

# **BT (CDL) Section of the Pensions Master Plan**

## **Statement of Investment Principles as Required by the Pensions Act 1995 and the Pension Act 2004**

January 2024

**The Trustee confirms that the following matters have been taken into account when preparing this Statement of Investment Principles:**

The Trustee has considered written advice from the Investment Advisor prior to the preparation of this Statement and has consulted British Telecommunications Plc, the Principal Employer, before agreeing this Statement and the investment strategy outlined in this document.

The majority of the Section's assets are invested in a buy-in policy managed by the Insurance Provider. All day to day investment management decisions for the residual investments have been delegated to the Investment Manager where applicable, where the Investment Manager is authorised and regulated by the Financial Conduct Authority.

The Trustee has full regard to its investment powers under the Trust Deed and Rules and the suitability of types of investments, the need to diversify, the custodianship of assets and any self-investment.

This Statement of Investment Principles will be reviewed at least every three years, or whenever changes to the principles or strategy are necessary. Any changes to this Statement will be undertaken having taken advice, as appropriate, and following consultation with the Principal Employer.

## **1. General**

This statement sets out the principles governing decisions about the investment of the assets of the BT (CDL) Section of the Pensions Master Plan (the “Section”). It has been prepared on behalf of the Section Trustee (the “Trustee”) to comply with section 35 of the Pensions Act 1995 (the “Act”) as amended by the Pensions Act 2004 and the Occupational Pension Schemes (Investment) Regulations 2005.

The Trustee reviews the Section’s investment strategy at least every three years, following each formal actuarial valuation of the Section (or more frequently should the circumstances of the Section change in a material way).

## **2. Consulted Parties**

As required under the Act, the Trustee has consulted a suitably qualified person in obtaining written advice from Isio Group Limited (“Isio” or the “Investment Advisor”) on the suitability of the investments, the need for diversification and the principles contained in this Statement. Isio is authorised and regulated by the Financial Conduct Authority (“FCA”).

The Trustee, in preparing this Statement, has also consulted British Telecommunications Plc, the Principal Employer (the “Company”), in particular on the Trustee’s objectives and investment strategy.

## **3. Investment Objectives**

The Trustee’s primary objectives for setting the investment strategy of the Section are set out below:

- “funding objective” – for the Section to be fully funded on a low risk basis, taking account of the strength of the Company covenant;
- “stability objective” – to have regard to the Company’s ability in meeting its contribution payments and to have regard to the volatility of funding and security measures;
- “hedging objective” – for the assets to hedge a significant portion of the interest rate and inflation risk associated with the Section’s liabilities on a low-risk basis.

In meeting these objectives, the Trustee, in consultation with the Section’s sponsoring employer, British Telecommunications Plc, has entered into a buy-in policy with the Insurance Provider, Phoenix Life Ltd (“Standard Life”). This policy is designed to meet all members’ benefit payments as they fall due. The buy-in policy was implemented on 13 March 2023.

The investment arrangements outlined in Points 7 & 8 have been designed with the above objectives, and the existence of the buy-in policy in mind.

## **4. Investment Powers**

The Trustee recognises that the assets must be invested in the best interests of members and beneficiaries and, in the case of a potential conflict of interest, in the sole interest of members and beneficiaries. The Trustee has overall responsibility for the prudent management of the Section’s assets. The strategic management of the Section assets is fundamentally the responsibility of the Trustee, acting on advice from Isio, and is driven by its investment objectives as set out in Point 3 above.

The majority of the Section's assets are invested in a buy-in policy managed by the Insurance Provider. The remaining residual assets that were surplus to the insurance premium for the buy-in policy are managed day-to-day by the Trustee.

These residual assets have been invested in a policy with Legal & General Assurance (Pensions Management) Limited. The day-to-day management of the residual assets is delegated to the investment manager, Legal & General Assurance (Pensions Management) Limited where the management of the assets is undertaken by Legal & General Investment Management ("LGIM" or the "Investment Manager"), who is authorised and regulated by the FCA.

## **5. Choosing investments**

The Trustee recognises that the investment strategy should reflect the characteristics of the Section's liabilities and meet the objectives outlined in Point 3:

- As the majority of the assets are invested in the buy-in policy managed by the Insurance Provider, the responsibility for these assets has been delegated to the Insurance Provider. However, the Trustee retains overall responsibility for reviewing the ongoing operation of and risks associated with the buy-in policy. This includes, but is not limited to the timeliness and accuracy of payments made to the Section.
- The residual assets that were surplus have been invested such that a proportion is held in matching assets that are expected to move in value broadly in line with the estimated value of the true-up premium adjustment that is expected to be required by Standard Life as part of the buy-in transaction terms post any data-cleanse.

