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Sent via email to assetmanagementmarketstudy@fca.org.uk

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Dear Ms Young

Asset Management Market Study: Interim Report

I am writing to respond to your interim report on the FCA's asset management market study on behalf of ShareAction, a registered charity established to promote transparency and Responsible Investment ("RI") practices by pension funds and other institutional investors. We are a member organisation and count amongst our members well-known NGOs and charitable foundations, as well as over 35,000 individual supporters.

We welcome this timely and necessary study. Millions of individuals in the UK rely on the investment returns delivered by asset managers for their financial security, both now and in retirement. The FCA's findings in this interim report indicate that poor competition and transparency in the asset management market have an adverse effect on savers' outcomes, and it seems probable that they will continue to do so unless the FCA takes strong regulatory action.

A number of academics and civil society representatives, including ShareAction's Chief Executive, wrote to the Financial Times in January 2017 recommending that the mission of the FCA "should start with the essential purposes that the finance industry plays in serving the outside world: keeping money safe; facilitating payments; risk sharing; intermediation."[1] The letter said that financial regulators are not typically asked to consider the broader purpose of the industry they are responsible for. However, it is when the financial system becomes disconnected from its purposes and from the ordinary savers whose money it uses, that we have seen the worst types of corporate excess, and risk taking and crises.

While the focus on costs and charges in the interim report is of key importance in safeguarding the returns of savers, including people in workplace pension schemes, we believe that the final report should focus more on the purpose of the asset management industry and on how best to promote behaviour which supports that purpose and avoids undermining it. It is important not to over-emphasise one single problem affecting savers' returns, however significant in itself, but to look critically at the industry as a whole. 'Value for money' should not be synonymous with 'low charges'. Instead, the FCA should look at how to build a culture in which the asset management business operates to add value to the overall investment system and, in such a well-functioning structure, this would include fair, not excessive, charges.

[1] Financial Times. "FCA's mission must start with the essentials" (January 2017). Available online at: https://www.ft.com/content/01287018-e170-11e6-8405-9e5580d6e5fb [accessed 20 February 2017].

Purpose of the asset management industry

David Pitt-Watson said in his lecture, *What They Do With Your Money*,[2] at the New City Agenda on 5 July 2016 that to establish whether the finance industry is doing a good job, one needs first to define its purpose, and then to evaluate its performance against that purpose. He imagined three triplets: one who lives in Holland, one in London and one in the US. They save the same amount, retire on the same day and, being triplets, have the same life expectancy. Yet the Dutch triplet's pension on retirement would be 50% higher than the others. Pitt-Watson said that this is partly because when the Dutch started thinking about pensions, they said 'What is it that we are trying to do here? What is the purpose of this pension?' They decided the purpose was to make sure that people had a reliable income from the time that they retired until the time that they died. In the UK, we lack a system designed for this purpose; rather we have one which takes savers' money, and hands it to one agent, who hands it to another, and another, and another, each of whom charges a fee.[3]

The temptation for regulators may be to let the investment system operate according to the rules of the market. This would be acceptable if it were a competitive, efficient market, but it is not. There are features of the pensions, investment and asset management sector which are akin to market failure. This is particularly important in light of the shift from DC pensions to DB. In DC schemes, the end investors (individual savers) bear all the risks and costs of investment. Despite this, savers are not treated as the customers of their pension schemes, since it is not the saver but still the employer who chooses the scheme in question. Pension savers are usually unable to move to a different provider without losing employer contributions and receive little information about how their money is invested. It is nearly impossible, therefore, for savers to take real responsibility for their own savings so as to ensure that they receive a sufficient income on retirement.[4] Yet in the DC world there is equally no single paternalistic entity with the information, capacity and incentive to ensure that individuals' savings are safe and prudently invested, with the ultimate purpose of providing them with a reliable and liveable income in retirement. The result is that we currently have a system in which those providing capital and bearing risk are disconnected from their money and open to exploitation and rent-extraction.

