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Pension Partnership

Corporate Governance and Stewardship
Financial Conduct Authority
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Dawn Turner
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30 April 2019

Dear Sir or Madam,

We welcome the opportunity to respond to the Financial Conduct Authority (FCA) and Financial Reporting Council (FRC) consultation of their discussion paper – *Building a regulatory framework for effective stewardship.*

As the Chief Executive Officer of Brunel Pension Partnership (Brunel), I present our views from the perspective of pension funds and their beneficiaries. Brunel brings together £30 billion investments of 10 like-minded Local Government Pensions Scheme funds, which provide for around 700,000 pension beneficiaries.

In summary, we are strongly supportive and commend the definition of Stewardship: '**Stewardship is the responsible allocation and management of capital across the institutional investment community to create sustainable value for beneficiaries, the economy and society**.' We agree with it in its entirety and would urge the FCA and FRC to resist those who wish to see it weakened.

We feel this definition is broad enough to encompasses a range of stewardship models, applies globally, to all assets classes and does not limit accountability to certain parts of the investment chain. It recognises stewardship at the asset allocation level and not just with regards to the companies in which we invest. We welcome the explicit recognition of beneficiaries to whom we are accountable. The definition implicitly recognises that broader impacts on the economy and society will impact on investments, particularly for large, long-term asset owners such as ourselves. We feel this definition of stewardship resonates with our own stated values, particularly of '**investing for a world worth living in**' and the aim of our responsible investment strategy in that "**Brunel aims to deliver stronger investment returns over the long term, protecting our clients' interests through contributing to a more sustainable and resilient financial system, which supports sustainable economic growth and a thriving society**."

Responsible Investment (RI) and Responsible Stewardship are part of our 12 investment principles. Our Stewardship Policy sets out our approach and underpins many of the comments made in response to the consultation. The key aspect of our **stewardship policy is that it is considered across all asset classes**. Operationally each asset class will require its own approach and we recognise there will be some areas in which there is minimal stewardship activity and requirements differ, but we feel the broader point is that it should be considered.

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Brunel is a supporter of the **Taskforce on Climate-related Financial Disclosures (TCFD)** and works collaboratively with others in the investment industry to promote its adoption, e.g. through the Green Finance Initiative. We commend two publications by the GFI which are pertinent to your consultation, particularly with respect to the roles of the FCA and FRC alongside other financial regulators in promoting climate and sustainability disclosures.

These are:

- Accelerating Green Finance
- Establishing the world's best framework for climate-related and sustainability-related financial disclosures

We would also commend the World Economic Forum's report, which provides support to Boards' ability to effectively respond to the implementation of effective stewardship.

- How to Set Up Effective Climate Governance on Corporate Boards Guiding principles and questions

In considering how the FCA and FRC can ensure high standards of Stewardship we are keen to see it **promoted and reinforced by other policy makers and regulators** in the UK, including but not limited, to Department of Work and Pensions (DWP), Ministry of Housing, Communities and Local Government (MHCLG), Prudential Regulation Authority (PRA) and The Pensions Regulator (TPR).

We would be delighted to follow-up on any of the comments made in our response and provide further support to the review. Please contact our Chief Responsible Investment officer, Faith Ward on faith.ward@brunelpp.org.uk.

Regards

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Signed by Dawn Turner

CEO, Brunel Pension Partnership Ltd



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# Discussion paper questions

### 1. Do you agree with the definition of stewardship set out here? If not, what alternative definition would you suggest?

We wholeheartedly welcome the proposed definition of stewardship, namely, *‘Stewardship is the responsible allocation and management of capital across the institutional investment community to create sustainable value for beneficiaries, the economy and society.’*

The strengths of the definition are that it:

a) Applies to asset classes beyond listed equities. Were it to fail to do so, a significant portion of an institutional investor’s portfolio would be unaffected by improvements in stewardship

b) Refers to capital allocation decisions, not just “what happens afterwards”

c) Recognises the ultimate stakeholders in investment decision-making, i.e. beneficiaries, the economy, and society

We agree with it in its entirety and would urge the FCA and FRC to resist those who wish to see it weakened.

We feel this definition of stewardship resonates with our own stated values, particularly of ‘investing for a world worth living in’ and the aim of our responsible investment strategy in that “Brunel aims to deliver stronger investment returns over the long term, protecting our clients’ interests through contributing to a more sustainable and resilient financial system, which supports sustainable economic growth and a thriving society.”

### 2. Are there any particular areas which you consider that investors’ effective stewardship should focus on to help improve outcomes for the benefit of beneficiaries, the economy and society (e.g. ESG outcomes, innovative R&D, sustainability in operations, executive pay)?

We recognise that good stewardship requires each investor to have developed their own priorities defined by the mandate type, coverage and their own processes.

We also recommend stronger focus on disclosure with specific reference to the Taskforce on Climate-related Financial Disclosures (TCFD). We believe that financial regulators should integrate the TCFD recommendations throughout the existing UK corporate governance and stewardship reporting framework.

