PENSIONS AND LIFETIME SAVINGS ASSOCIATION

PENSION TRUSTEE SKILLS, CAPABILITY AND CULTURE: A CALL FOR EVIDENCE

PLSA RESPONSE

5 SEPTEMBER 2023

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ABOUT THE PENSIONS AND LIFETIME SAVINGS ASSOCIATION

The Pensions and Lifetime Savings Association (PLSA) is the voice of workplace pensions and savings. We represent pension schemes that together provide a retirement income to more than 30 million savers in the UK and invest more than £1.3 trillion in the UK and abroad. Our members also include asset managers, consultants, law firms, fintechs, and others who play an influential role in people's financial futures. We aim to help everyone achieve a better income in retirement.

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EXECUTIVE SUMMARY

The PLSA welcomes the DWP and HMT's call for evidence to support trustees in improving their skills and capability, assessing the advice they receive and removing barriers to their effectiveness. Below is a high-level summary of our response, broken down by the three chapters of the call for evidence.

Chapter 1: Trustee skills & capability

Knowledge and understanding

- Industry feedback and survey results indicate that among larger schemes, trustees generally know – and meet – the knowledge and standards expected of them. Among trustees within smaller, harder-to-reach schemes, it is less clear whether the same is true, and additional assessment by TPR is required. Feedback has also indicated that trustee knowledge and understanding can vary widely on an individual-to-individual basis.
- Trustees generally have the right knowledge and understanding to invest in the full breadth of available investment opportunities. They make informed and rational choices about the appropriateness of investment in certain assets given the scheme's strategy and the potential upsides to each opportunity. As there are different factors to consider across DB and DC schemes, trustees investment decision-making varies accordingly.
- Regarding investment in private equity and other "productive assets," investment is more appropriate in open DB or DC schemes with a long maturity than in closed DB schemes, and this is one of the main reasons why investment in such assets is limited across the pensions market as a whole. The PLSA's assessment of why more pension investments are not allocated to such assets – and what action is needed to increase such investment – is set out in our recent paper, "Pensions and Growth: Supporting Pension Investment in UK Growth" (June 2023).

Regulatory environment

- Changes to the current regulatory environment that would create additional time constraints or burden to trustees should be avoided, as the greatest barrier to trustee knowledge and understanding is time. Trustees of smaller, less-resourced schemes likely feel this strain even more acutely. Should the Government decide to create additional regulatory requirements, these should be purposeful and measured. In addition, consideration should be given to the regulatory requirements as they stand, to streamline them and reduce undue processes that add burden.
- TPR should keep a register of all trustees. Mandating the collection of this information could serve as a useful first step to understand who currently serves as a trustee and to help with future assessment of trustee knowledge and necessary outreach. The register would also be helpful to disseminate existing resources to trustees, like the codes of practice.
- TPR should undertake a review of its Trustee Knowledge and Understanding (TKU) toolkit with the support of an industry working group, as TKU is currently not considered sufficiently demanding. TPR should use the register to track trustee completion of the updated TKU and this should be required as "accreditation" for all registered trustees. TPR should also consider more rigorous requirements for professional trustees.
- The inclusion of a professional trustee on a board generally improves the operation of the scheme. However, limited resources – particularly of smaller schemes who might especially benefit from the presence of a professional trustee – are a challenge. In addition, our members feel that there is scope to raise the standards required of professional trustees.

Good governance

- Current pension scheme regulation emphasizes the processes of scheme governance bodies rather than the individuals – or inputs – that comprise them. In our paper, "Good Governance – How to Get There" (August 2017), we stress that "the regulation of pension fund governance should focus on these inputs – if governance bodies are populated by the right people, situated within an appropriate and accountable structure, this maximises the likelihood of good decision-making, leading to good outcomes for scheme members." Well-balanced skills and collective knowledge among boards, as well as the support of a properly resourced executive team and an experienced and skilled chair, are also of utmost importance.
- Given that there are thousands of schemes of all different sizes and types, governance needs will vary for each scheme's individual circumstances. TPR should undertake an assessment of trustee board skills and effectiveness across all scheme types, particularly to support smaller schemes that are less resourced. There should be strong diversity among trustees themselves across skills, background and experience as well as protected characteristics, to best represent the members they serve.

