Written evidence from the Association of British Insurers (ABI) PSC0008

1. The Association of British Insurers' (ABI) members collectively hold £1.6 trillion of invested assets and pay £46m in insurance claims every day and will be crucial to the success of any strategy to finance the infrastructure for Net Zero. The insurance and long-term savings industry promotes resilience and risk management for those impacted by the physical risks posed by climate change, but also interacts with savers, customers and businesses to manage the transition risks that come from adapting society to decarbonisation.

2. Our sector will play a central role in both financing and then rolling out the significant reforms that will be introduced through the Government's forthcoming Net Zero Strategy, helping to set and achieve climate related targets. Our members also play a key role as stewards, ensuring good outcomes for their customers, ensuring investments are not exposed to climate related risks, and through driving change in the firms they are invested in.

Setting and Achieving Targets

3. Reaching Net Zero by 2050 – in line with the Paris Climate Goals - means action across the full scope of the insurance and long term savings industry's products and services, and across its investment portfolios to limit global warming to 1.5°C (applying to Scopes 1,2 and 3 of the international Greenhouse Gas (GHG) protocol). As a sector, we recognise that a long-term goal for 2050 is not enough – action needs to be taken now, and then followed through with regular milestones every five years.

4. ABI members have already played a leading role in establishing the financial sector initiatives that are part of the Race To Zero, including the Paris Aligned Investment Initiative[1], the UN-Convened Net-Zero Asset Owner Alliance[2] and the Net-Zero Asset Managers Initiative[3]. We expect the methodology used by these frameworks to evolve in the lead-up to COP26 and beyond so that it reflects the specific activities of different economic sectors.

5. In order to set targets that are appropriate to their specific fiduciary duties and the obligations they have made to customers; firms should use methodologies set by recognised external organisations. ABI members will be relying on these external frameworks to make assessments of counterparties, clients and contractual partners. In turn, we recognise that our sector's commitment to these frameworks and the targets firms set will increasingly be used by those investing into and procuring from ABI members to make their own assessments.

Helping to achieve those targets

[1] https://www.parisalignedinvestment.org/
[2] https://www.unepfi.org/net-zero-alliance/
[3] https://www.netzeroassetmanagers.org/

6. Our sector has a key role to play through responsible stewardship and engagement, in driving businesses across the economy to adopt GHG targets and take action to reduce emissions and adapt to climate change.

7. There are two key initiatives that represent best practice for investors applying responsible stewardship principles:
   - Firms who join the Net Zero Asset Owners Alliance and the Net Zero Asset Managers Initiative are obliged to show they are committed to the UN's six Principles for Responsible Investment.
   - For the UK sector, the Financial Reporting Council's UK Stewardship Code 2020 is a voluntary initiative that sets high standards for those investing money on behalf of savers, to ensure that there is responsible allocation, management and oversight of capital that allows for long-term, sustainable value for clients and beneficiaries.

8. There is already extensive evidence to show that action from investors has persuaded businesses to adopt targets and make more ambitious action on climate change a business priority. Collaborative action – through initiatives such as Climate Action 100+ and the Institutional Investors Group on Climate Change (IIGCC) – is the most effective means to exercise responsible stewardship, ensuring that there is a consistent voice from investors that compels businesses to act.

Pension Stewardship

9. ABI members take their stewardship role seriously, undertaking extensive analysis of investment opportunities to ensure their practices reflect providers' values, as well as engaging closely with the asset managers of their existing portfolio. Our members, as asset owners and asset managers have different fiduciary duties, and have specific obligations depending on the financial needs of savers and the objectives of employers and trustees, which will shape their investment strategy. Fundamentally, every provider's long-term obligations will mean ensuring scheme members are not exposed to climate risks through their investments. But their immediate obligation is to ensure good outcomes for savers in retirement and must ensure contractual obligations to policyholders are delivered.

Stewardship in practice

10. Our members are asset owners, asset managers, or both; their stewardship approaches differ by type of firm, but with common themes.

11. When investing in a new company, investment analysts at our members who are asset managers will look at the extent of ESG integration into the firm's practices, conduct a full screening of the company to ensure that they do not fall under a firms exclusion policy which can include, but is not limited to: labour standards, human rights, health and safety and the selling of weapons and weapons systems. For companies that are already part of the investment portfolio, our members use three key methods – exclusion, engagement and voting - to pressure companies to raise their practices on social risk factors. Asset owners may feed into this process.

