UKSIF
UK Sustainable Investment and Finance Association

Sinead Donnelly and Vicky Bird
Department for Work and Pensions
Strategy Policy and Analysis Group
Private Pensions and Arm's Length Bodies Directorate
Ground Floor North, Quarry House
Leeds, LS2 7UA

16th July 2018

Dear Ms Donnelly and Ms Bird,

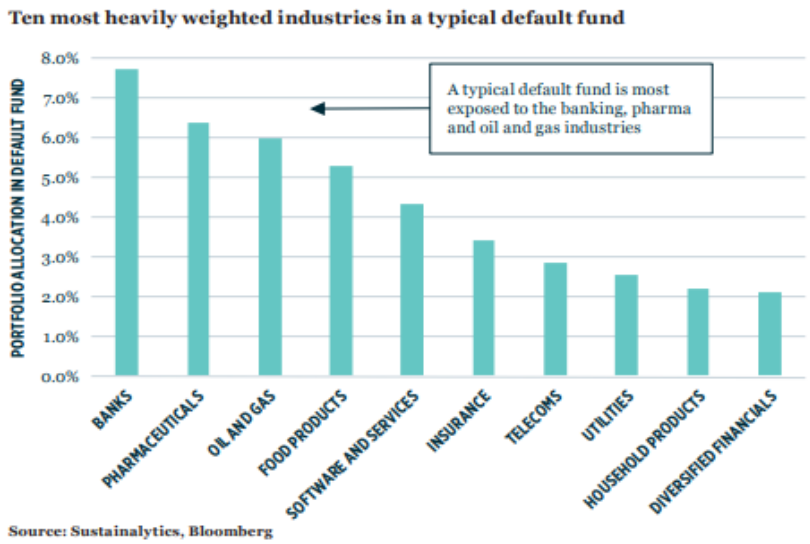
I am writing in my capacity as Chief Executive of the UK Sustainable Investment and Finance Association (UKSIF) in response to your consultation paper *Clarifying and Strengthening Trustees' Investment Duties.* As you are aware, clarification of trustees' fiduciary duties is an UKSIF public policy priority and I would like to take this opportunity to express our gratitude for engaging with us on this issue, over the past few years including meetings, calls, and the roundtable event earlier this month.

Q1: We propose that the draft Regulations come into force approximately 1 year after laying, with the exception of the implementation report, which would come into force approximately 2 years after laying.

a) Do you agree with our proposals?

Yes.

The coming into force date of DWP's draft regulations should not be delayed unless absolutely necessary. There is a particular urgency with which all schemes must begin to consider all financially material risks including where these arise from environmental, social and governance (ESG) factors.



Research conducted by UKSIF and the Climate Change Collaboration shows that 90% of fund managers expect climate risk will significantly impact the valuation of international oil companies within two years.[1] After banks and pharmaceuticals, oil and gas represent the third most heavily weighted sector in a typical default fund.[2]

[1] http://uksif.org/wp-content/uploads/2018/04/UPDATED-UKSIF-Not-Long-Now-Survey-report-2018-ilovepdf-compressed.pdf
[2] https://www.plsa.co.uk/portals/0/Documents/0619-ESG-risk-in-default-funds-analysis-of-the-UKs-DC-pension-market-260417.pdf

Trustees already have a range of priorities, but their approach to climate risk and other financially material ESG factors must be a priority too. We think an October 2019 in-force date gives schemes enough time to revise their SIPs and at the same time helps protect savers from climate risks. We note that LGPS schemes in comparison were given 5 months to develop new Investment Strategy Statements, the SIP equivalent for local government funds.[3]

b) Do you agree that the draft Regulations meet the policy intent?

Yes.

In addition, we note the Pension Protection Fund has separate regulations. Parts of these regulations, specifically in relation to the PPF's investment policies, closely mirror pension scheme requirements under Occupational Pension Scheme (Investment) Regulations 2005 (the Investment Regulations).[4] Whilst the PPF has an advanced investment policy which already considers financially material ESG factors and includes responsible investment criteria in its manager selection, these regulations should nonetheless be brought up to date and brought in-line with the changes being proposed in this consultation.

