

Consultation response by the APPT ESG committee: Climate and investment reporting: setting expectations and empowering savers

18/11/2021

Q1. We propose to amend the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021 to require trustees of schemes in scope to measure and report their scheme's Paris alignment by adding a requirement for them to select and calculate a portfolio alignment metric and to report on that metric in their TCFD report.

Do you agree with this policy proposal?

Yes. We believe it is important that climate metrics are forward looking wherever possible and that TCFD reporting encourages trustees to take action to be better stewards of capital over the long term. Portfolio alignment metrics are easy to understand and can provide a useful summary to stakeholders however data in this area is patchy so while we welcome its inclusion, it is sensible that targets using this metric are not required of schemes at the present time.

Q2. We propose that

(a) trustees who are subject to the requirements in Part 1 of the Schedule to the Climate Change Governance and Reporting Regulations on or after 1 October 2022 (including trustees to whom the requirements are re-applied in accordance with regulation 3(4), 4(4) or 5(4)) will be required to select, calculate and report on a portfolio-alignment metric and to publish the findings in their TCFD report within 7 months of the relevant scheme year end date in the same way as they are for other metrics.

Do you agree with these policy proposals?

Yes

Q3. We propose to incorporate the requirements to measure and report a portfolio alignment metric into the existing Climate Change Governance and Reporting Regulations so that the requirements are subject to the same disclosure and enforcement provisions as the other metrics requirements.

Do you agree with this policy proposal?

Yes

Q4. (a) Do you have any comments on the draft amendments to the Regulations?

(b) Do you have any comments on the draft amendments to the statutory guidance?

Please include in your answer any comments you have on whether you consider that they meet the policy intent stated in this chapter.

We particularly welcome comments on the definition of a portfolio alignment metric and whether respondents think it reflects the policy intent?

The definition was left intentionally broad to allow a range of approaches which we can see the logic for however if the intention is that this information is used by stakeholders to engage with companies or asset managers then it needs to be consistent.

Q5. Do you have any comments on the new regulatory burdens to business and benefits of requiring schemes to measure and report their Paris alignment?

Consistent data being requested will help reduce costs so mandating disclosures and aligning what trustees need to report on is key. Data needs to be audited to be of use, any self-reported data runs the risk of trustees / managers inadvertently rewarding those that deliberately understate their climate impact.

Many schemes, especially smaller schemes, are heavily reliant on investment consultants to lead the process. Greater standardisation of approach and data will help avoid this exercise becoming a high-cost modelling project. Standardisation would also help focus the trustees on making positive impact in terms of outcome rather than focusing on the intricacies of the modelling.

Q6. Do you have

(a) any comments on the impact of our proposals on protected groups and/or how any negative effects may be mitigated?

(b) any evidence on existing provision made by trustees in response to requests for information in alternative accessible formats?

(c) any other comments about any of our proposals?

Chapter 2 – Stewardship and the Implementation Statement

Q7. Should DWP include a vote reporting template in its implementation statement guidance which trustees are expected to use? If so, should such a template be based on the PLSA's vote reporting template? What changes, if any, would be needed to the PLSA template if it were to be adopted?

What are your views on the adoption of an engagement reporting template? Should it be separate from any vote reporting template or integrated with it, so that – in relation to equities – both voting and engagement activities are described for the same set of assets?

Disclosure is only useful in so far as it allows people to take decisions or direct their engagement activity. Reporting the voting activity in the implementation statement doesn't in our view help with this objective. We do not believe the PLSA template is appropriate for all schemes, it assumes boards will want to define their own voting policy and determine for themselves what 'significant votes' are. We strongly believe that this is a role that is not appropriate for all trustee boards as many do not have the skillset or governance budget to do this. E.g. why should trustees have to establish whether cyber security or female representation on a board is a more important issue for each individual company within a portfolio of many stocks.

In addition the way in which asset owners can influence behaviour is through acting collectively. Each board having a slightly different policy to report against does not give a consistent message to the underlying companies and is very time consuming for asset managers who could better spend that time on budget on actual engagement activity. Instead asset managers should be identifying which votes are significant for each company based on their sector, business plan and stated climate and ESG policies. The role of the trustees is then to challenge the choice of votes, if they feel that the manager is giving undue prominence to certain votes. Guidance could recommend that reporting is done vs the UN SDG's, trustees then have a consistent framework to use to engage with

asset managers and see where their voting behaviour is at odds with their rhetoric on climate and ESG issues.

Q8. Do you have any comments on our cross-cutting proposals for the draft Guidance on Statements of Investment Principles and Implementation Statements,

in particular that:

(a) they are written for members?

Both the SIP and Implementation statement are far too long and contain far too much detailed information to be read or understood by members. It is unrealistic to expect members to read and digest the content being suggested. The pensions industry has for many years issued long complex documents like this and spent no time on articulating why members should care about the information. Members would be better engaged through short videos on particular topics that might be of interest e.g. showcasing the ESG policy and the changes made as a result of targeting net zero. The guidance should allow for this kind of flexibility.