Chapter 2: The role of advice

- Trustees already work to find appropriate advice – as currently required in TPR's regulation and codes of practice – and use this to make judgements in the interests of their members. They generally receive an appropriate amount of external support to make investment decisions and take the investment advice that they receive seriously, in line with their fiduciary duties.
- Currently, trustees often decide against investment in alternative asset classes such as unlisted equities due to a range of factors relevant to the unique aspects of the scheme and its members. There are also certain market barriers that exist – unrelated to the quality of advice they receive – that result in trustees deciding against these types of investments. In the case of DB schemes, these barriers are related to the unsuitability of such assets for closed DB schemes with short maturities, and for open DB schemes due to the restrictive nature of the TPR's DB Funding Code. In the case of DC schemes, the current operation of the auto-enrolment pension's market is too focussed on cost rather than value for money. (DWP is already taking action on the latter.)
- There should be a focus on assessing the quality of external advice that trustees receive, which is highly contingent on the individuals who comprise the industry. Any research should look at whether there are differences in the quality of advice across scheme types and sizes, whether there are reasons for these differences and how any issues may be overcome.
- Consideration should therefore be given to bringing investment consultants within the regulatory perimeter of the FCA, to ensure a commonality of standards within the investment management industry. We also continue to believe the recommendation of the CMA to extend their regulatory perimeter to include the activity of investment consultants, given their important role in the investment chain.
- Another important issue to investigate is the degree to which decision-making on investment choices in the automatic enrolment market is due to the decisions of employers as advised by corporate independent financial advisers (IFAs). As we set out in our report, "Pensions and Growth: Supporting Pension Investment in UK Growth," (June 2023) we believe decisions by employers may be pushing down the amount of money spent on the investment allocation, which has resulted in lower investment in "productive assets."

Chapter 3: Barriers to trustee effectiveness

- Overwhelmingly, the greatest barrier to trustees performing their duties effectively is time and capacity. This is especially true for non-professional, lay trustees. The scale and complexity of the issues that trustees face, coupled with the lack of time to focus on these issues or engage in additional education, compound this challenge.
- Administratively heavy regulatory requirements that are highly focused on process are also an issue for many scheme trustees, especially for smaller schemes that lack time and resources as compared to their larger counterparts. TPR should focus on sharing the guidance it already has, particularly to less-engaged scheme trustees, who it can begin to identify through its register. Assessing current regulatory requirements and streamlining these appropriately may also be beneficial to help free up trustee time, especially if TPR bolsters its TKU toolkit and requires trustees to complete this.
- Trustee fiduciary duty is generally a well-understood concept among trustees, with trustees acting in the best interests of their members. Trustee duty does not, in and of itself, discourage investment in alternative asset classes. If certain asset classes are generally more suitable for pension fund members, then trustees will invest in them. This can be seen in the investment practices of open private sector DB pension schemes and in those of the larger DC Master Trusts.
- Additional resources, for example in the form of guidance, from TPR on alternative – and likely riskier – asset classes could be useful for schemes interested in such allocations. TPR could also create resources such as an industry-agreed-upon framework or checklist for investment decision making or a standard list of questions for trustees to ask investment consultants (as a check/challenge and to address blind spots).
- Trustees generally take careful consideration in balancing investment returns, costs and charges and services when making decisions in the long-term interests of savers. Balancing these considerations is an important element of trustee fiduciary duty to ensure that ultimately, scheme members receive the highest possible benefit. However, as noted above, decisions on investment also need to reflect the specific circumstances of the scheme, for example, whether it is an open or closed DB scheme, and the design of the DC scheme chosen by the employer.

INTRODUCTION / GENERAL COMMENTS

1. The fundamental duty of a trustee is to ensure that pension schemes are run properly and that member benefits are secure. The PLSA welcomes the DWP and HMT's call for evidence to support trustees in fulfilling this responsibility by improving their skills and capability, assessing the advice they receive and removing barriers to their effectiveness.
2. We appreciate the exploratory nature of the call for evidence, and since its release have conducted a survey of our membership and engaged in several roundtable and stakeholder discussions to assess industry feedback of the questions posed.
3. Through this outreach as well as additional research, it has become clear that there are certain areas where additional assessment is necessary from TPR to fully understand the current landscape within the trustee space and to determine the next best steps forward, particularly among likely small, less-resourced, and harder-to-reach schemes.
4. As a first step to address this, we recommend that TPR create a register of trustees. This is critical to understand not only who trustees are, but also to begin the process of understanding where outstanding gaps in knowledge and understanding may exist and to determine necessary outreach and support.
5. We also stress that TPR work to strengthen its Trustee Knowledge and Understanding (TKU) toolkit and require that all registered trustees complete this as the new uniform industry standard. There should be additional, higher requirements for those acting in the capacity of a professional trustee.
6. It is also widely understood that greatest barrier to trustees performing their duties effectively is time. Any changes to current regulations should bear this in mind and aim to lessen time-consuming regulatory requirements.
7. A shift in regulatory emphasis from governance processes to support for individual trustees is also key and would have a positive impact on the fundamental ingredient of good governance – the people charged with delivering it. An assessment of board effectiveness and skills to ensure well-balanced governance bodies would complement this shift.
8. Further, any changes to the regulatory environment that would steer trustees to make certain investment decisions – including towards unlisted equities – could undermine their fundamental and primary duty to secure member benefits for the schemes they oversee. However, where appropriate, trustees may decide these investments are suitable to some moderate degree.
9. It is also incredibly important to research the quality of external support and advice that trustees receive, and consideration should be given to bringing investment consultants within the regulator permitter of the FCA.
10. Finally, we would like to acknowledge that although this response specifically addresses topics related to DB, DC and MT trustees, many similar challenges exist among Pensions Committees for Local Government Pension Schemes (LGPS). We plan to address this in more detail in our response to the recent DLUHC consultation, due on October 2.
11. Our specific responses and recommendations to the questions in the call for evidence are detailed in the following section. We suggest reading the remainder of our response in its entirety, while referring back to certain answers as necessary. Please contact Krista D'Alessandro, krista.dalessandro@plsa.co.uk, with questions or concerns.