Q2: We propose to require all trustees of all schemes which are obliged to produce a SIP to state their policy in relation to financially material considerations including, but not limited to, those resulting from environmental, social and governance considerations, including climate change.

a) Do you agree with the policy proposal?
b) Do the draft Regulations meet the policy intent?

Yes.

It is important to highlight that what is being proposed is a clarification of case law as it currently stands, not a significant change. The Law Commission notes in its 2017 report *Pension Funds and Social Investment*, that 'trustees must always take account of financially material factors when considering investments.'[5] Yet when it comes to ESG factors, some trustees are unsure whether, and how, they can take such factors into account. Evidence for ESG being financially material has grown over recent years.[6] According to the law as it stands, when ESG factors are financially material they should be considered by trustees. The purpose of this exercise therefore is to clarify the law for trustees, by requiring them to develop a policy on how financially material factors are considered. It is also worth considering the need for this duty to be codified in law. In essence it is because the Pensions Regulator's (TPR) attempt to clarify trustees' duties through investment guidance did not have the desired effect.[7] UKSIF welcomed TPR's 2016 investment governance guidance as for the

[3] DCLG, Guidance on Preparing and Maintaining an Investment Strategy Statement, July 2017 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/627030/Guidance_on_preparing_and_maintaining_an_investment_strategy_statement.pdf
[4] The Pension Protection Fund (Statement of Investment Principles) Regulations 2005, available at http://www.legislation.gov.uk/uksi/2005/675/made
[5] Law Commission, Pension Funds and Social Investment 2017, available at https://www.lawcom.gov.uk/project/pension-funds-and-social-investment/
[6] For example MSCI, *Foundations of ESG Investing,* November 2017 available at https://www.msci.com/documents/10199/03d6faef-2394-44e9-a119-4ca130909226
[7] TPR, Guide to investment governance, 2016, available at http://www.thepensionsregulator.gov.uk/docs/dc-investment-guide.pdf

first time it acknowledged the potential for ESG factors to be financially material, and stated that where this was the case such factors should be considered in investment decisions.

Ahead of the publication of this consultation, we noted the concerns of a minority in the sector that the inclusion of climate change in the legislation (as drafted 'ESG, including climate change') was unnecessary or undesirable. The Pensions Regulator's 2016 DC Code of Practice explicitly acknowledged the financial materiality of climate change, over both the short-term and long-term, and that trustees should 'therefore decide how relevant these factors are as part of [their] investment risk assessment'. Despite this, a survey of pension professionals following the publication of the investment guidance found that 53% did not see climate change as a financially material risk to their own or their clients' portfolios.[8] The Chair of the HSBC pension scheme and special adviser to the Taskforce on Climate-related Disclosures, Russell Picot, has previously said "Climate risk is present in every investment portfolio I can think of". This is a major problem and the Government should consider it as such.

We also heard some opposition to the inclusion of the phrase 'including climate change' because climate change is "today's issue" or that "it will lead to a long list of other ESG factors being referenced in legislation". Let us be clear, climate change must be included in the legislation not just because it is financially material, but because it is the biggest and most urgent ESG factor, it is intrinsically linked to other ESG factors and because in many cases has the potential to exacerbate other risks. However, we also accept the Government's argument not to refer to this exclusively, in order to avoid being too prescriptive and agree that over time industry terminologies change. We want to future-proof this legislation (we note the position whereby the "SEE" clause became obsolete over time) by ensuring that, as the financial services sector moves forward, innovation in the sector is not constricted by the way the legislation is drafted.