This portion of the portfolio is being held in gilts and index-linked gilts at appropriate durations to broadly match the expected movement over time as given by Standard Life's price-lock portfolio, aiming to reduce asset & liability mismatch risk in respect of the true-up payment.

The remainder of the residual assets are temporarily invested in money-market instruments within the LGIM Sterling Liquidity Fund until which time the Trustee and Company agree a strategy for the remaining surplus, alongside cash held in the Section's Bank Account to meet short term expenses as they fall due.

- Finally, when choosing investments the Trustee considers risks, including Environmental, Social and Governance factors, which it believes to be financially material.

## **6. Investment Manager and Insurance Provider**

The Trustee, with guidance from its Investment and Risk Transfer Advisor, has chosen Standard Life to be the Section's Insurance Provider for the buy-in policy. Standard Life is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and Prudential Regulatory Authority.

The Trustee paid an insurance premium for this policy and as such there is no ongoing fee arrangement with the Insurance Provider.

When selecting the buy-in policy, the Trustee considered the costs and charges of paying the insurance premium to ensure this was competitive, alongside the performance of the Insurance Provider to carry out its obligation to meet any agreed members benefits through the monthly payment to the Section.

The Trustee believes that along with the Insurance Provider's stewardship and ESG policies that were considered when investing in the buy-in policy, which are detailed in Point 11 of this document, the objectives of the buy-in policy are aligned with the long-term views of the Trustee.

The Trustee, with guidance from its Investment Advisor, has chosen LGIM to be the Section's Investment Manager for the residual assets. LGIM is authorised and regulated by the Financial Conduct Authority.

The fee arrangement agreed with LGIM is summarised in section 14 of this document. These fees are based on assets under management and are not subject to any performance conditions. In addition, the Investment Manager pays commissions to third parties on trades they undertake in the management of the assets. The Trustee reviews the fees charged by the Investment Manager on a regular basis as part of its monitoring framework to ensure fees remain reasonable in the context of the Section's size and complexity.

The Trustee believes that along with the Investment Manager's stewardship policies, which are detailed in Point 11 of this document, the objectives of the funds are aligned with the medium- and long-term views of the Trustee.

If the Trustee believes that the Section's Investment Manager is no longer acting in accordance with the Trustee's policies regarding ESG and engagement with investee organisations, to assess and improve their medium to long-term financial and non-financial performance, the Trustee will take the following steps:

- engage with the Investment Manager in the first instance, in an attempt to influence its policies on ESG and stewardship; and
- if necessary, look to appoint a replacement Investment Manager or managers which are more closely aligned with the Trustee's policies and views.

The remuneration of the investment manager is not directly linked to performance, given the absence of performance related fees, or to ESG practices. However, the Trustee will review and replace the investment manager if medium- and long-term net of fees investment performance and ESG practices are not in line with the Trustee's expectations and views.

The Trustee believes that these steps will incentivise the investment manager to align its actions with the Trustee's policies and also for it to act responsibly.

The Trustee, with guidance from its Investment Advisor, has chosen to invest in open-ended pooled funds. For these funds, the Trustee's policy is to enter arrangements with no fixed end date. However, the Trustee will seek to enter arrangements where it has the power to terminate these in line with the liquidity of the underlying assets and as agreed in the mandate. The Section's open-ended investments are daily dealt. The Trustee will determine whether to terminate such arrangements on an ongoing basis through its regular monitoring of the Investment Manager's performance against objectives. The Trustee may also elect to terminate the arrangement with the Investment Manager when performing ongoing reviews of the suitability of the Section's asset allocation over time.

## **7. Strategic Investment Benchmark**

In addition to the buy-in policy, the Trustee has put in place the following temporary strategic investment strategy for the Section. The Section's residual assets are invested with LGIM, with a small amount held in the Section's Bank Account.

It should be noted that due to the residual assets forming part of the surplus and being used to meet ongoing and future expenses and liabilities including the true-up premium, the relative allocations below will fluctuate over time as these payments are made. As such, the Trustee would not look to explicitly rebalance the strategy back to the allocations outlined below over time.

