20 April 2012

UKSIF

Work and Pensions Committee Inquiry
Governance and Best Practice in Workplace Pension Provision

Submission from the UK Sustainable Investment and Finance Association (UKSIF)

Summary

1. UKSIF welcomes the Select Committee's Inquiry into governance and best practice in workplace pension provision. Our submission primarily addresses responsible investment and ownership. It is increasingly recognised that this is required to enable good member outcomes and therefore supports the Department for Work and Pension's (DWP) efforts to improve the take-up of auto-enrolment schemes.

2. Support for responsible ownership is an increasing focus of interest by the Department for Business, Innovation and Skills (BIS). It has asked Professor John Kay to conduct an independent Review of UK Equity Markets, examining potential measures to boost the long-term performance and governance of UK quoted companies. The Kay Review, whose interim report was published recently, builds on the previous BIS consultation on a long-term focus for capital markets.

3. In addition, following the Walker Review, the Financial Reporting Council (FRC) introduced the Stewardship Code to improve the governance of listed companies by encouraging responsible ownership. The FRC began consultation today (20 April) on selected changes to the Code, with a particular focus on what is meant by stewardship and the respective roles of asset owners, such as pension funds, and asset managers.

4. However, the issue of responsible investment and ownership has not yet been fully joined up with that of workplace pension provision by the Department for Work and Pensions (DWP), despite the importance of protecting the value of pension fund assets for both individual pension members and to maintain trust in pension funds as long-term savings vehicles, as well as the wider benefits to society from well-functioning capital markets and long-term responsible investment approaches.

5. UKSIF's key recommendations for action are:

   a) For the Government and relevant regulators to require or encourage employers to advance long-term responsible investment and ownership. One practical way of doing this would be to encourage or require employers to use the responsible investment approach announced by the National Employment Savings Trust (NEST) as a benchmark and/or minimum standard.

   b) For the Government to take a more 'joined-up' and cross-departmental approach to responsible investment and ownership, explicitly linking policy on workplace pension provision with the Financial Reporting Council's Stewardship Code and the Kay Review of UK Equity Markets.

   c) For Parliament to signal its commitment to long-term responsible investment and ownership practice in the UK through ensuring that the Parliamentary Contributory Pension Fund becomes an example of best practice in this area.

UK Sustainable Investment and Finance • www.uksif.org • Tel 020 7749 9950
Holywell Centre, 1 Phipp Street, London EC2A 4PS
Registered in England, company no. 2541424 • Company Secretary: Pamela Lindegaard

6. This memorandum builds upon UKSIF's previous submission to The Pension Regulator's Discussion Paper 'Enabling good member outcomes in work-based pension provision' and on our submissions to the Kay Review and the BIS consultation on 'A Long-term Focus for Corporate Britain'.

UKSIF would be pleased to provide oral evidence on any of the issues mentioned in this submission.

Introduction

7. The UK Sustainable Investment and Finance Association (UKSIF) supports the UK finance sector to be a global leader in advancing sustainable development through financial services. We promote and support responsible investment and other forms of finance that advance sustainable economic development, enhance quality of life and safeguard the environment. We also seek to ensure that individual and institutional investors can reflect their values in their investments.

8. UKSIF was created in 1991 to bring together the different strands of sustainable and responsible finance nationally and to act as a focus and a voice for the industry. UKSIF's 260+ members and affiliates include pension funds, institutional and retail fund managers, banks, financial advisers, research providers, consultants and non-governmental organisations. For more information about UKSIF, please visit www.uksif.org.

9. UKSIF supports long-term responsible investment and ownership. It focuses its corporate governance support on the interface between governance on the one hand and social, environmental and ethical issues on the other.

Ensuring good Defined Contribution (DC) scheme outcomes through responsible investment and ownership

10. The correlation between good member outcomes in work-based pension provision on the one hand and long-term responsible investment and asset ownership on the other is increasingly recognised by stakeholders and policymakers.

    For instance, the investment approach of the National Employment Savings trust (NEST) includes the following characteristics:

    a) The second of NEST's seven published investment beliefs is "as long-term investors, incorporating environmental, social and governance (ESG) factors within the investment process is in the interests of our members".
    b) NEST will seek to apply responsible investment principles across all the assets in which it invests.
    c) NEST has become a signatory to the UN-backed Principles for Responsible Investment (PRI) and the UK Stewardship Code. [Note: Employers could require this of their pension providers even if, for example, smaller workplace schemes chose not to join PRI directly themselves.]
    d) The range of five fund choices initially available (in addition to the default fund) includes the NEST Ethical Fund and the NEST Sharia Fund.

    Similarly, the Pension Protection Fund (PPF) outlines, in its Statement of Investment Principles, its commitment to "exercising its ownership rights, including voting rights, in order to safeguard sustainable returns in the long-term". It is one of some 250 asset owners worldwide that have signed up to the UN-backed Principles for Responsible Investment (PRI)[1]. Other UK-based PRI signatories include the BT Pension Scheme, the Environment Agency Pension Fund, the London Pensions Fund Authority (LPFA) and the Marks & Spencer Pension Scheme.

11. In addition, UKSIF believes that good member outcomes should encompass support for members' overall well-being as well as the achievement of their narrower financial aims. This includes their ability to reflect their social values and priorities in their pension fund investment decisions when they wish to do this. This is important to support equality and diversity as well as general member welfare and needs to include those decisions which religious members and others with protected characteristics may wish to make.