The Bank of England outlined 3 key risks stemming from climate change: Physical risk, liability risk and transition risk (i.e. risks associated with the global transition to a low-carbon economy), any of which may be relevant to a pension scheme's portfolio. Given the Government's domestic and international commitments to tackle climate change which we have already touched upon, it's clear that even where schemes do not believe the physical impacts of climate change will impact their investments, they need to acknowledge and asses their exposure to other risks stemming from climate change e.g. transition risk. Funds invested in companies like Peabody have already lost value- evidence of both transition risk biting, and that climate risk (and other ESG risks for that matter) can crystallise in the short-term too. Transition risk stems in part from public policy interventions on the part of regulators and governments and represents a wider recognition that as a society we need to address the risks associated with climate change and that finance has a key role to play.

Such interventions include financial initiatives which are partly or wholly intended to help tackle climate change and include (but are not limited to):

- The Paris Agreement;[9]

[8] Professional Pensions, *Climate change is 'overblown nonsense' and not a material risk, says industry,* 26 August 2016 https://www.professionalpensions.com/professional-pensions/news/2468851/climate-change-is-overblown-nonsense-and-not-a-material-risk-says-industry

[9] The Paris Agreement, https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement

- The Sustainable Development Goals;[10]
- The Taskforce on Climate-related Financial Disclosures;[11]
- The High Level Expert Group on Sustainable Finance;[12]
- The Bank of England's research on climate risk and financial stability;[13]
- The Green Finance Taskforce;[14]
- The Transition Pathway Initiative;[15]
- The Institute and Faculty of Actuaries Climate Change Risk Alert;[16]

Climate change is such a significant issue, and can have such an impact on investments, as indeed investment can have on tackling climate change, that policy makers have seen fit to establish this many initiatives. No other ESG factor has this many national and international initiatives reflecting its significance and the urgency with which it should be dealt. We therefore do not consider it too far a step to include reference to it in the regulations.

Many schemes do already consider financially material ESG factors over the short, medium and long-term. However, these schemes tend to be the sector leaders, and this is in spite of the regulations as drafted, not because of them. The point of these legislative changes is to aid trustees in carrying out their duties. Whilst many of the leading schemes will not need such assistance, the change to the law will raise standards for laggard schemes, resulting in more robust investment policies, as well as increased consistency, across all UK trust-based pension schemes. We see great value in investment guidance from TPR to supplement the regulations, but given past experiences of the efficacy of guidelines in changing behaviour, it seems clear trustees' fiduciary duty must be clarified in law in this manner.

It is important to also understand why the current drafting of the regulations is inadequate. A key problem for trustees, and driver of the confusion around what they can, should and must consider is the wording of the Investment Regulations. As drafted, the regulations require trustees to report their policy on 'the extent (if at all) to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments'. At the time it was drafted this "SEE" clause was a very progressive inclusion in the legislation, following an UKSIF-led campaign. However, societal expectations, our understanding of the science of climate change, and the ability of the financial services sector to better understand financial risk and opportunity have overtaken the regulations. The consultation paper correctly notes three key reasons the wording of the existing regulations has proved to be misleading:

- It conflates purely ethical considerations (which trustees may consider in some circumstances) with social and environmental considerations (which trustees must consider if they are financially material);

[10] The Sustainable Development Goals, https://sustainabledevelopment.un.org/sdgs
[11] The TCFD, https://www.fsb-tcfd.org/
[12] HLEG final report available at https://ec.europa.eu/info/sites/info/files/180131-sustainable-finance-final-report_en.pdf
[13] BoE, *The Bank's response to climate change*, June 2017 available at https://www.bankofengland.co.uk/climate-change
[14] GFT, *Accelerating Green Finance*, March 2018 available at https://www.gov.uk/government/publications/accelerating-green-finance-green-finance-taskforce-report
[15] Transition Pathway Initiative http://www.lse.ac.uk/GranthamInstitute/tpi/
[16] IFoA, *IFoA warns on climate change financial risks*, May 2017 available at https://www.actuaries.org.uk/news-and-insights/media-centre/media-releases-and-statements/ifoa-warns-climate-change-financial-risks

- It limits broader financial considerations which trustees may consider to social and environmental;
- The use of 'if at all' suggests trustees may choose not to consider such factors, even when they are financially material.