It is clear from the FCA's excellent and well-researched interim report that the UK has a pensions system which hands end-investors' savings from intermediary to intermediary, with little thought about the ultimate purpose we are trying to achieve. ShareAction would argue that pension savers should be assured that intermediaries are acting in their best interests – both their financial interests and taking account of their wider interests in living in a healthy environment, thriving economy and decent society. While we welcome the work being done by the FCA and the Department for Work and Pensions (the DWP) to ensure pension savers can access information about the charges levied on their pension pots, we would argue that pension savers should also have the right to receive high-quality, accessible information on where and how their funds are invested. Transparency around equity holdings and the stewardship of those holdings is important because these generate most of the returns that beneficiaries rely on in retirement. If asset managers are subject to greater scrutiny by those whose money they invest and are held accountable by them, this would contribute to a more transparent system in which excessive fees and irresponsible investment are harder to hide. Furthermore, a responsible approach to the investment of pension savings aligns with the need for the industry to think and operate with a long-term focus.

[2] New City Agenda (July 2016). Available online at: http://newcityagenda.co.uk/wp-content/uploads/2016/12/New_City_Agenda_05.07.16_David-Pitt-Watson.pdf [accessed 20 February 2017].
[3] Ibid, p6.
[4] Financial Conduct Authority. *Asset Management Market Study* (2016), p 24. Available online at: https://www.fca.org.uk/publication/market-studies/ms15-2-2-interim-report.pdf [accessed 20 February 2017].

Short-termism in the asset management industry

The interim report focuses primarily on the value provided by asset managers to investors net of costs charged. The report states that, overall, the FCA's evidence suggests that "actively managed investments do not outperform their benchmark after costs. Funds which are available to retail investors underperform their benchmarks after costs – while products available to pension schemes and other institutional investors achieve returns that are not significantly above the benchmark."[5]

John Kay said in his 2012 report[6] that closet indexation, where frequent performance monitoring encourages actively managed portfolios which closely mimic the composition of an index, presents a real issue in equity markets. By following a benchmark closely a fund manager can avoid periods of underperformance, if such performance is measured on a monthly or quarterly basis.[7] He said that the "interests of beneficiaries are largely interests in *long-term absolute performance*. The concern of asset managers – and the basis on which they are monitored by many asset holders, and by advisers to asset holders and retail investors – is *short term relative performance*. This misalignment of incentives creates many problems." He also commented that "competition between asset managers on relative performance is inherently a zero-sum game. The asset management industry can benefit its customers – savers – taken as a whole, only to the extent that its activities improve the performance of investee companies."[8]

This is particularly true of the £2.1 trillion managed on behalf of UK pension funds in 2015,[9] as pension funds often have long investment horizons. They are able to take long-term positions in companies and to undertake stewardship and engagement with those companies to help ensure that they are well-governed and successful over the long term. Short-termism is flagged as a concern in the academic literature commissioned for Annex 5 of the interim report. This states that investment oversight committees can "over-focus on short-term returns", with pension funds in particular seeming to 'herd' into investment strategies and buying investment products that may not necessarily reflect the specific needs of individual funds and their long-term investment time horizons.[10] Factors which are likely to affect the performance of companies over the long term, such as environmental, social and governance (ESG) factors, are highly relevant to outcomes for pension savers. However, pension funds and their managers often fail to take these factors into account in investment decision making, and regulation of these actors does little to challenge this.

There is one mention of environmental, social and governance (ESG) investment factors in the interim report, where it states: "Views are mixed on the prevalence of [ESG] strategies and how this may be changing over time. It appears that demand is being driven by investors changing their focus while providers are making efforts to take stewardship considerations into account. In a recent sample of 34 IA members, half reported that they managed at least some proportion of assets according to ESG considerations and, where they did, approximately one fifth of total assets were subject to ESG requirements."[11] While it is positive to hear that demand is being driven by asset owners and that providers are making an effort to take this into account, the statistics given in relation to the IA survey are concerning.

