

# Environmental Audit Committee

Oral evidence: [Green Finance](#), HC 617

Tuesday 6 February 2018

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[Watch the meeting](#)

Members present: Mary Creagh (Chair); Colin Clark; Mr Philip Dunne; Mr Robert Goodwill; Caroline Lucas; Kerry McCarthy; Dr Matthew Offord; Alex Sobel.

Questions 197-279

## Witnesses

I: Alice Garton, Company and Financial Project Leader, Client Earth; Dr Ben Caldecott, Oxford Sustainable Finance Programme; Russell Picot, Chair of the Trustee board of the HSBC Bank (UK) Pension Fund; and Polly Billington, Director, UK100.

II: Emma Howard-Boyd, Chair of the Environment Agency; Diandra Soobiah, Head of Responsible Investment, NEST; and Will Fox-Robinson, Director, UK Institutional Business and Head of LGPS, Natixis Investment Managers.

Written evidence from witnesses:

- [Client Earth](#)
- [Oxford Sustainable Finance Programme](#)
- [UK100](#)

## Examination of Witnesses

Witnesses: Alice Garton, Dr Ben Caldecott, Russell Picot and Polly Billington.

Q197 **Chair:** Can I call the meeting to order and welcome our witnesses this morning to our panel on Green Finance? For the purposes of Hansard, can you introduce yourself from left to right, beginning with you, Ms Garton?

**Alice Garton:** Alice Garton, Project Leader at Client Earth.

**Dr Caldecott:** Ben Caldecott, Director of the Sustainable Finance Programme at the University of Oxford.

**Polly Billington:** Polly Billington, Director of UK100.

**Russell Picot:** I am Russell Picot. I chair the HSBC Bank (UK) Pension Fund Trustee board. I am a special adviser to the FSB Task Force and I have several other roles.

Q198 **Chair:** Thank you all very much indeed for being here, and thanks to our audience. We are not used to having quite so many people in the room but it is nice to see everybody here showing such great interest in this important subject.

We have had quite a lot of evidence that—given the recent fall in clean energy investment in the UK, and given the imminence of our leaving the European Union, where we will no longer have access to European Investment Bank Funding—there could be a green investment gap facing the UK. Do you think those concerns are justified and, if so, what should the Government be doing to fill that gap? Starting with you, Ms Garton, please.

**Alice Garton:** We believe that the Task Force on Climate-related Financial Disclosures is an essential way of amending and adapting existing probes and guidance. Increasing the extent to which financial regulation applies to climate change is a business risk. We also think clarifying fiduciary duty to the extent it applies to asset owners and asset managers in the UK will help unleash some of that capital flow.

Q199 **Chair:** In your submission you said that “the Strategy does not go far enough, in policy terms, to make up ground that has been lost in recent years as a result of ‘erratic and uncertain policy-making’”.

**Alice Garton:** The Clean Growth Strategy—we have made a submission related to the Climate Change Act, which is something that I am not permitted to talk about at this particular hearing.

Q200 **Chair:** That is fine. Ms Billington, you are very specific about the lack of ERD funding to local authorities. What are your concerns?

**Polly Billington:** There is clearly a finance gap on clean energy. It is primarily an issue of development capital. As you point out, with the

prospect of the UK leaving the European Union, the access to the kind of funding that has currently been available to local authorities is under threat. However, the development capital is important because, although Government has invested in individual technologies previously—and we have seen how that has prospered—what we actually need to do to transform the energy system overall to make it more resilient in the future, is local transformation.

You need integrated projects at local level and the people who are going to be best placed to do that, because they have levers across a wide range of energy vectors, is the local authority. Those people have ambition. It is quite clear, from the University of Edinburgh's research into this, that there is ambition here. Also, that piece of research indicates that a large proportion of those local authority projects at the moment are in response to a Government intervention to meet a market failure, which are the Heat Network Delivery Unit and HNIP.

We should be building on things that the Government have done in the past, which is understanding that sometimes you need to intervene when the market isn't managing to deliver, but to do it at scale and to particularly look at integrating proven technologies. If we think we are going to be able to transform the energy system in this country to decarbonise it all together, simply, with very, very large projects feeding into the National Grid, we will have all the problems with intermittency that worry people.

Demand management: how you are going to increase flexibility, how you are going to introduce storage—almost all of those things are going to happen at a local level. The Government met the anxiety about heat, which is also inevitably delivered locally, by establishing the Heat Network Delivery Unit. Something equivalent—and our proposal is a clean energy action partnership—would give local authorities the capacity that they need, on a legal and financial basis, to be able to deal with private finance and, also, arguably, leverage in all of that private finance that people say is swilling around ready to be invested and that it is not being invested in the kind of energy projects that would arguably transform this country's energy system.

Q201 **Chair:** What could the Government do to help local authorities access that private sector finance? What do you think is not happening at that meso-level?

**Polly Billington:** If you have a clean energy action partnership, where the local authority has to come with a clear consortium of people who know and understand what is happening—they are not doing it on their own; they are doing it with their local university, local businesses and so forth—what the Government can do is bring development capital. Arguably, you would not even need to bring a new pot forward because there is lots of that money around already.

Local authorities don't have the capacity to know when to go to OLEV, when to go to HNDU, when to access Salix. All of these pots of money are

in the Government somewhere. Being able to find that money and then leverage in private finance, because private finance is used to things being big and quite straightforward. Local energy projects at the moment are too small. They need to be done at scale, so that private finance is going to be interested. If they are going to be done at scale, they need to have a national intervention to be able to support that.

Q202 **Chair:** Can you talk to us about the Heat Network Delivery Unit? We don't follow BEIS, so we don't know about it. Can you say when it was set up and what it does, please?

**Polly Billington:** I think I have included some references to it in our written submission and it is certainly available in the report, which is also online. That came out of the need, as the Government saw it, to meet the heat decarbonisation targets that the Climate Change Act requires. They developed it along the lines of saying, "Right, okay, what do we need to be able to help local authorities develop district heating systems?" They realised that what they needed was a little bit of development capital, a critical friend who can walk them through what is needed in order to be able to get projects ready for private investment.

One of the other important things to remember about local authorities and their attitude towards financial risk, as in contrast to private finance, is local authorities don't necessarily feel very comfortable, as you will understand, necessarily engaging with private finance.

There is a reason why we are not the biggest box office draw this morning. It is because Carillion is giving evidence along the corridor.

Local authorities will need legal and financial capability and capacity to be able to deal with that. They are also used to their finance being quite cheap. If somebody comes with a really exciting and innovative project, but it cannot be financed through Public Works Lending Board finance, then your chief finance officer will say, "Why on earth should we do that when we can carry on with business as usual and keep our borrowing cheap?" Understanding that, actually, 'business as usual' is all you will get if you are going to borrow that way, so we need to understand where else we can borrow and access to that finance is important.

Q203 **Chair:** Thank you. We will go back to your submission because we have not had a proper look at it, but how much money have they allocated to the Heat Network Delivery Unit?

**Polly Billington:** Off the top of my head, it is hundreds of millions but I would need to check. Can I come back to you?

Q204 **Chair:** Sure. That will be fine. Other colleagues, Dr Caldecott?

**Dr Caldecott:** Your question is important. Financing challenges and financing gaps will emerge and disappear in different bits of the system over time, as the financial system, as financial institutions see opportunities and plug gaps.

The big problem at the moment is, of course, we have had the Green Investment Bank privatisation, we also have the risk of the UK leaving the European Investment Bank, and those have been two important sources of funding for projects, so that is one thing.

The other thing is around the cost of capital. A real opportunity, which I think has been missed over the last few years, is around how we can encourage the refinancing in the debt capital markets of operational cashflow-producing infrastructure. If you can refinance your operating windfarm cheaply in the debt capital markets—through project bonds or through securitisation—that enables people that have invested in the construction of that asset to refinance cheaply and then recycle that money back into construction.

For a variety of reasons, that isn't working. It is not working in the UK. It is not working anywhere, and I think that should be a top priority for the Government and, indeed, if they decide to do things through another institution that is not the GIB in the future.

Q205 **Chair:** Thank you. Mr Picot?

**Russell Picot:** At a very high level, I would have thought that there was a natural fit between the long-term investing interests of UK pension schemes and the need to fund greening the infrastructure of the UK. The challenge is: how do you bring the money to fund the projects?

There are various ingredients that are necessary, so policy certainty to create confidence to invest. Most pension schemes don't select individual assets. They will invest through funds created by fund managers, so obviously the fund managers need to be creating the funds to then offer those to the asset owners. For the asset owners, pension schemes need to be determining the characteristics of what they are asking the fund managers to do. They need to create perhaps a mandate for a renewable fund or perhaps a green finance fund, and there are—as I am sure the Committee is aware—a number of barriers around actually achieving that in the system at the moment.

Q206 **Chair:** Thank you. We have a series of questions on that, but it was just specifically on the green energy investment gap and whether you saw that developing.

Did you find your number for the Heat Network?

**Polly Billington:** Yes. Initially, when it was in inception, it deployed over £40 million in grant funding to 131 local authorities to over 200 projects. That has now resulted in the Heat Network Investment Programme—£320 million to be deployed through investment in grant projects that have reached the end of their development phase. There are capital investment programmes to support up to 200 projects, leveraging up to £2 billion worth of wider investment.

Those figures are particularly important because quite often, when we talk to people concerned about market interventions, they are looking at very public investment, heavy proportions, and when you are talking

about proven technologies the potential for access to private finance is much bigger and, therefore, the investment from the public purse would get a bigger return.

Q207 **Mr Philip Dunne:** Could I follow that up? Maybe Mr Caldecott knows the answer to this question. Are you able to give the Committee a sense of the scale of both Government-subsidised schemes, which have gone into green energy projects over the last decade, versus the scale of private investment that has gone into green energy projects?

**Dr Caldecott:** I don't have those numbers to hand but the ONS tracks those figures. The key thing is to distinguish between the money that is allocated to underpin things like the Contracts for Difference and the Feed-in Tariffs and the Renewables Obligation, versus the money that is raised on the back of those cash flows.

Going back to the financing gap, obviously if there are cash flows and the Government have policy signals, then, in an OECD-country developed economy, with a very highly developed financial system, there really should not be a financing gap.

**Chair:** Interesting. Thank you.

Q208 **Caroline Lucas:** I want to pick up with Dr Caldecott to begin with, to ask if you could say a little bit more about your view on the extent to which there are serious market failures in the way our financial system currently accounts for long-term environmental risk.