RESPONSES TO CALL FOR EVIDENCE QUESTIONS

Chapter 1: Trustee skills & capability (Questions 1-12)

1. **Do trustees know what the knowledge and understanding standards expected of them are?**
2. **Do trustees currently meet the knowledge and understanding requirements expected of them? Are some types of trustees better than others?**

a) Among well-resourced and large (1,000+ members)[1] schemes, it is generally understood that trustees know and meet the knowledge and standards expected of them.

- The profile of respondents from a recent survey – 79% of survey respondents represent large schemes – supports this fact, with 87% agreeing that trustees *know* the expected standards of knowledge and understanding and 78% agreeing that trustees *meet* the knowledge and understanding requirements expected of them.

b) Although trustee knowledge and understanding is considered strong among large schemes, the knowledge and understanding of trustees within smaller, harder-to-reach schemes is less understood and requires additional assessment.

- Recent evidence from TPR's DC (2021) and DB (2022) surveys reinforces this fact, as it indicated that large schemes have a stronger awareness of the governance requirements expected of them – and a greater capacity to meet these standards – than small schemes (12-99 members) and micro schemes (fewer than 12 members).
- It is also generally understood that smaller, less-resourced schemes are more likely to be time constrained, and will face greater capacity challenges, including finding dedicated time to improve their knowledge and understanding.

c) Feedback has also indicated that trustee knowledge and understanding can vary widely on an individual-to-individual basis, across all scheme types and sizes.

- However, based on recent survey results, DB trustees are seen to have the highest level of knowledge and understanding. 37% of survey respondents believe DB trustees have the greatest level of knowledge and understanding, versus 10% who believe that of Master Trust trustees or 2% for DC trustees. This aligns with TPR's recent survey findings regarding the awareness and engagement with TPR's codes of practice among DB versus DC trustees.
- Importantly, many respondents clarified that: a) many trustees work on both DB *and* DC schemes, so the distinction between the groups is often moot; and b) the knowledge and understanding of any given trustee is, again, contingent upon the individual themself.

d) The Government should therefore take steps to assess the current conditions of knowledge and understanding among trustees across all scheme types and sizes and take action to support trustees as appropriate and necessary to their unique needs. Results from a recent survey of our LGPS members indicate the same is true for Pensions Committees. A TPR registry of all trustees could aid in the collection of information of this type, as detailed in the response to questions six and seven below.

[1] For the purposes of this response, a large scheme is one that has 1,000+ members. A small scheme has between 12 and 99 members, and a micro scheme is considered one with fewer than 12 members.

3. What are the barriers to improving trustee capability? What do you think government should do to ensure that all trustees meet the standards expected of them? Does trustee liability put off potential trustees?

e) Overwhelming, survey results and roundtable discussions indicated that the greatest barrier to improving trustee capability is time, with half of all survey respondents commenting that time is the main barrier to improving trustee capability, while other comments focused on ever changing regulations (13%), regulatory complexity (9%) and cost (8%) as additional barriers.

f) Administratively heavy regulatory requirements that are highly focused on process and procedures are also an issue for many scheme trustees, especially for smaller schemes that lack time and resources as compared to their larger counterparts.

- We would therefore not recommend any changes to the current regulatory environment that would add to trustee processes or administration unnecessarily, given that time is the greatest barrier to their knowledge and understanding.
- In fact, TPR should assess current codes and guidance and consider where they might streamline processes and cut down on time-consuming or excessive administrative requirements. This would also free up time for individual trustees to pursue additional education and training.

g) TPR should focus on honing its regulatory approach so that it is prioritizes the individual trustees that comprise scheme governance bodies, as detailed in our previous paper, "Good Governance – How to Get There" (August 2017).