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[5] Ibid, p15.
[6] Kay, J. (July 2012). *The Kay review of UK equity markets and long-term decision making*. Available online at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/253454/bis-12-917-kay-review-of-equity-markets-final-report.pdf [accessed 20 February 2017].
[7]Ibid, p40.
[8] Ibid, p11.
[9] Financial Conduct Authority. *Asset Management Market Study* (2016), p 31. Available online at: https://www.fca.org.uk/publication/market-studies/ms15-2-2-interim-report.pdf [accessed 20 February 2017].
[10] Ibid, p63.
[11] Ibid, p176.

There is increasing evidence showing that companies that perform well on environmental, social and governance (ESG) issues tend to produce better returns for investors.[12] The IA sample echoes a recent Professional Pensions snapshot industry survey,[13] where only 21% of respondents said that ESG factors were fully embedded in their investment approach. 39% said they do not take ESG factors into account and are not considering doing so.[14] Given the numerous examples of poor corporate practice on ESG having a real effect on investor returns – the recent furore at Sports Direct being just one – it is concerning that many trustees and fund managers still think of ESG as an optional, 'ethical' extra. As the Pensions Regulator's executive director for regulatory policy recently stated, trustees need to "wake up and smell the coffee" on ESG.[15]

Climate change and the low carbon transition poses particularly significant financial risks to pension funds and their members. According to the Economist Intelligence Unit, a worst-case scenario of 6°C warming could lead to a present value loss of US$13.8 trillion of manageable financial assets, roughly 10% of the global total (total stock of assets held by non-bank financial institutions).[16] At the same time, if the investment system does not take steps to move towards a low-carbon economy, then it could be left with as much as US$100 trillion in 'stranded' fossil fuel assets by 2050, according to Citigroup.[17] A recent report by the Cambridge University Sustainability Unit, "Unhedgeable risk: How climate change sentiment impacts investment", argues that the systemic nature of climate risk means that some portion of risk is unhedgeable for individual funds and that avoiding such risks will require system-wide approaches, such as strong regulation.[18]

In the course of interviews for our 2016 report *The hot debate on climate risk and pension investments: Does practice stack up against the law?,*[19] one pensions lawyer at a City firm said that she believed that pension schemes face additional investment costs if they take account of ESG factors such as climate risk in investments, and that this could not be justified from a legal perspective for DB schemes unless there were direct financial benefits for the employer. 12% of survey respondents felt that the additional expense of investment was the main reason climate risk was not being taken into account in pension investments. This is a concerning finding because, over the time-horizon of most pension schemes, ESG factors, including climate change, are highly likely to be financially material. We are concerned that there seems to be a perception that taking account of relevant ESG factors in investment is an optional extra that comes at additional expense, and that this may be preventing pension schemes from taking longer-term risk factors into account. A poorly

[12] E.g. Arabesque Partners and University of Oxford (2015). *From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance*. Available at http://www.arabesque.com/index.php?tt_down=51e2de00a30f88872897824d3e211b11 [accessed 24 January 2017].

[13] Respondents included trustees, pension scheme managers and pension scheme advisors. For more information, please see the full results of the survey (available at: http://msgfocus.com/files/amf_incisive_media/project_1870/PB230816.pdf [accessed 20 February 2017].

[14] Professional Pensions (August 2016). "Climate change is 'overblown nonsense' and not a material risk, says industry". Available online at: http://www.professionalpensions.com/professional-pensions/news/2468851/climate-change-is-overblown-nonsense-and-not-a-material-risk-says-industry [accessed 20 February 2017].

[15] The Pensions Regulator. (September 2016). "TPR: Trustees must wake up and smell the coffee on ESG". Available online at: http://www.professionalpensions.com/professional-pensions/news/2470190/tpr-trustees-must-wake-up-and-smell-thecoffee-on-esg [accessed 20 February 2017].

[16] The Economist Intelligence Unit (2015). *The cost of inaction: Recognising the value at risk from climate change.* Available online at: https://www.eiuperspectives.economist.com/sites/default/files/The%20cost%20of%20inaction_0.pdf [accessed 24 January 2017].