The Government and financial regulators should create and publish guidelines and appropriately reference these guidelines in the corpus of relevant UK rules, codes and guidance. The guidelines should clarify certain TCFD recommendations to make them more readily implementable, e.g. in relation to physical climate scenario analysis and the disclosure of assumptions.

Key to this process will be for relevant regulators to identify the most effective mode by which the guidelines can be accommodated within its regulatory remit.


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Financial regulators would need to assess the suitability of the existing rules, codes and guidance for the disclosures envisaged by the guidelines. Where the existing rules, codes and guidance are not suitable, then publishing separate or new guidance to assimilate the guidelines should be considered where it is within a regulator's powers to do so, and where any procedural formalities are complied with.

**3. To what extent do the proposed key attributes capture what constitutes effective stewardship? Which attributes do you consider to be most important? Are there other attributes that we should consider? If so, please describe.**

We support the key attributes identified in table 1. For desired activities and behaviours to be realised requires stewardship to be integrated at the heart of the decision-making in capital allocation, fundamentally thinking about the drivers of long terms sustainable value.

We believe disclosure is fundamental to driving changes in behaviour to have UK as a global leader in stewardship. We strongly support that incisive and forward-looking corporate reporting coupled with investors publishing annual Activities and Outcomes Reports is key to delivering effective stewardship.

We are supportive of the proposal to an annual Activities and Outcomes Report. We ask the FCA and FRC to recognise the dependency of those asset owners who outsource to asset managers on the sourcing of the information needed to populate such reports. The standard of asset manager RI reporting to clients is variable at best, and, with a few notable exceptions, can be quite poor. We would welcome support for improvements in the client reporting by asset managers in your response to this discussion paper consultation.

We would propose the FCA and FRC draw on the work of the PRI, UKSIF, IIGCC, PLSA, BVCA and other such organisations, and draws up a list of guidance documents that is held on the FRC website as a separate document that can be regularly updated. The FCA/FRC has advisory groups which would be well placed to support the development and maintenance of such guidance.

With respect to climate change, we believe regulators should embed the TCFD recommendations for disclosing climate-related risks in all relevant UK corporate governance and reporting frameworks. With the requisite support from financial regulators this can be achieved without additional legislation. However, at an appropriate moment, revisions to relevant legislation should further integrate the TCFD recommendations into the corporate governance and reporting framework. This would also provide an opportunity to: harmonise requirements across different entities (where existing rules, codes and guidance take different approaches); and make provisions for further accountability in relation to the information (e.g. specify location, make provision for shareholder approval similar to the directors' remuneration report).



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**4. What do you think is the appropriate institutional, geographical and asset class scope of stewardship? How can challenges associated with issues such as the coordination of stewardship activities across asset classes, or the exercise of effective stewardship across borders, be overcome?**

We believe stewardship applies across all assets, in all geographies. The UK Stewardship framework should operate on all assets, whether in the UK or not, managed directly or on a delegated basis by UK-based asset managers, investment consultants, asset owners and other relevant organisations in the investment/ investment operations chain. This is consistent with the FCA mandate to ensure integrity of the financial markets and ensure they work for all consumers.

**5. We welcome examples of how firms with different objectives and investment strategies approach stewardship. In particular, we welcome input on how stewardship practices differ across active and index-tracker funds, in the following areas:**

- **how firms prioritise and conduct stewardship engagements**
- **what investments firms have made in stewardship resources**
- **how stewardship activity is integrated with investment decisions.**

We believe high standards of stewardship can operate across both active and index strategies. There are many more commonalities than differences between active and passive management when it comes to stewardship.

For example, the importance of disclosure in

(a) allowing investors to make meaningful observations of material financial risks

(b) driving positive corporate change is common to both active and passive investors

Going one step further, the importance of stewardship disclosure from asset managers to their clients (including asset owners) is also common to both active and passive investors. Whether a client is invested passively (and therefore cares about market-level outcomes) or actively (and therefore cares about company-specific outcomes), the value of disclosure from supplier to client is similarly vital.

Further to our comments above, we believe there is an indisputable case for integrating the recommendations of the TCFD in stewardship disclosure requirements, irrespective of the manner in which portfolios are managed. That both active and passive investors alike have formally signed up to support the TCFD recommendations should make their integration into stewardship disclosure requirements less contentious.


