UKSIF
UK Sustainable Investment and Finance Association

<u>Environmental Audit Committee Inquiry</u>

<u>The Government's Approach to Sustainable Development</u>

<u>Written Evidence from the UK Sustainable Investment and Finance Association (UKSIF)</u>

Thank you for the opportunity to respond to the Environmental Audit Committee's inquiry on the Government's approach to sustainable development. The UK Sustainable and Finance Association is the membership network for sustainable and responsible financial services in the UK. We promote and support responsible investment and other forms of finance that advance sustainable economic development, enhance quality of life and safeguard the environment.

UKSIF's 240+ members and affiliates include financial advisers, institutional and retail fund managers, pension funds, banks, research providers, consultants and NGOs. For more information about UKSIF, please visit www.uksif.org.

<u>What key policies are needed over the course of this Parliament to adequately protect the environment, promote growth in the low carbon sector and improve wellbeing?</u>

It is absolutely right the Government prioritises protecting the environment, promoting growth in the low-carbon economy and improving wellbeing and push for an ambitious deal at COP21. Our responses to your questions are confined to financial considerations and policy changes which we believe would have a positive influence on the Government's approach to Sustainable Development.

<u>Fiduciary Duty</u>

1. Deciding where and how UK savings are invested can have a substantial impact in a range of policy areas. It is for that reason that we believe one small change to the investment regulations - to clarify the fiduciary duties of investment intermediaries - could have a significant impact on sustainable development in the UK. The Government is currently reviewing responses to DWP's consultation on changes to the occupational pension scheme regulations (OPSR) and, as we argued in our submission[1], it is crucial the recommendations put forward by the Law Commission are implemented.

2. The proposed changes would clarify in law that when investing, trustees of defined-benefit (DB) pension schemes *should* take financially-material environmental, social and governance (ESG) factors into account and, in certain circumstances, may take non-financial factors into account. The changes would also encourage investors to act as good stewards of capital through engagement with investee companies. These are the findings of the Law Commission report which examined the law relating to the fiduciary duties of investment intermediaries in 2014, yet there remains confusion over the responsibilities and duties of trustees. It is essential that the Secretary of State for Work and Pensions implements these changes to the OPSR which could have a dramatic effect on the way money is invested in the

[1] Available at http://uksif.org/wp-content/uploads/2015/04/UKSIF-Response-to-OPSR-Consultation.pdf

UK and increase the amount of money that will flow to the low-carbon sector.

3. The UK is already the biggest Sustainable and Responsible Investment (SRI) market in Europe and three recent examples which show institutional investors are recognising their duty to be long-term stewards of capital include:

   - The Pension Fund Roundtable (PFR), consisting of sixteen funds with assets of over £200bn, published a report outlining expectations on ESG and stewardship reporting.[2]

   - The Association of Member Nominated Trustees (AMNT) has announced the launch of its "Red Lines" voting initiative under which DB trustees will issue voting directions to fund managers.[3]

   - In April the "Aiming for A" coalition, organised ahead of the BP plc AGM, persuaded the company to adopt a series of policies linked to environmental assessment.[4]

4. However, these initiatives have taken place *despite* the UK's regulatory environment, not because of it. Regulatory certainty in this area - i.e. clarifying that trustees should consider financially-material ESG factors and may consider non-financial factors - could have a huge impact and greatly increase the amount of capital flowing towards responsible investments such as climate change adaptation and mitigation projects as well as investments intended to have a positive social impact. The Government must therefore ensure the proposed changes are implemented in full.

5. The dawn of pension auto-enrolment has meant there will be up to nine million more savers by 2020. These savings will be held in defined-contribution (DC) schemes and as such will not be affected by any positive changes to the OPSR which only affect DB schemes. It is therefore important that not only the OPSR is changed to reflect Law Commission guidance, but that "fiduciary standards" are also introduced for DC schemes. In particular, these standards should be placed upon the Independent Governance Committees, which examine the performance of default schemes.

6. Determining where our savings are invested can have a huge positive impact on protecting the environment, promoting growth in the low-carbon sector and improving wellbeing *as well as* providing good returns, all at negligible cost to the tax-payer.