[17] Citi GPS: Global Perspectives & Solutions (August 2015). *Energy Darwinism II: Why a low carbon future doesn't have to cost the earth.* Available online at: https://climateobserver.org/wp-content/uploads/2015/09/Energy-Darwinism-Citi-GPS.pdf [accessed 20 February 2017].

[18] University of Cambridge Institute for Sustainability Leadership (2015*). Unhedgeable risk: How climate change sentiment impacts investment*. Available online at: http://www.cisl.cam.ac.uk/publications/sustainable-finance-publications/unhedgeable-risk [accessed 20 February 2017].

[19] ShareAction and ClientEarth. (September 2016.) *The hot debate on climate risk and pension investments: Does practice stack up against the law?*. Available online at: https://shareaction.org/wp-content/uploads/2016/09/ClimateInvestmentDutiesInvestorReport.pdf [accessed 20 February 2017].

managed exposure to factors such as climate change and low carbon transition may have a much more significant financial impact on portfolio returns than any small increase to the cost of investment at the present time.

The Economist Intelligence Unit's 2015 report on the cost of inaction on climate change states: "Thirty years is a common time frame for pension funds and other long-term investors. But if investors wait until these risks actually manifest themselves, then the options they will have to deal with them will be significantly reduced".[20] Pension funds need to take steps to assess and manage climate risk at the present time, rather than wait until the effects of climate change become effectively unmanageable. While minimising the costs of investment is important, it would be a mistake to restrict them to the extent that asset owners and managers feel they cannot undertake the activities which will help to maximise and protect savers' returns over the long term.

Natasha Landau-Mills, Head of Stewardship at Sarasin and Partners, has described her vision of a sustainable and socially beneficial asset manager, whose fundamental role is stewarding clients' capital to create lasting value for beneficiaries. Initially, this process focuses on due diligence and dialogue to identify which companies to invest in. Then, once clients have become shareholders, priority shifts to monitoring company performance: "[t]he smart asset manager engages and acts as a long term owner… Transparency with beneficiaries is key, as is regular reporting - but not on performance relative to a market benchmark. Indeed, they wouldn't be measuring their risk in terms of a tracking error against that benchmark; they would be reporting back on how they have been delivering earnings on a consistent basis." ShareAction believes that this kind of asset management provides real value for savers, focusing on improving the performance of investee companies over the long term rather than simply trading to beat a benchmark on an annual basis.

Duty to act in best interests of investors

We strongly support the FCA's proposal to introduce a duty for asset managers to act in the best interests of investors. While we anticipate there may be some resistance from industry participants, we urge the FCA to take a robust stance on this proposal.

Asset managers are increasingly responsible for many of the day-to-day investment decisions which were previously, in a less complex investment world, made by pension trustees. However, there is a lack of clarity around whether this gives asset managers fiduciary responsibilities equivalent to those owed by pension trustees. Since millions of individual savers are reliant on the returns delivered by asset managers for their financial security in later life, it is vital to make sure adequate protections are in place for these individuals, especially given the poor returns indicated in this interim report and elsewhere.[21]

Pension fund trustees owe their beneficiaries the duties of loyalty and prudence, as those beneficiaries are seen as vulnerable and in need of protection by those making decisions on their behalf (a situation which typically generates fiduciary responsibilities for the decision-maker). If, in reality, pension trustees are delegating investment decisions to asset managers, there should be some regulatory mechanism to ensure that the fiduciary responsibilities are not diluted. Furthermore, one could argue that the asymmetry of

[20] The Economist Intelligence Unit (2015). *The cost of inaction: Recognising the value at risk from climate change.* Available online at: https://www.eiuperspectives.economist.com/sites/default/files/The%20cost%20of%20inaction_0.pdf [accessed 24 January 2017].