**Dr Caldecott:** This is an area of research that I spend a lot of time on. There is significant evidence that financial institutions have trouble pricing and understanding environmental risks—both those related to physical environmental change, like physical climate change impacts, but also how societies respond to those changes through regulation, technology, social norms and litigation.

There are a bunch of reasons for that and these are long-term issues. They are novel, often. The datasets are not there. They are non-linear. They exhibit that tendency. They are correlated and interrelated in different ways. Therefore, I have a bit of sympathy for financial institutions trying to navigate these risks but I would say that they are certainly not properly priced into decision-making in financial institutions in the UK or, indeed, internationally.

Q209 **Caroline Lucas:** What could be done in the short term to address that?

**Dr Caldecott:** That is going to require a number of different interventions, some of which have been identified by the European Commission High-Level Expert Group on Sustainable Finance and by others. Some of that is to do with disclosure. Some of that is to do with data. Some of that is about fiduciary duty. Some of that is about addressing governance problems. Some of that is about cognitive biases, behavioural biases that exist within institutions, training—a whole range of things.

Q210 **Caroline Lucas:** What would be helpful is if you could help us navigate our way through the very many different proposals there are out there. You have just outlined a number of them, and you have tax breaks for green bonds, easier access to finance for local authorities, enhanced disclosure, and clarification of fiduciary duty. There are all of these things swirling out there. Could you say a bit more about how you might advise policymakers to evaluate the merits of the various proposals? Otherwise, there is a risk of this kind of avalanche of, "We will do all of this stuff" and nothing gets done because the whole menu looks too huge.

**Dr Caldecott:** Sure. It is worth taking a step back and trying to remember what the objective is. Surely the objective is to use finance as a way to promote green and the transition to sustainability, and to prevent brown investments, investments that harm that transition. When the Committee is evaluating different instruments and policies that have been recommended by different stakeholders, how can they do that? How can they affect the real economy?

In the evidence, I have suggested four ways in which that could be done, the first of which is: does the policy or instrument reduce the cost of capital for green or does it increase the cost of capital for brown? That is probably the most significant thing. The second thing is: does it improve the liquidity or the number of buyers for green assets or does it decrease the number of buyers for brown assets? A third thing: does it generate some risk mitigation options for dealing with climate risk and other environmental risks? Lastly, you could have policies and instruments that do none of those things but, arguably, generate spillover effects and encourage systemic change in the system.

If recommendations do not do any of those things, you should probably throw them out. Certainly, some of the recommendations that I have heard people in the community make may not do very much on any of those four fronts, so it is worth having a consistent framework to assess these proposals.

Q211 **Caroline Lucas:** My final question is for anyone to answer. I am pretty sure you are going to say "both", but if the question was: should we be concentrating on specific green finance proposals to mobilise capital for clean energy projects, per se, or would focusing on greening finance as a whole, with wider systemic changes, have more of an impact? If I was to force you to say one or the other rather than both, do you get a sense of whether or not you go for the specific projects or the systemic approach?

**Dr Caldecott:** I would go for the systemic approach.

**Caroline Lucas:** Any other—

**Russell Picot:** So would I because I think perhaps one of the biggest levers we need to pull on is to change the discussions in boardrooms of companies, of fund managers, of pension schemes. It is about mainstreaming sustainability and green finance. If you just focus on the green finance piece, you might change at the margin but you will not actually change the stock of where money is invested. You can try to

achieve that change of boardroom discussion through different levers. Disclosure is one of those; gentle encouragement by Government, by regulators and so on, but I think if you change the boardroom discussion, so that climate risk and green finance becomes a normal part of board agendas, that potentially is transformational and would achieve the greatest possible benefit.

**Alice Garton:** I also agree with the systemic risk focus because, after all, what we are trying to do is to prevent a shock to the system that will result in losses, particularly to pension members. Yes, I think we want that outcome, ultimately, not to be green finance but for finance to be green and for a systemic approach.

**Polly Billington:** That would certainly help at local government level, where you have legal and finance officers who obviously have, arguably, more sway over decision-making than people who are put in the sustainability box. Unless and until sustainability is utterly mainstreamed, and people are not saying, "What can we get done quickly and cheaply?" but what happens quickly and cheaply is also long term and sustainable, then we will be in a much better position.

Q212 **Chair:** How sophisticated do you think the analysis of climate risks are? The Bank of England has talked about physical risks, transition risks and liability risks. That is all so far so obvious, but I was in a meeting with the Met Office yesterday and they were talking about how they measure risk, which is also to look at vulnerability and exposure.

Obviously, thinking from a local authority point of view, cities on rivers are more vulnerable to flooding than cities on hills that may be more vulnerable to other types of risk. The physical risks of climate change may be much more dangerous to a person in their nineties or a baby under six months than to the rest of the adult population, so, this vulnerability and exposure thing, has that been talked about or thought about in any either academic papers or any of the circles in which you move?

**Dr Caldecott:** The ability to test and understand exposures, using different scenarios, is pretty well developed, particularly for physical risks. The transition risks and liability risks the Bank of England has talked about because they are about societies responding to a stimulus. Political economy dynamics and things like that are often a bit harder to measure, so that is probably a newer area.

But I would say that, with scenario analysis and with the measures that we have at the moment, there is no reason why a financial institution, a company, a local authority or a Government, should not be undertaking this kind of risk analysis. Of course, there are going to be uncertainties but the quality of analysis is good enough to do very good assessments of risk.

**Russell Picot:** I think that three-bucket categorisation is helpful. My sense is that the system is in its infancy of measuring climate risk, be that transition risk and equities portfolio or, indeed, physical. From my

own experience, it is typical to think about physical risks if you are making long-term investment decisions, property or in infrastructure or something. When you are looking at transition risks on equity and bond portfolios, we have relatively few good examples of how you should try to risk manage that. There are some encouraging signs of that changing, but that needs to happen quite quickly.

- Q213 **Mr Philip Dunne:** Just picking that up, doesn't the property and casualty-insurance market assess these short-term risks all the time? It is their bread and butter business, is it not, the impact of climate risk on damage to property?

**Chair:** It is the exception that proves the rule, though, I think.

**Russell Picot:** I am sure they do and that is normally a one-year underwriting is my understanding. I am not an insurance specialist I should say.

- Q214 **Mr Philip Dunne:** But there are long-term pricing implications and they look at trends to see where hurricane risk is getting worse.

**Dr Caldecott:** A lot of the best physical risk modelling expertise is in the insurance and reinsurance industry, unquestionably. That expertise is going to be better for large insurance markets, so it is very focused on developed country markets.

However, that expertise on the liability side of an insurance business model does not carry over to the asset management side of the insurance business model. You might have heard evidence from insurers previously or in forthcoming evidence sessions where they might point that out, but it is a great inconsistency that these same institutions have these capabilities and yet are not applying them.

**Alice Garton:** There are some exceptions to that. There are now 15 insurance companies that have announced some kind of divestment policy in relation to coal investments on the asset side, and there are three insurance companies that have said they are going to stop underwriting new coal projects. They are going to forego the short-term profit of that particular project because they know in the long term that more coal will take us above two degrees, which has an impact on the insurance business. I think that is quite a significant development.

- Q215 **Mr Philip Dunne:** That takes me neatly on to my line of questioning, which is more about corporate behaviour. The Government has endorsed the Task Force on Climate-related Financial Disclosure proposals and is looking for voluntary adoption by public companies, many of which around the world have indicated they want to do that. Do you think that is the appropriate way to go? That is probably a question for you, Mr Picot.

**Russell Picot:** If I were to take a step back and say that, if this is going to work, we need all the players in the investment chain to play their part, so obviously listed companies and companies that access the public

equity debt markets need to produce high quality, quantitative and quality of data information about climate risk.

At the other end of the spectrum, the asset owners need to be including climate risk in their risk management and they need to be asking for information about climate risk in their portfolios. Therefore, you create the tension in the investment chain for the asset owners pulling on the chain through the fund managers who ask the listed companies for the information.

I focus at least as much on the role of the asset owners and the need for asset owners to be seeking this information, to be reflecting on it and publishing in either accounts or through stewardship reports or something to their own beneficiaries. That is what we need.

A period of voluntary adoption is helpful because I think there are a couple of areas that are quite new, both to the companies and indeed to investors, but frankly I don't think you can run a voluntary regime for something as important as climate risk forever and a day. It either becomes so important it needs to be put in codes or law or it just falls by the wayside.

**Q216 Mr Philip Dunne:** How are asset managers undertaking that function that you have just described? Have they set out guidelines for the trade associations and asset managers to respond in the way you have just described?

**Russell Picot:** A number of the asset owners have signalled publicly that they are supportive of the TCFD recommendations and are committing to providing information to their beneficiaries. It feels a little bit hit and miss at the moment. My own pension scheme has written directly to our 24/25 fund managers. We wrote them a letter asking them what they were intending to do on the recommendations to try to create the pressure within the system, but it would be great if many others were to follow suit.

**Q217 Mr Philip Dunne:** Is there a recommendation among the monitors of corporate governance that this is something worthwhile and might have impact on financial returns, or is that connection not made?

**Russell Picot:** The FRC has put out public consultation, I think amendments to the Corporate Governance Code and The Pensions Regulator has changed its guidance for DB and DC. If you were to try to change the system a bit more quickly than we are at risk of doing at the moment, I think some more positive noises would be really helpful. It can take an awful lot to shift inertia in the system, as I am sure the Committee is aware. My own sense is that, although there are an encouraging number of actors who are going to do the right thing, I think the evidence suggests that we need rather more than are currently proposing to adopt.

**Q218 Mr Philip Dunne:** The French have adopted legislation. Would other panellists like to comment on whether that is appropriate for the UK, or

whether you think the voluntary codes that we have at the moment are sufficient?

**Alice Garton:** I do believe that some kind of implementation is necessary. There could be two ways, either a new law, such as Article 173, or we use existing framework. Our view is that climate risk should be treated like any other business risk and it should be monitored by companies within their existing governance procedures. We should use the existing corpus of rules and guidance primarily. As Russell pointed out, they can be amended.

For example, the Corporate Governance Code consultation coming up at the moment, and the Stewardship Code consultation, the FCA has a number of ways that they can integrate climate risk into their existing corpus. They send "Dear CEO" letters around existing risks; for example, cyber security. They could do a similar thing on climate change.