Asset Class	Fund	% as at 31 December 2023
Cash	LGIM Sterling Liquidity Fund	81.9
Gilts and Index-Linked Gilts Portfolio	LGIM All Stocks Gilts Index Fund LGIM All Stocks Index-Linked Gilts Index Fund	8.9
Cash	Trustee Bank Account	9.3
<b>Total</b>		<b>100.0</b>

The objective of the Gilts and Index-Linked Gilts Portfolio is to hedge a significant proportion of the interest rate risk and inflation risk associated with the true-up premium. The allocation to the Sterling Liquidity Fund is designed to provide capital stability with growth in line with money market rates on the Section's residual surplus until which time agreement on the investment of the strategy has been reached between the Trustee and Company.

## 8. Performance Benchmarks for Residual Assets

The Trustee expects the performance of the Funds that the residual assets are invested in to match the benchmarks as detailed below:

Fund	Benchmark Index
LGIM Sterling Liquidity Fund	Sterling Overnight Index Average
LGIM All Stocks Gilts Index Fund	FTSE Actuaries UK Conventional Gilts All Stocks Index
LGIM All Stocks Index-Linked Gilts Index Fund	FTSE Actuaries UK Index Linked Gilts All Stocks Index

The Gilt and Index-Linked Gilt portfolio aims to hedge movements in the expected true-up premium from changes in interest rate and inflation expectations as given by the sensitivities of the Standard Life price-lock portfolio. However, it should be noted that differences in duration will result in curve risk to the extent that the pooled funds will not move exactly in line with the price-lock portfolio for changes in the shape of the interest rate and inflation curves.

## 9. Realising investments and rebalancing

It is the intention of the Trustee to hold the buy-in policy until the final covered member dies, with the payments due from the policy meeting Section benefit payments due.

The Section is currently cashflow negative with respect to meeting ongoing expenses from the residual assets. Where possible, the Section's allocation to cash in the Section's bank account will be used as

the primary source for these cashflows. If this is not sufficient, the Trustee will disinvest assets held with LGIM, after taking advice from its Investment Advisor.

The Trustee will consider advice from its Investment Advisor before undertaking any rebalancing or strategic changes with respect to the residual assets.

## 10. Risks

In determining its investment policy, the Trustee has considered the following risks:

- *funding and asset and liability mismatch risk* – the Trustee addresses this through the asset allocation strategy to invest in a buy-in policy as advised by the Section’s Investment and Risk Transfer Advisors and Section Actuary. In addition, for the true-up premium adjustment through the gilt and index-linked gilt portfolio which is subject to periodic actuarial and investment review.
- *credit risk* – As the majority of the Section’s assets are invested in the buy-in policy with Standard Life, the Section is exposed to the risk of insolvency and default on the policy. As noted, Standard Life is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and Prudential Regulatory Authority and is subject to regulatory solvency requirements. In addition, the buy-in policy is covered under the Financial Services Compensation Scheme (“FSCS”), protecting 100% of an individual’s pension pot with an insurer, as long as the regulatory environment and FSCS can be relied on.

The residual assets are invested in cash, money market instruments and UK government bonds (“gilts”) and as such have minimal credit risk;

- *market risk* – As the majority of the Section’s assets are invested in the buy-in policy with Standard Life, any market risk of meeting the obligations of any agreed members benefits is managed by Standard Life.

For the residual assets that are not invested in cash, the value of securities, including interest bearing assets, can go down as well as up. The Section may not get back the amount invested. However, the Trustee realises that this risk is implicit in trying to generate returns in line with the true-up premium and accept this for matching assets. This risk is expected to be low for money market instruments and the Trustee would review the investment in a negative interest rate environment.

- *underperformance risk* – this is addressed through monitoring the performance of the Investment Manager for the residual assets and taking necessary action when this is not satisfactory;
- *sponsor risk* – the risk of failure of the Section’s sponsoring employer. The Trustee monitors the strength of the sponsoring employer on an ongoing basis.
- *liquidity risk* – the Trustee may need to pay pension and lump sum benefits in the short-term and, therefore, address this risk by investing an appropriate amount in assets that are realisable at relatively short notice. In practice, all of the residual assets invested in by the Section provide at least daily liquidity.
- *environmental, social and governance (ESG) factors* – the Trustee acknowledges that ESG factors, including climate change, can have a financially material impact on the future returns on its investments and the Trustee’s actions to mitigate these is detailed in the following section.