[21] For example, between 2002-2012, the median performance of pension funds in the OECD was returns of +2.5% p.a., while the UK median was -0.7%. Between 2008-2012, the UK scored 23rd out of 29 countries studied. The Financial Inclusion Centre estimated that the hypothetical loss to UK pension funds over the 10 years might be in the range of £112bn-£215bn (Financial Inclusion Centre, using OECD data, December 2014 full report. Available online at: http://inclusioncentre.co.uk/wordpress29/wp-content/uploads/2011/04/OECD-Pension-fund-performance-Financial-Inclusion-Centre-briefing.pdf [accessed 20 February 2017].)

information and power in the relationship between trustees and asset managers is not adequately taken account of in the characterisation of trustees as 'sophisticated investors'. This interim report notes that "trustees of pension schemes… face a range of challenges in their role and their dealings with asset managers… We found that there is a relationship between some of the challenges facing oversight committees and their size, with smaller schemes (in terms of assets under administration and the number of trustees), generally being less well-resourced and knowledgeable."

The interim report notes that trustees interviewed suggested it was difficult to find out the full costs of their investment with larger investors potentially being better equipped to push for full costs information.[22] There were numerous comments at the FCA's institutional investor roundtable about the great difficulties participants had experienced in trying to obtain information from their asset managers, ranging from the fees they were charged to the voting decisions made on their behalf. The interim report's findings indicate that the quality of asset managers' reporting to trustees is also a real cause for concern, with "information presented to institutional investors about the performance of their investments… often presented in a format difficult for investors to understand and engage with" and quarterly reports for trustees put together by asset managers often including "lots of information which can make it difficult for them to identify the important points they should be focusing on, so making it difficult to assess performance." This fits with ShareAction's own extensive work monitoring transparency by the asset management and pension sectors to ultimate savers. Poor disclosure by asset managers to pension funds means that it is difficult for those funds to make adequate disclosures to savers. Thus, this is contributing to a system in which the saver has no oversight of what is happening to their money.

There was considerable agreement at the FCA's institutional investor roundtable that pension funds are improperly categorised as sophisticated investors and are in need of additional protections, which would flow to the beneficiaries of schemes. This is borne out by the statistical analysis of pension trustees' views on value for money in The Pensions Regulator's 2015 *Trustee Landscape Quantitative Research*, which states: "schemes generally expressed high confidence about receiving value for money from their external advisors. Across all of the advisor types, 91% of schemes were confident or very confident that they received value for money."[23] Given that the Transparency Task Force's recent report recently found more than 100 charges are routinely levied on pension savers, many of them hidden, and suggested that the number of fees levied on a pension is three times higher than previously thought, it is deeply concerning that so many pension trustees were blithely unaware of the true costs underlying the services they receive from their fund managers. A small minority (3%) of schemes said that they felt that they were not receiving value for money from the external advisor about whom they had been asked. Of these, some did say that this was because the market/industry overall does not offer value for money, or that they had reviewed the costs and charges and this suggests they do not offer value for money. However, others simply said that they do not have the necessary knowledge or expertise to know whether they are receiving value for money or that they had not reviewed whether they are receiving value for money.

There are also widespread misconceptions about how far trustees are able to delegate their duties. In the Professional Pensions snapshot industry survey mentioned above, one respondent said, in answer to a question about how far ESG factors such as climate risk are taken into account in investments, "It is a factor in manager selection but beyond that we depend on managers for individual decisions" and another commented, "We use fund

[22] Financial Conduct Authority. *Asset Management Market Study* (2016), p61. Available online at: https://www.fca.org.uk/publication/market-studies/ms15-2-2-interim-report.pdf [accessed 20 February 2017].
[23] The Pensions Regulator. (October 2015). *Trustee Landscape Quantitative Research: A report on the 2015 Trustee Landscape research*, p40. Available online at: http://www.thepensionsregulator.gov.uk/docs/trustee-landscape-quantitative-research- 2015.pdf [accessed 20 February 2016].

managers and get comfortable they have strong governance". Numerous Local Government Pension Scheme funds demonstrated, in response to FOI requests,[24] that they are also labouring under this misconception. For example, in response to a question about what steps funds are taking to assess and manage climate risk, one fund said: "None: this is delegated to fund managers." Another responded to say: "Pension Fund investments are all managed externally and the ESG decisions are delegated to Fund Managers who have been provided with a copy of the Fund's policy". A third said: “"The investment decision making is with the external managers, who take account of all risks, including climate change, in the decision making process."

