TUC

trustee network

member trustee news

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New consultations on DB funding

Alongside the Chancellor's Autumn Statement, the government announced in December that the DWP is looking to help businesses manage their pension costs by consulting on two proposals:

- to give the Pensions Regulator a new statutory objective to consider the long-term affordability of deficit recovery plans to sponsoring employers; and
- to allow schemes undergoing valuations in 2013 or later to smooth asset and liability values.

Whilst the announcement has been welcomed by many industry commentators, others have warned that, whatever the pros and cons of smoothing, it does not reduce the actual cost of pension provision. Whilst more flexibility may be good news for scheme sponsors, by way of reduced deficit contributions, it may result in reduced security for members, at least in the shorter term.

The Regulator has confirmed that pending the outcome of the consultation, it is 'business as usual':

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Welcome

Welcome to the spring edition of the TUC trustee news, the first since the TUC's Trustee Conference in November. Over 90 people attended the conference, with very positive feedback. Comments included "very informative and worthwhile – also good for networking" and "Enjoyable conference and good to meet up with other trustees as we all have the same difficult job in difficult times".

Keynote speakers included Pensions Minister Steve Webb, whose paper on Defined Ambition schemes is featured on page 7, and Professor John Kay: reactions to his report on short termism in equity markets can be found on page 8. This year's conference will take place on Tuesday 26 November, so put the date in your diary now!

There is a questionnaire enclosed with the newsletter, asking for your views on the conference. **We want to hear from those who don't attend as well as those who do** so please do take the time to respond – thanks in advance! Presentations from the 2012 conference are available online at **www.tuc.org.uk/economy/tuc-21777-f0.cfm** (A data

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"We welcome the wider debate that a transparent consultation will bring to these fundamental issues, the outcomes of which will need to be clearly understood and worked through, and we encourage trustees and their advisers to participate. Until it is clear as to whether the regime will be altered in any way, there is no change in the responsibilities of trustees and sponsors.

They should continue to develop their plans as set out in the regulator's statement *Pension Scheme Funding in the Current Environment* published in April 2012, and other related guidance, and in line with the statutory timetable."

You can read more about the TUC's views on this issue at **http://touchstoneblog.org.uk/2012/12/smoothly-does-it/**

TUC Fund Manager Voting Survey

The TUC's tenth annual Fund Manager Voting Survey, published in November, analyses the voting records of 26 fund managers, pension funds and voting agencies across 76 company resolutions between January and December 2011. The survey found a sharp divide in investors' voting stances. Two survey respondents supported over 85 per cent of management proposals on which votes were sought, while three respondents supported less than 25 per cent.

The survey shows encouraging progress in the public disclosure of fund managers' voting records, with 26 of the 28 survey respondents now making at least some voting data publicly available. In 2003, when the first TUC Voting Survey was published, just one institutional investor – the Co-operative Insurance Society – made its voting record public.

However, the TUC still has concerns over the quality of data being made available by fund managers, with some only disclosing votes against and abstentions, and others only providing headline statistics.

While many investors cited the Stewardship Code as a reason for making their voting more public, it appears to have had little effect on their voting stances; the TUC would like the Code toughened up so that fund managers are required to consult their clients over their approach to voting and engagement. Former TUC General Secretary Brendan Barber said: "Fund managers have considerable power over the behaviour of corporate Britain but they wield influence in very different ways. It's encouraging to see more fund managers publicly disclosing their voting records, even if the quality of reporting is a little patchy. However the sharp divide in voting positions sends an important message to pension funds and other fund manager clients – when it comes to voting and engagement, it makes a huge different who you invest with. Clients should engage with their fund managers to ensure they are happy with the approaches being taken."

The TUC 2012 Fund Manager voting survey is available at **http://bit.ly/R5nWAP**

Concerns over fund managers' accountability and lack of transparency have also been raised by FairPensions in their new report, *The Missing Link: Lessons from the shareholder spring*, published in November. Only one of the twenty asset managers assessed in the report disclosed reasons for all significant votes, with a further eight giving reasons only for votes against management. The report also casts doubt on institutional investors' appetite for tackling high pay, revealing that 72 per cent of institutional investors responding to the government consultation opposed plans to give them a binding vote on executive pay. The report can be found on the FairPensions website at **http://fairpensions.org.uk/press/missinglink**, which also provides a chart showing how fund managers voted on executive pay at 10 of last season's AGMs.

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request form, to help trustees identify economies of scale, is available at the same address – this arises from the conference workshop on investment management costs led by Chris Sier of Stonefish Consulting.)

The end of last year also saw auto-enrolment get under way, so the focus on DC provision continues. You can read more about the new code on charges and the Regulator's latest guidance on page 5.

