KPMG Investment Advisory

The Pensions Regulator: DB investment guidance

30 March 2017

The Pensions Regulator ('tPR') released their inaugural investment guidance on 30 March 2017 for defined benefit pensions which follows their guidance on integrated risk management ('IRM') issued in December 2015.

This is a helpful step and represents a continuation of the tPR's progressive approach to helping trustees and companies manage their schemes. We highlight some of the key points of note.

TPR's full DB Investment Guidance can be found at: www.thepensionsregulator.gov.uk/guidance/db-investment.aspx

The guidance covers six sections when looking at the investment strategy and governance for DB pension schemes:

- **Governance**: encouraging collaboration between trustees and sponsors with clear understanding of what is required.
- **Investing to fund defined benefits**: having a clear strategy based on defined objectives.
- **Matching assets**: understanding the purpose of matching assets and considering use of Liability Driven Investment.
- **Growth assets**: understanding the underlying risks of growth assets to ensure true diversification.
- **Implementation**: managing the risk associated with operations, asset transitions, liquidity and collateral management.
- **Monitoring**: ensuring monitoring is prioritised, timely and actionable as part of an IRM framework.

When setting the investment strategy, the regulator highlights that a good strategy is likely to involve clear objectives combined with a journey plan that is consistent with the wider IRM. This needs to be combined with a strategy that is consistent with risk tolerance and liquidity requirements, implemented and monitored within an effective governance framework.

In particular we would draw attention to two aspects covered within the report:

Cashflow negative – the guidance highlights that schemes should understand the impact of the maturity profile of a scheme and "sequencing risk" (also known as path dependency). Further, it highlights that the level of risk taken needs to factor in a range of issues and that being cashflow negative alone does not inform the level of risk or strategy that a scheme should pursue. We are supportive of this approach and our paper on "Cashflow Negative isn't such a negative" can be found at: https://assets.kpmg.com/content/dam/kpmg/uk/pdf/2017/03/cashflow-negative.pdf

Fiduciary management – the guidance also highlights some of the challenges around Fiduciary Management noting that the skills required to be a successful consultant are not exactly the same as those required to be a successful investment manager. tPR highlights the importance of ensuring appropriate measures are in place to identify, mitigate and manage conflicts through for example appointing an independent third party to advise. If you are considering Fiduciary Management, our paper on how this can be approached can be found at: https://home.kpmg.com/content/dam/kpmg/uk/pdf/2017/03/fiduciary-management.pdf

We are supportive of tPR's focus on investment strategy as we believe it is core to a scheme's ability to deliver successful outcomes.

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