However, pension fund trustees' legal duties to act in the best interests of members, to exercise "prudent" investment behaviour and to balance risks against returns cannot be wholly delegated to fund managers. Trustees must still comply with these duties when undertaking the functions that have not been delegated. The day-to-day investment decisions, such as the types of investments to hold, may be delegated to asset managers but trustees retain supervisory and overall strategic decision-making power. This normally includes determining the overall investment objectives and making strategic investment decisions, such as the risk/return profile appropriate to the membership, and the proportion of investments to hold to achieve this. Trustees also retain legal responsibility for monitoring fund managers. They can be held responsible for the acts or defaults of asset managers if they have not taken all reasonable steps to satisfy themselves that their asset managers: have the appropriate knowledge and experience to manage scheme investments; are carrying out their work competently; and are complying with the Occupational Pension Schemes (Investment) Regulations 2005.[25]

Institutional investors at the FCA’s roundtable commented that there is a widespread misconception that trustees would be liable for any decisions made without the agreement of their investment consultants, despite the fact that this is not borne out by section 36 of the Pensions Act 1995. As the FCA’s commissioned research[26] indicates, trustees have a tendency to rely heavily on individuals, such as investment consultants, whom they perceive as having greater investment knowledge. This was also the finding of a study sponsored by SEI’s (NASDAQ: SEIC) Institutional Group, in conjunction with IFF Research and Dr Iain Clacher, Associate Professor in Accounting at Leeds University, published in January 2016, which showed that many trustees of defined benefit (DB) schemes are failing to challenge their investment consultants, attributing these results to the prevalence of group think. The survey of 100 DB trustees showed 59% did not frequently consider alternatives to their consultants' recommendations.[27] The Pensions Regulator’s 2015 Landscape Research also accorded with this view, saying that “it was rare that the trustee board disagreed with its external advisors. Across all of the advisor types, the majority of schemes indicated that they rarely (58%) or never (24%) disagreed with this advisor (with 14% sometimes disagreeing and 1% always disagreeing).”[28]

[24] Freedom of Information ("FOI") requests were sent to all the LGPS funds in 2015 by the NGOs Community Reinvest and Friends of the Earth to ask questions about the funds’ management of climate risk. ShareAction and ClientEarth have also recently supported individual savers to correspond with their pension funds and ask similar questions.

[25] ShareAction and ClientEarth. (September 2016.) *The hot debate on climate risk and pension investments: Does practice stack up against the law?*, p10. Available online at: https://shareaction.org/wp-content/uploads/2016/09/ClimateInvestmentDutiesInvestorReport.pdf [accessed 9 September 2016].

[26] Financial Conduct Authority. *Asset Management Market Study* (2016), p68. Available online at: https://www.fca.org.uk/publication/market-studies/ms15-2-2-interim-report.pdf [accessed 20 February 2017].

[27] IFF Research and Clacher, I. (January 2016). Available online at: https://www.seic.com/enUK/about/16880.htm [accessed 20 February 2016].

[28] The Pensions Regulator. (October 2015). *Trustee Landscape Quantitative Research: A report on the 2015 Trustee Landscape research*, p39. Available online at: http://www.thepensionsregulator.gov.uk/docs/trustee-landscape-quantitative-research- 2015.pdf [accessed 20 February 2016].

The FCA has found that that investment consultants mostly fail to identify asset managers that outperform their peers,[29] that consultants' interests may not always be aligned with those of their clients;[30] and that it is essentially impossible for investors to monitor how well their consultants are performing.[31] In particular, there is no standardised, comparable, industry-wide methodology for measuring asset allocation advice,[32] although this has a significant effect on investment returns. Competition clearly cannot work effectively in these circumstances and there seems to be a strong case for bringing these services within the FCA's remit, so that it can assess and set standards for the advice given.