- This includes assessing the current levels of knowledge and understanding among all scheme trustees, strengthening TKU and requiring all trustees to complete this (see our response to questions eight through ten), and providing additional, curated tools and resources to trustees of different scheme types and sizes as necessary.
- It also includes ensuring that qualified individuals are appointed to trustee boards and empowered to act in a way that supports the success of the scheme and its members.
- The role of the scheme Chair is especially important in creating an effective working dynamic, setting the scheme's strategic direction and ensuring that appropriate issues are prioritised. Even with a governance body comprised of strong, experienced trustees, a poor Chair can ultimately lead to poor meetings and decision making. Given this, the appointment of the Chair should be a consideration and priority for regulatory monitoring.
- Like the Chair, well-resourced and efficient executive support is critical to the success of the governance body and should also be a focus for regulatory assessment (and strengthening as necessary).

h) Any new regulatory requirements must be measured and purposeful. There are thousands of schemes of many different types and sizes. While all schemes should have good governance, this means governance needs will vary according to each individual circumstance. TPR must therefore ensure that any new regulations support individual trustees across schemes of all sizes and types to fulfil their role, rather than creating unnecessary, additional processes.

- This greater focus on the individual trustees – or inputs – into scheme governance bodies would involve a dedication of Government resources to oversight and assessment of boards to ensure that standards are met and maintained. Although this would be a significant shift to the current regulatory focus, such a change would make a positive difference to the fundamental ingredient of good governance – the people charged with delivering it.

- Once again, we discuss this in more detail in our paper, "Good Governance – How to Get There" (August 2017). We stress that "the regulation of pension fund governance should focus on these inputs – if governance bodies are populated by the right people, situated within an appropriate and accountable structure, this maximises the likelihood of good decision-making, leading to good outcomes for scheme members."
- Well-balanced skills and collective knowledge among boards, as well as the support of a properly resourced executive team and an experienced and skilled chair, are also of utmost importance.

i) Further, TPR should also examine a broader array of measures that assess trustee boards, including board effectiveness reviews and trustee skills analysis. This would help determine whether trustee boards have a range of technical expertise and skill types including soft skills such as leadership, negotiation, communication, and relationship building. TPR should then tailor its outreach and develop resources to reflect the gaps highlighted through these assessments.

j) We recognize that developing a well-rounded trustee board takes time. Consideration for a professional trustee to support less-resourced schemes – whether temporarily or permanently – should be assessed, as the inclusion of a professional trustee on a board generally improves the operation of the scheme. However, limited resources – particularly of smaller schemes who might especially benefit from the presence of a professional trustee – are a challenge. In addition, our members feel that there is scope to raise the standards required of professional trustees.

k) We also support the TPR's current efforts to build a clearer picture of trustee diversity, most recently through its diversity and inclusion survey, and results from this survey should be considered in the assessment of board effectiveness and balance. Trustee governance bodies will only better serve scheme members if they understand them, and part of this understanding is knowing and representing the experiences and needs of members with diverse characteristics and backgrounds.

l) Further, among some trustees (particularly those that are less engaged and likely under resourced), feedback has indicated a lack of awareness of the current resources and materials available, like the codes of practice. As TPR's current codes of practice are both clear and accessible, the impetus should be to share these resources widely (and where necessary) versus to create additional regulation.

- A targeted engagement strategy that promotes the available resources would therefore be beneficial. A new checklist of high-level regulatory considerations for trustees could also be a useful tool to create and share, which could then signpost trustees to the existing codes of practice.

m) TPR should also undertake a review of its Trustee Knowledge and Understanding (TKU) toolkit with the support of an industry working group, as TKU is currently not considered sufficiently demanding. Improving this educational tool – and requiring its completion as a marker of "accreditation" once it has been updated in line with industry feedback – could help to standardize the foundational knowledge held by all trustees as well as to highlight where trustees from different scheme types may have gaps in understanding. For more details, see our response to questions eight through ten.

n) Feedback indicates that trustee liability does not put off potential trustees. For professional trustees backed by corporate trustee firms, this is especially true.

- However, whether personal liability is an issue among lay trustees of smaller schemes – especially for those that have less engagement with the Government and other trustee stakeholders – remains unclear. This again stresses the importance of the Government's role in outreach to those less-engaged and harder-to-reach trustees. As already mentioned, a TPR register of all trustees could aid in the collection of information of this type (see answers to questions six and seven below).

4. Do trustees (including Master Trust trustees) have the right knowledge and understanding to invest in the full breadth of investment opportunities? If not, what can be done to improve this?

5. Is there enough understanding of advice around the consolidation of schemes?

o) Trustees (including Master Trust trustees) of well-resourced, large schemes (1,000+ members) generally have the right level of knowledge and understanding to invest in the full breadth of investment opportunities. According to our recent survey, 92% of respondents believe this is true, and less than one in ten (6%) feel it is not. Consistent with other feedback, the knowledge and understanding of small schemes (12-99 members) and micro schemes (fewer than 12 members) requires additional assessment.

p) Trustees use the combined knowledge of their governance body and the advice from their advisers to make appropriate investment decisions for scheme members, and we believe that trustee statutory duty to take appropriate investment advice and ensure the correct balance of collective skills and knowledge across the trustee board provides appropriately robust governance. An assessment of these two areas – trustee advice and board effectiveness/skills – would be beneficial.

q) Trustees should have a strong overall understanding of investment issues to fulfil their duties; however, it is not the role of a trustee to be an investment expert across every investment class, as this would be unrealistic alongside their other responsibilities.