[1] http://www.unpri.org/signatories/ Accessed 19/04/12

Transparency

12. UKSIF believes that the Committee's terms of reference regarding transparency of charges and costs is too narrow; instead, we think that the Committee should widen its scope to address greater transparency and disclosure of information by DC schemes on responsible investment and ownership principles and beliefs together with how these principles and beliefs are implemented in practice. This would incentivise employers to compete on the long-term responsible investment and ownership practices which they offer to their employees.

13. UKSIF believes that improved member outcomes and wider public benefits would result from requiring public disclosures of workplace DC pension funds' responsible investment policies and how these are implemented. Enhanced disclosure would also enable interested members to integrate their values into their investment decisions, in turn deepening members' commitment to their pension savings. While some DC pension schemes are required to disclose their Statement of Investment Principles to pension scheme members on request, this requirement is not comprehensive or widely understood and there are no requirements related to the disclosure of how these principles are implemented in practice.

Clarity of communication to pension scheme members

14. UKSIF welcomes the Committee's acknowledgement that transparency needs to be tied to good communication to pension scheme members to support their investment decisions and assessment of risks. More specifically, we believe that concise, clear communication about a workplace pension scheme's responsible investment policies and how these are implemented in practice is key to ensuring good outcomes for members.

15. There is clear evidence of employee demand for this; market research conducted by YouGov for UKSIF in October 2011 found that:

    a) A majority of people in the UK wanted the introduction of auto-enrolment to be linked to high standards of responsible investment for qualifying schemes. **58%** of British adults surveyed believed that **employers' pension schemes should match or beat the standard set by the NEST workplace pension scheme** in managing social and environmental issues.

    b) **23%** of British adults with investments felt that their pension fund or financial adviser was doing **too little to inform them of responsible ownership activities**.

    c) **55%** said they **did not clearly understand what their savings and investments support**

    d) **53%** of adults with investments believe financial products that take **social and environmental issues into account have an important, or very important, part to play in the long-term growth of the UK economy**.

    This research suggests that there is both an appetite amongst workplace pension scheme members for investments which are managed responsibly and a lack of understanding about how their investments are currently managed.

16. We are also aware that many major companies which are generally regarded as leaders in sustainable business practices miss the opportunity to educate their DC pension scheme members about long-term responsible investment and ownership. Indeed, often no information is provided to members about the value of good stewardship even when the DC pension provider is a signatory to the Stewardship Code and/or the UN-backed Principles for Responsible Investment (PRI). In addition, employers often fail to provide access to opportunities to invest specifically in sustainability leaders or in companies likely to benefit from demand for solutions to key social and/or environmental problems.

    This is in spite of the market research described above and wide-ranging evidence of the importance of corporate responsibility and sustainable business practices to employees. This research and evidence suggests that clearly-communicated details of the DC pension scheme's responsible investment and ownership practices would assist the employer to attract and retain high quality employees and boost the likelihood that employees would remain enrolled in the pension scheme.

Recommendations for action

17. We propose the following measures as effective steps towards an environment where a long-term responsible approach to investment which delivers high-quality outcomes for members becomes an integral part of pension fund investment practice.

Encouragement of employers to advance long-term responsible investment and ownership

18. To achieve good member outcomes, it is vital that investment managers are incentivised to engage in long-term responsible investment and ownership practices. This requires clear demand for such practices from investment clients.

19. UKSIF therefore believes that the Government and relevant regulators like The Pensions Regulator should require or encourage employers to advance long-term responsible investment and ownership.

20. One practical way of doing this would be encourage or require employers to use the responsible investment approach announced by the National Employment Savings Trust (NEST) as a benchmark and/or minimum standard.

21. A further way would be to encourage or require workplace DC pension schemes to disclose to pension fund members and the general public their responsible investment and ownership policies and how these are implemented in practice.

22. These measures would, we believe, improve the quality of pension provision and deepen member engagement with and commitment to their pension savings.

A cross-departmental approach to responsible investment and ownership

23. While some Government departments, notably the Department for Business, Innovation and Skills (BIS), have shown strong support for responsible investment and ownership, this has not been reflected in a similar level of policy support by the Department for Work and Pensions (DWP).

24. To support good member outcomes as well as wider public benefits, the Government should take a more 'joined-up' and cross-departmental approach to this issue, explicitly linking policy on workplace pension provision with the Financial Reporting Council's Stewardship Code and the Kay Review of UK Equity Markets commissioned by BIS.

A clear signal of commitment from Parliament

25. Parliament should signal its commitment to long-term responsible investment and ownership practice in the UK through ensuring that its own workplace pension scheme offers an example of best practice in this area. This would encourage other workplace pension schemes to improve their practices.

26. Specifically, Parliament could encourage the Parliamentary Contributory Pension Fund (PCPF) to

    a) make a statement of commitment to the Stewardship Code, adding its name to the list of supportive asset owners on the Financial Reporting Council's web site
    b) become a signatory to the UN-backed Principles for Responsible Investment (PRI)
    c) report online its long-term responsible investment and ownership policies and how these are implemented in practice.

27. In addition, Parliament could hold an annual debate on the PCPF's long-term responsible investment and ownership policies and how these have been implemented in practice over the previous year. For example, PCPF trustees could be asked to report to Parliament on how their fund managers have engaged with companies on executive pay and how key votes on this topic have been cast.

Contact details: Caroline Escott, Programme Director & Head of Government Relations
Email: caroline.escott@uksif.org Tel: 020 7749 9950