SQUIRE PATTON BOGGS

Setting a Responsible Investment Strategy

A Guide for UK Pension Schemes

The Pension Schemes Act 2021 introduces requirements for larger pension schemes to undertake mandatory governance and reporting in relation to the effects of climate-related risks. Our Quick Guide provides more detail on the publication of TCFD reports. However, the risks and opportunities connected to responsible investment will already be clear to many schemes, irrespective of size.Reputational risk may exist where any scheme is not clear about how its assets are invested, as we highlighted in this blog.

By summer of 2022, there will be further impetus for schemes to have considered climate change and stewardship practices, when it is expected that The Pensions Regulator's (TPR) new Single Code of Practice will come into force. It is anticipated that TPR will expect trustees to have undertaken a risk assessment covering investment risks relating to climate change, the use of resources and the environment; social risks; and the potential for depreciation of assets arising from systemic risks.

Here is our guide, in the form of a self-assessment checklist, on the key steps for trustees to consider when setting and implementing a responsible investment strategy in a manner that is appropriate and proportionate for their scheme.

1. Understand your responsibilities, risks and opportunities	• Have you received training on responsible investments, e.g. from your investment consultants? • Do you understand the difference between financial and non-financial factors and when you can take them into account? • Have you considered all relevant risks, including in relation to investment performance, reputational issues, litigation risks (i.e. brought against the scheme or an investee company) and sponsor alignment?
2. Set your beliefs	• Do you have a set of investment beliefs? • Who has set those beliefs: full trustee board, investment sub-committee or investment consultants/fiduciary manager? • Do they cover environmental, social and governance issues, and any other aspects of importance to the trustees? • What approach do you wish to take as a trustee board (e.g. minimum compliance, tailored to your scheme or industry-leading innovation)? Have you assessed the risks of each approach (e.g. will doing more than the minimum now make it easier to comply if the bar is raised in the future)? • When do you think your portfolio will be carbon neutral? • What weighting, compared to other factors, should responsible investment considerations be given when assessing new or existing mandates? • Has there been engagement by the membership on these issues that should be taken into account? • What conversations have been had with the scheme sponsor to reduce the risk of misalignment of goals (in some cases, including consideration of the employer's own approach to investment of its capital)?
3. Document your beliefs	• What does your SIP say about voting, stewardship and wider responsible investment beliefs and is it compliant with your statutory duties? • How will your approach interact with the requirement to produce an implementation statement? • Are there any elements of your strategy or beliefs that you would not wish to be publicly disclosed (and, therefore, may be better documented outside of the SIP)? • Is it appropriate to have a separate document setting out the trustees' responsible investment policy? • Will this policy cover high-level beliefs or describe how the trustees intend to implement their beliefs?

4. Test your current investment portfolio	• Have you identified all asset classes to which your investment beliefs/policy are relevant? • What advice do you need from your investment consultant on the extent to which your current portfolio aligns, or does not align, with your beliefs? • Will you engage in scenario testing or establish specific voting guidelines? If so, what other resources or advice are required? • How will you engage with your investment managers on these issues, and when? • Are there any structural barriers to changing your current arrangements, such as asset allocation or legal structure, which should be taken into consideration?
5. Implement the changes	• Are your investment consultants asking appropriate due diligence questions of investment managers at the procurement stage? • Do the investment managers' appointment documents contain commitments in respect of their ESG credentials and their willingness to align themselves to the trustees' beliefs? • Should specific investments be excluded, and is that reflected in the investment documentation? • What information do you require from investment managers in order to monitor their actions and the overall position of the portfolio? • Are investment managers required to give you the information you require?
6. Report on progress	• Does your business plan take account of statutory reporting and publication deadlines, such as the SIP, implementation statement and TCFD requirements? • Would you be prepared for enquiries by members or TPR in relation to your strategy and beliefs? • Should an information sharing protocol be agreed with the scheme sponsor (or existing agreements updated) to include reporting on any trustee decisions and mandate changes, and to provide the trustees with information for the purposes of covenant-related integration of ESG issues?
7. Plan for breaches	• Would your contracts with your investment managers enable you to pursue them for failing to invest appropriately in line with their policies (or the trustees' policies)? • Have you planned to take action if circumstances came to light that revealed your assets have been invested contrary to your beliefs or in a way that may be damaging (whether reputationally or financially)?
8. Review, monitor and engage	• How will you measure and challenge investment managers in relation to their commitments, and how often? • How will you map your policies and beliefs to TPR's requirements in the Single Code of Practice? • How will you maintain knowledge and understanding to keep up with regulatory changes?

If you would like more information, please get in touch with your usual firm contact or Chris Harper, Pensions partner.

Chris Harper
Partner, London
T +44 20 7655 1025
E chris.harper@squirepb.com