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[2] Available at http://www.uss.co.uk/UssInvestments/Responsibleinvestment/Documents/guidetoRIreportinginpublicequity.pdf

[3] More information available at http://www.engagedinvestor.co.uk/could-red-lines-help-small-schemes-invest-responsibly/14746360.article

[4] More information available here https://www.churchofengland.org/media-centre/news/2015/04/98-vote-for-climate-change-resolution-at-bp-agm.aspx

Transitioning to a low-carbon economy

7. The Government must take serious steps to promote the transition to a low-carbon society. This includes its efforts to tackle climate change and decarbonise the UK economy. The Secretary of State for Energy and Climate Change recently announced her Department's priority was to "power the economy while decarbonising in the most cost-efficient way". However, with recent announcements to reduce spending on renewable energy subsidies the Government's focus seems to have moved away from the decarbonisation aspect. Investor confidence is key for renewable projects. Introducing changes to these subsidies makes these projects less attractive to potential investors over the short-term and this represents another example of policy risk involved in renewable investment. Some low-carbon infrastructure projects can take over ten years to build, which is why investors need long-term policy predictability. The reduction in confidence that results from these policy changes is detrimental to the transition to a low-carbon economy.

8. Context is important here. The announcement on the renewables shake-up comes at a time when the world is preparing to come together at COP21 to agree an ambitious deal to limit global temperatures to 2C. This is a global effort unlike anything we have experienced before, and leadership is required from the UK. We are extremely concerned about the signal we send out to our international partners with policy changes like these. Countries such as the United States have taken big steps towards reducing greenhouse gas emissions and have recently announced the 'Clean Power Plan' which aims to cut emissions from US power stations by a third within 15 years. In contrast, this Government is prematurely ending support for one of the cheapest renewable energy source in the UK, continues to subsidise the fossil fuel industry and undermines the commitment to an 80% reduction in emissions by 2050.

9. A lack of consistency on domestic policies makes it more difficult for the UK to meet its legally binding climate change targets or to show leadership in Paris in December; it risks rendering any rhetoric on the need for both developed and developing nations to curb their own emissions meaningless.

Does the Government's current fiscal and legislative agenda accord with the action required and, if not, why not and where might it be improved?

10. The consultation on the OPSR has ended and submissions are currently being reviewed by the Government. There is some apprehension within the SRI industry that, because the consultation took place before the general election, the new Government will either water-down potential changes to the OPSR or not implement any at all. This would defy the substantial work and recommendations of the Kay Review of *UK Equity Markets and Long-term Decision Making* in 2012, the Cox report on *Overcoming Short-termism within British Business: The key to sustained economic growth* in 2013 and the Law Commission report on the *Fiduciary Duties of Investment Intermediaries* in 2014.

11. We do not believe the Government's current fiscal and legislative agenda fully accords with action required to fight climate change globally as stated already.

Where should responsibility lie in Government for ensuring the sustainable development approach is adopted by all Government departments?

12. Sustainable development represents some of the most serious group of issues facing humanity. If the Government is serious about embedding sustainable development into the way the UK is governed then it should ensure responsibility sits explicitly with the Prime Minister. Recognising the mechanics of government, it could also be made a priority objective at the Treasury and incorporated it into the Chief Secretary to the Treasury's brief. The CST is responsible for public expenditure, including on spending reviews and strategic planning, capital investment and infrastructure deals and is therefore well positioned to ensure a sustainable development approach is incorporated throughout government.

13. Having a minister within the Treasury take ownership of this agenda would also help tackle the perennial concern that it may represent an obstacle to sustainable development. In 2013 it emerged that HMT blocked a review of the impact of climate change and resource depletion which had cross-Whitehall support. Senior economists from DECC, BIS and the FCO had warned of the impact these trends could have on "the UK's potential for sustainable growth, its terms of trade, exposure to commodity price shocks and the security of resource supply." This is one of a number of examples of the Treasury getting in the way of progress on the sustainable development front, and having a minister with a clear responsibility to ensure it is embedded within government would be one way to solve this.

We trust that our comments are self-explanatory, but if you would like any further information or have any questions please do not hesitate to contact us.

Yours sincerely,

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