These are legitimate reasons to amend the wording via the draft legislation. In practical terms, the confusion created by the legislation has been a barrier for some trustees in meeting their fiduciary duties. But it poses problems elsewhere too. For example, the UK Government has commitments under the Climate Change Act to reduce greenhouse gas emissions by 80% compared with 1990 levels by 2050. In addition the UK's ratification of the Paris Agreement commits the Government to help to keep global warming to well below 2°C and to pursue efforts to limit it to 1.5°C. The transition to a low (or net-zero) carbon society will be unachievable without private investment, with an estimate of $93 trillion needed for investment in low carbon infrastructure globally over the next 15 years.[17] Clarification of the duties of pension scheme trustees represents a clear policy signal that the UK Government is committed to tackling climate change, and a necessary policy shift to enable the UK economy to take account of climate risk. We welcome the work of the Green Finance Taskforce, whose recent report argues that 'informed investors are willing to act on clean investments, especially when schemes are required to specify a policy in relation to ESG risks.'[18]

The draft regulations also help to meet policy intent across Government. In December 2017 the Treasury outlined its priorities for the asset management sector in the second UK Investment Management Strategy. These included social and impact investment, green finance and Islamic finance. Amending the legislation will also help the fund management sector to meet a growing demand for these specialist services at the institutional level.

We note and accept the Government's argument that whilst many financially material risks such as ESG are long-term, they are not so exclusively. We have already discussed our research showing fund manager expectations of the valuation of international oil companies to be significantly impacted by climate risk within the next two years as an example of this. The Kay Review found that short-termism is a problem in UK equity markets and stated that 'equity investment… serve[s] the long-term interests of promoting economic growth in the UK, and the interests of beneficiaries taken as a whole.'[19]

Due to Kay's conclusions we feel it would be disappointing to lose all mention of the 'long-term' in the legislation. Whilst risks and opportunities may arise in the short, medium and long-term, pension schemes – especially those into which most people are now being automatically enrolled – have long-term investment horizons and consequently should have long-term investment strategies. We acknowledge the Government's assertion that the use of long-term may create the impression for some trustees that there are no short-term impacts to be considered. However we believe the

[17] Green Growth Platform, Financing the Low Carbon Transition, available at https://www.cisl.cam.ac.uk/publications/publication-pdfs/financing-the-global-low-carbon-transition.pdf
[18] Green Finance Taskforce, *Accelerating Green Finance*, 2018 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/703816/green-finance-taskforce-accelerating-green-finance-report.pdf
[19] Kay Review, 2012 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/253454/bis-12-917-kay-review-of-equity-markets-final-report.pdf

alternative – that the omission of 'long-term' could lead to the impression amongst trustees that there are no long-term impacts to be considered – is worse. We welcome the recently published Corporate Governance Code by the Financial Reporting Council (FRC) which includes substantial reference to the 'long-term'.[20] Patently this does not preclude corporate boards from taking account of shorter-term concerns, but does help to emphasise the importance of value creation over the long-term.

The potential problem of trustees not understanding that ESG can be material over the short-term is something which can be rectified with appropriate guidance from TPR. The inclusion of 'long-term' in the legislation will help to focus trustee minds on the long-term nature of investment and send a strong signal to other intermediaries in the investment chain. Therefore we would welcome the following:

> *(3) A statement of investment principles must be in writing and must cover at least the following matters-*
> *(b) their policies in relation to-*
> *(vi) financially material considerations, including how those considerations are taken into account in the selection, retention and realisation of investments including over the long-term;*

The Government's consultation paper makes some remarks about the language being used in the consultation paper.