- *non-financial risks* – the Trustee has not taken these into account when deciding the choice of the Section's investments.

The Trustee will monitor these risks from time to time, particularly those deemed to have high likelihood or significant adverse impact, and will look to introduce further control measures as appropriate to contain the overall level and distribution of risks to within acceptable limits.

#### **11. Environmental, social and governance (ESG) policies and stewardship**

The Insurance Provider, Standard Life, is responsible for managing the majority of Section's investments in accordance with the buy-in policy in place with the Section. As such the Trustee has delegated the responsibility for the exercise of all rights (including voting rights) attaching to the investments to the Insurance Provider.

For the residual assets, LGIM is responsible for managing the Section's investments in accordance with the management agreements in place with the Trustee. The Trustee has delegated the responsibility for the exercise of all rights (including voting rights) attaching to these investments to the Investment Manager.

The Trustee is responsible for setting the Section's investment strategy and implementing that strategy through appointing investment managers and/or insurance providers. When setting investment strategy and selecting investments, the Trustee's first priority is the financial interests of the members. The Trustee regularly reviews the return objectives, risk characteristics, investment approach and investment guidelines of each of the Section's current investment mandates. The Trustee is satisfied that all existing mandates fulfil the needs of their target investment strategy and by extension, that the Section's Insurance Provider is managing the Section's assets in a manner which is consistent with members' financial interests.

The Trustee acknowledges that certain ESG factors, including climate change, are financially material and may therefore influence the risk and return characteristics of the Section's investments and the likelihood that the Section's objectives will be achieved.

The Trustee recognises the importance of ESG factors on long term investment performance and both immediate and future downside risks. The Trustee has set an appropriate monitoring framework to ensure the Section's Investment Manager is regularly reviewed. This is to promote greater transparency in understanding the reasons behind performance trends and key risk exposures, and also engagement activity and compliance with the Trustee's stated ESG policy. Regular monitoring, with specific reference to ESG factors should incentivise the Section's Investment Manager to assess and improve the medium to long-term performance of investee companies, both financial and non-financial. To confirm, no consideration has been given to non-financial considerations, nor has the Section's membership been consulted on such issues.

These statements are made noting that the Section's assets are predominantly invested in the buy-in policy and as such, the Trustee is restricted in its ability to directly influence the Insurance Provider on the ESG policies and practices of the companies in which the buy-in policy invests within.

#### *For the residual assets that are invested with LGIM*

The Trustee recognises the importance of regular monitoring of the Investment Manager's performance, remuneration and compliance against its ESG policy to ensure that the Section's assets are being managed appropriately. The Trustee believes that regular monitoring ensures that key risks

to longer term performance, including those relating to ESG factors, are quickly identified and concerns communicated with the relevant investment manager.

In addition to performance measures, the Trustee will review the engagement activity of the Investment Manager to ensure that active engagement is taking place where possible to influence positive change in relation to ESG factors within investee companies. The Trustee also monitors any voting activity of the investment manager to ensure votes are being used and are aligned to its views on ESG.

As part of the selection, retention and realisation of the Section's investments, the Trustee, in consultation with its Investment Advisor, has reviewed the ESG and stewardship policies of the Investment Manager and are comfortable that these policies are consistent with its views. In particular, the Trustee notes the following:

- The Investment Manager has clear views on ESG factors and stewardship which are clearly articulated in formal policies on these issues.
- The Trustee's policy in relation to any rights (including voting rights) attaching to its investments is to exercise those rights to protect the value of the Section's interests in the investments, having regard to appropriate advice. The Trustee expects the investment manager to engage with investee companies (and other relevant persons including, but not limited to, investment managers, issuers/other holders of debt and equity and other stakeholders) on aspects such as performance, strategy, capital structure, management of actual or potential conflicts of interest, risks, corporate governance, social and environmental issues concerning the Trustee's investments. The Trustee believes that such engagement will protect and enhance the long-term value of its investments.
- The Investment Manager regularly publishes detailed results of how its stewardship policies are enacted in practice and the Trustee expects the Investment Manager to provide regular updates on how they exercise those rights and actively engages with companies in which it invests, including how often the Investment Manager votes against company proposals. The Trustee will review this on a regular basis in line with its monitoring policy mentioned above.
- Regarding the Section's residual assets, the nature of these assets dictate that the ESG factors are less likely to be financially material. The Trustee does however have confidence that the Investment Manager has adequate governance practices in place to capture key regulatory developments which might influence the future management/ performance of these assets.

