CDSB Climate Disclosure Standards Board

The Climate Disclosure Standards Board (CDSB) would like to thank DWP for the opportunity to offer our written response.

CDSB is an international consortium of nine business and environmental NGOs. We are committed to advancing and aligning the global mainstream corporate reporting model to equate natural capital with financial capital. We do this by offering companies a framework for reporting environmental and climate information (the CDSB Framework) with the same rigour as financial information. In turn, this helps companies to provide investors with decision-useful environmental and climate information via the mainstream corporate report, enhancing the efficient allocation of capital. Regulators also benefit from compliance-ready materials. Recognising that information about natural capital and financial capital is equally essential for an understanding of corporate performance, our work builds the trust and transparency needed to foster resilient capital markets. Collectively, we aim to contribute to more sustainable economic, social and environmental systems.

CDSB has been working with HM Government and internationally for the past decade and the CDSB Framework has been referenced in the guidance to the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013, the London Stock Exchange's ESG reporting guide, as well as in corporate governance codes and ESG reporting guidelines, among others, in the European Union and Australia.
CDSB commends the Department for Work and Pensions (DWP) for proposing changes to the regulations to require trustees to explain their approach to ESG factors in investing, report on what they did to implement this approach in practice and publish a statement on how they take account of members' wider views (with specific requirements differing by type and size of scheme).
This response represents high level responses to the DWP's questions and is aligned with responses from ShareAction, ClientEarth and the Green Finance Initiative.
Please find our comments below and do not hesitate to contact us if we can be of further assistance.

Kind regards,

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Climate Disclosure Standards Board

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Overall comments

We support all the changes in this consultation and we believe that others in support of responsible investment would also welcome them.

This is because they:

- Start to address concerns by the investment community that financial markets do not yet take sufficient account of ESG, including climate change, risks and opportunities relevant to future shareholder value because of a lack of comprehensive and comparable information in “mainstream” corporate reports;
- Would make it a minimum requirement for pension trustees to have investment policies that address all material financial risks, including those related to ESG and climate change. In turn, this should support asset managers and other actors further down the investment chain to account for ESG and climate change risks in their decision-making processes;
- Support the overall message that more ESG and climate change information disclosures are required within the mainstream annual report of organisations so that better informed decisions can be made to efficiently allocate capital to protect and enhance value. This follows the recommendations from the G20’s Financial Stability Board Task Force on Climate-related Financial Disclosures (TCFD), which produced its final report in June 2017, establishing recommendations for disclosing clear, comparable and consistent information about the risks and opportunities presented by climate change. Supplemental guidance is provided for asset owners and assets managers;
- More clearly explain trustees’ roles and duties in respect of material ESG factors (including climate change and natural capital) and members’ wider ethical concerns, thus removing confusion.
- Require trustees to have much broader stewardship policies than the narrow focus on voting in the current regulations. This should push engagement with investments up the agenda for trustees and make sure they think about how to do this in practice;
- Require, via the reporting mechanism, trustees to think about how well they have implemented their policies. This should prevent the Statement of Investment Principles from being a static document that is not used in practice by trustees;
- Clarify that trustees can (if they want to) consider the non-financial interests of members. This should encourage trustees to bear in mind the impact of investment on members' lives, wider society and the environment; and
- Will not change the core legal principle that trustees have discretion on how to invest. These changes are clarifying the law as it stands, not changing it.

However, we believe the current draft does require stronger and more explicit references to the UK Financial Reporting Council’s Stewardship Code and the Financial Stability Board’s Task Force on Climate-related Financial Disclosures.

For more detailed comments on specific consultation questions, please see our specific comments below.

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Responses to specific questions

Q1. We propose that the regulations come into force approximately 1 year after laying, with the exception of the implementation report, which would come into force approximately 2 years after laying.
a) Do you agree with our proposals?

Yes, because:
- One year gives trustees sufficient time to review their Statement of Investment Principles to make it compliant with the new requirements;
- Although trustees may need to change their Statement of Investment Principles to meet the new regulations, the changes relate to points which trustees should already be considering as part of their existing fiduciary duties.
- Allowing two years for the report gives trustees time to oversee and report on how this new Statement of Investment Principles has been implemented in practice.

