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Making investment arrangements easier

May 2016

Introduction

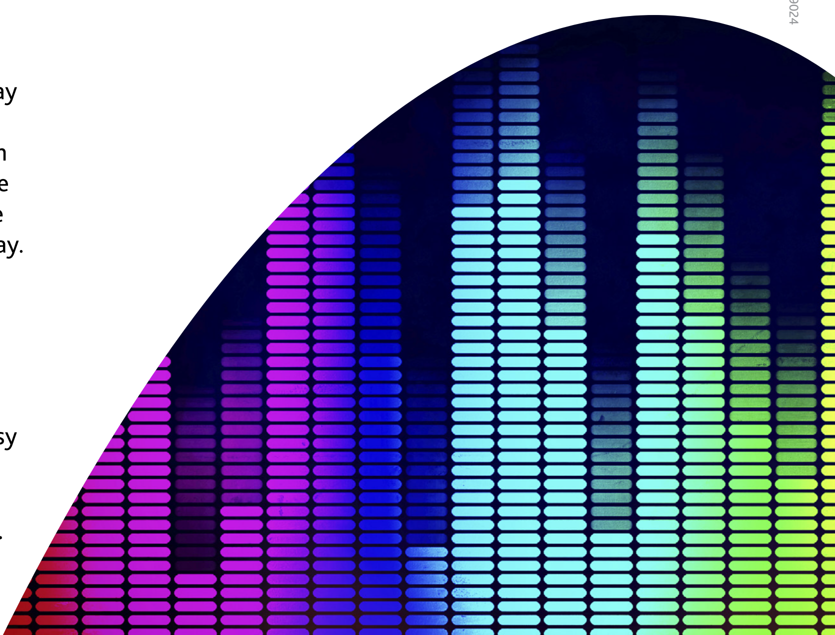
Pension scheme investment isn't easy. The strategic decisions are difficult enough, and the jargon doesn't help either. Once the strategic decisions have been made, attention turns to implementation. Each provider will have its own investment products, which could be based on investment agreements, insurance policies or investment funds. Sometimes these are based in the UK, but increasingly they are based off-shore. Whilst the products may be different, the issues for trustees are the same: to understand the key terms and structural risks, and where possible to negotiate improvements.

10 tips for successfully implementing your investment strategy

1. Check that the product is one permitted by the rules of your scheme. This is particularly important if trustees are investing in swap contracts. Because contracts are taken out in the name of the trustees, it is important to make sure that they are permitted investments, so that the scheme's assets stand squarely behind them.
2. Check that the product really does what its name suggests at the outset. If it's called a cash fund, does it really just hold cash?
3. Make sure you understand the structural risks. For example, many investment funds are structured as umbrella products. If your scheme invests in a low risk fund, will it be exposed if a high risk fund within the same umbrella product becomes insolvent, or is each fund legally ring-fenced? This will depend on the design of the product, and on the law where it is based. We have a separate note about investment fund structures for segregated and pooled funds.
4. Be prepared to negotiate. Investment products are often presented in a way that is designed to make them look non-negotiable. But this isn't always the case, especially if trustees are investing a significant amount. In general, investment agreements are the most negotiable, with insurance policies and investment funds less so.
5. Raise key commercial terms at an early stage. A provider may be more flexible when it is competing with others about commercial terms than when it has been told it is the chosen provider. Give close attention to the liability accepted by the provider, the standard of care and exit provisions. Also make sure that the trustees' liability is limited in an appropriate way.
6. Consider how assets are going to be transferred to the provider: will there be a separate agreement covering the transfer, and if so what are its terms? Also consider the exit terms when making an investment. Is it easy to get your money out and are there notice periods or penalties? Can disinvestment be delayed if the underlying assets are not easy for the provider to sell?

Continued on next page >

7. Think about ongoing monitoring. How is this to be done? What information must be provided? Will errors be disclosed as they occur and how will they be put right? If swap contracts are used, how is the collateral to be managed and the security of the counterparties monitored?
8. Make sure you understand the total cost. The total cost is not always transparent, especially in investment funds or multi-manager products, where there can be a layering of costs. If there is a performance-related fee, make sure it is clear how this works, and that it is calculated over an acceptable period. Ask for examples to be provided, showing what happens if performance fluctuates over a long period.
9. If you are using interest rate and inflation swaps, you will need to check whether ISDAs or similar documents will be needed, and allow time to agree these.
10. Don't forget the big picture. Understand how all your providers work together (for instance how the custodian deals with the investment manager) and make sure the agreements reflect this. Also, don't forget to check whether your statement of investment principles needs updating and, where appropriate, consult with the employer about this.



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Further reading

We have prepared a briefing paper on segregated and pooled funds and the cross-liability risk. Please ask your usual Pinsent Masons adviser for a copy.

Pensions law can be tricky… but it doesn't have to be. These 'making it easier' guides explain key issues in simple terms, giving practical help to trustees and employers.

The series is growing; additional copies can be downloaded from www.pinsentmasons.com

Current topics include: Using advisers; Scheme changes and Becoming a trustee

Comments and ideas for further topics are welcome…

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9024