Meanwhile in the DB universe, the Chancellor's commitment to consult on scheme funding has been welcomed by many, but also seen as undermining the Regulator's funding guidance; this will be a difficult few months for trustees who have valuations in progress.

DB schemes where accrual continues will also be seriously affected by the plans to end contracting out: the White Paper was published just as this edition was being finalised, so we'll cover that in detail in the next edition.

News in brief

State Pension forecasts

Following changes to government online services, state pension forecasts can now be obtained from **www.gov.uk/state-pension-statement**. Statements can also be ordered by telephone or in writing. The Combined Pension Statement Service (formerly known as Combined Pension Forecasts), which enables trustees or employers to include State Pension information in their annual benefit statements, has also been relaunched: information is available at **www.gov.uk/combined-pension-statements-employers.**

SMPI changes

Following consultation, the FRC has published a revised version of actuarial standard TM1.This sets out the assumptions to be used in annual statutory money purchase pension illustrations (SMPIs). The most significant change is the removal of the cap of seven per cent pa on the rate at which pension scheme investments are assumed to build up. Providers will have to make justifiable assumptions about the investment returns that can be achieved taking account of the nature of members' investments. FRC will monitor the assumptions used in SMPIs to assess the impact of the removal of the cap. The new requirements will come into force for SMPIs with illustration dates on or after 6 April 2013.

Purple trends

The seventh edition of the *Purple Book* was published by the PPF in November. The publication, based on data from 6,316 schemes, provides confirmation of a number of trends, including:

- Scheme funding on a s179 basis deteriorated in the year to 31 March 2012 – the funding ratio (assets divided by liabilities) fell from 100 per cent to 83 per cent.
- The proportion of schemes that are open to new members and new accruals continued to decline.
- The proportion of scheme assets allocated to bonds and alternative investments continued to rise.

Seminar

The TUC is hosting a seminar on DC governance on 15 May with shadow pensions minister Gregg McClymont MP. Details at **http://tucpensions2.eventbrite.com/#**

Stewardship Code update

According to the Financial Reporting Council's annual update, published in December, the Stewardship Code, introduced in 2010, has been a catalyst for greater engagement between companies and their shareholders in 2012. There are now over 250 signatories to the Code, including 57 asset owners, mainly the UK's larger pension funds. Recent changes to the Stewardship Code ask investment managers to explain what use they make of proxy advisers, and ask asset owners such as pension funds to reflect their stewardship policies in the mandates they award to managers.

The NAPF has published a stewardship policy to help pension funds fulfill their stewardship responsibilities. The policy sets out six best practice principles for pension schemes to follow, such as setting mandates for asset managers to explicitly cover stewardship responsibilities and reporting to pension scheme members on how policy is implemented. It also includes an implementation questionnaire and short guidance document to help pension funds sign up to the Code.

Some consultants have also provided guidance on the new Code requirement that "... asset owners should seek to hold their managers to account for their stewardship activities." For example Mercer commented that "The trustees should view stewardship as a means of enhancing the existing investment manager monitoring process and a key part of their duty to beneficiaries" and have suggested some questions which trustees should be asking themselves, perhaps as part of an annual review:

- Do our investment managers effectively engage with companies regarding Environmental, Social and Governance (ESG) issues on behalf of our scheme?
- Do our investment managers effectively report on their engagement and voting activity? Is there any additional disclosure that would be beneficial to the scheme?
- Do we effectively report our scheme's stewardship activities to members?
- Are we (and our investment managers) making best use of collective engagement opportunities?

Meanwhile two recent surveys have shown increasing awareness of the importance of stewardship issues from both pension funds and asset managers. The NAPF's eighth annual engagement survey indicated that pension funds are embracing their stewardship responsibilities and are beginning to foster a market for stewardship. 71 per cent of respondents (up from 48 per cent in 2011) took stewardship into account in manager selection. In addition, 90 per cent stated that they had reviewed their asset managers' application of the stewardship policy. However, less positively, the survey showed that investment consultants proactively raised the issue of stewardship with pension funds in only two out of five cases (38 per cent).

Another survey, by Aviva Investors, of 31 global fund managers, found high levels of awareness of the importance of ESG factors, with nine out of ten saying that non-financial impact issues were important to clients and consultants, while 79 per cent said ESG criteria will be part of all mainstream funds in future. Nearly three quarters (72 per cent) said there was a link between total investor returns and a company's ESG performance. However, 68 per cent of asset managers said no board member held responsibility for socially responsible investment and only 52 per cent are signatories of the UN Principles for Responsible Investment. Despite 84 per cent saying they actively voted on holdings, only 61 per cent publicise their voting record.