We do not believe any further delay to the regulations coming into force is appropriate.

b) Do you agree that the draft regulations meet the policy intent?

Yes, we believe they do.

Q2: We propose to require all trustees of all schemes which produce a SIP to state their policy in relation to the consideration of financially material considerations including, but not limited to, those resulting from environmental, social and governance risks, including climate change.

a) Do you agree with the policy proposal?

Yes, we agree with the policy proposal because:
- Many ESG issues will have a financial impact on pension schemes' investments, e.g. climate change or the treatment of workers across a company's supply chain. However, as highlighted there has been confusion amongst some trustees and advisors about whether and how they should take these issues into account. In this regard, trustees should make a distinction between:
  - Material risks known to the trustees at the time of reporting and already affecting the schemes, its strategy and financial planning;
  - Matters of systemic importance (including climate change and natural capital considerations) - where the organization is required to report information that can be assessed at aggregate level in macroeconomic analysis or by policy makers - relevant to the organisation's license to operate.
- The wording in the existing Investment Regulations is outdated and unclear. In addition, it also conflicts with guidance from The Pensions Regulator which adds to the confusion.
- These changes should raise standards across the board, and over the long-term should help to reduce the risk to pension members - protecting and enhancing value of funds.

b) Do the draft regulations meet the policy intent?

Yes, we believe the draft regulations do meet the policy intent. We agree with the broad definition of "financially material considerations" because:
- Pension trustees should see ESG issues, where material, as equivalent to mainstream considerations and therefore assessed alongside other investment risks and considerations.

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- Climate change needs to be highlighted as a key systemic risk and cross-cutting issue – unlike some other ESG risks, climate change cannot be seen or tackled in isolation. Climate change needs to be considered at all stages of the investment process: trustees should consider it in their investment strategy and not simply delegate it to asset managers. In this regard we would like to bring the DWP's attention to our position paper: Materiality and climate-related financial disclosures1.

Q3: When trustees prepare or revise a SIP, we propose that they should be required to prepare a statement, setting out how they take account of scheme members' views.

a) Do you agree with the policy proposal?

Yes, we agree with this policy proposal because:

- We also believe that it is "good practice for trustees to inform the design of investment strategies with an understanding of scheme members' views", and that it "aids with assessing value for members, which trustees of DC schemes must do".
- It will not change the core legal principle that trustees have ultimate discretion on how to invest. Members would not have any rights to dictate investment policy.
- This is an opportunity for trustees who want to raise low engagement levels – it could help build trust and increase engagement with members. The Government's review of auto-enrolment published in December 2017 found that engagement with members has an important role to play in improving outcomes.
- In DC pension schemes, the saver bears the investment risk and therefore has an interest in how their money is invested.

b) Do the draft regulations meet the policy intent?

In general, we believe it does because:

- It is helpful to clarify that non-financial factors include wider interests and environmental impact, as well as ethical views.
- However, we believe that new regulation 2(2)(c) requires amending to "the views which, in the reasonable opinion of the trustees, members of the scheme hold or are likely to hold". Otherwise, trustees might worry that they haven't obtained enough evidence for their opinion to be regarded as "reasonable".

Q4. Do you agree with our proposal not to require trustees to state a policy in relation to social impact investment? If not, what change in legislation would you propose, and how would you address this risk of trustee confusion on this point?

- We support the reference to social impact in the definition of non-financial factors. This should give trustees comfort that they can consider the opportunities posed by social impact investing.
- However, we are not confident whether the minor changes proposed will actually result in much change in trustees' practice. If the Government is keen to create a culture of social investment, we are not sure that this will be catalysed by the proposed changes.

[1] Climate Disclosure Standard Board (2018) Position paper – Materiality and climate-related financial disclosures. [Online]. Available from: https://www.cdsb.net/materilaity

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Q5: We propose that trustees should be required to include their policy in relation to stewardship of the investments, (including monitoring, engagement and voting) in the SIP.

a) Do you agree with the policy proposal?

