Department for Work & Pensions	**Impact Assessment (Final)**	
Title of measure		The Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019
Lead Department/Agency		Department for Work and Pensions (DWP). Department for Business, Energy and Industrial Strategy (BEIS) lead on the parent Directive. Her Majesty's Treasury (HMT) also has an interest.
Planned coming into force /implementation date		June 2019 in force/October 2020 implementation
Origin (Domestic/EU/Regulator)		EU Directive 202017/828
Policy lead		Karen Maskill
Lead analyst		Tom Mouland
Departmental Assessment		Self-certified
Total Net Present Social Value (over 10 year period): (2016 Prices, 2017 present value) -£15.3m	**Equivalent Annual Net Direct Cost to Business (EANDCB) (over 10 year period): £1.8m**	**Business Impact Status:** Non-Qualifying Regulatory Provision

Summary – Intervention and impacts

Policy Background – Issue – Rationale for Intervention – Intended Effects

The financial crisis showed that there were many shortcomings in corporate governance and the stewardship of listed companies contributed to this. Stewardship is the responsible allocation and oversight of investments by pension schemes, asset managers and insurers, to create sustainable value for beneficiaries, and promote the long-term success of companies, the economy and society. Part of this involves improving transparency which will help to reduce the information asymmetries between schemes and their members.

The European Union revised Directive 2007/36/EC[1] ("the Shareholders' Rights Directive) and published EU Directive 2017/828[2] (commonly known as 'SRD II'). This Directive encourages investors to adopt a long-term focus in their investment strategies and be transparent about how they invest to allow for comparison between schemes so that engaged members better understand their investments.

The UK played a significant role in the negotiation of the Directive and shares its key objectives, particularly improving business standards on corporate governance and stewardship

The Department for Work and Pensions (DWP) plans to transpose two Articles of the Directive relating to scheme's policies on engagement with investee firms (investee firms are collectively, the company in which the scheme invests and its subsidiaries), asset managers and others and the transparency of trustees regarding their investment strategies. The extent of the changes in SRD II means that the legislation transposed from the original Shareholders' Rights Directive needs minor amendment. The changes align with UK domestic policy priorities, and some of the requirements are already legal obligations for some types of UK pension schemes. This Directive is part of the EU's framework for financial regulation, and it is sensible to transpose it with a minimal impact approach. The deadline for transposition of SRD II is 10 June 2019. If the Withdrawal Agreement is ratified, the UK will be obliged to transpose EU law during the implementation period, and if Article 50 period is extended up to or beyond the transposition deadline of 10 June 2019, the UK will be obliged to transpose as a Member State.
In the event of a 'no deal' scenario we will not be required to transpose the Directive but will look to make the changes in the longer term as they make it attractive for investors to operate here and be confident in the UK's Governance systems.

Transposing these Articles will strengthen the responsibilities associated with holding investments in members' best interests and outlining and detailing schemes' arrangements with their asset managers.

[1] Directive 2007/36/EC
[2] Directive 2017/828

Publishing the information on-line will build greater transparency and accountability allowing members to compare schemes and better understand their investments empowering members to hold their pension schemes to account.

We will be able to demonstrate transposition of the requirements of SRD II for schemes' policies on engagement with investee firms and transparency of investment strategies, with minimal impact to industry.

Brief description of viable policy options considered (including alternatives to regulation)

1) Do nothing

Following the EU referendum in June 2016 we considered the 'do nothing' option in terms of whether the transposition of EU Directives was still appropriate as the UK began planning to leave the EU. However, the Government's position is clear that should the UK secure a Withdrawal Agreement before exit day we will enter into an implementation period from 29 March 2019 until 31 December 2020. During this implementation period there will be common rules across the UK and the EU, during which time the UK will still be obliged to transpose applicable EU law into UK law.

It is important that schemes have robust stewardship and governance systems in place to ensure the UK continues to be attractive for investors and they can be confident in the UK's governance systems. Not transposing the Directive would go against the UK's agenda of maintaining the competitiveness of British business and ensuring a robust stewardship regime, therefore the UK would be considering the requirements of the Directive in the future without our current obligation to transpose.