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**6. To what extent do you agree with the key barriers to achieving effective stewardship identified in this DP? What do you believe are the most significant challenges in achieving effective stewardship? We would particularly welcome views on the investment required to embed effective stewardship in investment decision-making.**

We agree with the barriers identified in the discussion paper. We would emphasise three points:

a) Company Boards' ability to respond to effective stewardship

b) Poor stewardship reporting by asset manager on clients

c) Role of investment consultants

a) We would also commend the World Economic Forum's report that provides support to Boards' ability to effectively respond to the implementation of effective stewardship in relation to climate change. Please see How to Set Up Effective Climate Governance on Corporate Boards Guiding principles and questions

b) Please see our response to question 3 with regards to poor asset manager reporting to clients

**c)** We would significantly enhance the requirements on investment consultants. For example, with respect to the reporting requirements proposed in the proposed UK Stewardship Code, we recommend that the provision for service providers is "In the context of their business model and the activities undertaken, service providers should explain how they support their clients in the delivery of all the principles and provisions outlined in the code". In other words, they should also have to cover everything. Further guidance is needed to set out the minimum expectations for different sorts of activities. For example, manager selection, manager monitoring, investment beliefs, trustee training etc. We recommend the work of the AMNT https://amnt.org/wp-content/uploads/2018/12/FINAL-investment-consultant-December-2018-report.pdf and imminent work by the PRI to assist in the development

**7. To what extent do you consider that the proposed balance between regulatory rules and the Stewardship Code will raise stewardship standards and encourage a market for effective stewardship?**

We support the scope of stewardship activities encompassing all those across all asset classes and across the investment chain. To aid the effective flow of information we advocate improved disclosure and transparency. This is particularly crucial for managing systemic issues such as climate change. Please see our response to question 3.

**8. To what extent are there are issues with proxy advisers that are not adequately addressed by SRD II and proposed revisions to the Stewardship Code?**

The requirements are currently too light. For proxy voting services, those signing up to the Code need to have beliefs that guide their advice that go beyond governance issues. To that end they should set out their approach on key thematic areas, e.g. remuneration, climate change, modern slavery, plastic pollution, etc, and expectations on how they are addressed. They should also have a statement on how they apply this to their voting recommendations and services. Finally, given they work for both investors and companies, a conflict of interest policy is needed, and a process to resolve any conflicts arising.

**9. We welcome feedback on other specific aspects of the regulatory framework described above. In particular, we are interested in views on:**

**i: Whether and to what extent the FCA's proposed rules for asset owners should be extended to SIPP operators?**

Yes, SIPP Operators should become signatories of the UK Stewardship Code.

**ii: The case for regulatory rules to expand the reach of stewardship beyond listed equity**

Yes, we support the application of stewardship across all asset classes.

**iii: Whether there is a role for UK regulators in encouraging overseas investors to engage in stewardship for their asset holdings in the UK**

Yes, we would support UK regulators in encouraging overseas investors to engage in stewardship for their asset holdings in the UK.

**iv: The extent to which additional rules might be necessary either to improve stewardship quality or prevent behaviours that might not be conducive to effective stewardship**

Relevant financial regulators should integrate the TCFD recommendations throughout the existing UK corporate governance and reporting framework. The Government and relevant financial regulators must clarify in their guidelines that


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disclosing material environmental risks, including physical and transition climate-related risks, is already mandatory under existing law and practice.

Companies and investors should use the TCFD framework to develop their financial, corporate governance and stewardship disclosures, and Government should conduct a review of disclosure in 2020 to monitor and encourage market adoption amongst both issuers and users.

If market adoption is inadequate, we support the Environmental Audit Committee's (EAC) report on green finance, which recommends making it mandatory for large companies and asset owners to report their exposure to climate change risks and opportunities.

### v: For differences between active and index-tracker strategies in the practice of stewardship, whether there are particular regulatory actions we should consider to address any perceived harms.

We believe high standards of stewardship can operate across both active and index strategies. There are many more commonalities than differences between active and passive management when it comes to stewardship.

For example, the importance of disclosure in

(a) allowing investors to make meaningful observations of material financial risks

(b) driving positive corporate change that is common to both active and passive investors

Going one step further, the importance of stewardship disclosure from asset managers to their clients (including asset owners) is also common to both active and passive investors. Whether a client is invested passively (and therefore cares about market-level outcomes) or actively (and therefore cares about company-specific outcomes), the value of disclosure from supplier to client is vital.

Further to our comments above, we believe there is an indisputable case for integrating the recommendations of the TCFD in stewardship disclosure requirements, irrespective of the manner in which portfolios are managed. That both active and passive investors alike have formally signed up to support the TCFD recommendations should make their integration into stewardship disclosure requirements less contentious.

### vi: Whether the FCA's proposed rules to implement certain provisions of SRD II should apply on a mandatory, rather than 'comply or explain', basis.

Yes.



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**10. We welcome feedback on whether, to support effective stewardship, we should consider amendments to other aspects of the regulatory framework that affect how investors and issuers interact (such as the LRs, PRs and DTRs)?**

We recommend a deeper review of the FCA regulatory framework to identify opportunities to enhance stewardship and consider if any of it has resulted in unintended behaviours that counter to the ambitions of good stewardship. We specifically recommend the TCFD recommendations are properly integrated into the UK corporate governance and reporting framework, and note that the guidelines would need to be appropriately referenced in the corpus of relevant rules, codes and guidance such as the FCA Handbook (including listing rules and prospectus rules), corporate governance code and stewardship code.



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