12. Asset managers make up a crucial part of investment management and are guided by the providers' stewardship principles as well as the UN Principles for Responsible Investment. For asset managers', stewardship will often look like:

- Engaging effectively with companies and, when necessary, escalating this engagement to drive better long-term performance from the business as a whole.

- Using voting rights to encourage positive commitments or practices.

- Delivering robust reporting on their ESG engagement activities, including details on the factors they discuss, and any actions or outcomes agreed during these meetings.

- Conducting in-depth quarterly reviews for individual portfolios, in which every aspect of the fund in question is examined, including risk profile, volatility, performance and fund positioning as well as the individual investments of the fund.

13. A provider may choose to exclude companies that do not meet their ESG criteria either during the initial research phase or reduce their holdings in them if they do not comply with more recently implemented responsible investment policies – examples are given below.

14. Our members who are asset owners also set out expectations for asset managers to adhere to, demonstrating how they apply the overarching responsible investment principles during investment. When working with an asset manager, our members will confirm that their voting policy is similar to their own, to minimise future conflict, as there is an expectation that asset managers influence the companies they invest in to create positive change.

15. With regards to voting policies, providers who have not already integrated the higher standards set by the UK Stewardship Code 2020 are working towards these increased standards to drive forward their disclosures to customers around their voting policies, methods and records. An ABI analysis of members disclosed voting records show that firms have acted in relation to companies they are invested in on social factors, including:

    - Voting for shareholder resolutions on employment practices (gender pay) at Alphabet, Google's parents' company.[4]

    - Voting against damaging environmental policies by Carnival Cruises and engaging with the firm to raise governance and environmental standards. After multiple failed attempts to influence the firm through multiple channels reducing exposure to them.[5]

    - Divesting from Bank of America after attempts to require increased reporting on its gender pay gap and disclosure of its D&I initiatives.[6]

    - Engaged with Amazon over its workers' rights and factory conditions at the distribution centres and voted for the appointment of an independent chair and the publication of a gender pay gap report covering its global operations. Also, voted against Jeff Bezos because he serves as both CEO and chairman and believed that an independent chairman to oversee the board was in Amazon's best interests.[7]

[4] https://library.aviva.com/tridion/documents/view/in90132.pdf
[5] https://www.rlam.co.uk/globalassets/media/literature/reports/69348-stewardship-and-responsible-investing-report-2020.pdf
[6] https://library.aviva.com/tridion/documents/view/in90132.pdf
[7] https://employer.royallondon.com/globalassets/docs/shared/investment/69348-stewardship-and-ri-report-

- Decided to not invest in Aaron's Inc after finding its disclosures on its business model to charge high APR interest rates to be opaque and confusing, in particular for vulnerable customers.[8]

16. ABI analysis of member firms' policies shows a clear preference for stewardship over divestment and exclusions. Members will only divest from companies that do not improve ESG factors that are set out in their responsible investment principles, if extensive engagement, which includes voting, does not result in change. This approach is backed by ABI members consumer research, which has shown that their customers prefer stewardship to improve a company's performance on ESG metrics before divesting.

17. As a means of reducing carbon emissions and tackling climate change, the distinction sometimes drawn between stewardship and divestment is artificial. Divestment is an option open to asset owners and asset managers as part of the stewardship process. In the short term, divestment may help individual investors meet specific reporting targets, but – given the wide availability of alternate sources of investment for these high-emitting sectors – it is less likely to result in any immediate real-world reductions in emissions.

Climate Conscious Investments

18. There are a growing range of financial products that offer pension funds investment opportunities into sustainable and green finance, and a growing number of tools to help pension providers make these decisions. However, this is an evolving sector and we would expect the range of options to expand considerably in the coming years.

19. In an autumn 2020 survey of ABI members who offer Automatic Enrolment we found that that all have, or are in the process of, integrating ESG risk factors into their entire proposition, including default funds. Customers do not have to self-select in order to be invested in a fund that takes into account ESG risk factors.[9]

20. The key role Government and regulators can play is enabling innovation with consistent signals across different sectors and transparency about how the targets set in UK Carbon Budgets will be implemented. This will give investors certainty and allow for greater product development.

International Environment

21. Climate change is a global issue and the international environment has a key role in shaping standards and regulations to which the industry adheres. Consistency in the international arena is vital in supporting stewardship efforts and in ensuring ESG standards are met.

