

Severn Trent Pension Scheme

Statement of Investment Principles – Pensions Choices (Defined Contribution) Section

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1 Introduction

Scheme Details

- 1.1 This document describes the principles governing decisions about investment made by the Trustee of the Severn Trent Pension Scheme (the Scheme).
- 1.2 The main objectives of the Section are:
- To enable Pension Choices members to obtain benefits in retirement by investing their accumulated contributions in one or more of the funds made available to them by the Scheme Trustee; and
 - To provide an appropriate range of funds which recognises that members' investment needs may change throughout their working lives and also that some members may not feel able to select an investment strategy for themselves.
- 1.3 The Scheme is a registered pension scheme for the purposes of the Finance Act 2004.
- 1.4 Administration of the Scheme is vested in Severn Trent Pension Scheme Trustees Limited (the Scheme Trustee), which is responsible for the investment of the Scheme's assets.
- 1.5 In preparing this Statement the Trustee has consulted with the Company and its Investment Adviser (both of whom will also be consulted should the policy be revised in the future).
- 1.6 The Pension Choices Section is due to be transferred to the Aviva Master Trust and as such the underlying investments are subject to change allowing for the mapping across to the funds available on the Aviva platform.

Pensions Act

- 1.7 Under the Pensions Act 1995 (as updated by the Pensions Act 2004), trustees are required to prepare a statement of the principles governing investment decisions. This document fulfils that requirement.
- 1.8 The Scheme Trustee has consulted Severn Trent Plc on the content of this document and will consult Severn Trent Plc on any changes to the document. However, the ultimate authority and responsibility for deciding the investment policy of the Scheme lies solely with the Scheme Trustee.
- 1.9 In drawing up this document, the Scheme Trustee has sought advice from the Investment Adviser. The Scheme Trustee will review this document at least once a year.

Financial Services and Markets Act 2000

- 1.10 In accordance with the Financial Services and Markets Act 2000, the Scheme Trustee will determine general investment policy, but will delegate day-to-day responsibility for selection of specific investments, and determining the proportion of the underlying funds that are invested in the various asset classes, to the appointed Investment Manager, which may include an insurance company or companies. The Investment Manager shall provide the skill and expertise necessary to manage the investments of the Scheme competently.

Responsibilities

- 1.11 The Scheme Trustee is responsible for all of the investment decisions in respect of the Section.
- 1.12 The Scheme Trustee has set up an Investment Committee (“IC”). The responsibility of the Investment Committee is as follows:
- To monitor the performance of the Section and the Section’s manager, in respect of the Pension Choices;
 - To provide a summary to the Scheme Trustee quarterly meeting of the Section’s investments and any changes made during the quarter;
 - To make available a range of investment options that, whilst avoiding excessive complexity, should assist members in achieving the following objectives:
 - Optimising the value of retirement benefits from the given contributions.
 - Protecting the value of those benefits in the years approaching retirement against market falls.
 - Protecting the value of those benefits in the years approaching retirement against fluctuations in turning fund values into retirement benefits.
 - Tailoring their investments to meet their own needs.
 - To monitor the ongoing appropriateness and and make recommendations to the Scheme Trustee for any change to the the lifestyle options.
 - To review the ongoing appropriateness of the Section’s investment strategy, the associated risks, and its implementation;
 - To review annually the Section’s compliance with the SIP.
- 1.13 The Scheme Trustee shall remain responsible for all other investment activity.
- 1.14 The Scheme Trustee also takes advice from the Scheme Actuary and Investment Adviser.
- 1.15 Severn Trent Plc does not have the authority to place limits on the Scheme Trustee as to how it can invest the money.