- The combined knowledge and understanding of a trustee board allows each to maintain expertise in varying areas, with some – but not necessarily all – specializing in investment.
- This stresses the importance of building strong, well-balanced trustee boards with a diverse range of technical and soft skills. Some, typically larger, trustee boards will also be supported by investment committees. The role of the Chair in facilitating an appropriate balance within the trustee governance body is critical.

r) The role of a trustee adviser is also especially important in relation to investment opportunities, as the adviser is expected to inform the trustee of any new investment opportunities. It is the job of the trustee to then exercise their judgement using the information and advice they receive – bearing in mind the specific needs of the scheme members they represent – when determining the appropriateness of a certain investment type.

s) Further, as many schemes continue to consolidate, the advice around consolidation must be equally understood. However, consolidation should only happen where it is in the best interests of the members, and as trustees are responsible for overseeing member outcomes, they are best positioned to consider possible scheme consolidation.

6. Do you think that the government should require all trustees to provide information to enable TPR to keep a register of all trustees?

7. If the government were to require this information, would it be best achieved through the scheme return or through a separate trustee return?

t) We believe it would be beneficial for TPR to keep a register of all trustees, with the majority of survey respondents (58%) in agreement.

- In line with industry feedback, we recommend collecting this information through the scheme return. In the case of professional trustee firms, registering relevant parties at a group level may be more efficient, rather than having these individuals named across multiple scheme returns.
- Collecting this information could serve useful in several ways. As a first step, it would help to determine who currently serves as a trustee (either lay or professional), which may help to determine outreach to currently less-engaged schemes. It may also prove useful in determining the training completed by all trustees (see response to question three as well as questions eight through ten on TKU) or other forms of accreditation. Further, collecting this information could allow future assessment of trustee knowledge and understanding and board effectiveness/skills reviews for schemes of all types and sizes.

8. Do current accreditation frameworks provide a high enough bar to equip trustees who become accredited to properly fulfil their role, including in making investment decisions?

9. What proportion of your trustee board are accredited trustees?

10. If we required each scheme to have a certain proportion of accredited trustees, where should this bar be set? Should Master Trusts be required to have a greater proportion of accredited trustees than single-employer schemes?

u) TPR should strengthen its current TKU toolkit with the support of a diverse representation of trustees from all scheme types and sizes, as well as other appropriate stakeholders from across the pension's industry. The completion of this updated toolkit should be required by all registered trustees as a form of "accreditation." Similar feedback from a recent survey of our LGPS members suggests that strengthening current training courses for Pensions Committees would also be beneficial.

v) Ultimately, we believe that implementing this new form of "accreditation" will work to the benefit of scheme members across all scheme types and sizes, not just those who happen to already be in a large, well-resourced schemes. However, it is important to note that survey respondents and industry feedback largely stressed concern over accreditation mandates, particularly in that it could add to existing constraints on trustee time and capacity (without first assessing the training needs of trustees and tailoring this appropriately). This is why we suggest tasking an industry working group to strategically consider the TKU toolkit update and how to measure its successful completion (additional details below).

w) As the PLSA has previously noted, and in line with feedback from across the industry, TKU is not considered sufficiently robust to serve as a foundation for trustee knowledge and understanding. The completion of the toolkit as it stands also does not provide the requisite level of knowledge and understanding for a scheme trustee to ensure good scheme governance. This is particularly the case given the complex legal, policy and financial considerations trustees must navigate.

x) An appropriate and well-rounded industry working group should assess the current toolkit and develop an updated version. There are several important considerations to bear in mind through this process.

- First, as previously stressed, trustees have limited time and capacity, and the industry working group should highly consider this when developing the new toolkit. The updated toolkit should only be as long as necessary, and there should be sufficient time allotted for trustees to complete this.
- In addition, feedback from recent roundtables has stressed that "test-taking" as a form of assessment could unnecessarily rule out individuals who would otherwise be highly capable and qualified trustees. This is critical from a diversity perspective, to ensure that trustees with varying soft skills, expertise, backgrounds and characteristics are able to qualify and create well-balanced governance bodies, which we've already stressed are highly important. The industry working group should consider test-taking and other potentially unnecessary barriers, while still implementing strong yet appropriate success measures.
- We also recognize that there are numerous, highly experienced trustees that already have the necessary knowledge and understanding to perform their duties well. However, in order to raise the standards for trustees across the entire industry – and to implement uniformity in foundational trustee knowledge – we consider the completion of the new TKU necessary.
- TPR should also consider using the updated toolkit to identify areas where trustees of different scheme types lack the appropriate knowledge and understanding (perhaps by assessing the "success rate" of the completion of different sections within the toolkit), eventually using this information to create curated resources and additional training opportunities. For example, for trustees of DC schemes, information and support on decumulation options could serve beneficial, especially if determining a default decumulation solution for its members. Again, the assessment of existing trustees is critical to develop the appropriate tools for them, and a one-size-fits-all approach will not address the unique challenges and growth areas for each individual trustee.
- For existing trustees, some level of annual continuing professional development – that bears in mind the limited time of trustees as it is – may help ensure that trustees have the most appropriate, relevant and up-to-date knowledge and information. This continuing education should be tailored to trustees of schemes of different types and sizes with varied skills gaps and needs, following appropriate assessments.