There are lots of ways we can improve the existing framework as it applies to climate risk, and I am sympathetic to both regulators and industry that this is a new area. That scenario analysis is complex, so I can see that to give a couple of years to try to test the systems is a good idea. Ultimately, I think we will need a mandatory law. By 2020, if regulators in the industry have not achieved significant improvements in climate risk disclosure, I would suggest that we would need legislative implementation. Again, that can be either by amending existing legislation or a standalone new law, for example, the Modern Slavery Act, something that requires directors and trustees to report on climate risk.

Of course, if you have a new standalone law, it is very important that it works effectively with the range of existing codes, guidance and laws, so you could have a cross-reference provision within that Act where there is a principal risk and it is reported in the strategic report. For example, if you are an oil and gas company, you could have a cross-reference, so that that would be the long-term view.

**Dr Caldecott:** Could I also say something on this? I am on the Green Finance Taskforce, and I chair its TCFD implementation workstream. It is certainly my view that the Taskforce should recommend that the TCFD becomes mandatory. I think the best way of doing that, in the first instance, is that regulators should update the relevant rules and codes to make sure that they make reference to the TCFD. That would ensure that the TCFD is completely flush with the existing UK corporate governance framework – you cannot get more mainstream than that.

Of course, if the regulators don't do that effectively then I think there is a strong case for legislation and there could be amendments to the Companies Act as well. That is something else to mention.

The other thing to say is that, while the TCFD is very important, you have to remember that it is only focused on one thing, which is climate risk. We should have a corporate governance and corporate disclosure framework in this country that does two things: one is that it discloses

risks related to the environment—of which climate risk is one—but also has a framework for disclosing impacts, the impacts that companies and investors are having on the climate but also on the SDGs and other things as well. Therefore, the aspiration should be to have a framework that can do both effectively. Some of it might be mandatory; some of it might be voluntary.

- Q219 **Mr Philip Dunne:** That is a very interesting line we could run for some time, but could I just ask Ms Billington about the impact on local authorities? We touched on pension funds with local authorities and on activities with local authorities. Should they be doing more to report the kind of impact that they have on the environment?

**Polly Billington:** It is not strictly a matter of our report and our research up until now. I know that local authorities have a lot of pressure from a small number of people about how they invest their pension funds, and that is something that makes them anxious. Some have made big decisions about how they divest from fossil fuels. What we have been talking about would give them very strong signals to make those decisions, not only for ethical reasons but for hard headed financial ones.

In terms of accounting and making sure that local authorities are assessing their own risks, we need to understand of course that the difference between corporate governance is when you are talking about how you invest your money to get money back, and local authorities are normally talking about how they spend their money. Over time—and I am somewhat anxious about the timeframe because I know we have the laws of physics to face and the laws of politics moves somewhat slower—I would be keen to make sure that what does happen in the corporate governance world ends up delivering for local authorities, in terms of the way that they assess their risk.

- Q220 **Mr Philip Dunne:** National indicator 118 was stopped in 2010, so they do not have a requirement to report on climate risk. Do you think that has had any negative impact on their behaviour?

**Polly Billington:** Local authorities tend to be quite good at doing exactly what they are told and, if they don't have something that they are doing exactly what they are told, in the current financial climate, the risks are that they won't do anything above what they are absolutely obliged to do.

What has been interesting is that our network, which involves currently 80 local authorities, are ambitious enough to be able to want to make the Climate Change Act by 2050 a reality on the ground, not only by influencing national government to say, "We could do with those kind of national indicators, thanks, not only for ourselves but also to make sure that we have a level playing field", but also they are learning from each other. In those circumstances, you can put more burdens on local authorities and obligations on them to do things or you can work out how they are doing things themselves and establish standards from the ground up.

Things like those national indicators have been very useful, about making sure that everybody has to do it. That means that the standards grow across the board. That needs to be a benign relationship between making sure those standards are there and encouraging greater ambition beyond those standards.

Q221 **Mr Philip Dunne:** But it has not inhibited them from taking steps themselves to improve their own green energy performance?

**Polly Billington:** It hasn't inhibited them but it has deprioritised it for a number of local authorities. There are more than 400 local authorities in this country. I am very proud that our members are the 80 most enthusiastic and ambitious.

Some of these things are that, in the market, you would say that they have some kind of market edge because they are being more ambitious. They also compete among each other, and that is good because that raises ambition. But if this country is to meet its own climate change obligations under its own legislation, and also meet its independent nationally determined contributions under Paris, then you cannot leave it to 80 local authorities. There has to be something that is going to accelerate it even further than that.

Q222 **Colin Clark:** You have already discussed TCFDs, so we may be going over some of the same territory but you may want to make further comment. We have heard that some businesses have concerns about implementation of TCFD. How could the Government implement TCFD in a way that balances the need of companies against the need for robust disclosure, Ms Garton?

**Alice Garton:** The Government could provide base scenarios so there are ways of supporting companies, making it more cost effective. Also, if we use the existing corpus of rules, guidance and framework approach, then it enables companies to adapt the level of disclosure or analysis they are undertaking according to their size, industry and complexity, which is important. Yes, I recognise that we need to ensure the cost of compliance is realistic and equivalent to the size of the company.

Q223 **Colin Clark:** Mr Picot, would you like to comment?

**Russell Picot:** There is a very understandable concern around something that is unfamiliar. That said, the degree of investor pressure particularly around the high emissions sector is very considerable. You will have seen, over the last year or so, shareholder resolutions laid down on a very broad basis on some of those.

If I was to draw a parallel with an industry that I worked in for many years, which was the banking industry, the banks under very considerable investment pressure around their capital positions voluntarily moved to make forward-looking targets available to the market. Why? Because they needed to, to restore confidence, so where the investor pressure really bites then companies will respond.

The best thing we can do is to get strong encouragement for flow. There are a number of groups that are meeting. For example, the oil and gas companies meet to talk about scenario analysis, what they are going to disclose and so on. They should be encouraged. That is a good thing because we need those industries to produce the information, then the investors need to look at that information and there needs to be an exchange of views: what is useful, what is practicable, what really works.

Q224 **Colin Clark:** On that point, we have heard that some corporate bodies felt that they did not have enough information. You are saying that oil and gas are doing something to get together, to undertake scenario analysis or understand what scenarios are appropriate when it comes to climate change. How can this problem be addressed? What is the fundamental problem?

**Russell Picot:** Scenario analysis is certainly a developing tool. There are relatively few publicly available sources that companies can access to actually generate the scenario, so there is a need to get more of those datasets out there. Greater familiarity: there is a need to deepen the support for companies within the system, so invest in consultants and the like who can be very helpful to move companies along this path.

**Dr Caldecott:** There is clearly a bunch of ways in which Government regulators can support the preparers to become familiar with scenarios and some of the recommendations of the TCFD, but I would just say that a lot of businesses do do scenario planning and they do think about managing a whole bunch of different risks. In the spirit of the TCFD, this should be integrated completely into that existing scenario analysis and planning that they do. I don't think it need be such a burden if it is seen in that way. Again, that is why we need it to be mainstreamed into the existing UK corporate governance framework because, if it is seen as a different thing, it will be seen as more of a burden.

Q225 **Colin Clark:** I think you have addressed my next question. Again, Dr Caldecott, your submission has warned that policymakers should be focused more on asset data than risk disclosure. Can you talk us through your thinking on that?

**Dr Caldecott:** The main point I was making was that it would be wrong to assume that disclosure, particularly voluntary disclosure, will provide you with the data—as in investors, civil society, Government—that is actually required to do appropriate risk analysis of company exposures to these different risks. There are a number of reasons for that, one of which is that disclosures don't tend to ask questions about underlying assets that companies own. They trust that companies will calculate the risk exposure themselves and then disclose it to you.

Some of that disclosure, unfortunately, in the recent past has not been very accurate. The coverage is very poor. Not all companies disclose. Even if all companies disclosed, we are only really talking about listed companies not non-listed companies. Then it is only companies in some jurisdictions disclose information, so I think the disclosure conversation is

more about improving corporate governance and that is incredibly important. It is about encouraging companies to think about these issues and manage them.

The data issue can be solved in different ways, and it needs to be solved in a different way because we are not going to get companies to disclose all this information any time soon. The way in which it can be solved, which is new because of developments in remote sensing and data processing, so basically developments in space and in satellites, developments in how we can process information, machine learning, allow us to see the assets that companies own, what they are doing, at levels of detail that are unprecedented, so we can get the data that we need to complete the analysis without asking companies to disclose that information. That also has a benefit, in that it will encourage and enhance disclosures. If somebody goes, "We have this data on what you are doing and what assets you have, is this right or wrong?" then the companies can correct that quite easily. That is the underlying thinking.

**Q226 Chair:** Can you give us an example of anyone disclosing the data or where that data is currently out there, and can you give us an example of what sort of physical things you mean? Because if we are looking at a mining or an oil and gas company, I am not clear how we can see what they have if it is under the sea or under the ground.

**Dr Caldecott:** Yes. There are different challenges for different types of asset but, for example, take a power utility, a power company. It has a bunch of physical assets: power stations. In its disclosures, it is not going to tell you where its power stations are. You might be able to get that information elsewhere. It is not going to tell you how much carbon each of those power stations emits. It is not going to tell you very much about anything to do with the characteristics of that asset, although it might, in the UK and other developed countries, disclose that information to the power regulator.

That is the sort of data that I am talking about when I am talking about asset level data, and with that information you can then go, "Okay, let's see how exposed that asset is going to be to precipitation or flood risk or heat stress in 10 years' time or five years' time. Let's understand how it might be affected by climate policy or concerns about air pollution" and so on and so forth. Then you can aggregate that information at an asset level to a company and, if you have the right ownership information, you can look at the exposure that asset managers and pension funds have as well.

**Q227 Chair:** Do any companies currently do this?

**Dr Caldecott:** Companies don't tend to disclose any asset level information at all, so the way we are getting the asset level information is through a variety of different public and proprietary datasets. We are also doing a lot of work at Oxford, together with Stanford and others, to use satellite imagery and machine learning to get this information.

**Chair:** Fascinating. Thank you.

Q228 **Mr Robert Goodwill:** We have heard that, as far as the TCFD is concerned, having a voluntary start is the right way forward and that the number of more forward thinking and enlightened funds are reacting to the challenges. I did not get the impression what timescale you felt it might be worth looking at when you move from the mandatory approach, so that everybody can be on board. Are there any thoughts on that?

**Russell Picot:** I think we should do two things but, first of all, we should be clear about the process that we would go through to move from where we are today to mandatory, and I think some sort of roadmap that sets out the steps and the milestones would be helpful. Secondly, in my mind, I don't think we can wait five years. This is too important to wait that long, so for me it is probably two to three years. I guess we will know probably in June-July time, how much progress we have made in the UK because we will get all the annual reports out and we can see who has done what.