2 Aims and objectives

Primary Objective

- 2.1 The primary objective of the Pension Choices section is to provide, on a defined contribution basis, benefits for members on their retirement or benefits for their dependents on death before retirement.
- 2.2 In light of the regulatory changes following the Budget announcement in March 2014, the Trustee reviewed the investment strategy of the default option for the Severn Trent Pension Scheme DC Section and a revised strategy was implemented in 2016.
- 2.3 The Trustee recognises that members have differing investment needs and that these may change during the course of their working lives. It also recognises that members have different attitudes to risk. The Trustee believes that members should make their own investment decisions based on their individual circumstances. The Trustee's objective is therefore to make available a range of investment options that, whilst avoiding excessive complexity, should assist members in achieving the following objectives:
- Optimising the value of retirement benefits from the given contributions.
 - Protecting the value of those benefits in the years approaching retirement against market falls.
 - Protecting the value of those benefits in the years approaching retirement against fluctuations in turning fund values into retirement benefits.
 - Tailoring their investments to meet their own needs.

3 Investment arrangements

- 3.1 The current range of funds chosen by the Scheme Trustee is detailed in the Appendix, although the Trustee is in the process of transferring the DC Section to Aviva Master Trust. The Scheme Trustee will assess and review performance against the fund benchmarks on a regular basis. These investments are separate from the defined benefit investment of the Scheme.

Investment strategy

- 3.2 Pension Choices offers two investment approaches. Members can either invest their account using the Default Arrangement - a set formula called the LifeModel - or select their own funds from the range offered by the Scheme Trustee called FreeModel.

LifeModel

- 3.3 Under LifeModel, members' accounts are invested in a fixed range of funds chosen by the Scheme Trustee on investment advice.
- 3.4 The LifeModel strategy provides automatic asset allocation switches for members who do not want to make strategy decisions. This works as follows:
- **More than ten years to selected retirement age** – contributions invested in the Legal & General Global Equity Fund which invests in UK and overseas equities.
 - **At 10 years from retirement** – gradual switch into the Pre-Retirement Fund which invests in bond funds, predominantly the AAA-AA-A Corporate Bonds Over 15yr Index Fund.
 - **At three years from retirement** – partial switch into cash.
 - **At retirement** – 75% invested in the Pre-Retirement Fund and 25% in cash.

- 3.5 In adopting this approach the Scheme Trustee has considered risk from a number of perspectives, including:

- The risk that the investment return over members' working lives will not keep pace with inflation (or inflation risk)
- The risk that investment market movements in the period immediately prior to retirement lead to a substantial reduction in the anticipated level of pension (or investment risk)
- The risk that relative market movements in the period immediately prior to retirement lead to a reduction in the anticipated level of pension (or pension conversion risk).

- 3.6 The LifeModel option is therefore effectively constructed in two phases:

- **Growth phase (up to 10 years before selected retirement date)** – to maximise, as far as is reasonably possible, the return on members' accounts by investing in assets that give members the best opportunity to achieve competitive long-term returns.
- **Consolidation phase (from 10 years before selected retirement date)** – to seek to protect the returns already achieved, and the annuity and cash purchasing power of the members' accounts as they approach retirement.

FreeModel

- 3.7 Members are offered a range of investment funds that has been selected by the Scheme Trustee and which covers a broad range of investment risk. The individual funds, their long-term aims and asset mixes are detailed in the Appendix.

Fee Structure

- 3.8 The Scheme Trustee has agreed a fee scale with the Investment Managers which they believe to be competitive. Details can be found in the Appendix.

Review process

- 3.9 The continuing appropriateness of the chosen Investment Managers, the funds and the fee structure will be reviewed from time to time.

Social, environmental and ethical considerations, including climate change

- 3.10 The Scheme Trustee has decided to invest the assets in a range of pooled funds. Although it has satisfied itself as to the general overall suitability and management of those funds, the Scheme Trustee has no control over the underlying investments. The equity Investment Manager produces a report on its corporate governance policies as part of its quarterly reporting to the Scheme Trustee.
- 3.11 An ethical fund is available for members who wish to invest on this basis and details of this can be found in the Appendix.

