David Farrar
Private Pensions and Arms Length Bodies Directorate
Department for Work and Pensions
1st Floor, Caxton House
Tothill Street
London SW1H 9NA

7 December 2017

Dear Mr Farrar,

I am writing in my capacity as Chief Executive of the UK Sustainable Investment and Finance Association (UKSIF) with regard to DWP's disclosure of costs, charges and investments in defined-contribution (DC) occupational pensions consultation. You will be aware of our views on many of the questions in the paper through formal and information conversations with my colleague, Fergus Moffatt, and myself over the past 24 months and I would like to thank you for taking the time to meet us.

Our response focuses on chapter 2 of the paper relating to investment disclosures. Before answering specific questions we make some general remarks relating to the Government's proposals to reform rules on the statement of investment principles (SIP).

<u>SIP Extension</u>

We agree with the Government that 'an expanded SIP, published or given on request, may be of interest for the most engaged members who would have further information about the principles trustees have followed in selecting and managing investments'. We think an expanded SIP would not only be of interest to already-engaged members, but the resulting increase in transparency and trust will encourage other members to become more engaged. More joined up thinking throughout Government is crucial to enable departments to achieve their policy ambitions. As it continues to reflect on how it will implement changes to rules governing SIPs, we would recommend DWP fully consider the recently published Corley report which makes two recommendations in this specific policy area:

> *'44. Pension scheme trustees – Statement of investment policies: Trustees to state their policies in relation to stewardship, long-term risks and members' ethical and other concerns in the scheme's Statement of investment principles (as per the Law Commission's recommendations). In addition to include specific policies relating to social impact.*
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> *45. Pension scheme trustees – Expand the Statement of investment principles (over time): Over time trustees may consider including wording in the Statement of investment principles relating to their intent to favour investments with positive impact and/ or to avoid investments with a negative impact.'*[1]

We have long advocated for the law governing the SIP to be updated to properly reflect both the Law Commission's recommendations and current TPR guidance that trustees state their approach to

[1] Growing a culture of social impact investing in the UK, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/664321/Full_Report_Growing_a_Culture_of_Social_Impact_Investing_in_the_UK.pdf

consideration of ESG factors, ethical investment and stewardship. Trustees should be clear on how they take into account financially material factors and non-financial factors.

Regarding the former, a recent survey showed that 53% of pension professionals did not consider climate change to be financially material to their clients' portfolios. This is frankly shocking and we would support amendments to the Occupational Pension Scheme (Investment) Regulations 2005 which reflect the Law Commission's recommendations to enable savers to be sure their investments are being looked after in a prudent manner.

When DCLG updated the LGPS investment rules (and moved from a SIP to an Investment Strategy Statement) it published clear guidance for administering authorities on how these documents should be structured and what information could be published in relation to a fund's investments, including on ethical and social investment. A similar approach by DWP would help to clarify the law for those involved in pension scheme administration, particularly in relation to consideration of non-financial factors.

SIP Publication

UKSIF supports the proposal that schemes should be required to publish SIPs and we agree it would result in more clarity for the general reader. We not only agree that 'the content of the SIP, if not necessarily the entirety of the annual report and accounts, will also be broadly comprehensible, and the requirement to publish might reasonably be expected to encourage greater clarity for the general reader' but feel this is also an essential part of driving transparency and increasing public engagement with pensions.

We recognise that in some cases schemes use boiler plate, 'vanilla' SIPs with standard text to explain positions on a range of matters. We do not, however, consider this to be a justification in itself to reject the proposals for schemes to publish SIPs. This is for two key reasons:

1) A vanilla or boiler plate SIP may well be indicative of a scheme which considers engagement with members to be unimportant. Publication could prompt change when viewed by members and third parties, and lead to more tailored SIPs over time.
2) Many of these boiler plate vanilla SIPs are failing in their application of the rules, with many still referring to the extent to which they consider social, ethical and environmental factors. This not only perpetuates the incorrect assumption that financially material environmental and social issues are of the same importance as non-financial or ethical factors, but it contravenes the rules explicitly set out by The Pensions Regulator in 2016.

QO12. Do you believe that members, and recognised trade unions should have the right to request this information and that the requirement to disclose this on request is proportionate?

It is right the Government focuses on giving members access to information relating to their investments, particularly since being members of DC schemes, the risk lies with the saver. As you are aware, this is different to the position in defined-benefit (DB) schemes. Not everyone will have a direct interest in where their savings are invested; automatic enrolment was necessary precisely because of the disengagement between the public and pensions. However this should not prevent those savers who are interested in how their savings are invested from being able to access that information, nor should it stop the Government and TPR from actively encouraging greater engagement between members and schemes.

Polling from Good Money Week over the past ten years has consistently shown a demand for sustainable and responsible investment products.[2] This may be in relation to more robust investment strategies which consider ESG or which enable savers to reflect their own values to create a positive social or environmental impact.[3] Despite this, over three-quarters (76%) of the UK public with a pension don't know how much, if any, of their pension is invested ethically, while 30% believe they have no say over how their pension is invested. Savers should be made aware that responsible, sustainable and ethical financial options exist.

In some cases disclosure of funds on offer may be seen as a differentiator and could deter – or attract – some candidates from working at a particular organisation. In this example any short-term burdens for trustees should be weighed up against potential long-term benefits for the employer. Our polling backs this up and shows that 25% of people would challenge their employer if they found out their pension was invested in a company that acted against their personal values.

QO13. Do you agree with the proposed timing and penalties for pooled fund disclosure on request? Do you agree with the policy that trustees should disclose the pooled funds invested in over the previous scheme year? If not, what alternatives would you propose?