2) Non – Legislative transposition

We considered whether we could transpose the engagement strategy and transparency requirements of the Directive purely by non-legislative means. Much of what is required by SRD II is already transposed in existing UK legislation and The Pensions Regulator's (TPR) Codes of Practice.

However, we came to the view some aspects of the engagement strategy and transparency elements are sufficiently divergent from what is currently set out in UK law to require us to amend legislation in order to fulfil our obligation to transpose.

3) A mixture of legislative and non-legislative transposition (preferred option)

For the engagement strategy and transparency elements of SRD II, the overarching requirements will be put in place by legislation to which this impact assessment relates. Practical details will be explained by non-legislative means in TPR Codes of Practice.

Preferred option: Summary of assessment of impact on business and other main affected groups

The UK's position is that as occupational pension schemes are highly significant asset holders who are responsible for peoples' retirement savings, it is necessary to make some minor changes to pensions legislation in order to align with the Directive.

The Pension Protection Fund (Pensionable Service) and Occupational Pension Schemes (Investment and Disclosure) (Amendment and Modification) Regulations 2018[3] (the 2018 Regulations) amended legislation for some UK schemes set out in a phased implementation approach;

- firstly, a requirement for both defined contribution (DC) and defined benefit (DB) schemes to develop an engagement strategy within their Statement of Investment Principles (SIP) and for DC schemes to publish this from 1 October 2019; and

[3] http://www.legislation.gov.uk/uksi/2018/988/contents/made

- for DC schemes to publish annually how their engagement strategy has been implemented (through an implementation statement) from 1 October 2020.

In order to implement SRD II there needs to be:
(i) minor amendments to the content of the engagement strategy in their SIP;
(ii) minor amendments to the content of annual reports
(iii) a requirement for DB schemes to publish how their engagement plan and annual report have been implemented in alignment with DC schemes.

As both DC and DB schemes will already have an engagement strategy, these are minor changes. Therefore, we do not expect compliance with the changes to regulations to be particularly onerous.

We do not propose bringing these dates forward to minimise disruption although the base line legislation will be in place by 10 June transposition deadline.

We have been working with other Government Departments and stakeholders to develop our approach to implementation. We will lay regulations to amend the Investment and Disclosure Regulations to ensure that schemes have a clear understanding of what is required.

The UK is largely compliant with SRD II and will therefore be able to transpose without imposing much additional burden on industry. Nevertheless, there will be costs associated with these changes for trustees to familiarise themselves with the changes, review and update documentation and publication of relevant information – full details below in the costs and benefits section. The cost estimates are:

- £10.1m in year 1;
- £0.9m every subsequent year

The estimated annual net direct cost to business (EANDCB) over a policy period of 10 years is £1.8m.

Departmental Policy signoff (SCS): Hilda Massey	Date: 24 April 2019
Economist signoff (senior analyst): Claire Frew	Date: 11 April 2019
Better Regulation Unit signoff: Prabha Mistry	Date: 9 April 2019

Additional detail – policy, analysis, and impacts

The policy issue and rationale for Government intervention

1. The financial crisis showed that there were many shortcomings in corporate governance and the stewardship of listed companies contributed to this. Stewardship is the responsible allocation and oversight of investments by pension schemes, asset managers and insurers, to create sustainable value for beneficiaries, and promote the long-term success of companies, the economy and society.

2. UK trustees of occupational pension schemes have an important role to play in the oversight of the firms in which they invest and to whom they lend. It is important that trustees fulfil the responsibilities associated with holding the investments in members' best interests – whether directly or by others on their behalf - through the full range of stewardship activities.

3. It is important that schemes have robust stewardship and governance systems in place to ensure the UK continues to be attractive for investors and they can be confident in the UK's governance systems.

4. And at a member level, there is an information asymmetry between trustees who set the investment strategy of pension schemes and members who are saving for retirement in these schemes. Government intervention to improve the transparency of investment decisions can help to reduce this information asymmetry.

5. The EU's position on stewardship for pension scheme trustees, as set out in SRD II, closely reflects the UK's position once the 2018 Regulations come into force.