Yes, we agree with this policy proposal because:

- Stewardship in its broadest sense (including monitoring and engagement, as well as voting) is a vital part of protecting and enhancing the value of pension investments.
- There are simple actions which even smaller pension schemes can take towards stewardship, such as collaborating with other investors and ensuring asset managers have good stewardship practices.
- These changes should drive demand for forward-looking, robust stewardship activities from asset managers by pension funds.

b) Do the draft regulations meet the policy intent?

Yes, we believe that they do.

Q6: When trustees of relevant schemes produce their annual report, we propose that they should be required to prepare a statement,

- setting out how they have implemented the policies in the SIP,

- explaining and give reasons for any change, and

- including the latest statement on how they have taken account of the views which in their opinion scheme members hold in the annual report.

a) Do you agree with the policy proposal?

In general, we agree with this policy proposal because:

- This will prevent relevant schemes from disclosing only vague, high-level statements on their approach to ESG factors. For further guidance on the disclosure of ESG-related information in organisations annual reports, the CDSB Framework is widely perceived by the market as an essential tool for the implementation of the TCFD recommendations and integration of climate change into risk management.
- Trustees will have to make sure (a) they are producing clear investment policies; and (b) they are scrutinising the outcomes of how these policies are being implemented.

b) Do the draft regulations meet the policy intent?

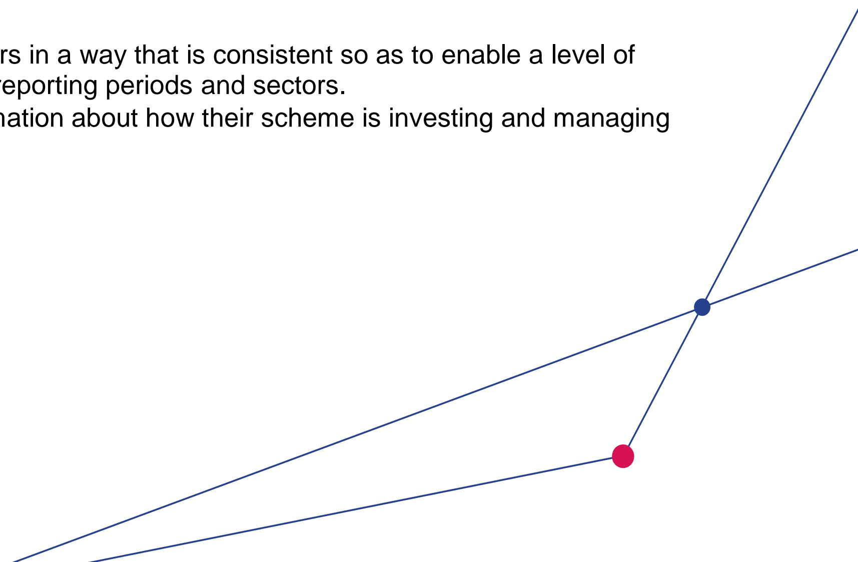
Yes, we believe they do.

Q7: We propose that trustees of relevant schemes should be required to publish the SIP, the implementation report and the statement setting out how they will take account of members' views online and inform members of this in the annual benefits statement.

a) Do you agree with the policy proposal?

Yes, we agree with this policy proposal because:

- Information of value is provided to stakeholders in a way that is consistent so as to enable a level of comparability between similar organisations, reporting periods and sectors.
- Pension holders should have access to information about how their scheme is investing and managing risks on their behalf.



- Transparency in this respect should help drive up standards.
- Publishing these documents online involves little cost or effort.

b) Do the draft regulations meet the policy intent?

Yes, we believe they do.

Q8: Do you have any comments on the business burdens and benefits, and wider nonmonetized impacts we have estimated in the draft impact assessment?

- We believe that these changes require trustees to update and improve policies, add a statement on consideration of member views and explain how policies have been implemented;
- Given its importance to an acknowledged systemic risk to the economy, it is vital all actors in the investment chain including pension trustees consider climate change where it is a material financial factor for their investments; and
- The costs and time involved are appropriate for a scheme to bear if it is taking long term investment seriously, as it should.