Q229 **Mr Robert Goodwill:** Thank you. Turning to regulators, the UK obviously has a number of financial regulators, both within the Bank of England and also in Government Departments, Treasury, Work and Pensions and so on. Which of these regulators would you see as having a role in implementing the TCFD recommendations, and which specific actions on TCFD would you see as a priority from the UK financial regulators? Volunteers?

**Alice Garton:** The key regulator would be the Financial Reporting Council, followed by the Financial Conduct Authority and The Pensions Regulator. The Financial Reporting Council has oversight of corporate reporting. Indeed, to also link back to your previous comment about a voluntary approach for the next couple of years, it is important to understand that large swathes of the TCFD, from many companies, are already mandatory through our existing laws.

Section 414C of the Companies Act requires listed companies to report against a range of factors, how they are acting in the long-term best interests of the company and a range of stakeholders as well, so long-term interests, the environment, the community. If you are, for example, in a fossil fuel sector then climate change is obviously a principal risk and long-term factor that affects your business model and should already be in the strategic report.

The FRC has oversight of that reporting. We filed some complaints two years ago in relation to Cairn Energy and SOCO International, two oil and gas companies who are not referring to climate change in their directors' report and the impact that it might have on their business model. We asked the FRC to make some kind of public statement about how climate risk must be material or more likely than not is material to oil and gas companies and they did not. It is a closed investigation. We do believe the FRC could be taking much stronger steps in relation to the extent climate change and climate risk, as a business risk, fits within the existing framework in the Companies Act, so the Financial Reporting Council is key.

The other important thing to remember about the regulators is the FRC is the only regulator that is not set up by an Act of Parliament and is not directly accountable to Parliament, so there is an ongoing discussion with a number of investors about the role of the FRC, more broadly, and whether it needs to be restructured. I believe that has come up in the context of the Carillion investigation and the audit oversight. The FRC is an absolutely key regulator and will continue to be, and there are a number of questions there.

One of our strong recommendations for the inquiry would be that we also look at the extent to which financial regulators themselves are adequately using the existing laws, and whether they can recommend ways they can improve their oversight and enforcement procedures as they apply to existing climate risk.

**Q230 Mr Robert Goodwill:** Thank you for that. I will probably ask you further. Under the Climate Change Act, the DEFRA Secretary has the power to ask public bodies to prepare adaptation reports every five years. You have suggested that he should require financial regulators to prepare adaptation reports in the next round of reporting due next year. What benefits do you feel that would have?

**Alice Garton:** I think this is an important opportunity, the adaptation reporting power. Just as we are asking companies and investors to conduct scenario analysis on the way climate risk affects their particular business models, I see the adaptation of boarding power as a kind of scenario analysis for financial regulators. It requires them to think in the long term about how this issue will affect those that they oversee, again, because the tragedy of horizons—as Mark Carney coined—applies equally to regulators as it does to those that they oversee. The adaptation of reporting power is a way that they can properly and thoroughly assess the implications to various sectors, and then determine which laws already apply and how they can be used more effectively.

**Dr Caldecott:** But let's not forget that it was DEFRA sending a letter to the Bank of England that enabled and encouraged the Bank to do its initial work on climate change, so that adaptation-reporting power has already had a significant impact.

**Q231 Mr Robert Goodwill:** That is helpful. Finally, Ms Garton, it would seem to be your specialist subject if you were on "Mastermind", but how does the structure of the UK's financial regulations impact the ability to take action on climate-related disclosures?

**Alice Garton:** How does the structure of the—

**Q232 Mr Robert Goodwill:** Yes. How does that impact the ability? Is it a hindrance or a help? Do we need to free things up a bit or do we need to regulate in a more detailed way, possibly?

**Alice Garton:** More broadly speaking, we need to ensure financial regulators are working more collaboratively on climate risk, and I think

the adaptation or putting power again is a good way of doing it. I understand there is already some of this happening.

Another recommendation that has come out of the High-Level Expert Group in the EU, which might be an interesting example, is to integrate into the supervisory authorities some climate risk elements within their mandate, so you actually put it at the top of the agenda for the regulators as well. Again, that is something that could come out of the adaptation reporting power.

Our view is that, as a lawyer, there are more than enough laws out there. They are just not being used effectively, and what we are seeing is that climate change has moved from an ethical environmental issue to a core business issue. That core message is not being picked up by regulators themselves because they are also caught in short-term horizons. Nor is it being picked up by industry companies and investors. This forward-looking, long-term scenario analysis is designed to correct that.

**Russell Picot:** I agree with everything Alice has said, so I think one of the challenges we face is one of cost and constraint. If I look at the pension schemes, The Pensions Regulator probably has the same issues. It has a lot of short-term issues that it is concerned about, so how do we get climate risk up the ladder of priorities? Within the existing framework, they could do more. They could, for example—and I think this is a law of large numbers game. This is about changing behaviour of, say, the top 20 or 30 UK pension schemes to mobilise their asset pools. Just writing to them or making a speech of expectation around this, or sending them a questionnaire asking about climate risk, I think could go a long way.

This is an important issue. The country's pension schemes are DB or DC, so if you are a member of a defined contribution pension scheme—that is most young people nowadays—the reality is that you are probably going to be 40 to 50 years away from retirement, and whatever those sorts of timescales climate risk and ESG factors will be material to the financial performance of your funds. I think that is almost a statement of the obvious.

This has to be a topic of discussion for every DC trustee board. I think in the defined benefit space, it is more difficult because the timeframes are generally shorter and of course defined benefit pension trustees are really worried about their deficits, about the quality of their covenant and so on, but in the DC space I think it is clear that climate risk is a real financial risk and it ought to be the subject of discussion and risk management and I would like to see The Pensions Regulator doing more in this space.

**Alice Garton:** Also, the Financial Conduct Authority because nearly 5 million of those DC scheme members are regulated through contract-based schemes by the Financial Conduct Authority, so we have both The Pensions Regulator, trust based and DC schemes and then the FCA. There should be parity between the two, in terms of how the duty is being exercised by trustees on one side and the governance committees under the FCA, to treat climate risk. That is why we would also recommend the

DWP has made some recommendations on ways that you can clarify both the TPR and FCA's oversight and existing laws, and we would commend those as well.

**Q233 Dr Matthew Offord:** I want to explore that point a little bit more, particularly with Ms Garton and Mr Picot. Do pension regulators and also pension funds see climate change as a material issue or as an ethical issue?

**Russell Picot:** I think some pension funds see it as a financial issue and some don't.

**Q234 Dr Matthew Offord:** Why?

**Russell Picot:** That may be to do with the level of knowledge and understanding around the trustee board. They may struggle to get high quality advice as well. I work for a scheme that has an enlightened sponsor. HSBC is a bank that understands climate risk, thinks it is a major shaper of its business and, therefore, when we started our own journey to look at climate risk a few years ago, we had a very natural, easy relationship with the bank to talk about this and they were very supportive. That is perhaps not true for every set of trustees in every company.

**Q235 Dr Matthew Offord:** I was going to pick on you with my next question, as you have direct experience. How do you incorporate financial risk considerations into the financial decisions that you make?

**Russell Picot:** We have done two or three things. We have established, through trustee discussions, a series of beliefs. We believe that climate risk is a financial risk and we have three pillars. First of all, we are, as a matter of policy, supportive of broad based initiatives to try to achieve a two degree better under Paris. That is because we recognise acting alone we won't be as effective as acting in concert with others.

Secondly, we have had a concrete discussion around climate risk and what we could do about it, and some months ago we moved our defined contribution default fund, which is where most of our DC members are—about 80,000 DC members—into a fund that we developed with Legal & General and FTSE Russell, called the Future World Fund. It is a broad based index product but it has a climate risk tilt, so it seeks to adjust the risk profile and try to manage climate risk.

Then the third element is that we have an ESG engagement policy. We believe in engagement rather than divestment, primarily, but we don't believe in a passive approach. Even though our equity product is a passive product, we believe that as an asset owner we should be setting out our expectations of our fund managers about their behaviour. We would expect them, for example, to support resolutions for climate risk disclosure. We would want them to encourage TCFD recommendations to be complied with.

As part of that, we are very active within the whole asset owner scheme. For example, I chair the Institutional Investors Group for Climate Change

Investor Practices Programme. That is the group that is looking at TCFD. It has about 140 European asset owners and asset managers. Again, because we believe that, collectively, we have a much greater chance of achieving the successful outcome.

There is no doubt that the prospect of transition to four degrees is a pretty scary prospect. My trustee board worries about that issue because morally it is pretty unacceptable but financially it would generate a pretty poor return for our beneficiaries, so we think there is an issue that behoves action by us in concert with others and we take it very seriously.

**Alice Garton:** On that point about the scenario analysis, I have been speaking to some people in Australia working for one of the big audit firms advising the banks and investors on scenario analysis and helping them go through the process. Interestingly, they have been doing the scenario in two degrees, four, five, six degrees, and it is the high levels that have freaked them out basically, from five to four degrees. They have suddenly realised the implications to their business models if we stay on the track that we are on now. That is very significant because it triggers their legal duties to act in the long-term best interests of the company, so to what extent can they take mitigation steps now in their role as institutions to keep within the two degrees.

Q236 **Dr Matthew Offord:** I just wanted to move on to the whole panel to ask your opinion about the interpretation of fiduciary duty in the United Kingdom. Is it too narrow? Is it too wide?

**Dr Caldecott:** I am going to defer to Alice.

**Alice Garton:** Again, the existing law is fine. It is the interpretation of it and, once again, it is a misunderstanding of the nature of the risk, which goes back to your first point. We wrote to 12 contract-based pension providers over the last year asking questions about climate risk and how they are managing it. At least 10 have come back, again assuming that climate risk is an ethical, environment and social governance issue that should be put aside in a box with corporate sustainability reporting. This is why we need the financial regulators to step in and make it clear that this risk has changed—it is now a core business issue—and encourage those to have a look impartially.

Climate change can be quite an emotive issue because it has been very politicised for 30 years, and we need to drop all of those preconceptions and look at the evidence impartially using your professional judgment. I would challenge anyone to do that and not realise what a significant financial risk it is, but it is getting that evidence in front of the pensions' providers, the company directors, and the regulators themselves, which is key.

**Polly Billington:** Can I add to that, in relation to local authorities obviously? You have pensions committees and so forth and we all know—you have been a counsellor yourself—counsellors do it part time. They are not necessarily full time on the job, and they are very clearly

influenced by finance officers who will be very cautious on this front and for that reason I would back up what Alice said.