With regard to the use of the term 'sustainability', we agree that it should be omitted from the legislation. UKSIF is a staunch advocate for sustainable and responsible investment in the UK, but we are also aware that sector jargon can be interpreted differently or take on different definitions over time. In the context of the legislation the term sustainability has the potential to create confusion over the purpose of the pension, being read as environmental, financial or corporate sustainability. In addition the European Commission are currently looking at definitions in a proposed European Union taxonomy for sustainable finance. As part of this they may seek to define 'sustainable investment'. It would be unfortunate if an EU definition influenced UK pension practice. A key purpose of amending the legislation is clarity for end users and it makes sense omit the use of 'sustainability' in this instance.

Engaging with investee companies on corporate governance is a crucial part of an investor's fiduciary duty. However increasingly it is being recognised that investors can and should engage on governance issues across other asset classes too. There may be other asset classes than equity within a portfolio which may suffer from risks linked to governance issues such as infrastructure or fixed income and trustees should be encouraged to engage on these issues where they are material.

The Government is right to note the difference between social factors as part of ESG which may pose a risk or an opportunity to investors, and social impact, an emerging asset class. Again, clarity for end users is the goal of the amendments outlined by the Government and the use of the term 'social impact' in the description of ESG – a departure from the currently well understood terminology – would not help to achieve this goal. Again, the European Commission is proposing various definitions

[20] FRC, A UK corporate governance code that is fit for the future, July 2018 available at https://www.frc.org.uk/news/july-2018/a-uk-corporate-governance-code-that-is-fit-for-the

of ESG in its consultations on amending the MiFID II and Insurance Distribution Directives, and the risk of confusion should be minimised.[21] Whilst no one has "ownership" of the language, UKSIF has called for consistency in the way such terms are used, particularly in legislation and regulation. We are satisfied with the approach being taken by the Government here.

Q3: When trustees prepare or revise a SIP, we propose that they should be required to prepare a statement, setting out how they will take account of scheme members' views.

a) Do you agree with the policy proposal?
b) Do the draft regulations meet the policy intent?

Yes.

The Law Commission was clear when it said that:

> *'Although financial return should be trustees' predominant concern, the law is sufficiently flexible to allow other, subordinate concerns to be taken into account in some circumstances. The law permits pension trustees to make investment decisions that are based on non-financial factors (such as environmental and social concerns), provided that:*
>
> *1) They have good reason to think that scheme members share the concern; and*
> *2) There is no risk of significant financial detriment to the fund.'*

This is the context in which the consultation asks this question and in which we frame our response.

Engagement rates between UK pension funds and members are extremely low.[22] There are many reasons for this: a lack of financial literacy on behalf of UK savers, employers merely doing the statutory minimum to tick the "compliance box", and the belief that people simply do not have a say in how their pensions are invested.[23] Automatic-enrolment has been a huge success in the UK and has resulted in 9 million new savers (or people saving more). However, it was a policy introduced to bypass the lack of engagement in UK pensions, not to address it. Poor engagement is a problem which persists.

UKSIF believes that more and better engagement between schemes is both a desirable outcome and an achievable one. One way in which this could be achieved is through better communications from the fund on how it creates a positive impact to society or to the environment. The demand is clearly there, and 47% of the British public want to make both money and a positive difference to the world.[24] A crucial problem is that often, even when funds are "doing good", this information is rarely communicated to members or when it is, members are not aware of it. For example, statistics for Good Money Week 2017 showed that 76% of the public with a pension don't know how much, if any, of their pension fund is invested ethically. Further, companies cannot afford to dismiss their

[21] European Commission legislative proposals on sustainable finance, available at https://ec.europa.eu/info/publications/180524-proposal-sustainable-finance_en
[22] Just 12% of firms happy with workforce pension engagement, Professional Pensions, March 2018 available at https://www.professionalpensions.com/professional-pensions/analysis/3029328/just-12-of-firms-happy-with-workforce-pension-engagement
[23] Research for UKSIF during Good Money Week 2017 showed that 30% of savers believe they have no say in how their pensions are invested, *Good Money Week Public Polling Report 2017*, available at http://goodmoneyweek.com/sites/default/files/download/public_polling_report_2017_gmw.pdf
[24] Ibid.

