it will make the job of a trustee unnecessarily complex.

Adapting trustees

Pension scheme trustees are once again having to adapt their practices to make sure they are complying with TPR's new rules.

Ensuring that they are aware of and fully prepared to abide by the regulations could be key to avoiding being subjected to the regulator's interventions.

However, Sackers partner, Ralph McClelland, warns that this is just "one issue for busy pension scheme trustees" and this may just be the tip of the regulation iceberg.

"As with any change of this sort, there's work to be done with scheme boards in formulating beliefs, consulting with sponsoring employers, liaising with managers and advisers, and going through the governance required to agree changes to the scheme statement of investment principles," he explains.

"There is also a real sense in which this is only the beginning of the exercise. Articulating a policy is one thing, but the policy is meaningless if it is not adhered to in practice."

Willis Towers Watson director and head of sustainable investment, Adam Gillett, agrees that there are more trustee guidelines to come, and believes that it is necessary to ensure that the performance of trustees and their schemes continues to progress.

He states: "There's more regulation coming, this is just the thin end of the wedge rather than the end game. They've got to keep upping their game and what is good practice will keep getting a higher bar."

Gillett says that the "most important narrative" of the changes is that this is just the beginning of a journey into creating more sustainable investment practices to help tackle climate change. The scale and urgency of the climate challenge is such that we need to "harness" the regulations and mindset around sustainable finance to achieve worldwide change, he adds.

Summary

- Since TPR confirmed the changes in sustainable investment disclosure policy in June, trustees have been urged to prepare themselves or risk falling foul of the new regulations.
- Some believe that the guidelines are necessary to ensure that pension schemes are moving with the times and doing their bit to tackle climate change.
- However, others think that TPR has overstepped the mark and the changes will result in nothing more than a prescriptive tick-box exercise that catches out trustees.

Higher standards

Higher standards will now be expected of trustees, but they seem to be ready for the challenge. A recent study by Hymans Robertson finds that 70 per cent of trustees are supportive of the changes and 96 per cent feel prepared for their implementation. It appears as if the changes are having the desired effect, with the study finding that 84 per cent of trustees have increased training on responsible investment, while 91 per cent say that they have spent more time discussing sustainable investment in trustee meetings over the past year.

Furthermore, it's not only the trustees that seem to feel positive about the changing guidelines, and some argue that implementing a sustainable investment strategy will benefit members and investors with positive returns. Hymans Robertson's research finds that 49 per cent think that it will improve investment returns, while Newton Investment Management chief commercial officer, Julian Lyne, says that TPR's new guidance "should be viewed as good news for investors of every kind" as ESG factors are "key drivers for the long-term sustainability of companies".

Royal London director of policy, Steve Webb, agrees: "The good news

is the balance of the research suggests that this need not involve sacrificing returns and, in some cases, can generate enhanced performance.

"Those responsible for managing other people's money will need to ensure they are not behind the curve when it comes to taking account of these important issues."

Keeping up with the curve is another reason cited as to why these new regulations are so important. Attitudes towards sustainable finance is changing rapidly as people wise up to the environmental challenges facing the planet.

Gillett believes that new regulations are key to ensuring that the pensions industry does its part in tackling climate change. He says: "We need to pull every single lever we have as individuals and collectively, and regulation is a hugely powerful one of those levers. We should be trying to use it as best we can because we don't have a lot of time and the scale of the challenge is pretty enormous."

Overload

Despite the positives, some in the industry are not as enthusiastic about the changes. Concerns have been cited that the increased requirements are going to increase the already heavy workload for trustees. Some see it as a time consuming exercise that will add to the already complicated legal compliance required of trustees and put people off becoming trustees. Furthermore, although TPR insists that it is not just a tick-box exercise, there are concerns that it could become one as the regulations could be prescriptive and encourage trustees to just be compliant, rather than always having the best member outcomes as their top priority.

"There is a danger that trustees will suffer from intervention overload," begins BESTrustees president, Alan Pickering. "Everything that we do should have at its heart the maintenance or improvement of member outcomes and there's a real danger that process becomes an end in itself and not all of these processes will directly improve member outcomes.

"What's more, the prescriptive nature of some of the interventions is such that we're having to get legal sign-off to make sure that not only are we doing the right thing, but we're doing the right thing in accordance with a prescriptive set of rules. There's a real danger that focusing on a prescriptive process, avoiding falling foul of detailed regulations, can actually be counterproductive.

"If it becomes unduly technical and unduly compliance orientated, I think that quality people are not going to step up to the plate. "

The Pensions and Lifetime Savings Association believes that the new regulations are too all-encompassing and that "TPR should focus on targeting disengaged schemes rather than putting new obligations on all schemes", as most schemes are already well-run and this may impede them in achieving the best outcomes for members.

As with any increased governance exercise, Lyne warns that the ESG risk disclosures are "likely to entail additional costs" and sustainable investments could "potentially impact performance too".

Pickering adds: "That legal sign-off costs money that might be better used elsewhere. I'm not saying to the lawyers 'please make sure members can understand this' I'm saying, 'please make sure that I cover my back'.

"I ought to be glad that we haven't had a government for the past three years, goodness knows how much we'd have to tackle."

Written by Jack Gray