New code on **DC charges**

New guidance on the costs of DC pensions *Pension Charges Made Clear: Joint Industry Code of Conduct* was published in November. The intention of the Code is to provide more consistent disclosure to employers of those charges that are paid from member pension pots. It is intended to apply to all parties providing services to employers in setting up and administering pension schemes for auto-enrolment, including insurance companies, trust-based pension schemes and financial advisers. It will be fully implemented from April 2013 and will be monitored and reviewed by a working group every year from summer 2013.

The key features of the code are that:

- All charges should be clearly and accurately stated in writing.
- A standard template summarising the pension charges levied should be given by the provider.
- The provider must give examples of the effect of charges on pension pots, either directly or via a dedicated web tool.

The TUC has welcomed the new code of conduct. Former TUC General Secretary Brendan Barber said: "The code is a big step forward. Employers need help in choosing the best auto-enrolment pension, and their staff need to know they have made a good choice too. This new code brings greater transparency to charges. This is vital as even small variations can make a big difference to the pensions people receive. It's good to see consumers, unions, employers and the pensions industry working together on this code. This co-operation must continue to ensure compliance with the code."

The Code can be found at **www.napf.co.uk/PolicyandResearch/Charges-code-of-conduct.aspx**

Automatic enrolment: updated guidance for trustees

The Pensions Regulator has updated its guidance for trustees of schemes which may be used for automatic enrolment. The guidance includes a five-step checklist:

1. Find out if the scheme can be used: the Regulator provides a 'qualifying scheme tool' to help assess if a scheme meets the criteria for auto-enrolment.
2. Review the scheme against the Regulator's six principles and the quality features of a good DC scheme – in particular, if the scheme is small, make sure that it can achieve sufficient economies of scale to offer value for money. In particular, tPR says "If the scheme has been running for many years and has not been kept up to date, you must be confident that it can meet the standards set out in the principles and quality features".
3. Review the default investment strategy: you need to ensure that the default strategy reflects the new membership profile and meets the needs of the members. Your trustee board should review this on a regular basis.
4. Examine your administration processes: you will need to check that the scheme's administrators have the processes in place to cope with an increase in scheme membership. You should be satisfied that the administrator will be able to deal with opt in and opt out requests.
5. Member communication: whilst the duty is on the employer to provide the right information to the right individual at the right time, you may be asked to fulfil this duty on behalf of your employer. TPR provides a template to assist with this.

You can read more and find additional resources on the Regulator's website at **www.thepensionsregulator.gov.uk/trustees.aspx**

Better earners have better pensions

The TUC has published a 'TUC Pension Scorecard' that assesses the health of workplace pensions provision across the UK. The report shows that public sector workers are more than twice as likely as private sector workers to be contributing to a workplace pension scheme, while those earning over £300 a week are twice as likely to be paying into a pension as those earning less than that a week. Low-paid workers who are saving into a workplace pension are also likely to have lower combined employer and employee contribution rates (under eight per cent) than better-off staff. The report also highlights concerns about the growth of contract-based schemes over trust-based schemes, a trend that looks set to continue as auto-enrolment kicks in. Contract-based schemes often have lower contribution rates and have poor governance structures. The report concludes by saying that while auto-enrolment will help to improve pension provision, and could help to drive up contribution rates and membership of trust-based schemes, it alone cannot deliver the level of pension savings needed to guarantee a decent income in retirement. The Pensions Scorecard report is available at **http://bit.ly/VMfc4D** Two working papers are also available, on better DC (by Bryn Davies) and on the future of DB (by Hilary Salt); these can be found respectively at **http://bit.ly/WV9kVN** and **http://bit.ly/TPHDY3**

Impact investment

A report from Social Finance and Finethic, *Microfinance, Impact Investing and Pension Fund Investment Policy Survey*, published last October, has looked at the reasons why, unlike some pension funds in Scandinavia and the USA, UK pension funds have been slow to consider 'impact investments' (defined as investments into social businesses that deliver financial returns alongside measurable social impact), such as clean energy, microfinance or social housing.

The report, based on a survey of 47 pension funds, with £143bn assets under management, found that respondents were interested in impact investments, with 23 per cent of respondents already including impact investments in their portfolios and 47 per cent stating that they expect to pursue such investments in the next two years.

Respondents were mostly interested in infrastructure investments. They found a number of barriers that have prevented Impact Investment from gaining momentum, including a lack of awareness and understanding about the opportunities available.

There is also a problem over mismatch of size: most funds that have the internal resources to understand the asset class often require minimum investment sizes (larger than £200m) which is far beyond the capacity of a typical impact investment opportunity, whereas pension funds that would consider smaller minimum investment sizes lack the internal resources to understand the asset class. However, the question of maximum returns and fiduciary duty has been the biggest and most important issue for impact investments and the report explores this in more detail.