International Standards

2020.pdf

[8] https://employer.royallondon.com/globalassets/docs/shared/investment/69348-stewardship-and-ri-report-2020.pdf

[9] *The Role of Pensions in Driving ESG Investment*, Association of British Insurers, February 2021 https://www.abi.org.uk/news/blog-articles/2021/02/the-role-of-pensions-in-driving-esg-investment/

22. International standards will play a central role in ensuring consistent decision making and like-for-like comparisons. Even where companies that are being invested in are based in the UK, they will almost always have a wide international network across their suppliers and value chain. International standards should build on the progress already made in establishing consistent standards – including through the networks listed in our answer to the previous question.

23. The ABI is a formal supporter of the Task Force on Climate-related Financial Disclosure Principles and welcomes the UK Government's world-leading commitment to making these mandatory across the economy by 2025. As investors and underwriters, our sector will depend on consistent and complete data to inform decision making.

24. Currently, there is little international consistency in sustainability reporting, including for climate risks. There are various reporting frameworks with different or overlapping scope and a variety both of reporting aims and of requirements, recommendations or guidance. Many companies can choose which to apply and the extent to which they do so, and where national requirements exist and differ, there is extra cost to multinational reporters. Hence investors do not generally have the quantity, quality, and comparability of information which they require, and it is difficult for preparers to identify and supply this information.

25. A global set of internationally recognised sustainability standards would make good these deficiencies and therefore is needed.

26. The ABI supports the initiative of the IFRS Foundation to establish a Sustainability Standards Board, whose top priority will be to set sustainability standards for use on a global basis. Our members operate in global markets and where consistency matters. Any development in UK standards should result in consistency with global developments. We encourage the Government to continue actively partaking in the development of global standards on ESG risk factors and reporting to ensure that the standards work for UK firms operating internationally.

The Regulatory Environment

27. Through the Climate Financial Risk Forum, the industry's regulators the PRA and FCA, have demonstrated regulatory leadership, whilst working collaboratively with industry to drive change. This represents a strong basis for further work on climate change and – in the view of the ABI – positions the UK as a world-leader in terms of how our regulators are seeking to address climate change.

28. In addition to the work being undertaken by the CFRF, there are a number of significant regulatory initiatives currently underway that will assess the effectiveness of the industry's preparations for climate change, including:
    - **Implementation of TCFD principles** – the ABI is a formal supporter of the Task Force for Climate Related Disclosure and welcomes the UK Government's world-leading commitment to making TCFD mandatory across all businesses by 2025. We have responded positively to a number of recent consultations on TCFD implementation from different Government departments and regulators. It is vital that different regulators do more to ensure the implementation of TCFD principles is consistent and logically sequenced across different regulatory

regimes (especially as ABI members will often be obliged to produce TCFD reporting for more than one regulator) – as inconsistency will undermine the role that TCFD can play in driving consistent decision making on climate issues.

- **Bank of England Climate Biennial Exploratory Scenario** –Due to be launched in June 2021, this exercise includes 10 of the UK's largest insurance and long-term savings providers (with other firms also participating on a voluntary basis). This exercise will involve an extensive process of engagement and data gathering with counterparties and a comprehensive assessment of the risk management required for climate change. As well as informing how prudential regulation will need to evolve to accommodate the impact of climate change, this exercise will provide considerable evidence of the actions needed to reduce the sector's exposure to climate risk.
- **Managing the financial risks from climate change** – in April 2019, the PRA set out its expectations on how banks and insurers should manage the financial risks associated with climate change. Firms will report for the first time on how they have adopted these requirements by the end of 2021.

29. The ABI has been playing an active role, working directly with regulators and through regular member working group meetings and organising industry roundtables, to ensure these initiatives are effective.

30. Given the scale and scope of these exercises – and the significant volume of data, evidence and analysis they will generate – our recommendation is that the lessons learned from these is absorbed before any further regulatory interventions are considered.

About the ABI

The Association of British Insurers is the voice of the UK's world-leading insurance and long-term savings industry. A productive and inclusive sector, our industry supports towns and cities across Britain in building back a balanced and innovative economy, employing over **300,000** individuals in high-skilled, lifelong careers, two-thirds of which are outside of London.

The UK insurance industry manages investments of over **£1.7 trillion**, pays nearly **£12bn** in taxes to the Government and supports communities across the UK by enabling trade, risk-taking, investment and innovation. We are also a global success story, the largest in Europe and the fourth largest in the world.

The ABI represents over **200** member companies, including most household names and specialist providers, giving peace of mind to customers across the UK.

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