Q9: Do you have any other comments on our policy proposals, or on the draft regulations which seek to achieve them?

The TCFD recommendations provide specific supplemental guidance for the financial sector that includes asset owners and asset managers. Pension trustees, exercising their fiduciary duty on behalf of members are asset owners, either directly or through asset managers. They bear a major portion of the exposure to potential transition and physical risks to a low carbon economy. Similarly, asset owners will benefit from the potential returns on the investment opportunities associated with the transition to a low carbon economy. The following is taken from the TCFD Annex Section D, Chapter 3:

> Asset owners sit at the top of the investment chain and, therefore, have an important role to play in influencing the organizations in which they invest to provide better climate-related financial disclosures. Disclosure of climate-related risks and opportunities by asset owners allows beneficiaries and other audiences to assess the asset owner's investment considerations and approach to climate change. This may include an assessment of the asset owner's integration of appropriate climate-related financial information into its investment activities in various ways, for example, in setting investment strategy, making new investment decisions, and managing its existing portfolio. By encouraging climate-related financial disclosures by asset owners, beneficiaries and other stakeholders will be in a position to better understand exposures to climate-related risks and opportunities. Further, climate-related financial disclosures by asset owners may encourage better disclosures across the investment chain—from asset owners to asset managers to underlying companies—thus enabling all organizations and individuals to make better-informed investment decisions.

We suggest that this supplemental guidance is referenced and appropriately integrated within the proposed regulations.

Q10: Does the revised statutory guidance accurately address the policy proposals?

Yes, we believe they do.

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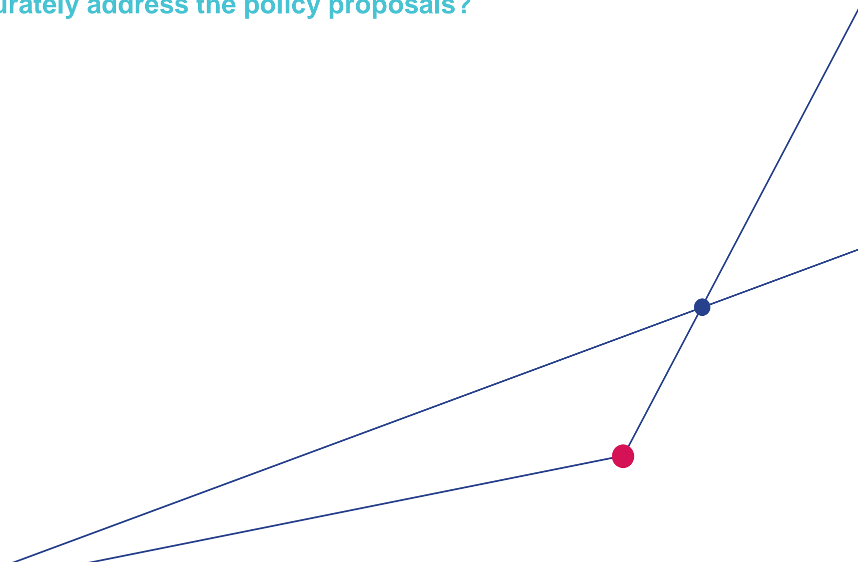

Q11: What evidence or views do you have of how well the other requirements in the SIP are working? What areas for further consideration and possible future change would you suggest?

In accordance with the recommendations from the Green Finance Initiative Working Group on Data, Disclosure and Risk, and the plans set out in the Green Finance Taskforce Report, we suggest that the Government considers further cross-departmental work together with relevant regulators to support the successful adoption, implementation, monitoring and enforcement of the TCFD recommendations, so that other parts of the investment chain are required to disclose information relating to climate-related risks and opportunities. In turn, this will promote the availability and the flow of material climate-related financial information. This will allow each member of the investment chain to make better informed decisions, protecting beneficiaries, accelerating the growth green finance in the UK, reducing systemic risk and helping deliver the investment required for the UK to meet its carbon reduction targets in line with the UK Climate Change Act (2008) and 2015 Paris Agreement.

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