6. SRD II encourages investors to adopt a long-term focus in their investment strategies, not only considering social and environmental issues, but also being transparent about how they invest and approach their engagement as shareholders. The changes we plan to introduce in order to implement Articles 3g and 3h include:

    1. DC and DB schemes to be transparent about their arrangements with their asset managers and include this in their Statement of Investment Principle (SIP);

    2. DC and DB schemes to include in their SIP their policy regarding the realisation of investments including how targeted portfolio turnover or turnover range is to be defined and monitored;

    3. DC and DB schemes to describe in their SIP how they monitor investee companies' capital structure;

    4. DC and DB schemes to describe in their SIP how they monitor actual and potential conflict of interest in relation to their engagement;

    5. DB schemes to publish their SIP to align with DC schemes;

    6. On an annual basis DC and DB schemes to publish their engagement policies and how they have cast their votes in the general meetings of companies in which they hold shares in their annual reports. This information is required to be available free of charge on their or their asset manager's website or by any other means that are easily available on line.

7. If the Withdrawal Agreement with the EU is ratified, the UK will be obliged to transpose EU law during the implementation period, and if Article 50 period is extended up to or beyond the transposition deadline of 10 June 2019, the UK will be obliged to transpose as a Member State.

8. This Directive is part of the EU's framework for financial regulation and as its requirements are aligned with the UK's own priorities it is sensible to transpose it with a minimal impact approach.

Policy objectives and intended effects

9. These changes are intended to make the UK more attractive for investors to operate here and be confident in the UK's governance and stewardship systems. Pension schemes are significant investors and members must be confident that schemes are exercising oversight and making their investments strategy transparent.

10. The changes being made as part of SRD II transposition will codify what some schemes in the UK will already be doing when the 2018 regulations come into force and ensure that all schemes will be totally transparent about their investment strategies.

Policy options considered, including alternatives to regulation

Option 1: Do nothing

11. Not transposing the Directive would go against the UK's agenda of maintaining the competitiveness of British business and ensuring a robust stewardship regime. Also pension schemes would not be playing a visible part in the UK's post EU exit stewardship of investments agenda.

12. The Government position is if the Withdrawal Agreement is ratified, the UK will be obliged to transpose EU law during the implementation period, and if Article 50 period is extended up to or beyond the transposition deadline of 10 June 2019, the UK will be obliged to transpose as a Member State.

13. 'Do nothing' is not in line with the Government's position on continuing to meet our treaty obligations to transpose EU Directives during an implementation period in the event of a Withdrawal Agreement. This could also lead to an 'infringement procedure' or referral to the Court of Justice.

14. The UK pensions industry is aware of and expecting SRD II and it would create confusion if we do choose to ignore it at this late stage.

Option 2: Non- Legislative transposition

15. TPR's Codes of Practice explain in practical detail what the regulator expects from trustees in complying with the law. In scenarios where the UK's existing law is sufficiently close to an EU Directive, or is sufficiently broad, the UK can transpose those elements of the Directive by changing the relevant Code of Practice so it aligns with the Directive.

16. We considered whether we could transpose the occupational pension requirements of SRD II purely by such non-legislative means in order to minimise the amount of legislation changes. However, some of the changes to the SIP and Implementation Statement do not exist in UK law and requires us to make small amendments to legislation in order to fulfil our obligation to transpose.

Option 3 (preferred option): A mixture of legislative and non-legislative transposition

17. The existing legal requirement for developing an engagement strategy in the SIP and disclosing the implementation statement does not cover all schemes and does not allow the entirety of the of the requirements set out in the Directive to be expressed only in an updated TPR Code of Practice. Doing so would make TPR's Code of Practice unenforceable and may put the UK in the position of sub-delegating to TPR without the power to do so.

18. Our chosen option is therefore to take a proportionate approach which includes both legislative and non-legislative elements, keeping the legislative component to a minimum as far as is possible.

19. We have worked with the lead sponsoring Government Department for this Directive (Department for Business, Energy and Industrial Strategy) and Her Majesty's Treasury to agree the least onerous approach and have discussed with industry stakeholders how to implement these Articles which will minimise any impact on business, whilst still achieving policy objectives.

20. In the event of a 'no deal' scenario we will not be required to transpose the Directive but will look to make the changes in the longer term as they make it attractive for investors to operate here and be confident in the UK's Governance systems.

Baseline scenario

21. Both DB and DC schemes are already required to have a SIP in place. Existing regulations require SIPs to be reviewed and where necessary updated at least every three years. This is referred to as a triennial cycle.