employees' values as irrelevant: 25% of people would challenge their employer if they found out their pension was invested in a company that acted against their personal values.[25] Better engagement on pensions can also be a key tool for companies in attraction, retention and development of talent.[26]

We note there has been some considerable confusion about the intent of the proposed policy on members' views and the effect the introduction of such a policy as drafted could have. There are three key points which the Government should make far more explicit with the dual aims of providing more clarity for trustees over what is expected of them in this regard and to quell opposition to a much needed policy intended to help to tackle the problem of low engagement rates.

First, is worth restating that, as drafted, the regulations require a statement from schemes on *the extent* to which member views are considered. They would not require schemes to take account of members' views if they do not wish to do so, although this would need to be stated. There has been considerable confusion on this point, particularly in the trade press since the Government's consultation document was published, and it should do more to clarify exactly what the proposal would require of schemes.

Second, the Law Commission has been clear in setting out the two stage test referred to earlier for when trustees *may* consider such views i.e. that scheme members share the concern and that there is no risk of significant financial detriment to the fund. With regard to the former there is an obvious difficulty for trustees in attaining members' views and, since unanimity of views is extremely rare, judging whether the proportion of members with that view is sufficient to act upon it. The Law Commission's 2014 report was helpful in this regard:

> '*We think that the courts would judge the issue in the round, focusing on whether trustees applied their minds to the right question and sought an answer in a reasonable way… We do not think that there needs to be 100% agreement. If a majority are opposed to an investment while the rest remain neutral, we think that would be enough*.'[27]

Its 2017 report went further:

> '*The more difficult question is where a significant number hold one view but a minority disagree strongly. We said that where the issue was clearly controversial, the courts would expect trustees to focus on financial factors, rather than becoming embroiled in disagreements between the members on non-financial factors.136 If the issue is not*

[25] UKSIF submission to Work and Pensions Select Committee Inquiry on Freedom and Choice in Pensions, November 2017, available at http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/work-and-pensions-committee/pension-freedom-and-choice/written/71896.pdf
[26] CBI and Aegon, *Engaging with Saving*, March 2018 available at http://professionalpensions.com//digital_assets/37451f54-6e19-49fa-a9ae-77e72e47b49d/CBI_Aegon-Pensions-report-2018.pdf
[27] Law Commission, Fiduciary Duties of Investment Intermediaries, 2014 available at https://www.lawcom.gov.uk/project/fiduciary-duties-of-investment-intermediaries/

> *controversial, and there is good evidence of agreement from some people, we think that trustees may act on these views even if many people fail to engage.'*[28]

Polling for Good Money Week showed that 30% of people thought they had no say in how their pension assets are invested.[29] This is incorrect and UKSIF believes that, where appropriate, schemes should consider the views of members. TPR has published guidance for trustees on how such views may be sought which we welcome.[30] As a side note, and as we have expressed to you in meetings, we have some reservations on the extent to which Government treaties may be used as a vehicle to intuit member views. We accept that this was the conclusion of the Law Commission which gave the example of the Convention on Cluster Munitions. Our view is that it is not the agreement signed by the UK Government itself that means people find investment in cluster bomb manufacturing is wrong, nor would the lack of such a treaty have any impact on such views. It is the idea of cluster bombs themselves rather than the political or legal agreement signed by a national Government that drives the ethical view.

The latter test is relatively more straight forward, stemming from *Harries v Church Commissioners*[31] and requires that there is no risk of significant financial detriment and that trustees must seek professional advice on the issue.

