UKSIF

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David Cook
Financial Services Authority
25 The North Colonnade
Canary Wharf
London E14 5HS
Email: dp09_02@fsa.gov.uk

Dear David

Turner Review and Discussion Paper 09/2

Thank you for the opportunity to comment on these documents. Our response addresses Discussion Paper Question 38: “Are there any lessons which have been learned in other sectors which could be applied to banking?”. We believe that many of our comments are relevant also to other regulated sectors. We have commented additionally on the objectives and governance of the FSA itself.

UKSIF, the sustainable investment and finance association, promotes responsible investment and other forms of finance that support 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. Our overall strategic objective is to ensure that the UK finance sector is the world leader in advancing sustainable development through financial services.

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 200+ members and affiliates include pension funds, institutional and retail fund managers, investment banks, financial advisers, research providers, consultants, trade unions, banks, building societies and non-governmental organisations. For more information, please visit www.uksif.org.

This response is based on our members’ experience within financial services. Social and environmental investment analysts now have up to two decades of practical experience in investment management companies. This has resulted in a deep understanding of the social and environmental opportunities and risks faced by companies and industry sectors, and the barriers to integrating this understanding into City decision making.

Financial reform for a sustainable recovery
Successful financial regulation must not only address the lessons of the credit crisis but also prevent a future climate and resources crisis that would be even more damaging. Financial reform which does not address these future challenges is unlikely to deliver a sustainable recovery. Creating a robust financial services framework for the capital re-allocation and responsible ownership needed to build a low carbon, resource efficient and socially sustainable economy is an essential part of financial reform.

A key indicator of success for financial reform should be the degree to which UK financial institutions take a clearly strategic approach to sustainable development issues. This includes fully integrating carbon intensity and impacts on ecosystems and social sustainability into their decision making.

Stress testing and impact assessment
We recommend that stress testing at the institutional and system levels should address exposure to risks from climate change, resource depletion, aging populations and associated social and political issues.

UK government scenarios might be used for this. Tools should be kept up to date as scientific and other knowledge deepens.

Greater use of environmental impact assessment should be explored both for regulatory changes and in assessing financial institutions. Impact on well-being as well as resilience should also be considered.

ESG issues in corporate governance and executive remuneration
We suggest that the FSA should require all financial institutions to take a "comply or explain" approach to the issues identified in the Association of British Insurers (ABI) guidelines on responsible investment disclosure[1]. This includes requiring ESG matters to be addressed in risk management, board training and access to information, and executive remuneration.

Consultation Paper 08/25 "The approved persons regime – significant influence function review" and Consultation Paper 09/10 "Reforming remuneration practices in financial services" recommend appropriate frameworks for enabling this to take place. We hope that the FSA will give due emphasis to ESG matters during their implementation.

Transparency on ESG issues and Forward Looking Sustainability Strategies
In our view, many financial institutions are still not providing responsible investors and other stakeholders – and hence presumably the FSA itself - with the information that they need to integrate sustainability issues into their analysis. For example, there is often limited forward-looking guidance on the institution's sustainability strategy.

More generally, we are concerned that, when information is not disclosed freely, executives can influence ratings and investment analysis and so prevent an efficient market by withholding key insights from those who draw unflattering conclusions.

We recommend that the FSA, possibly via the UK Listing Authority, should ensure that financial institutions report publicly on a range of relevant ESG information. They should be required to disclose their sustainability strategy and all information provided for financial ratings. Investors should be offered the ability to comment directly on sustainability disclosures and strategies by a separate vote on the enhanced business review, including on a forward looking sustainability strategy.

Rewarding voluntary achievement and encouraging norms
The FSA should publish voluntary indexes and similar assessments of sustainable and responsible behaviour to highlight good practice and set norms. In time, it might reward high ranking institutions more explicitly eg. with lighter touch regulation or lower fees. The Health and Safety Executive's Corporate Health and Safety Performance Indicator (CHaSPI) provides an early example of this type of approach, while the OECD offers an example of success in setting transnational norms, eg. on tax.

In addition, we recommend that financial institutions should be required, on a "comply or explain" basis, to sign and implement appropriate international codes of conduct, such as the Equator Principles[2] and the UN-backed Principles for Responsible Investment[3]. They should be encouraged to work together to develop further codes where material gaps in provision exist.

FSA regulatory objectives, skills and governance
As long ago as 1998, UKSIF expressed concern that the FSA's statutory objectives did not explicitly require it to promote and enable sustainable development. It is now well accepted that the finance sector has an important role to play in addressing future threats to the public interest such as climate change and ecosystems degradation. In the light of this, we suggest that the FSA should review the impact of its regulatory objectives on its ability to take the wider public interest, including sustainable development, into account. This includes the ability to integrate societal risks, such as climate change and demographics, effectively into stress tests and to use "soft regulation" measures to encourage socially and environmentally desirable behaviours. If appropriate, it should make representations to government to enable it to adopt a wider remit.

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[1] Available at www.abi.org.uk/Members/circulars/viewAttachment.asp?EID=15636&DID=14121.
[2] Details at www.equator-principles.com/index.shtml.
[3] Available at www.unpri.org.

We suggest that the FSA should review also its board composition to ensure sufficiently wide knowledge and experience of sustainable development and sufficiently strong challenge on both consumer issues and the wider public interest.

In addition, we recommend that the FSA should keep under review and, where necessary, improve its skills in understanding and addressing sustainable development; and regulators worldwide should share skills in addressing public interest issues such as this.

With best wishes

Penny Shepherd

Penny Shepherd MBE
Chief Executive
UKSIF – the sustainable investment and finance association