22. The 2018 Regulations require SIPs to be published only for DC schemes.

23. DC schemes are already required to produce and publish an annual report each year. DB schemes are required to produce an annual report, but this does not have to be published.

Therefore, only the requirements to include additional information (we have assumed schemes will use their SIP rather than a separate document to make this information transparent) and annual reports, and the requirement for DB schemes to publish this information on-line represent additional impacts, and are estimated below.

Expected level of business impact

24. Changes in the 2018 Regulations demonstrated that the costs of complying with the SRD II will be minimal. We have worked with a group of key industry stakeholders to develop options for how different types of schemes could achieve an effective system of governance at a proportionate level of cost, and this work will continue during the development of TPR's Code of Practice. The impacts are set out below.

Monetised and non-monetised costs and benefits

Summary

25. The total estimated cost in year 1 is £10.1m and every year after that £0.9m. The estimated annual net direct cost to business (EANDCB) in 2016 prices and discounted to 2017 is £1.8m.

Costs and benefits to business

<u>Scope of measures</u>

26. SRD II applies to IORPs as falling within the scope of Directive (EU) 2016/2341[4] (IORP II) in accordance with Article 2 and Article 5 of that Directive, therefore SRD II does not apply to Public Service schemes and schemes that in total have less than 100 members. Therefore, Public Service schemes or schemes with less than 100 members are excluded from the volumes. This measure only applies to occupational schemes.

Table 1: Volumes of schemes to be used in the estimates.

Number of scheme members	Defined benefit (DB) & hybrid[5]	Defined contribution (DC)[6]	**Total**
2-99 (DB)/12-99 (DC)	1,985	1,130	**3,115**
100+	3,539	1,050	**4,589**

Costs to pension schemes

27. Familiarisation costs – There will be costs to all trustees to familiarise themselves with the new regulations and Statutory Guidance. We assume a speed of one minute to read 300 words so assume a trustee will take around 10 minutes to read and digest the 4-5 pages of information at an hourly rate of £28.50[7] for each trustee.

28. We estimate from TPR research that there are an average 3.4 trustees per scheme with more than 100 members[8].

29. Across all 4,589 schemes in scope with 100 or more members this gives a one off familiarisation cost of £60,000[9].

30. Ongoing costs to review and update SIP (engagement strategy) – all schemes with 100 members or more members will need to update their SIP to include the new requirements for monitoring investee companies' capital structure, managing conflicts of interest and details of their arrangements with their asset managers.

31. It is reasonable to expect that schemes should have this information to hand, as it relates to their existing procedures and arrangements and would involve updating their existing SIP which they are already required to produce. This assumption was tested at a stakeholder roundtable in March 2018 where participants confirmed this information was easily accessible and at hand.

32. It is expected that the cost of updating the SIP to reflect these procedures would be largely one off in order to collate this information in the SIP for the first time. As policies

[4] EUR-Lex - 32016L2341 - EN - EUR-Lex
[5] PPF Purple Book 2018. Figure 2.1, estimated 2018 universe. Data relates to 31/03/2018
[6] TPR scheme return data 2018. File 1, Table 1.3. Data relates to 31/12/2017.
[7] The median hourly wage for a corporate manager or director is £22.44 in the Annual Survey of Hours and Earnings 2017 revised, Table 2.5. This is uplifted by 27% for overheads from the previous version of the Green Book.
[8] TPR 2015 research shows that there are an average of 3.6 trustees for schemes with 100 – 999 members and 3.0 trustees with 1,000+ schemes. We have created a weighted average using the volume of schemes in these brackets to get 3.4 average for schemes with 100+ members
http://webarchive.nationalarchives.gov.uk/20170712122409/http://www.thepensionsregulator.gov.uk/docs/trustee-landscape-quantitative-research-2015.pdf

[9] £28.50 per hour * 3.4 trustees * (10/60 minutes) * 4,589 schemes

or requirements are updated, these can be included in the SIP as part of the usual triennial update cycle.

33. We previously received estimates from stakeholders that the cost to update a SIP is usually in the range of £2,000 to £5,000[10] and the average of these estimates was £3,166. These updates would involve reviewing all the information within the SIP, of which the additional requirements would form a relatively small additional part.