Arguably, the intervention by one of the Ministers on this before Christmas suggesting that there should be more freedom to interpret fiduciary duty to have an ethical dimension, which I think a lot of people welcomed, arguably would give us a step back because we need to be absolutely robust about this. Southwark Council, which is one of our members, said one of the very reasons why they chose to divest from fossil fuels was because it does not make good financial sense to do so for their pension holders.

So we need to see it in that way and until climate risk is properly factored into that we will end up with people sort of wanting to put it to one side, saying it is too difficult and those people who are not on this full time and who are having to take the advice of financial officers will find themselves ending up, arguably, overseeing pension funds that are still investing heavily in fossil fuels well into a future where those assets will be exposed.

**Q237 Caroline Lucas:** Can I just come in very quickly? It is just that I wonder if you would agree that one of the problems as well is that trustees outsource the responsibility for their portfolios to their investment managers and to bring this right home—I do think we need to confront the fact that the parliamentary pension fund is one of the worst culprits in this. There has been a cross-party group of MPs who have been trying, first of all, to get the Parliamentary Pension Fund to say where they invest their stocks. Eventually we succeeded and there were the fossil fuel investments that we imagined would be there but the correspondence that we have been having with the trustees has been incredibly problematic.

Just one little example: we had a letter back saying, “The trustees have only finite resources and must steward those resources for the benefit of the scheme as a whole without expending a disproportionate time on correspondence with some members”, the Cross-Party group this was, “in relation to a single issue”. The single issue being climate disclosure and climate investment. It therefore says, “It’s not possible for the trustees to engage in further prolonged discussion by correspondence with you on the merits or otherwise of the trustees’ investment approach”. I was so shocked to get that. How dare they? But the point being—I was going to ask if Mr Picot, in particular perhaps, given his background, would be willing to come and give a presentation to Parliamentary Pension Fund managers so that they might understand what is at stake here.

**Russell Picot:** I would be absolutely delighted to. Could I make an overarching point? It seems to me that—two points. First of all, I agree with Alice. When we step through climate risk we explored the legal dimensions of that and were comfortable we could achieve it. I think it would help to broaden it around ESG because it seems to me that—I think we have done climate risk in my mind. The next step is to look at ESG factors and potentially alignment with the sustainable development

goals. That is even more demanding than climate risk. There is going to be new barriers. I think that we are going to have at least the same dimension of information deficiency with companies around the SDGs so I think there is a case for some sort of a taskforce to address what information should be provided to the market on the SDGs to create the dataflow, the fund managers to create the products, for us to make the investment.

The second point is, if the UK is serious about decarbonising and being successful, it seems to me that there needs to be a broad-based piece of thought around education, about equipping our young people to think about sustainability in a different way. So it needs to become part of business degrees and economics degrees. It needs to form part of the syllabus and curriculum for engineers, accountants, lawyers, doctors and investment professionals. Only by doing that will we create the flow of young talent that is going to be equipped to help this country achieve the very desirable end state that we all want.

**Polly Billington:** I agree with Russell but can I add that it is also people who have decision-making power now that need that education? If we wait until those highly educated young people who understand sustainability are in charge, we will have waited too long. It is people who have decision-making powers now that need to be aware of quite the risks that they are taking.

**Russell Picot:** It is both.

**Polly Billington:** Okay then, and we are fine.

**Chair:** This Committee's battles on trying to get various things through, particularly on the global goals, are ongoing and very well documented and this is a subject, no doubt, to which we will return. We are not able to suspend between panels, I do not know why—possibly to do with the enormous bucket of water that was thrown over my friend's back. That will teach you for using a plastic glass: plastic strikes back. So we are going to go straight to our next panel without suspending but thank you all very much indeed. It has been a very useful session.

## Examination of Witnesses

Witnesses: Emma Howard-Boyd, Diandra Soobiah and Will Fox-Robinson.

Q238 **Chair:** We are carrying on. For the purposes of Hansard can I welcome our second panel, some of whom were in the room listening? Can you introduce yourself from left to right please?

**Emma Howard Boyd:** I am Emma Howard Boyd and I chair the Environment Agency, but I am here today because of my background in finance. I also chair the Investment Committee of the Environment Agency Pension Fund and am member of the Green Finance Taskforce.

Q239 **Diandra Soobiah:** Hello, everyone. My name is Diandra Soobiah. I am the head of Responsible Investment at the National Employment Savings Trust or NEST.

**Will Fox-Robinson:** Hi. I am Will Fox-Robinson. I am from Natixis Investment Managers. This is my second time to Parliament. The first time was 24 years ago when my dad brought me here because I was thinking about studying the British system of politics. It felt like a very important place then and it definitely feels like an exceptionally important place now considering the issues we are discussing. Natixis have thought about sustainable investment—

Q240 **Chair:** Sorry. That is fine—I just asked you to introduce yourself. We will ask the questions. You will have a chance to say your bits and pieces as we go through.

I am going to kick off the questioning, if that is okay. Asset owners like pension funds make long-term decisions directing trillions of pounds of investment, as we have been hearing about. Is the UK doing enough to unlock the potential held in these assets to assist the UK's efforts to become a low carbon economy? Mr Fox-Robinson, you are ready to go. Why don't you kick off?

**Will Fox-Robinson:** I think it is important to think about it as more of a stakeholder discussion—that is, what pension funds are doing, what Government are doing and what asset managers are doing. It would be nice to think about if we could encourage a debate of whether, in a UK perspective, companies could set goals to meet the sort of global goal of carbon.

**Emma Howard Boyd:** If I look at the way that the Environment Agency Pension Fund has been managing its assets, and particularly having heard some of the questions that you have been asking the previous panel, I think there is a huge leadership role for pension funds to invest in the long-term and take account of many of the risks that we have been addressing from a climate perspective.

The Environment Agency Pension Fund has a climate risk policy embedded within its investment strategy. So for well over a decade we have been looking at environmental sustainability issues and the way that we have been managing our fund. It very much links to the sponsor body, the Environment Agency, the staff, whose pension funds we are managing.

We have over 10,000 staff, over 40,000 beneficiaries invested into the pension fund and our liability stretch out to the next century. Given the work that our staff do through the Environment Agency, it is absolutely clear this understanding of future climate risk. I, as a trustee of that pension fund, am very much in a position to say that we would be in breach of our fiduciary duty if we were not taking into account climate risk and that is the whole way we have set about managing our pension fund.

I think there is an opportunity at the moment: given that we are part of the Local Government Pension Scheme, through the pooling of those schemes there is an opportunity to spread work that we have been doing through our pension fund to the Brunel Pension Partnership, which we are part of.

I also see one of the roles that I have is a convenor with other chairs of pension funds to go through that whole leadership process, making sure that we are spreading our knowledge to other pension fund trustees. Before Christmas I convened a group of pension fund chairs. Russell Picot mentioned the statement of support that we issued back in November, some 16 UK pension chair or chairs of investment committees, to commit to working on the TCFD disclosures together and help ourselves make sure that the way we are managing money on behalf of our stakeholders drives the right kind of change. I think there are things that Government can do but there is also something that we can all do in terms of the leadership that we show around this agenda.

**Diandra Soobiah:** So NEST is the largest pension fund in the UK by membership. The vast majority of our members are in their 20s and 30s, which means that NEST has to invest for the long-term time horizon. We have an in-house team who manage the asset allocation, but a large promise of what we do is working collaboratively with others in the investment chain and external stakeholders and we do this to create impact in responsible investment.

The reason why we have a responsible investment approach is to essentially deliver enhanced risk adjusted returns for our members and we do this by fund manager selection and monitoring, so working very closely with the people that we appoint to manage our members' money. We do this through voting and engagement with investee companies and we also incorporate ESG factors within our risk management processes. We have identified carbon as being of a material risk to our investment portfolios and carbon is one of those risks that we assess alongside other financial risks in our framework.

We have now started to address this directly in our asset allocation. Last year we helped develop and invest in a climate-aware fund that now sits within our asset allocation and that is where—

Q241 **Chair:** How much has gone into that?

**Diandra Soobiah:** It is up to now 40% in the foundation phase where our youngest members are invested, 40% of our equity allocation and 30% across the total scheme assets, and over time we will look to increase that. Essentially we have done this in our asset allocation where 99% of our members are invested. So this is not part of an ethical fund choice or a side fund choice, this is engrained in our investment approach in 99% in our members.

Q242 **Chair:** Mr Fox-Robinson, your business has \$86 billion under management and you do business for corporate and UK local authority

pension funds and insurers. What awareness have you found among your—particularly the UK local authority pension funds that Ms Howard Boyd was talking about of these risks? Is that something you are telling them about or are they asking you about it?

**Will Fox-Robinson:** Ms Howard Boyd is a leading light in the industry and she has chaired a working group, just before Christmas, on land degradation and natural capital, so bringing together different players in the industry. That is one thing.

Last week, we were invited to one of our client's committee meetings in the evening and we were invited along with two other investment managers and we were there to solely talk about what we were doing in terms of ESG and sustainable investment and how it related to their portfolio. They had been put under pressure by their civil society groups to explain how they invested and what they were doing about carbon footprinting.

I have been in the asset management industry since 2001. Three years ago, we would never have expected to be in that conversation. At the moment every—and hopefully going forward—every conversation I have with potential clients and prospects, "What are you guys doing about ESG? What are your thoughts?"

Q243 **Chair:** You have signed up the UN principles for responsible investment in 2008. You are trying to specialise in this ESG and—how are you looking at the global goals in terms of your incorporation of them into what you do?

**Will Fox-Robinson:** Very importantly, we engage. Last year we did a survey and we found—we surveyed 7,000 people across 22 different countries. Some 70% of the retail investors think it is very important to invest in companies with good environmental records; 62% of institutional investors agree or strongly agree that incorporating ESG was a standard practice and should be going forward. So when it comes to thinking in the future, Mirova, our affiliate who focuses on sustainable investment, they think about investing money in probably four different ways.

Their philosophy is—to begin with they do not invest alongside or in companies that disregard the UN SDGs. It is a central plank to what we do. Secondly, they think about long-term and value. Thirdly, they want to think about companies who are investing in trends that shape the future. Lastly, they believe in engagement to help support companies thinking about what they are doing.