11. Should there be more rigorous requirements for those acting in the capacity of a professional trustee? What sort of requirements/standards should professional trustees be meeting? Should there be mandatory accreditation?

12. How would you define a professional trustee for the purposes of legislating for all professional trustees to be accredited?

y) We believe there should be more rigorous requirements for those acting in the capacity of a professional trustee. In fact, most respondents (84%) in our recent survey feel that professional trustees should have mandatory accreditation.

z) Professional trustees should not only be required to complete the updated TKU toolkit (consistent with our recommendations in questions eight through for an "accreditation" requirement of all trustees) but should also be required to meet additional (yet to be determined) accreditation marks.

aa) Further assessment of these additional requirements – perhaps by the TKU industry working group – is necessary but could possibly include a higher standard to successfully complete the updated TKU toolkit or another appropriate qualification.

bb) Previously[2] our members have been supportive of all trustees completing CPD, regardless of whether they are a professional or not, albeit acknowledging that any training should not be considered 'once and done,' that all training is not all created equal and that a box-ticking approach should be avoided.

cc) Regardless, the accreditation of professional trustees should be sufficiently robust and stretching. However, any standard should not be so stretching as to overly restrict the pool of potential trustees.

dd) Further, any future accreditation requirement should apply to professional trustees employed through a professional trustee firm as well as to professional trustees who are hired independently (independent trustees).

Chapter 2: The role of advice (Questions 13-17)

13. What are your observations on the external support trustees are given to make investment decisions, particularly in relation to unlisted equities?

14. What changes could be made, including to the regulatory environment, to improve trustee support in relation to unlisted equities.

15. To trustees: To what extent do trustees use investment consultants to support decisions around allocations to unlisted equities? Did they subsequently increase? Is there a deficiency of knowledge or expertise by investment consultants of these types of investments?

ee) General feedback indicates that trustees receive appropriate external support to make investment decisions, with around three-quarters of survey respondents (72%) agreeing that trustees have and use appropriate external support to make investment decisions, particularly in relation to unlisted equities. According to a recent survey of our LGPS members, the same was true among Pensions Committees, with around three-quarters of respondents agreeing that Pensions Committees have and use investment consultants to an appropriate degree in relation to unlisted equities.

- Although many were neutral (52%), survey respondents were more likely to disagree (36%) than agree (11%) that there is a deficiency in knowledge or expertise among investment consultants. However, additional feedback also indicated that the quality of external support trustees receive may vary on a case-by-case basis.

ff) Is it also well understood that holding advisers and investment managers to account is embedded into trustee duty, to ensure scheme members are protected against imprudent advice that could lead to poor investment decision-making. Trustees take this seriously and use their

[2] See, for example, our responses to questions three and four of the PLSA response: TPR Future of Trusteeship and Governance.

judgment – as well as other factors – to determine whether to accept or reject the investment advice they receive in the interest of their members.

- Trustees also work to find and use appropriate advice, as is currently detailed in TPR's regulation and codes of practice. Industry feedback also stressed that trustees work with their advisers over the course of some time and form strong, working relationships to build mutual understanding about the investment needs of scheme members. Advice is therefore rarely a 'one-off' event, and specific investment opportunities will generally be discussed and iterated many times.
- However, one issue to be investigated is the degree to which decision-making on investment choices in the automatic enrolment market are due to the decisions of employers as advised by corporate IFAs. As we set out in our report, "Pensions and Growth: Supporting Pension Fund Investment in UK Growth," we believe decision by employers may be pushing down the amount of money spent on the investment allocation, which has resulted in lower investment in "productive assets."

gg) Changes to the regulatory environment that would steer trustees to make certain investment decisions – including towards unlisted equities – could undermine their fundamental and primary duty to act in the best interests of the scheme members they oversee, and we believe this would be inappropriate.