The Trustee will keep its investments under review, and should they feel that the Investment Manager no longer acts in accordance with its views on ESG, the Trustee will take the following steps:

- Engage with the Investment Manager in the first instance, in an attempt to influence their policies on ESG and stewardship; and
- If necessary, look to appoint a replacement investment manager or managers that are more closely aligned with the Trustee's policies and views.

These statements are made noting that the Section's residual assets are invested in pooled funds and as such, the Trustee is restricted in its ability to directly influence its Investment Manager on the ESG policies and practices of the companies in which the pooled funds invest.



## 12. Governance

The Trustee of the Section is responsible for the investment of the Section's assets. The Trustee takes some decisions and delegate others. When deciding which decisions to take itself and which to delegate, the Trustee has taken into account whether the Trustee has the appropriate training and expert advice in order to take an informed decision. The Trustee has established the following decision-making structure:

<b>Trustee</b> <ul style="list-style-type: none"> <li>• Select and monitor planned asset allocation strategy;</li> <li>• Select and monitor investment advisors and investment managers/insurance providers;</li> <li>• Select and monitor any direct investments;</li> <li>• Responsible for all aspects of the investments of the Section's assets, including ESG considerations and implementation.</li> </ul>
<b>Investment Advisor</b> <ul style="list-style-type: none"> <li>• Advises on this statement;</li> <li>• Advises the Trustee on areas of strategy, manager selection, ESG and implementation as required;</li> <li>• Provides required training when engaged on a separate basis by the Trustee.</li> </ul>
<b>Investment Manager</b> <ul style="list-style-type: none"> <li>• Operates in line with the agreement with the Trustee, which the Trustee believes is consist with the terms of the SIP;</li> <li>• Manages in accordance with the agreement, including decisions around the selection and retention of underlying investments;</li> <li>• Is responsible for the stewardship of underlying investments.</li> </ul>

When deciding whether or not to make any new direct investments the Trustee will obtain written advice and consider whether future decisions about those investments should be delegated to a fund manager. The written advice will consider the suitability of the investments, the need for diversification and the principles contained in this statement. Isio was appointed to provide investment advisory services including the provision of this advice.

The Trustee recognises that, as the Section is predominantly invested in a buy-in policy, there is limited scope to influence the controls and restrictions used in the management of the underlying assets and acknowledge that derivatives may be used by the Insurance Provider.

The Insurance Provider's objective is to invest so as to replicate the agreed members benefits as per the buy-in policy terms.

The Trustee recognises that for the residual assets, as the Section is invested in a range of pooled funds, there is limited scope to influence the controls and restrictions used in the management of the underlying assets and acknowledge that derivatives may be used by the manager within the funds.

The Investment Manager's objective is to invest so as to replicate the benchmark indices and their performance.

The Trustee has delegated all day-to-day decisions about the investments that fall within the mandate to the Insurance Provider through a written contract for the buy-in policy and to the Investment Manager through a written contract. These duties include:

- Realisation of investments;
- Taking into account ESG factors;
- Voting and corporate governance in relation to the Section's assets.

The Trustee expects the Insurance Provider to manage the assets delegated to them under the terms of their contract and to give effect to the principles in this statement so far as is reasonably practicable.

### 13. Custodian

The Section's investments are held in a buy-in insurance policy and for the residual assets predominantly accessed via an insurance policy with Legal & General Assurance (Pensions Management) Limited.. The investments in the buy-in policy are held in larger pools of investments managed by the Insurance Provider. The custodianship arrangements are those operated by Standard Life for all clients investing in the relevant buy-in policies.

The residual asset investments in pooled pension funds are a share (measured in units) of larger pools of investments managed by the Investment Manager. The custodianship arrangements are those operated by LGIM for all clients investing in the relevant pooled funds.

### 14. Fees

As noted above, the Section does not pay ongoing fees for the buy-in policy with Standard Life and has instead paid a premium.

The Investment Manager levies the following annual management charges.

<b>Fund</b>	<b>Annual Management Charge (p.a.)</b>
LGIM All Stocks Gilts Index Fund LGIM All Stocks Index-Linked Gilts Index Fund	0.03% of assets
LGIM Sterling Liquidity Fund	0.075%

LGIM also charges a policy fee of £1.5k p.a.

**As agreed by the Trustee at the Trustee Meeting on 31 January 2024  
January 2024**