The report is available at **www.socialfinance.org.uk**

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DWP's '**Defined ambition**' outlines risk-sharing options

The DWP's paper, *Reinvigorating Workplace Pensions*, setting out the government's ideas on 'defined ambition' pensions and the future of workplace provision was published in November.

The paper, which can be found at **www.dwp.gov.uk/docs/reinvigorating-workplace-pensions.pdf**, focuses on a number of radical ideas for risk-sharing in workplace pensions provision, from both a 'DC plus' and 'DB minus' perspective.

These include:

- Conversion of benefits – where the employer promises a defined level of benefit, and when the member retires or leaves the scheme, the benefit is converted to a cash lump sum of an equivalent value – this is then used either to purchase a retirement income, or to transfer to a DC scheme.
- Mutualised money back guarantees – where a guarantee ensures a saver gets back at least what they put in, funded by a levy on members' funds.
- Guaranteed fixed-period returns – purchased from providers such as insurance companies on members' behalf.
- Standardised income guarantee insurance – an insurance policy against investment losses paid for out of individual members' accounts.
- Employer-funded "smoothing fund" – where the employer contributes towards a central fund that is used to manage a targeted outcome at retirement.
- Collective DC – where risk is shared amongst the membership and projected benefits calculated, but not promised.

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> » *The government is also exploring the idea of a 'star rating' system for DC pension schemes ... a smaller number of larger scale, multi-employer pension schemes might offer both employers and employees value for money.* «

There is, however, no clear timetable yet for any legislative changes that would be needed to implement many of these 'DA' ideas.

The paper also reaffirms the Minister's intention to monitor DC charges, and to implement a cap if necessary. The government is also exploring the idea of a 'star rating' system for DC pension schemes, and whether a pensions market with a smaller number of larger scale, multi-employer pension schemes might offer both employers and employees value for money. However, the paper includes few firm proposals on how greater scale may be achieved in existing DC provision, and only limited references to governance issues. While the paper stresses the importance of higher contributions into DC pensions, it does not consider what policy changes may be required to incentivise individuals to save more.

The Kay Review

The Department for Business Innovation and Skills has published a response to the Kay Review of UK equity markets, which can be found at **www.gov.uk/government/news/government-responds-to-the-kay-review**

The government's response has been welcomed by the TUC, but the then General Secretary, Brendan Barber, also expressed concern that there might be pressure to dilute the recommendations: "Any attempt to move the City away from the short-term, quick buck approach of recent times is an ambitious one and we're pleased to see the government giving the Kay recommendations such support. However, as other attempts at reform have illustrated, the City will not change the way it does things without significant pressure. Ultimately the change of culture we all want to see may not happen unless the government abandons the voluntary approach and changes the law governing how Britain's boardrooms operate."

The government's response sets out the work which is being taken forward including:

- working with EU counterparts to end mandatory quarterly reporting and help reduce the excessive focus on short-term earnings
- endorsing clear minimum standards of behaviour for all investment intermediaries to ensure they act in the long-term best interests of their clients.
- asking the Law Commission to review the legal obligations on intermediaries (including those arising from fiduciary duties) to take appropriate long-term factors into account.
- asking the Financial Services Authority (FSA) to ensure that the regulatory framework promotes high standards of behaviour throughout the investment chain
- encouraging investors to establish an investors' forum to champion constructive engagement with companies
- endorsing good practice statements for company directors, asset managers and asset holders, which emphasise the need for trust-based relationships and advocate more collective action by institutional shareholders; better disclosure of costs in the investment chain; increased transparency and fairness in stock lending; and better alignment between pay and long-term performance.

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The government will be publishing a progress report in summer 2014 to report on their progress in taking forward these recommendations, and steps taken by companies and investors.

Meanwhile, the FSA has published research that throws further light on conflicts of interest within the fund management industry. In its report, *Conflicts of Interest Between Asset Managers and Their Customers: identifying and mitigating the risks*, the FSA warned that firms were often failing customers' interests in relation to cost and suitable investments. It said during a review of asset management firms between June 2011 and February 2012, a number of firms were found to have no adequate framework for identifying and managing conflicts of interests. The FSA also found breaches in its regulations for use of customers' commissions and fair allocation of trades. Attitudes and culture of senior management were cited as a main source of these issues. The FSA said feedback has been given to the firms involved in the study and a further round of visits will be conducted at a later date.

The report is available at **www.fsa.gov.uk/static/pubs/other/conflicts-of-interest.pdf**

Comment from the TUC can be read at **http://touchstoneblog.org.uk/2012/11/wake-up-call-from-the-fsa-on-conflicts-of-interest-in-investment/**