- Regarding unlisted equities specifically, trustees often decide against these investments based on risk returns and other factors, such as the balance between the composition of scheme membership (i.e., the average time until retirement) and the liquidity of funds. There are also varying drivers for the investment decisions of trustees in DB versus DC schemes.
  - In the case of private sector DB schemes, most are closed to new accrual, which means that they have short investment timelines and investing in highly risky and long-term illiquid assets is not generally suitable. Instead, the Government should focus on: 1) amending TPR's DB Funding Code to allow more investment in this area for open private sector schemes who have more capacity to invest in illiquid assets and; 2) providing support to open funded, public sector LGPS, which remain open to new accrual and are less mature than the majority of private sector DB schemes, which would allow investment in more growth-oriented assets.
    - In addition, certain types of schemes such as fully funded, closed DB schemes may not need the possible heightened risk and returns that investment in alternative asset classes could afford to deliver member benefits.
    - We would also like to highlight that the dominant regulatory trend over the last ten years (or more) has been to encourage DB schemes to de-risk and following the gilts crisis, to maintain a higher level of liquidity. Any regulatory changes to increase investment in riskier assets would be inconsistent with previous regulator guidance.
  - In the case of DC schemes, the operation of the automatic enrolment market adds a downward pressure on the budget for investment. This limits investment capacity in more expensive asset classes, making it very difficult to invest in illiquid assets. The Government should look more closely at the decisions made by employers when choosing automatic enrolment schemes and the advice they receive from corporate IFAs, to ensure the recommendations are based on value for money and saver outcomes rather than costs alone. This same consideration should be given to the advice trustees are given by employee benefit consultants (EBCs).

- It is therefore generally not a lack of knowledge among trustees or their advisers of these investment opportunities, but rather a calculation of the appropriateness of the investment type itself, especially when considering trustee fiduciary duty to act in the best interests of scheme members. Though there may be a place for a small portion of these unlisted equities in a balanced portfolio of investments, this is likely to be limited given the heightened risk. The task of selecting any appropriate unlisted equities should be delegated by trustees to specialist advisers and consultants and should be subject to close monitoring.

hh) There are also certain market barriers – unrelated to the quality of advice that trustees receive – that result in trustees deciding against investment in certain asset classes like unlisted equities. To overcome these barriers, and to help spur investment in illiquid assets for both open DB and DC schemes, the Government should work to ensure: 1) a reliable pipeline of suitable investment opportunities; 2) appropriate investment vehicles run by the British Business Bank or the private sector; 3) a stable and long-term economic strategy; and 4) suitable regulatory and fiscal measures.

- The private equity funds themselves would need to take an interest in certain entities investing in them in return, and this may or may not include every pension scheme. Beyond this market barrier, certain specialized expertise may also be necessary to enable schemes to invest in private equity funds.
- Investment in high growth companies (akin to venture capital) within the UK would require a strong pipeline of investment opportunities for trustees to consider, and we are supportive of the continued development of this pipeline.
  - The nature of these types of investments requires that any given portfolio include a high number of opportunities, again highlighting the need for a strong pipeline. This is both because investment tickets for venture capital tend to be small and because a portfolio that includes several companies assumes that most will not generate substantial (if any) returns, in the hopes that at least one will take off and produce considerable returns to make up for this (which assumes a high level of risk in and of itself).
  - Managing investment portfolios with such complexity would also create far more intensive governance considerations for trustees – such as fund management and monitoring – when trustees are already widely time constrained.
- The level of risk associated with these types of investments is also a concern for many trustees, especially when considering the dispersion of returns.
  - For example, DC schemes would need to determine an appropriate model for default return rates while simultaneously ensuring fairness for all scheme members. This is particularly challenging given that the timing of producing a high return – generated from the success of any given company – is almost impossible to discern. It raises the question: How do you ensure that these boons in returns are fairly dispersed among members exiting the scheme now versus later?

16. What changes could be made to investment management to support pension scheme investment decision-making?

17. To trustees: How does legal advice impact your investment decisions? What is a n acceptable level of tolerance for investment risk? Is there a culture of ‘risk aversion’?

ii) Consideration should be given to bringing investment consultants within the regulatory perimeter of the FCA, as recommended by the CMA, to ensure a commonality of standards within industry. The FCA is already responsible for regulating the financial services industry, which includes protecting consumers and promoting fair competition. The monitoring and assessment of investment consultants by the FCA would therefore be a natural fit to ensure that trustees and pension schemes receive fair and impartial advice that protects member benefits.

jj) The Government should focus on undertaking research into the quality of external support and advice that trustees receive. As in the case of trustees, there should also be a focus on the individuals (or inputs) who comprise the industry (see question three for more details).