34. We assume that an update like this would only need to add the additional documentation required by the three new factors in the SIP, and will not require a complete update of the whole document. Therefore, we take the lower estimate of the cost to update a SIP (£2,000) - as a conservative estimate of the cost of updating the new factors. This is equivalent to 79 hours, or two weeks work, of a professional (£2,000/£25.40[11] per hour) in order to include the additional information on monitoring investee companies' capital structure, managing conflicts of interest and details of their arrangements with their asset managers.

    Assuming all schemes face this cost when they come to update their SIP, this would give an overall cost of £9,200,000 (4,589 schemes * £2.000) to add this information to a SIP.

35. <u>Ongoing costs to Publish SIP (engagement strategy) on-line</u> – DC schemes are required to publish their SIP and Implementation Statement on-line from October 2020 therefore this is a new requirement for DB schemes only.

36. Many DB schemes will already have a website so they will already have a suitable web hosting arrangement and process for uploading information. For those that do not, the requirement is only for them to publish on a suitable website, such as the sponsoring employer's website, or that of their asset manager. Therefore, we assume that this will take 20 minutes[12] at an administrator's wage of £19.48[13] an hour to upload the report to a website.

37. The SIP has to be published from October 2020 so we assume they all publish in the first year of the policy when they have revised the SIP in order to be compliant on 1 October 2020.

38. Schemes will need to re-publish whenever they revise the SIP. Schemes already have to review the SIP at least every three years and revise it where appropriate. We assume that all schemes will have to re-publish every three years though in reality some might publish more often. The estimated costs incurred are small and so we consider sensitivity analysis to be disproportionate.

39. This gives an overall cost for DB schemes to publish a SIP of £23,000 in the first year of the policy (3,539 schemes * £19.48 * (20/60 minutes) and then £23,000 every third year after that as schemes publish over the triennial cycle.

---

[10] 'Impact Assessment for The Occupational Pensions Schemes (Investment and Disclosure) (Amendment) Regulations 2018 published at http://www.legislation.gov.uk/uksi/2018/988/pdfs/uksiod_20180988_en.pdf

[11] The median hourly wage for a professional is £20.00 in the Annual Survey of Hours and Earnings 2017 revised, Table 2.5. This is uplifted by 27% for overheads from the previous version of the Green Book.

[12] This is consistent with the assumption in the disclosure of costs and charges impact assessment, http://www.legislation.gov.uk/uksi/2018/233/pdfs/uksiod_20180233_en.pdf. This is also consistent with stakeholder feedback gathered about the process which stated from no cost to 2 hours of work.

[13] The median hourly wage for an administrator is £15.34 in the Annual Survey of Hours and Earnings 2017 revised, Table 2.5. This is uplifted by 27% for overheads from the previous version of the Green Book.

40. Ongoing costs to provide additional information in the annual report – all schemes with 100 members or more members will need to update their annual report to include the new requirements for:
    1. how their engagement policy has been implemented;
    2. how they have cast votes in the general meeting of companies in which they hold shares.

41. Again, this is information which schemes should already have to hand as it relates to their existing policies and voting records. Assuming these are to hand, reasonable to estimate that this information should take around a day for a professional to compile and document in the report.

42. This would generate an annual cost of £930,000 (4,589 schemes * 8 hours * £25.40[14] per hour professional wage including on costs).

Direct benefits to pension schemes

43. These changes will codify what some schemes in the UK will already be doing when the 2018 regulations come into force and ensure that all schemes will be totally transparent about their investment strategies. These measures have the potential to make it clearer for firms to meet the duty of being transparent about their investment strategy and providing oversight of the firms in which they invest. Transparency will allow schemes to improve their strategies and policies by learning from the good practices of other schemes. As engagement policies are not published and transparent currently it is not possible to measure the improvements as there is no base line, therefore, it would be disproportionate to estimate the size of these direct benefits so they have not been included in the EANDCB calculation.

Costs and benefits to pension scheme members

Costs to members

44. These measure place no requirements on members. Therefore, there are no additional familiarisation or ongoing costs to members from these measures.

Indirect benefits to members

45. These additional requirements will strengthen the responsibilities associated with holding investments in members' best interests and outlining and detailing schemes' arrangements with their asset managers. Improved transparency will reduce information asymmetries between schemes and members and allow engaged members to compare schemes and better understand schemes' investment strategies enabling members to hold schemes to account.