Q244 **Mr Robert Goodwill:** When ethical investment funds came along, people invested in them and they accepted the fact they might make a lower rate of return than companies that invested in building arms and munitions or testing animals or making cigarettes. Are you saying that by investing in this more ethical and greener way you accept that your pension fund holders are expected to do that or are you now saying in the investment environment we have now you can make good returns on

these sort of investments and that you do not need to invest in some of the more unacceptable, in some people's views, type of activities?

**Will Fox-Robinson:** Our central thesis is that investing sustainably, ESG, is an alpha driver, so it is a way of making money. We are not there to just provide our clients with great things to do where they are—

Q245 **Mr Robert Goodwill:** It sounded a little bit like that when you were talking to your clients in the evening and saying, "Well, we do not want you to invest in this thing". You can do both, can you, quite effectively?

**Will Fox-Robinson:** Absolutely.

Q246 **Chair:** Ms Howard Boyd, because you have a very well performing fund—

**Emma Howard Boyd:** Absolutely. We see that the whole approach of embedding the way we look at climate risk and environmental sustainability across our entire portfolio is about adding long-term returns. So at the moment our assets are bigger than our liabilities so we are fully funded as a pension fund. We have good performance as well, outperforming our benchmark over a year, over five years.

I think the other thing, given that it is part of the Local Government Pension Scheme, is that it is value for money. So our contributions into the pension fund are lower than the average within the Local Government Pension Scheme. I think from whichever way you look at it, it is showing that this is doing well for our beneficiaries and I would argue that it is because of that long-term and broad approach that we are able to bring these returns to our beneficiaries.

Q247 **Colin Clark:** Can I follow up, Chair? Just to come back to what Ms Soobiah was saying—you identified carbon as a risk. Does that mean you would advise your fund managers not to invest in oil or gas?

**Diandra Soobiah:** No. The way that we incorporated the fund solution to this is that we are under-weighting those biggest carbon risks that we have identified in the fund so we are going to be under-weighting those companies who generate the biggest carbon emissions and will be managing those down. We are going to be over-weighting those companies that seem to be at the forefront of making that transition to a low carbon economy. So over-weighting companies in renewable energy and green technology.

All the work and the research that we have done has told us that it is much more effective to stay invested and engage with those companies and encourage change and support them to the transition to a low carbon economy. They are essentially the biggest risk in the system and they are the most responsible for—30% of the companies are most responsible for 95% of carbon emissions emitted globally.

We ought to stay invested and focus on generating change among those biggest risks and that is what the fund has enabled us to do and we will work with those companies over a long-term time horizon to help set

expectations and what they can do to change and a lot of it is around reporting and making disclosures about how they intend to do that.

- Q248 **Colin Clark:** Just on that point, agriculture and forestry would be seen to be more green right now—part of agriculture. There is a debate about which one is sequestering the most carbon. How, from an investment point of view, do you cost that in? The attitude towards forestry and agriculture may change, and you may take a view at this point.

**Diandra Soobiah:** The research that we have done shows that the biggest oil and gas companies are most responsible for global carbon emissions. Agriculture, as well, factors in. The way the fund works is that we have taken a very strong sector-specific approach on managing those biggest risks. The data, which we have access to, may show that agriculture and forestry are also quite carbon intensive.

We will be also focusing on companies within those sectors as well and asking questions around green technology that they may be able to use. What are their plans for making energy efficiencies and savings? Those kinds of things will come through requesting disclosure and through engagement as time arises but the starting point for the fund is to focus on oil and gas as the biggest risks.

- Q249 **Colin Clark:** I can see all of that.

**Diandra Soobiah:** Then that will transition as we move forward.

**Emma Howard Boyd:** If I could add that I think you also need to look at the approach that you take to your different asset classes so that the way our fund managers, who work on our behalf, will approach equities, so investing in listed companies, will be very different than our allocation to real assets portfolios where again the team at the Environment Agency Pension Fund has worked very closely with the manager of the real assets portfolio to look at how to take investment into forestry, into land, over the long-term. So I think it depends on the asset class that you are investing in and the approach to the underlying asset that you are investing in as to how you are factoring in different aspects of climate risk and environmental sustainability.

**Diandra Soobiah:** At the moment, we do not have direct investment in those commodities that you are referring to but we may well have exposure through those global equity qualified companies, agriculture investment companies, we may engage with. At the moment we are not exposed to direct commodities but it is something we may be in the future.

- Q250 **Alex Sobel:** I think I should first declare that I have a pension with NEST—full disclosure there. I think you may have covered some of this or aspects of this. How do you interpret your fiduciary duties pension fund management in regards to environment risk such as climate change?

**Diandra Soobiah:** We have identified climate change as a big material risk for our members and not just a risk: we have also identified it as an opportunity for upside for our members, particularly our youngest

members. The vast majority of our members are in their 20s and 30s so they are most likely to be impacted, financially impacted, by the issue of climate change. For us this is about meeting our fiduciary duty and managing financial risks for our members.

It is interesting what you ask. You would think that all the evidence points to climate change being a big economic risk in the future but when I have made presentations on our climate-aware fund I still have questions from members of the audience asking, "How do you square this with your fiduciary duty?" and numerous times throughout that presentation I have said, "This is about managing material financial risk for our members in the long-term" and I cannot emphasise that point any more than I already have.

I have given them examples of how we are moving more into these companies that are instrumental in the transitioning to a low carbon economy and generating renewable energy. These are the companies that are going to be generating value in the long-term and members are going to be benefiting from that in the long-term so this is about financial value. So this, most definitely, for us meets that fiduciary duty but unfortunately it is not seen to be the case by all pension funds in the UK at the moment and that is something that we are looking to help encourage change around.

**Will Fox-Robinson:** In terms of fiduciary duty, if I speak from what we have done as a business. From a Mirova perspective, we see it as obviously creating value for our clients, creating value for the business but also from the fiduciary side engaging with companies and what they are doing to try to improve their practices or their reporting. In terms of the clients recently we launched a fund in the US that is targeted at millennials. Millennials are in a great position where their social values, being cognisant of sustainability in the environment is matched up wonderfully with their timeframe. One of the committee spoke about 40 or 50 years. It is being able to channel that money to give them a return matching how they believe is something we felt is our responsibility.

**Emma Howard Boyd:** I think I have already made it very clear that we see, as trustees, we would be in breach of our fiduciary duty if we were not taking into account climate risk and broader environmental social and governance issues. I think we see it as very important to speak about that as much as possible because of what we have been able to demonstrate through the performance of our funds.

We go about delivering this through three main ways. First, decarbonising. Similarly to what HSBC has done with the Future World Fund, three or four years ago we worked with one fund manager to decarbonise our passive portfolio. That is one way we deal with climate risk. The other is about specific allocations to those companies that are solving environmental issues and climate related issues. We have a target of at least 25% of our portfolios going into those sorts of activities.

The third one is around how we work with others and because—through one lens three and bit billion is a lot of money. Through global markets, it is tiny. We spend a lot of time collaborating both with our fund managers but with other asset owners. One initiative that is very important for us is the Transition Pathway Initiative that we launched over a year ago with the Church of England and their various funds to work with others to understand how our portfolios are transitioning to a low carbon world, so very much in line with TCFD recommendations. We now have five trillion assets under management supporting that piece of work.

We are working our way through sector by sector to understand how boards are responding to climate risk but also how over time we can see whether companies that have made a commitment towards a two degree world are transitioning their business towards that. This is information that we are, as we work through the sectors with the involvement of the London stock exchange as well as the London School of Economics Grantham Institute, putting into the public domain because we want other asset owners to understand how this work is helping us understand what is within our portfolio.

Again, a lot of focus on transparency and working together to make sure that we can understand how businesses are transitioning over time.

Q251 **Alex Sobel:** There seems to be a commonality approach here but you all, particularly Diandra and Emma, alluded to others in the market who had a different approach to fiduciary duty. What do you think the differences are between your approaches and why? Why have you taken your approach and others, who have pension fund managers, taken a different approach?

**Emma Howard Boyd:** I think from my perspective it is very patchy. In convening chairs of pension funds, you get people who immediately want to come along to a roundtable discussion because they are already on that journey. They are already doing things. There are those that understand that they need to do something. I have also recently had someone say, "I don't think he'll come along because it's not his cup of tea". So I think there is just patchiness within the system. I think some of the points that were made earlier around education, absolutely key, but I think also we do not have time to wait for the next generation so we also need to work on; how do we educate those who are chairs of pension funds or working in the asset management industry to understand climate risk.

I think it is also, from my perspective—a lot of the attention has been on the mitigation agenda; how do we invest in renewables? Sitting, as I do, as chair at the Environment Agency, I think it is also important that we put as much time on the resilience agenda so aiming for maximum two degree worlds, hopefully lower, but also understanding that we need to plan for whether it is too much water, too little water, in the way that we are investing, so putting as much focus on the resilience agenda as on the mitigation agenda.

**Diandra Soobiah:** So just in regards to your question NEST is quite a unique case with a young scheme, relatively speaking. When we were set up we did a lot of research and consulted across the industry around what our investment approach should look like and there was strong support for NEST being a responsible investor and taking a leading approach in this area. The incorporation of ESG factors in the investment approach should be seen as quite fundamental, which meant that this is something that the trustee brought into from very early on. We had that top-level commitment. For us there was very little wrangling with the trustees. They were very supportive and this then filtered down to the way that we run the money for our members.

We have an investment belief, which denotes that ESG should be seen essential to any investment process, and that this is something that I do not think other schemes have. They do not have that kind of trustee commitment of that investment belief and an enhanced commitment in their SIP for example. This is something that we strongly believe in and I think other schemes, who are seen to be smaller, quite resource constrained, think that it takes a lot of work to be incorporating this type of approach and can support a new investment process.

They may have trustees that have been quite resistant to change. We have heard a lot of reasons for people just not taking this issue seriously and because they do not believe that it has an impact on their member's risk adjusted returns and we are truly long-term. All pension funds should be long-term investors and as a result of that need to be incorporating ESG risks and opportunities in their approach because they tend to play out over much longer term timeframes.

I think more needs to be done to help educate trustees in this area. Consultants should definitely be assuming a much more powerful role. They have a lot of influence in the market. They need to be speaking to their pension fund clients about this but they are not doing enough in that area. I think that is why we have a lot of patchiness, as Emma said. Some pension funds are taking a leading position and are seen to consistently lead whereas you have the smaller pension funds that just are not doing very much; are not encouraged to because of that lack of commitment in-house.

Q252 **Alex Sobel:** Just a last one for Emma. Are you satisfied with the response of regulators and the Government to the Law Commission recommendations regarding the duties of pension fund trustees to consider environmental risks as a material concern?