4 Investment beliefs and risk management

Responsible Investment

- 4.1 The Scheme Trustee recognises that the consideration of financially material factors, including ESG factors, is relevant at different stages of the investment process.
- 4.2 The Scheme Trustee recognises that climate change could pose systemic risks which could in turn affect the returns achieved from their investment strategy.
- 4.3 The Scheme Trustee has not at this stage made explicit allowance for climate change in designing the lifestyle strategies in which members may invest, although this will be reviewed periodically. Instead, the Scheme Trustee does expect the active managers to take into account all financially material factors, including climate change, in the selection of assets within their portfolios and to be able to demonstrate their approach when challenged.
- 4.4 In adding new active managers to the platform, the Scheme Trustee will explicitly consider the managers' ability to integrate the consideration of ESG factors within their investment process. The Scheme Trustee will also periodically review their investment manager and seek evidence that the manager is meeting the Scheme Trustee's expectations.
- 4.5 In passive mandates, the Scheme Trustee recognises that the choice of benchmark dictates the assets held by the investment manager and that the manager has minimal freedom to take account of factors that may be deemed to be financially material. The Scheme Trustee accepts that the role of the passive manager is to deliver returns in line with the market and believe this approach is in line with the basis on which their current strategy has been set.
- 4.6 The Scheme Trustee has not imposed any constraints on the investment arrangements or managers employed relating to non-financial factors.

Stewardship & Engagement

- 4.7 The Scheme Trustee believes good management of companies should lead to more sustainable and predictable returns. The Scheme Trustee is unable to control the exercising of rights (including voting rights) attaching to investment held by the Investment Manager in pooled funds but will monitor the general approach adopted by the Investment Manager.
- 4.8 The Investment Manager has signed up to the UK Stewardship Code. The Investment Manager seeks to actively engage with investee companies and vote on resolutions. The Investment Manager publicly discloses their voting activity on its website.
- 4.9 The Scheme Trustee supports the principles set out in the UK Stewardship Code. The Scheme's listed equity Investment Manager adheres to the UK Stewardship Code. In accordance with the Code, the Manager's policies on voting and engagement are disclosed on their websites.

Risk measurement and management

- 4.10 The Scheme Trustee recognises that the key risk is that members will have insufficient income in retirement or an income that does not meet their expectations. The Scheme Trustee considered this risk when setting the investment options and strategy for Pension Choices.

- 4.11 Risk management is considered as part of each normal strategy review. In addition, the Scheme Trustee measures risk in terms of the performance of the assets compared to their benchmarks on a quarterly basis along with monitoring any significant issues with the investment managers.
- 4.12 The Scheme Trustee considers the following sources of risk in designing and reviewing the investment options:
- **Deterioration in investment conditions near retirement** – the final level of pension secured will depend upon investment conditions at retirement. A sharp deterioration in these conditions in the period just prior to retirement will have a substantial impact on the benefits provided. The Scheme Trustee will ensure that the range of funds offered will enable members to take the necessary steps to safeguard against this.
 - **Risk from excessive charges** – if the investment management charges are excessive, then the value of members' accounts will be reduced unnecessarily. The Scheme Trustee will monitor the Investment Manager charges to ensure that they will not unnecessarily reduce members' accounts.
 - **Lack of member investment knowledge** – management of pension assets is a specialist function and one that many members will not feel adequately equipped or inclined to undertake. The Scheme Trustee believes that this risk is addressed by providing, within the set of investment options, the LifeModel strategy which is designed to adapt automatically to the changing needs of a typical member as they progress through their working life.
 - **Operational risk** – the risk of fraud, poor advice or acts of negligence. The Scheme Trustee has sought to minimise such risk by ensuring that all advisers and third party service providers are experienced and that suitable liability and compensation clauses are included in all contracts for professional services received.

Appendix

Pension Choices section – defined contribution funds

The Scheme Trustee has designed and designated the Legal & General Global Equity Fund as the equity fund in which LifeModel members are invested and in which FreeModel members can choose to invest. The Legal & General Global Equity Fund invests in passively invested funds managed by Legal & General Investment Management Limited (“Legal & General”):-

Legal & General Global Equity Fund – this fund invests in pooled index funds managed by Legal & General in the following proportions.

40% UK Equity (5% Capped) Passive Fund
13% World (ex UK) Developed Equity Index Fund
40% World (ex UK) Developed Equity Index Fund (GBP currency hedged)
7% World Emerging Markets Equity Index Fund

A description of each of these funds is provided below.