Costs to The Pensions Regulator (TPR)

46. TPR will need to update their guidance to trustees. TPR are already making amendments to their guidance and monitoring processes to take account of for the 2018 regulations, so we would expect the additional impact of these changes to be modest.

[14] The median hourly wage for a professional is £20.00 in the Annual Survey of Hours and Earnings 2017 revised, Table 2.5. This is uplifted by 27% for overheads from the previous version of the Green Book.

Summary of costs

Table 2: Summary of central familiarisation and ongoing costs

	Schemes	Cost	How often?	Assumptions	Rationale
Familiarisation with the requirements	4,589 schemes with 100 or more members.	£60,000	One-off	10 minutes to familiarise, by 3.4 trustees per scheme at £28.50 p.h trustee cost	Assuming reading speed of 300 wpm
Updating SIP	4,589 schemes with 100 or more members	£9,200,000	One-off	£2,000 per scheme	Involves updating SIP to include existing policies. Cost based on lower end of cost range to updating entire SIP from 2018 regulations
Updating annual report	4,589 schemes with 100 or more members	£1,050,000	Per annum	8 hours * £25.40 professional wage	Assume this would take one day for a professional to update
Publishing SIP for DB schemes	3,539 DB schemes with 100 or more members	£23,000	Tri-annually (equivalent to £7,300 per year)	20 minutes * £19.48 administrator wage	Assume 20 minutes for administrator to upload onto existing website

Sensitivity Analysis

47. The main sensitivity to the costing is the assumption on the cost of publishing the additional SIP information. This the single largest component of the EANDCB calculation and an area of uncertainty given this is a new requirement, and we do not have direct information from businesses on the cost of providing this information. This is set out below.

48. <u>Sensitivity around cost of providing additional information to SIP</u>– the central scenario figure of £2,000 is based on cost estimates to update a whole SIP provided by stakeholders for the previous impact assessment (in the range of £2,000 to £5,000 with

an average of £3,166[15]). This is a reasonable proxy source for the broad scale of costs associated with producing a SIP. The lower end of the range was selected for the central scenario as it is judged that adding additional information would cost less than updating an entire SIP.

49. As a reasonable low end scenario, we assume that updating the required information would take around one week's work (40 hours) for a professional (£25.40 per hour) or £1,016 to collate and update the required information in the SIP.

50. As a reasonable high end scenario we assume that the cost of providing the additional information to the SIP is equivalent to the average estimated cost of updating a whole SIP of £3,166. Costs for each of these scenarios are detailed below.

Table 3: Sensitivity analysis

Scenario	Cost per scheme	One off costs
Central	£2,000	£9.2m
Low	£1,016	£4.7m
High	£3,166	£14.5m

51. Even under the high scenario, the EANDCB would increase by less than £1m per year[16].

Small and Micro Business Assessment (SaMBA)

52. SRD II applies to IORPs as falling within the scope of Directive (EU) 2016/2341 (IORP II) in accordance with Article 2 and Article 5 of that Directive, therefore SRD II does not apply to Public Service schemes and schemes that in total have less than 100 members.

53. Therefore, small and micro businesses, where they run their own pension schemes are excluded from this directive as this policy only applies to schemes with 100 or more members.

Monitoring and Evaluation

54. We recognise the importance of monitoring and evaluation. As this instrument builds on the earlier Shareholders' Rights Directive making minor amendments to the Regulations governing the investment principles and disclosure requirements for occupational pension schemes, and the annualised net cost to business is estimated at less than £2m per year, it is not considered proportionate to conduct formal monitoring or review. It will be easier for Regulators, Government and others to monitor the quality of reporting due to the requirement to publish a range of information. Should any issue arise with the policy, we will assess the evidence and, if appropriate, consider whether any changes may be necessary.

[15] 'Impact Assessment for The Occupational Pensions Schemes (Investment and Disclosure) (Amendment) Regulations 2018 published at http://www.legislation.gov.uk/uksi/2018/988/pdfs/uksiod_20180988_en.pdf

[16] £14.5m-£9.2m = £5.3m. Divided by 10 years is less than £1m per year.