**Emma Howard Boyd:** I think there could be greater clarification. I think it would help address a lot of the issues that we have talked on today to give a bit more clarity around fiduciary duty because it is very often one of the terms that people hide behind before starting to drive change. I think that is key.

Q253 **Chair:** Do you think that the fact that the guidance has not been updated for contract-based pensions is a problem?

**Emma Howard Boyd:** I think we need to make sure that we have a consistent approach and join up all the regulators for all the different types of schemes and be aware of how the markets are transitioning for pensions as well. Where there is, perhaps, good governance or more considered governance in funds that have been in existence for a while, the way that market is transitioning is not necessarily giving member representation.

I have no doubt that over the 20-odd years that the Environment Agency Pension Fund has been in existence it has been very helpful having member nominated representatives sitting around the pension committee to bring that real experience of what is happening out in the field and thinking about that in the context of ultimately their hard-earned and deferred salary for the future.

Q254 **Chair:** Mr Fox-Robinson, does Natixis have a different approach to contract-based schemes or trust-based schemes? Do you manage only fund-based schemes?

**Will Fox-Robinson:** Trust-based. My experience is trust-based. We are building a business here in the UK on contract-based but it is still very early stages.

Q255 **Chair:** Do you apply your fiduciary duty and investment principles to those contract-based schemes?

**Will Fox-Robinson:** Absolutely.

Q256 **Chair:** In a way the market is going faster than the regulation on this.

**Will Fox-Robinson:** Yes.

Q257 **Colin Clark:** I am going to ask about engaging with the beneficiaries and we have just covered part of that just now. How might pension funds best engage with their beneficiaries on sustainability issues and are some pension governance structures better than others for this?

**Emma Howard Boyd:** We do put a lot of emphasis into engaging with our beneficiaries in a range of different ways but I do think there is an opportunity with the whole pooling process to take that almost to the next level. Some pension funds will have annual general meetings and allow their stakeholders to come in and hear a little bit more about how their pension fund is being managed. It is not something that the Environment Agency Pension Fund has done but being part of the Brunel Pension Partnership I think there could be an opportunity to open up that dialogue. I think from Brunel's perspective that could bring some of the learning of the Environment Agency Pension Fund to the other shareholders and other pension funds within that pool.

Certainly I am aware that the London Pension Fund Authority and its new pooling arrangements has those sorts of annual general meetings to bring the world of pensions alive and I think tell stories of ultimately what is being invested in, which I think is where it does make a difference to

your everyday person on the street when they hear what is happening with their pension fund from an investment—

Q258 **Colin Clark:** That is a very tall order to bring pension to life but anyway.

**Diandra Soobiah:** Yes, absolutely is the challenge. We have six million members. It constitutes a very diverse membership. We have in the past been able to reach out to cohorts of memberships, small cohorts, and issue surveys but we want to essentially reach up to them more broadly and tell them about what we are doing and get them to engage with their pensions.

We know research all points to the—people just do not engage with their savings but we want to use responsible investment as a hook into telling people interesting stories about how we are managing their money. We want to start reaching out and tell them about how we vote on their behalf, the companies that we are engaging with on their behalf and hopefully that those stories might resonate with some of them.

We also have done research around millennials being interested in the area of climate change, sustainability, responsible investment matters. That is, perhaps, an another avenue through that we are looking at reaching out to but with auto enrolment now, with more and more people saving into the pension the challenge is, how do you adequately communicate with all of those people and do they even want you to. We think responsible investment is quite a good way in.

**Will Fox-Robinson:** If anything, I think you are right. It is difficult to get people engaged in pensions. You are absolutely right. That is a challenge our industry faces and all three of us face. Personally I believe it is the millennials that will make the difference because their social values are more aligned to sustainability and the environment itself whereas the previous panellists talked about, is it going to be too late for the next—decisions being made now, is it going to be too late? Is our world going to be too impacted for those coming through for the millennials themselves? That is why educationally it is very important for us to link what we can do and their values so they can get in and make some decisions about it now.

Q259 **Colin Clark:** I just wonder if millennials have a—I am trying to think. I am not a millennial so I probably should not comment. I am just wondering why they have higher values.

I think probably grandparents—not that I am one—might have equally as high morals. The Government have raised concerns that member service can be self-selecting. I suppose this is really on the point. What steps do you take to ensure your evidence is robust when it comes to assessing the views of your beneficiaries? We were talking about the difficult to engage. So how do you actually make sure it is—the questions are self-selecting then you are setting them up to go down a path.

**Diandra Soobiah:** I think our strategy would be to simply tell them what we do and tell them a story about how we manage their money and try to

link it through to a real life issue. They are invested in household names and we want to tell them about that. We want to tell them about how we are talking to boards of these companies to help generate better financial terms for them in the long-term.

For us it is about telling them positive stories rather than surveys and then ask them, "This is an approach that we use to help run and manage your money. Do you want to hear more about this? Are there any issues that are important to you that you would like to see addressed in the way that your money is managed? Please tell us about it." So rather than generic self-selected surveys I think we can make it a lot more of a duty, much more dynamic in the way that we communicate with members but the challenge is getting that wide-reaching approach to cover as many members as you possibly can.

**Emma Howard Boyd:** I think transparency at the very least is absolutely key to this. We make sure that in our annual report there is a very strong section going into the detail of how we are working with our fund managers around all of the issues that I have talked about. I think that is a key, as a minimum, to make sure that there is transparency between the pension fund and the beneficiaries.

**Will Fox-Robinson:** We, as an asset manager, would not directly communicate with the members simply because we would communicate with the trustee bodies.

Q260 **Colin Clark:** So the trustees are making the judgement rather than the members. Nataxis surveys suggest a high level of engagement with environmental, social and governance considerations among pension scheme holders than professional investors. However, we have heard that institutional investors are ahead of the retail market in the UK. Would improving citizen's financial literacy help when it comes to greening finance?

**Will Fox-Robinson:** Yes, absolutely, is the answer quite simply.

Q261 **Colin Clark:** That would be true of any financial investment as opposed to simply greening, would it not?

**Will Fox-Robinson:** It would, but I think the values are more aligned or their understanding is better in the environment around them than things that could be more esoteric.

**Emma Howard Boyd:** I think you need to look at every level. There is education in schools. There is education as people enter the workforce and that is where the auto enrolment schemes can help in terms of financial literacy. I think it is also the training that people undertake as they become financial experts, making sure that environmental issues and broader social governance issues are part of that because of that training. I think work can be done there.

I also think, and this is something that has come up in the Green Finance Taskforce, the issue is about how you share the knowledge between the

different regulatory bodies. So the Environment Agency as an environmental regulator is not a financial expert. Similarly, some of the financial regulators are not environmental experts. How do we bring some of those areas of expertise together to shine a spotlight on the long-term risks that are emerging? Again, one of the things that I have made sure, being part of the Green Finance Taskforce, is where a lot of the focus has been linked to the Green Growth Strategy that we also look at resilience matters as well.

You can see how members of the mainstream finance community, who have understood things like energy efficiency and the low carbon transition, have not necessarily understood the importance of looking at resilience at the same time. Light-bulb moments, when understanding that there is no point in investing in energy efficiency in buildings if you have not looked at whether those buildings are also at flood risk or in a part of the country that is also going to have water stress. Whether it is across Government Departments or across industries, there needs to be a joining up at this time for thinking.

Q262 **Colin Clark:** If I could just ask a supplementary to this because what is going around in my head is that in the western world I can see how you will bring pressure to bear on companies to change the way they behave. What about in the developing world? Does that not mean there is a gap that somebody somewhere will invest in companies who have a different attitude, who do not have the same environmental goals? I think about a country like China where they are rapaciously using up commodities and still building coal power stations. There must still be investment going into that. Is there a parallel investment going on or do people just—pension funds will be taking a different view?

**Diandra Soobiah:** I think with the Paris agreement all countries have committed to reducing carbon emissions so you would expect the governments and the regulators will be looking to become more energy efficient and reduce their own carbon emissions. With regards to how we manage it, we have identified those biggest risks in those companies and they are all essentially located in the developed markets so that is our starting point.

I think emerging markets are just that. They have the ability to change and adapt more quickly because their infrastructure is not as well developed as the infrastructure in the developed world so they have, perhaps, more of a chance to implement renewable energy from the outset because their infrastructures are just nowhere near as developed as they are here. Coupled with engagement from investors and regulators we hope that that movement will be taking off more in emerging markets than it is here. I think we have a lot more work to do in the developed markets to reverse those attitudes.

**Emma Howard-Boyd:** Another way of looking at it is how the financial system, the banks, and the investment managers are themselves going through a transition. You have some niche players, boutiques, that are very much focused on embedding this in their entire investment

strategies. Whatever asset class or wherever they are investing in the world, they are looking at their investments through that lens.

In the same way that we are looking at how an oil company might transition to a different type of business, banks and asset managers, the large ones, are also going through a transition. That is something that, as we go down this journey towards a lower-carbon world, ultimately and hopefully assets will transition to investing in the low-carbon world. We are in that transition for the larger banks and the larger fund managers and the larger insurance companies, and we have to encourage all of those institutions to make that transition as well.

**Will Fox-Robinson:** We would not invest with those types of companies. The way we invest in the emerging markets is through either making loans or taking equity stakes in businesses that create profitable businesses that create an impact on their environment.

For example, recently we have looked at loaning money to a lobster co-operative in Belize, and we feel, by lending them money and improving their supply chains—ie investing in refrigeration units—they can better regulate the actual amount of lobsters they are taking out of the sea because they do not need to take so many.

Q263 **Colin Clark:** Good. One last question on NEST. What does NEST do as an autoenrolment scheme to raise awareness of how pensions savings are invested and the wider social environment and implications of this?

**Diandra Soobiah:** Raise awareness among membership? We are a relatively young scheme, and that is something we are looking to do more of as we get bigger. How we tell our members about the companies in which we are investing and how they operate in the societies in which they function and the environments in which they operate is going to be a really important story for our members. That is something that we are extremely mindful of as long-term investors. When we invest in corporations, we want them to have sound corporate governance and be mindful of the societies and environments in which they operate.

Q264 **Chair:** The question is, what do you say to your members? When you enrol in NEST, as our colleague has done, do you get a leaflet saying, "This is how it is invested"? There is surely just one point at which you sign up where you have the moment of maximum interest. After that, it is just—

**Diandra Soobiah:** Yes. A lot of the work we have done to date has been with the employer because this is essentially workplace pension, and we have had that engagement and communication with the employer. Now that staging is complete, all the employers have now been enrolled and have enrolled all their workers. The next stage of the communication strategy now is to start reaching out to members.