- There is currently a lack of publicly available and easily accessible data regarding what type of advice trustees receive (or even where they are getting this from). This makes it difficult to determine what (if any) changes could be made to the investment consultant industry to support pension scheme investment-decision making. Therefore, it would be beneficial for the Government to undertake this assessment work as a first step.
- This research should focus on the external support trustees receive for relevant issue areas, including (but not limited to) investment, actuarial, regulatory, administrative, governance and communications.
- Eventually, a register that demonstrates the specific skills and knowledge of investment consultants would also be beneficial, so that scheme trustees are able to better discern the quality of the investment advice they receive. Ensuring that the standards for the individuals within the industry are measurable and strong is also of utmost importance.

kk) Different scheme types and sizes have varying needs. There is an assumption that smaller schemes cannot afford the same level of investment advice as their larger counterparts. However, smaller schemes with fewer members (and often less complicated investment strategies) may not *need* the same type of investment advice. Again, research into the quality of advice that schemes of all sizes receive – to determine things like whether small schemes are not receiving quality advice – would be a useful first step.

ll) Legal advice does not negatively impact trustee investment decision making or create additional risk aversion. As with investment management advice and any other external support that trustees receive, trustees weigh legal advice using their judgement and proceed in the best interests of scheme members. Trustees use legal advice as an additional source of information, weighing any risks they are made aware of with discernment and taking into consideration the numerous factors that guide their decision making.

Chapter 3: Barriers to trustee effectiveness (Questions 18-25)

18. Is fiduciary duty a well-understood concept? Do current regulations and guidance support trustees to make investment decisions which seek higher returns for members? If not, what changes would be useful?

19. Do trustees currently make investment decisions in the long-term interests of pension savers? If not, what barriers are there to trustees making investment decisions in the long-term interests of savers.

mm) Trustee fiduciary duty is generally a well-understood concept among trustees. Comments from the PLSA's recent survey suggest that most trustees act in the best interest of members, with many responding that if alternative asset classes are the right investment path, then trustees will invest in them (see answer to questions 13 through 15 for more detail).

- There are also considerations that trustees must make depending on the specific scheme they are charged with overseeing. Schemes with members who have a younger age profile may consider investment in alternative asset classes more readily than those whose age profile is older, given liability matching is a less significant driver and the ability to balance the longer time it may take to see returns.
- DB versus DC schemes also have varied considerations, and closed DB schemes in particular need to prudently balance return, risk and liquidity to ensure member benefits can be paid. Issues related to liquidity are also a substantial consideration for DC funds given daily dealing requirements.

20. How do trustees balance investment returns, costs and charges, and services when making decisions in the long-term interests of savers?

nn) Trustees generally take careful consideration to balance investment returns, costs and charges, and services when making decisions in the long-term interests of savers.

oo) To balance these considerations is an important element of trustee fiduciary duty to ensure that ultimately, scheme members receive the highest possible value for money.

pp) Trustees also consider the additional costs, governance and administration that accompany investment in alternative asset classes, bearing ultimate member benefit in mind.

21. Do trustees' fiduciary duties discourage investment in alternative asset classes? If so, please explain with examples.

22. Is the way in which trustees exercise their fiduciary duties preventing trustees from seeking the best returns for pension savers? If so, what is causing this?

23. Do those actors who have the most influence on advice to trustees on long-term investment decisions experience any challenges or barriers in provision of their advice on illiquid assets? If so, what would unblock this?

qq) Feedback indicates that generally, trustee duty does not discourage investment in alternative asset classes, with almost half of all survey respondents agreeing to this statement. This was also widely agreed upon in a recent survey of our LGPS members, regarding Pensions Committees fiduciary duties.

- The very nature of fiduciary duty is to act in the best interest of scheme members, and trustees will invest in an asset class if it is suitable and appropriate to its members. In other terms, trustee fiduciary duty does not preclude investment in any particular asset class.

rr) Overall, feedback has not indicated that those actors with the most influence on advice to trustees, particularly relating to long-term investment decisions, experience challenges or barriers in the provision of their advice on illiquid assets.

24. Would trustees find it helpful if they received more direction from regulators when assessing their investment decision making? In addition to our work on Value for Money we are also interested in whether the advice for trustees provided by regulators via training and guidance supports our objective to shift the focus from cost to value?

ss) Additional resources from TPR on alternative (and likely riskier) asset classes could be useful for schemes that may like to pursue some investment in this direction.

tt) We also support the exploration of opportunities to communicate with stakeholders in the private equity and venture capital space to develop these resources and other educational tools.

uu) In addition, feedback has indicated that tools such as an industry-agreed-upon decision tree, a framework for decision making, or a checklist to consider before making investment decisions could be helpful to scheme trustees. We note variations of these exist within the sector.

vv) A standard list of questions for trustees to pose to investment consultants (as a check/challenge strategy as well as to address blind spots) could also be beneficial.

25. Do lay trustees have enough time and support to perform their duties effectively? Do professional trustees? If not, what changes would support this?

ww) As stressed throughout this response, the greatest barrier to trustees performing their duties effectively is time and capacity. Regulatory complexity – and its focus on extensive governance process – adds to this. Answers to questions one through three detail additional information on this as well as specific changes that could be made to support trustees.

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