UK Equity (5% Capped) Passive Fund – this fund aims to provide long term growth by providing exposure to the broad UK equity market but restricting the allocation to any single stock in the FTSE All-Share Index to 5%. The fund seeks to track the total return of the adjusted FTSE All-Share Index.

World (ex UK) Developed Equity Index Fund – this fund provides access to developed overseas equity markets (excluding advanced emerging markets) via index funds, and aims to capture global equity market returns (excluding UK). It tracks the FTSE AW Developed World (ex UK) Index. It is invested in five pooled index funds – North America, Europe (ex UK), Asia Pacific (ex Japan) Developed, Japan and Middle East/Africa.

World (ex UK) Developed Equity Index Fund (GBP Hedged) – a currency hedged version of the World (ex UK) Developed Equity Index Fund which aims to remove the impact of currency movements associated with investing in overseas equities.

World Emerging Market Index Fund – this fund provides exposure to emerging market equities. It aims to track the FTSE AW All Emerging Markets index.

The Trustee has also chosen to offer members a range of passive and actively invested funds. Descriptions of these funds are provided below.

Legal & General World (ex UK) Index Fund – this fund provides access to overseas equity markets via index funds, and aims to capture global equity market returns (excluding the UK). It tracks the FTSE World (ex UK) Index. It is invested in five pooled index funds – North America, Europe (ex UK), Asia Pacific (ex Japan), Japan and World Advanced Emerging (ex Asia Pacific).

Legal & General Ethical Global Equity Index Fund – this fund invests in securities which form part of the FTSE4Good Global Equity Index. The FTSE4Good Index series for socially responsible investment was designed with the support of UNICEF, the United Nations Children’s Fund, and the use of data provided by EIRIS, the Ethical Investment Research Service. The FTSE4Good Advisory Committee is responsible for the management of the FTSE4Good selection criteria and for undertaking the review of all FTSE4Good Indices. Half of the FTSE fee goes to UNICEF.

Legal & General UK Equity Index Fund – this fund aims to provide long term growth by seeking to track the total return of the FTSE All-Share Index.

UK Equity (5% Capped) Passive Fund – this fund aims to provide long term growth by providing exposure to the broad UK equity market but restricting the allocation to any single stock in the FTSE All-Share Index to 5%. The fund seeks to track the total return of the adjusted FTSE All-Share Index.

Legal & General Pre-Retirement Fund – this fund aims to capture bond market returns and offer some protection against changes in non-index linked annuity prices. The Fund has a dynamic asset allocation where Legal & General has the discretion to change the allocation to the underlying passive funds in which the Fund invests.

Legal & General Over 5yr Index-Linked Gilts Fund – this fund aims to offer some protection against changes in annuity prices as members approach their selected retirement date and is designed to capture the returns of the UK gilt market. It tracks the FTSE A Index-Linked (Over 5 Year) Index and invests in medium to long-term gilts.

Legal & General Cash Fund – this fund aims to deliver competitive rates of return from cash deposits and other short-term investments. It is likely to be of specific interest to members who want a cash sum on their selected retirement date and offers security of capital over the short-term, rather than growth in the longer term.

Legal & General Property Fund – this fund is an actively managed fund which invests both directly and indirectly in UK freehold and leasehold commercial property across the office, retail and industrial sectors. The fund aims to outperform the BNY Mellon CAPS pooled property fund survey median, a peer group of similar property funds, over three and five year periods. The fund offers members diversification away from equities and bonds.

The fee scale for the Legal & General funds is as follows:-

Fund	Fund charge (% p.a.)
Legal & General Global Equity Fund	This will be a blend of the underlying fund charges which equates to c0.2% p.a. The Scheme is charged an additional £500 p.a. for maintaining the fund.
Legal & General World (ex UK) Index Fund	0.22
Legal & General Ethical Global Equity Index Fund	0.30
Legal & General UK Equity Index Fund	0.10
Legal & General UK Equity (5% Capped) Passive Fund	0.11
Legal & General Pre-Retirement Fund	0.15
Legal & General Over 5yr Index-Linked Fund	0.10
Legal & General Property Fund	0.70
Legal & General Cash Fund	0.125