(b) these are trustees' statements, not their consultants'?

The required content and data requirements to complete the implementation statement mean that in practice considerable consultant input is likely to be required. They are both seen as 'tick box' compliance exercises by most trustee boards and the new guidance would not change this.

(c) Implementation Statements should set out how the approach taken was in savers' interests?

This element runs the risk of adding content that doesn't add much to implementation statements. Further guidance would be required to clarify what is in savers' interests, for example whether it is strictly financial interest relating to risks (including climate) in particular companies, or if it draws on the concept of a universal investor benefiting from improved returns generally as standards improve.

(d) trustees should be able to include material from voluntary disclosures, such as Stewardship Code reporting, as long as they meet the requirements in the Regulations?

We would question the purpose of including these, and challenge whether or not it helps the reader or trustee take any action.

Q9. (a) Do you have any comments on our proposed Guidance on stewardship policies?

As noted above, trustees driving the focus of engagement topics for asset managers is the wrong way around and dilutes the opportunity for meaningful collective action. A consistent framework such as the UN SDG's would provide all stakeholders with what is needed i.e. a way of engaging consistently and setting standards of behaviour for both asset managers and companies. It would also make it more apparent when managers were talking a good game on ESG a climate issues and then behaving in a different way.

(b) Do you have any comments on our proposed Guidance on significant votes?

Trustees rarely have the governance budget to determine the significant votes for every company within their portfolio – the volume of holdings and voting activity is simply too high. Asset managers, who are significantly closer to the companies than trustees are much better placed to make this judgement call. A consistent framework such as the UN SDGs would help all stakeholders engage with the process.

Q10. Do you have any comments on our proposed Statutory Guidance on the information to be included in the Implementation Statement with regard the requirements under the Disclosure Regulations, Schedule 3, paragraph 30(f)(i)-(iv)?

The implementation statement is too long and contains far too much information to be a decision useful document. These changes do not address that.

Q11. Do you have any comments on our proposed Statutory Guidance on meeting the Implementation Statement requirements in the Disclosure Regulations relating to choosing investments?

The purpose of the document needs to be clearly defined. Including a statement that investments were chosen in line with section 36 of the Pensions Act 1995 is unnecessary for pensions professionals and meaningless to most members.

Q12. Do you have any comments on our proposed Guidance on meeting requirements in the Investment Regulations and Disclosure Regulations relating to investment strategy?

Having clearly defined requirements based on a specific audience would be more useful. The regulator will require more detail on this than is useful to members. Where things are delegated to asset managers this should be recorded as for example voting activity is delegated to pooled fund managers.

Trustees being expected to explain the extent to which this is in members' interests. This is ambiguous and clarification would be required to get a meaningful response.

Q13. Do you have any comments on our proposed Guidance on meeting requirements in the Investment Regulations and Disclosure Regulations relating to financially material considerations (including ESG and climate change)?

- The draft non-statutory Guidance on the SIP sets out that processes should be in place for ESG issues to be integrated into trustees' investment decisions. This may include – for example – that tenders and mandates contain requirements to integrate ESG into investment decisions, minimum standards for tendering firms and trustee commitments on monitoring and reviews. This is sensible and should be how all schemes are governed however adding a statement on this does not add value to the reader as its too long and complex for members and the regulator already has this expectation.
- Some activity is delegated to fiduciary managers and asset managers. E.g. trustees cannot dictate individual voting activity especially on pooled funds.
- The IS should explain any outcomes of work relating to ESG carried out by the trustees or others on their behalf. Trustees are expected to explain how this is in members' interests. This is going to make the IS incredibly long where schemes are taking action to invest differently in light of their ESG policies. This needs further clarification as to whether it is at portfolio or company level.

Q14. Do you have any comments on our proposed Guidance on meeting requirements in the Investment Regulations and Disclosure Regulations relating to non-financial matters?

Gathering member views on topics is expensive and the responses are often limited so care needs to be taken when interpreting the results of such engagement. When schemes are investing through pooled funds, it is difficult to generate any meaningful action. Members will have different views on what topics are most important to them, and relaying this diversity of views to asset managers isn't particularly helpful in guiding them to voting or engaging in a particular way. It also risks acting as a

disincentive to member engagement if they have a way of expressing a view and that is then not acted on.

Q15. Do you have any comments on our proposed Guidance on meeting requirements in the Investment Regulations and Disclosure Regulations relating to arrangements with asset managers?

Adding this detail to SIP's and IS's adds additional complex information that make these documents even harder for members to understand. It is difficult to see how disclosing this information in these statements will lead to different outcomes – a trustee board willing to disinvest on ESG grounds, would disinvest regardless of the information being included in the SIP or IS. Requiring disclosure on these points will not change that. What could change asset manager behaviour is agreement on minimum standards on voting and engagement against a consistent set of standards (e.g. UN SDG's) that the pension scheme industry demands with one collective voice.