Finally, and as discussed in more depth in ShareAction's 2012 report *Whose Duty?*[33] the legal regime protecting savers in contract based schemes is significantly weaker than fiduciary duty which applies in the trust-based setting. Under trust law, the beneficiaries are seen as vulnerable and in need of protection by the trustees but the contract law framework defines savers as active consumers capable of making informed decisions. In theory, the beneficiaries of contract-based schemes are protected legally by the binding terms of their contract. In practice, the asymmetries of information between parties to contracts for complex financial products mean that these agreements can be, and often are, written in a way that favours the provider and imposes unfair terms on customers.[34] It is manifestly unfair that savers' level of protection is dependent on the quirks of the law which governs the pension schemes their employer happens to offer.

Recommendations

We would recommend that the FCA:

- **Introduces a strengthened regulatory duty for asset managers to act in the best interests of investors.**
- **Brings the provision of advice by investment consultants within its regulatory perimeter.**
- **Strengthens the FCA's rules for non-trust based pension schemes so that providers are required to act in the best interests of savers.**
- **Commissions academic research and industry surveys on the purpose of the asset management industry and how this purpose can be better achieved. The FCA should use this work to inform recommendations made in the final report of this market study.**
- **Places a duty on asset managers, not only to demonstrate how their fund delivers value for money to investors, but how their investment strategies reflect the investment horizons and long-term objectives of investors. In reporting to clients, asset managers should include a narrative report setting out how their investment strategy is consistent with the investment horizons of the client (e.g. the longer-term horizons of pension funds).**
- **Requires asset managers to supply pension fund clients with a short consumer-friendly annual report on the scheme's equity and other holdings; how they have considered key strategic risks and how these are being**

[29] Ibid, p151.
[30] Ibid, p160.
[31] Ibid, p163.
[32] Ibid.
[33] Fair Pensions. *Whose duty? Ensuring effective stewardship in contract-based pensions* (2012). Available at: http://shareaction.org/wp-content/uploads/2016/01/WhoseDutyReport.pdf [accessed 20 February 2017].
[34] ShareAction (June 2015.) *Realigning Interests, Reducing Regulation*, p25. Available online at: http://shareaction.org/wp-content/uploads/2016/01/ReducingRegulationReport.pdf [accessed 9 September 2016].

managed to protect savers' long-term outcomes; and a clear statement of the scheme's approach to Responsible Investment and good stewardship, and how this approach has been implemented over the past year, including disclosures of voting on shares. Pension funds should be required by the DWP to publish these reports on their website so that savers can access them. This is key to creating accountability all the way down the investment chain.

- **Works with the Government and other regulatory bodies to address issues arising from the inappropriate management by pension schemes and their fund managers of ESG risks (recognising that these are financial risks) – in particular, climate change. For example, assisting The Pensions Regulator with preparing a report on the pensions industry's exposure to risk under the Adaptation Reporting Power (pursuant to the Climate Change Act). A Climate Change Adaptation Report on the impact of climate change on the UK insurance sector was previously produced by the Prudential Regulation Authority.[35] Risks facing the pensions sector are equivalent to, if not greater than, than those facing the insurance sector, due to pension funds' diversified portfolios and the systemic risk presented by climate change.**
- **Ensures that any regulatory approach taken on minimising costs of investment does not impact on the ability to undertake stewardship of assets and other responsible investment activities that serve end-investors' interests, particularly those with long-term investment horizons. It is hard to see how a failure to properly steward investments is compatible with a duty to act in the best interests of savers. A poorly managed exposure to long-term risks and opportunities may have a much more significant financial impact on portfolio returns than any small increase to the cost of investment at the present time.**

Yours sincerely,

Rachel Haworth
Policy Officer

[35] Prudential Regulation Authority. *The impact of climate change on the UK insurance sector* (September 2015). Available at: http://www.bankofengland.co.uk/pra/Documents/supervision/activities/pradefra0915.pdf [accessed 20 February 2017].