Q265 **Chair:** Have you as a fund or scheme ever sent anything to the members of your scheme directly, or are you relying on the employers? Do the employers do it all?

**Diandra Soobiah:** Not around the investment strategy. Obviously they get their statements at the end of the year, but not with regards to our investment approach. It has been through the employer.

Q266 **Chair:** With their statements, you do not include a statement of investment principles, for example, which would surely be an easy way to tell people the principles behind your investment?

**Diandra Soobiah:** Yes. We may well do. I am not the person to ask.

**Chair:** All right. Thanks. We will move on.

Q267 **Mr Robert Goodwill:** I work for an employer who has signed up with NEST, so I will wait and see what comes through the post for both myself and my staff.

We have heard the considerations that you take into account when you choose the investments that you make, and I think many who are concerned about the environment would be reassured and encouraged by what they have heard. Of course, once you have invested in a company, you then become, either individually as an institution or collectively, very powerful within that company as shareholders. We have seen a number of instances on shareholder action and things like executive pay, where the institutions maybe were not quite as forthright as some of the small private investors.

We have seen some situations—for example, with ExxonMobil being forced to disclose its exposure on climate change risk. The question is, to what extent do the funds you are responsible for take an active stewardship role when it comes to energy investment and climate change? What are the benefits if you do that for your beneficiaries, or do you sit there and let the dividends come in?

**Will Fox-Robinson:** Sorry. Are you talking about the pension funds?

**Mr Robert Goodwill:** Pensions. Pension investments.

**Emma Howard-Boyd:** We have been very focused, particularly in the environmental space and particularly with UK companies, where on the climate risk agenda we can co-file resolutions. Two or three years ago, with BP and Shell, we, with others, felt it was important to file shareholder resolutions and vote in support of a sort of activity. That is where, for us, at the Environment Agency Pension Fund, it is this working with others to make sure that we continue to raise issues either via our fund managers or through collective activity. That is a very important piece of our engagement strategy to make sure that we are using our voting rights to send signals to the companies on a range of different issues and then put that information into the public domain.

**Diandra Soobiah:** To echo what Emma has just said, it is really important that when you have an investment strategy around climate change, that is essentially coupled with a very strong stewardship approach. It is very important that the fund managers who you select are holding companies to account on matters like climate change.

As such, our fund manager has committed to supporting nearly all shareholder resolutions on climate change strategy and reporting, so that is hugely beneficial, now that there is a lot of reporting around these votes and the public domain, and we are now sending a message to these companies publicly that they need to be changing. That is really powerful when a big asset manager votes against them.

As an asset manager, we are always speaking to our fund managers about how they vote in these companies, and we want them to be as open and transparent with us as possible. We have our own voting policy in place, but we expect them to vote thoughtfully and considerately in line with their own policy and have a degree of alignment with ours as much as possible.

We have put into effect a process where we have the ability to override a select number of votes where we feel that our fund manager has voted not in the interests of our members. There are things as an asset owner that you can do to work with your fund manager to get as many tools in your box to help encourage change throughout the investment chain. It is about working together with them and it is healthy when people do disagree, but it is about getting the right justification and rationale and transparency as to why that has happened. Working closely and collaboratively is definitely something that we put a lot of emphasis on.

**Will Fox-Robinson:** Sure. I echo both of those views. Last year we did 390 meetings with 196 companies to discuss how they were behaving and discuss their reporting requirements, their governance structures. If the Committee would like, I will very happily share an engagement report with you, which I can send on.

Q268 **Mr Robert Goodwill:** Are there any areas—tobacco, for example—where you would say, “Look, we are not going to have anything to do with any investment that resulted in people smoking and investing in companies of that sort”?

**Will Fox-Robinson:** We do not see smoking as beneficial to the future of the human race, so we would not invest in tobacco companies.

Q269 **Mr Robert Goodwill:** Even if that was a very profitable operation and your beneficiaries would benefit from investment in that area?

**Will Fox-Robinson:** Even if that were very profitable. Absolutely. My understanding of the medical science is that smoking is detrimental to the human race, so it is just not within our investment strategy, even though it is profitable. We believe we can make money for our investors using ESG criteria and responsible investment strategies.

Q270 **Mr Robert Goodwill:** In other areas—for example, nuclear energy—would you base your decisions on science or public opinion, or would you just take each case on its merits?

**Will Fox-Robinson:** Our decisions are based on our fundamental research, and that includes a number of inputs from different industry

players, how we view their sustainable records, and what their profitability could be in future.

- Q271 **Mr Robert Goodwill:** I think fracking would be another one, maybe, that is quite controversial. Some people would be very upset to know that their pension fund was going into that. Other people might take a different view. You are on a bit of a slippery slope, possibly, when you start making those decisions. How will you get a degree of balance in there?

**Will Fox-Robinson:** Fracking, again: we would not invest in oil companies' fracking, just because it is not in line with our investment strategy.

- Q272 **Chair:** We have heard some incentives for investment managers to concentrate on short-term returns over long-term growth. What do you do to ensure your decisions align with the best long-term interests of your beneficiaries? We have heard from NEST about that, your UBS Climate Aware Fund, but maybe from Emma and Will.

**Emma Howard-Boyd:** It is also really important, the terms that your fund managers to look at. For us, we have, as trustees, annual meetings with each of our fund managers. We very much want to look over a long-term period, so we are not interested in quarterly performance. We want to hear what is happening over the longer term.

It is also the signals that you are sending to the fund managers around investing for the long term. Those are absolutely key to make sure that it is coming across in the way that you are signalling how you want your fund managed on that basis.

**Will Fox-Robinson:** Long-term, to create real value, we have to invest for the long term. That comes down to the client perspective, as Emma has noted, the engagement with the manager, and also the culture of the investment firm itself. Because we take long-term positions, we believe that is the best way simply to deliver a return to our clients.

- Q273 **Chair:** Thank you. The TCFD has published its recommendations last year, calling on large companies, financial institutions and asset owners to report on risks and opportunities. How should the UK now respond? Legislation, changes to governance codes? What is the best route?

**Emma Howard-Boyd:** This is a subject that is very much at the forefront of those of us who are sitting on the Green Finance Taskforce. We are observing what is taking place in other parts of Europe, Paris notably with Article 173. I think there is a desire for some pace here. Many fund managers are not just managing money in the UK but in parts of Europe as well, and this desire to move towards mandatory—after all, we are talking about comply or explain.

Some of the ideas that were offered by the earlier panel around embedding this thinking into the financial regulators, the way they operate, the corporate governance code, are ways where we can perhaps act quite nimbly. Certainly, from my experience working previously in the

fund management industry, there have been many fund managers calling for embedding environmental issues into the governance code as well as the stewardship code. There is appetite to move quickly on this, and particularly from some of the larger financial institutions. We have to work out what is the most effective way of driving change more quickly.

Q274 **Chair:** Will you be doing that in your pension fund? Will you be implementing its recommendations?

**Emma Howard-Boyd:** I have already talked about the statement of support, how we will start reporting against TCFD. It is how we are feeding through to ultimately companies through initiatives like the Transitions Pathway Initiative, where we want more information to understand. Yes, we are very much wanting to make sure that we are adhering to the TCFD recommendations.

Q275 **Chair:** What about NEST, Ms Soobiah?

**Diandra Soobiah:** Even though it is still quite early days—the principles were only fully published last year—it is a really strong start for companies to start making disclosures against this framework. I still think more promotion and awareness is needed across different participants in the investment chain and to really encourage that widespread take-up of the principles disclosure, to make disclosures against those principles. Yes, it just needs a bit more time to unfold and that broad encouragement.

The FRC has already put out its consultation on the stewardship and proper governance codes, and little has made it in on environmental reporting. Perhaps there will be conversations around whether or not it is the right place for it. Perhaps in the stewardship code there is some space for it. I still think people in the investment chain need to be encouraging one another to do it.

We plan to report against those principles soon. We are doing a lot of work on climate change, and we really want to tell our beneficiaries what we are doing around it and report on it more formally. We really hope that this sets a precedent with other pension funds and particularly sets expectations to our asset managers and corporations alike. The more people who start reporting against this will spur a consensus of take-up for other participants.

Q276 **Chair:** Mr Fox-Robinson, will your company be reporting the risks as recommended by TCFD?

**Will Fox-Robinson:** We will. It is a long journey. Obviously, the recommendations were only published in June, I believe, last year. If we were to think about the way Article 173 has delivered good behaviour in France inasmuch as it has encouraged greater disclosure, it has pushed more sustainable investment practices into people's thinking, absolutely it is a part and I think we are all in agreement in the way it should be encouraged.

Q277 **Chair:** Have you any anxieties about the costs of compliance? Obviously,

there are a whole series of things that Government have put on to businesses in terms of stamping out human slavery and supply chains, all these different reports that they are required to do. Have you any ideas about how Government could implement TCFD in a way that minimises the costs of compliance?

**Will Fox-Robinson:** Good question. It is probably something I would have to come back to you on, to be fair.

Q278 **Chair:** If you want to have a think about that, that is fine. Yes, write to us. Ms Howard-Boyd?

**Emma Howard-Boyd:** If I look at the longer-term costs of not doing anything, it is something that we all need to work on. Signals are really important. When we published our annual report last summer, we sent a letter to all of our fund managers and we decided to send it to the chief executives.

Again, it is about sending the signals right into the core of the fund managers, the organisations, that manage money on behalf of our beneficiaries, to signal how important working on things like the Transition Pathway Initiative are for us understanding the risk that is inherently a potential within our portfolio. There is a lot we can all do to drive that change and think about how you send very strong signals, not just to those individuals who are the portfolio managers, but ultimately to the people whom they reporting to, that this is something of growing importance to ultimately our beneficiaries.

Q279 **Alex Sobel:** This is one for Emma. Under the Climate Change Act, the Defra Secretary has the power to ask public bodies to prepare adaptation reports every five years. How do you view the proposal requiring financial regulators to prepare adaptation reports in the next round of reporting due this year?

**Emma Howard-Boyd:** It is really important to take that opportunity, as we heard earlier, how the Bank of England and the PRA responded to previous requests for those reports, which led to the whole work of TCFD. Yes. Using those moments of the reporting to signal how important this is to embed within financial regulators is something that I would encourage.

**Alex Sobel:** Thank you.

**Chair:** Thank you all very much indeed for a very interesting session. It is now closed.