Finally, when trustees have the views of members they do no need to act on them. Of course, in an ideal world engaged schemes would be able to collate members' views on non-financial issues and where appropriate consider them as they design their investment policies. They do not have to do so, however, and the Law Commission again provides some clarity:

> *'Trustees may consider the views of the beneficiaries when making their investment decisions, but there is no legal requirement for them to do so.'*[32]

The Government should stress these three points in its final response. We have heard the view expressed that trustees seeking members' views are somehow ducking their duties or pushing their investment responsibilities onto scheme members. The Law Commission has noted that investments which take account of members' views on non-financial will only take place '*in some limited circumstances*'. There is a genuine misconception amongst some in the sector that this represents a "cop out" for trustees and that the introduction of such a policy will not enable them to somehow "hide behind" scheme members. Clearly this is neither a desirable situation, not the one being proposed and the Government should make this abundantly clear.

Q4: Do you agree with our proposal not to require trustees to state a policy in relation to social impact investment? If not, what change in legislation would you propose, and how would you address this risk of trustee confusion on this point?

Broadly.

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[28] Law Commission, Pension Funds and Social Investment, 2017 available at https://www.lawcom.gov.uk/project/pension-funds-and-social-investment/
[29] Data available at http://goodmoneyweek.com/sites/default/files/download/public_polling_report_2017_gmw.pdf
[30] TPR, the DC Code of Practice, 2016 available at http://www.thepensionsregulator.gov.uk/docs/code-13.pdf
[31] [1992] 1 WLR 1241
[32] Law Commission, Fiduciary Duties of Investment Intermediaries, 2014 available at https://www.lawcom.gov.uk/project/fiduciary-duties-of-investment-intermediaries/

Social impact is a legitimate form of investment. It is an emerging asset class which is permitted by the law as it stands, and the draft regulations make this clear. Because this is the case, we see no reason that the legislation itself need reference it. Additionally, in line with the justifications used by the Government for omitting the term 'ESG' for fear of it becoming outdated, "social impact investment" is a term which means different things to different people and is likely to evolve. We consider this legislation should be future proofed as far as is practicable and would not benefit from the inclusion of the term social impact investment. We would welcome further guidance from TPR on social impact investment.

Given their nature, social impact investments span the full spectrum of sustainable and responsible investment as the table below shows. Some may achieve above market rate returns whilst others may be more philanthropic in nature. Therefore they may be financially material, non-financially material or be both. It will be up to trustees' discretion to determine when a social impact investment is appropriate. Again, we would welcome guidance from TPR on choosing social impact investments.

Source: Bridges Ventures[33]

Finally, as drafted, the amended legislation refers to 'social impact' as a non-financial matter. We think if the Government is referring to the way in which the investments of the fund may help to address societal challenges then wording that reflects this more clearly would be welcome. We are concerned that the current wording, 'social impact', may confuse trustees who are already considering social impact investments which, as we have outlined may be financially material, non-financially material, or both.

Q5. We propose that trustees should be required to include their policy in relation to stewardship of the investments, (including monitoring, engagement and voting) in the SIP.

- **a) Do you agree with the policy proposal?**
- **b) Do the draft Regulations meet the policy intent?**

Yes.

UKSIF strongly welcomes the Governments recognition that good stewards of capital do more than vote at the AGMs of the companies in which they are invested. Responsible investors are good

[33] LAPF Investments, The case for private equity impact investing, 2016 available at https://www.lapfinvestments.com/2016/08/the-case-for-private-equity-impact-investing-3/

stewards of the investments throughout their portfolio helping to create and add value- on asset classes including listed and unlisted debt, fixed income and alternative asset classes such as direct investments in infrastructure projects.

We welcome the removal of '[if any]' from the current regulations which may have suggested to trustees that it was acceptable to have no position on stewardship or that trustees could delegate it to their managers. Requiring trustees to also have a policy on engagement is also a welcome step forward, and we fully support the expansion of the definition of 'relevant persons' to which trustees should engage with to include companies, managers and other shareholders. Such an expansion makes it abundantly clear that all schemes, regardless of size, are able to have a policy on how they act as good stewards of capital. Additionally the legislation should note that relevant persons may include policy makers and regulators with whom schemes may engage for the benefit of trustees.