Information relating to pooled fund disclosures should be disclosed within a reasonable timeframe. This is an issue of trust: Longer waiting times for disclosure of this information may well lead to a decrease in trust amongst savers. This has the potential to undermine the entire point of this exercise, and could even lead to more disengaged members and higher opt-out rates.

We have no comment on proposed penalties.

Our view is that this should be included in the Trustee Toolkit at the earliest possible opportunity. We understand recent rules relating to investment governance for DB and DC trustees have not yet been incorporated by TPR. The new rules should not be overly burdensome on trustees with appropriate training and educative materials within a reasonable timeframe, and the Government should outline its expectations on when such material will be available for trustees.

QO14. Do you agree that restricting disclosure on request to only the pooled funds in which members were directly invested is more helpful to members and less burdensome to trustees?

Yes.

QO15. Do you agree with our proposed policy on disclosure of top-level pooled funds only, combined with 'look through' of unit-linked contracts and mandates to the 'first tier' of underlying pooled funds?

Schemes should be required to outline their approach to ESG, ethical and social investment and how they choose the funds on offer. Access to information on where savings are held will be indicative of

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[2] UKSIF's Good Money Week polling was recently collated and submitted to the Work and Pensions Select Committee and is available at http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/work-and-pensions-committee/pension-freedom-and-choice/written/71896.html

[3] A recent meta-study by Oxford University and Arabesque Partners showed how the integration of ESG factors can drive outperformance: https://arabesque.com/research/From_the_stockholder_to_the_stakeholder_web.pdf

how these policies are implemented in practice and help to increase trust and engagement. Ensuring members have access to information on where their savings are held is key to driving more engagement with pensions and could help to drive higher contributions.

Disclosure of this information by private investors should also help to support the Government's wider policy commitments including on the Paris Agreement, the Climate Change Act, the Green Finance Taskforce and the 25 Year Environment Plan.

QO16. Are there any circumstances where trustees and scheme managers would not be aware and would be unable to obtain information about the pooled funds in which their members are directly invested?

We would view a situation where trustees and scheme managers are unaware or unable to ascertain information on where funds are invested as being concerning yet relatively rare. We welcome the Government's approach to investigating the extent to which this might be the case, since it may breach trustees' fiduciary duty and would only decrease trust and transparency in the financial services sector.

Reporting on ESG and the stewardship activities of fund managers is one area which must improve for two key reasons: First, the state of reporting was such that in 2015 the Pension Fund Roundtable (a coalition of 16 pension funds representing over £200bn AUM) created a guide for schemes to engage with and monitor managers on reporting. It was created specifically with smaller schemes in mind and it may be helpful for DWP to consider it in more detail.[4] Second, the Shareholder Rights Directive requires fund managers to disclose medium to long-term investment risks to schemes.[5] Managers which fail to adequately report on these issues therefore risk losing business and breaching the law.

Our long-standing position has been that investment consultants should improve the ESG advice they give to clients. This was reflected in a recent statement we helped to organise, signed by twelve UK investment consultants committing signatories to raise with clients new investment guidance by TPR relating to financially material ESG factors. We have sympathy with DWP's aims here, but the key point is that the investment consultants – and the fund managers – play key roles in disclosing relevant sustainability information, yet are sectors regulated by the FCA. For the Department to effectively meet its policy intent it must engage properly with the FCA to ensure these actors are not obstructing trustees' ability to provide satisfactory ESG information.

QO17. Do you agree with our proposal that schemes should give standard information about the availability of further information about pension scheme investments in the annual benefit statement?

Yes.

Are there any reasons why this requirement would be burdensome or undesirable?

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[4] The Pension Fund Roundtable, *A Guide to Responsible Investment Reporting in Public Equity,* January 2015 available at https://www.manifest.co.uk/wp-content/uploads/2017/03/Guide-to-Responsible-Investment-Reporting-in-Public-Equity-26.01.15-1-1.pdf

[5] The Shareholder Rights Directive, available at http://eur-lex.europa.eu/legal- content/EN/TXT/PDF/?uri=CELEX:32017L0828&from=EN

No, we welcome the opportunity for members to request more information, but note that financial literacy and awareness should continue to be improved for this to have more impact. This is an area in which Good Money Week tries to play a positive role in raising awareness and was highlighted in the Corley report. This is another area where more joined up thinking throughout government would be helpful, particularly with the Department for Education and HM Treasury.

QO18. Thinking about the current administrative processes undertaken by the scheme, can you give an indication of the additional time/costs of incorporating our proposals into existing processes?

No comment

QO19. Are there any areas where the regulations do not meet the policy intent?

No. The proposals are both proportionate and workable, and meet DWPs policy intent.

QO20. Are there any other proposals in this consultation on which you would like to offer comments?

The Taskforce on Climate-related Financial Disclosures published its final report in June, which made a range of recommendations geared towards the creation of a voluntary reporting framework designed to help businesses disclose climate-related financial information.[6] Disclosure of such information is essential if we are to meet our obligations in the Paris Agreement and limit average global temperature rises to 2°C. The TCFD report published additional guidance for the financial sector and specific guidance for asset owners. We would urge DWP to consider this guidance as it looks to develop policy around what information is disclosed by trustees. We would also highlight a recent report by the PLSA and Client Earth on pension schemes and climate change which makes a range of helpful recommendations.[7]

I hope the views I expressed are clear, if you have any questions or would like to meet in person to discuss this further 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)

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[6] The Taskforce on Climate-related Financial Disclosures, Final Report, June 2017 available at https://www.fsb-tcfd.org/wp-content/uploads/2017/06/FINAL-TCFD-Report-062817.pdf
[7] PLSA and Client Earth, *More Light, Less Heat: A framework for pension fund action on climate change,* December 2017 available at https://www.plsa.co.uk/Policy-and-Research-Document-library-More-light-less-heat