

What Impact has the UK amendment to the Pensions Act had on the take up of SRI by Pension Funds: Success or Failure?



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Who is UKSIF?



- ⌘ The UK's membership network for Socially Responsible Investment (SRI)
- ⌘ Primary purpose: to promote and encourage the development and positive impact of SRI amongst UK based investors.
- ⌘ Broad membership: fund managers, brokers, banks, building societies, financial advisers, trade unions, and NGOs.

Background to SRI Amendment to 1995 Pensions Act



- ⌘ First proposed at The UKSIF Annual Lecture by John Denham in 1998, then Pensions Minister.

- ⌘ Apparent objectives:
 - ☑ to promote responsible share ownership and generate a 'Civil Economy';
 - ☑ to encourage and stimulate increased analysis of corporate social and environmental performance by investors;
 - ☑ to foster a climate encouraging business to adopt CSR best practice by listed companies.

The SRI element to reform the the 1995 Pensions Act



- ⌘ Placed a requirement on trustees to declare via a Statement of Investment Principles (SIP):
 - ☒ “the extent (if at all) to which social, environmental or ethical (SEE) considerations are taken into account in the selection, retention and realisation of investments; and the policy (if any) directing the exercise of the rights (including voting rights) attaching to investments”. (HMSO, 1999, Section 35(3)(f))

- ⌘ Legal constraints:
 - ☒ “It is... clearly inappropriate and indeed unlawful for trustees to pursue ethical goals in such a way as to prejudice the financial interests of the members” (Denham, 1998)

Initial Pension Fund Response

- ⌘ UKSIF research in 2000 showed that 59% of pension funds, representing 78% of assets, had incorporated SRI policies into their SIPs
 - ☑ Engagement (also known as shareholder activism) rapidly became the preferred approach to SRI for UK pension funds.
 - ☑ Many also claimed to have an “integrated assessment” approach - i.e. integrating such issues where material to share price.

- ⌘ Initial government view:
 - ☑ “has made a valuable contribution to CSR.” (Douglas Alexander, Minister for CSR, 2001)

Fund Manager Response

- ⌘ A number have developed engagement/shareholder activism policies - a few offer bespoke products.
- ⌘ In 2002 the Institutional Shareholders' Committee issued a new code on activism, mainly in response to Myners Review. The broad code includes CSR (briefly):
 - ☒ *"shareholders and/or agents may want to intervene include when they have concerns about... the company's approach to corporate social responsibility"* (ISC, 2002, p4)
- ⌘ It recommends that investors:
 - ☒ Monitor investee company performance
 - ☒ Intervene where necessary
 - ☒ Evaluate the impact of their engagement
 - ☒ Report back to clients / beneficial owners

PLC Response

- ⌘ Broader and better disclosure of CSR performance:
- ⌘ ABI Guidelines - an institutional response to Pensions Act changes
 - ☒ Promote disclosure of Significant Risks arising from SEE in Annual Report and Accounts
 - ☒ Current ABI view on PLC reporting:
 - Full reporting = 10%
 - Moderate = 34%
 - Limited = 41%
 - None = 15%
- ⌘ Some PLCs have developed specific Investor Relations competence.

International perspective



- ⌘ UK defining new standards of best practice

- ⌘ SRI elements of Reform to Act have been replicated internationally:
 - ⌘ Australia
 - ⌘ Belgium
 - ⌘ France
 - ⌘ Germany
 - ⌘ Italy
 - ⌘ Sweden

Post 2000 UK studies

- ⌘ **However**, recent studies have identified a gap between SRI policies and practice for most UK pension funds:
 - ☒ JustPensions 2002 report “Do UK Pension Funds Invest Responsibly?” – most don’t.
 - ☒ Recent UKSIF research showed that Fund Managers are engaging on behalf of £84bn of pension fund holdings in UK listed companies...
 - ☒ ... 24% of assets NOT the 78% our 2000 research would have anticipated

- ⌘ Early indications of an implementation gap in SRI policies v practice

Implementation gap confirmed by DWP/HMT review



- ⌘ “The Myners Principles and Occupational Pension Schemes: Volume 2 of 2 – Findings from quantitative research:
 - ☒ **Less than ten per cent of pension schemes have acted on activism** and either established their own policy, or been influenced in their choice of fund manager by the policies they offered in this area.
 - ☒ Amongst the sub sample of the survey that answered questions on the Myners Principle of Clear Objectives, **only half (49 per cent) were meeting the legal obligation to disclose their SRI policy**, or lack of one, in their SIP”

Closing the Implementation Gap



- ⌘ UKSIF believes that the reporting of engagement activities is key:
 - ☑ Extend the amendment?
 - ☒ Reporting requirement
 - ☑ Guidance from regulators on pension fund reporting?
 - ☑ Guidance from the ISC on reporting to clients/ beneficial owners?
 - ☑ Development of the Eurosif Transparency Guidelines

Myners Activism Proposal



- ⌘ **HMT’s ‘Myners principles for institutional investment decision-making: review of progress’** proposes to revise principle 6 (activism) to require compliance with the ISC:
 - ☒ “trustees should comply with the ISC statement of principles on the responsibilities of institutional shareholders and agents, and ensure that the principles are incorporated into fund managers’ mandates. In line with the principles, trustees should also ensure that managers have an explicit strategy, elucidating the circumstances in which they will intervene in a company; the approach they will use in doing so; and how they measure the effectiveness of this strategy”.
- ⌘ Supported by a “voluntary, independently compiled report on implementation”
- ⌘ UKSIF strongly welcomes this suggested approach

Conclusions



- ⌘ Difficult to separate Pensions Act impact from broader government efforts to generate Civil Economy.

- ⌘ Successes:
 - ☑ Early indications of broad policy statement take up.
 - ☑ Some product development.
 - ☑ Investment consultants developing competence.
 - ☑ CSR performance improvement by PLCs.
 - ☑ International replication.

Conclusions



⌘ Failures:

- ☒ Significant lack of compliance with letter of SRI SIP regulation.
- ☒ Significant gap in policy and practice.
- ☒ Lack of monitoring of implementation by schemes.
- ☒ Not much explicit demand reported.

Conclusions



- ⌘ Therefore, while there are elements of both success and failure, it has failed on some important aspects.
- ⌘ Current DWP/HMT proposal on Activism is a welcome attempt to redress the elements where it has failed.
- ⌘ Further reviews will be required to monitor success and establish whether proposals surrounding extending the reporting requirement successfully close the implementation gap.