At a recent meeting at DWP we noted that it would be preferable for the Government to work with the Financial Reporting Council as it seeks to develop thinking around stewardship duties given the upcoming review of the Stewardship Code.[34] The feeling amongst some stakeholders in the room was whilst engagement between DWP and the FRC was welcome, since the Stewardship Code had traditionally only been utilised by the fund management sector alignment between the two definitions of stewardship was unnecessary. Certainly, under the current regulations, the Stewardship Code has been directed more at managers. The new regulations, with their focus on good stewardship, voting and engagement across different asset classes and expanded definition of relevant persons offer a huge opportunity for the FRC to bring more pension schemes "inside the tent". In addition to signing up to the Stewardship Code to highlight their approach to stewardship, schemes can also join organisations like UKSIF, IIGCC or the PRI.

Q6. When trustees of relevant schemes produce their annual report, we propose that they should be required to:

> **-prepare a statement setting out how they have implemented the policies in the SIP, and explain and give reasons for any changes made to the SIP, and**
>
> **-include this implementation statement and the latest statement outlining how trustees will take account of members' views in the annual report.**

a) Do you agree with the policy proposal?
b) Do the draft Regulations meet the policy intent?

Yes. This is a welcome addition to the regulations and should not be an onerous duty for schemes for the reasons outlined by the Government. A statement setting out how trustees have implemented the policies in the SIP will put "meat on the bones" of schemes' investment policies and help to avoid high level, boiler plate disclosures. The increase in transparency on schemes' investments will help focus trustees' minds, may help to boost engagement and will have a positive impact on holding schemes to account. The statement should be signed by the Chair of the trustee board.

Further guidance from TPR would be welcome, particularly with regard to how schemes' assess and act upon the views of members.

[34] FRC, *UK Stewardship Code*, https://www.frc.org.uk/investors/uk-stewardship-code

Q7. We propose that trustees of relevant schemes should be required to publish the SIP, the implementation report and the statement setting out how they will take account of members' views online and inform members of this in the annual benefits statement.

a) **Do you agree with the policy proposal?**
b) **Do the draft Regulations meet the policy intent?**

Yes. Fiduciaries should be transparent on how they invest beneficiaries' money, and pension scheme members should be able to access information about how their savings are being used. This is a key aspect of boosting engagement and it should not be onerous on schemes to publish this information. In future years some schemes may consider publishing such information to be a competitive advantage in retaining or attracting members.

Q8. Do you have any comments on the business burdens and benefits, and wider non-monetised impacts we have estimated in the draft impact assessment?

The issues which have been discussed are intended to enable trust-based schemes to meet their fiduciary duties. If the burdens involved in meeting these duties are genuinely too onerous for schemes then we suggest they are inadequately resourced and by extension are unable to act in the best interests of their members.

As we have said, we believe it likely that schemes doing sustainable and responsible investment well, and which engage with and listen to members, will have a competitive advantage in retaining or attracting new members to the scheme.

Q9. Do you have any other comments on our policy proposals, or on the draft Regulations which seek to achieve them?

To help schemes consider the risks and opportunities associated specifically with climate change, UKSIF and ShareAction launched a climate change checklist for pension trustees at Ownership Day 2008.[35] This was launched alongside the Pensions Regulator which endorsed the checklist. We recommend this be highlighted as one tool to help schemes properly consider the impact of climate change on their investments.

I hope our answers are clear. If you have any comments or if we can provide clarification on any of the points we have made please do not hesitate to contact me via fergus.moffatt@uksif.org.

Yours sincerely,

Simon Howard
Chief Executive
UK Sustainable Investment and Finance Association (UKSIF)

[35] UKSIF and ShareAction, *Climate Risk – A guide for pension scheme trustees*, 2018 available at http://uksif.org/resources/a-checklist-for-pension-trustees/