BlackRock.

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Anne Kennedy, Melanie Jarman,
Emma Walmsley, Tom Rhodes,
Mark Rogers and Vanessa Calvache
Climate Change and Responsible Investment Team

Submitted via email to: pensions.governance@dwp.gov.uk

RE: Climate and investment reporting: setting expectations and empowering savers – consultation on policy, regulations and guidance

Dear Anne, Melanie, Emma, Tom, Mark, Vanessa,

BlackRock[1] is pleased to have the opportunity to respond to the consultation on climate and investment reporting, issued by the Department for Work and Pensions.

BlackRock manages the pension savings of over 10 million people in the UK. Our role is to support trustees responsible for overseeing their retirement assets by providing education and information on climate risk considerations, designing products and solutions that support their investment beliefs and respond to their investment needs, engaging with investee companies on material sustainability risks and opportunities, and providing transparency on these activities.

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Overarching comments

We continue to believe that climate risk is investment risk, and our investment conviction is that sustainability and climate-integrated portfolios can provide better long-term risk-adjusted returns to investors. Similarly, investment stewardship, i.e. engagement with companies and the exercise of shareholder rights, is an important way of promoting sound corporate governance and sustainable business practices by companies, and in turn delivering better outcomes for investors. We therefore welcome the emphasis the DWP is placing on ensuring that all actors throughout the investment chain are fully engaged with these issues.

At the same time, the draft guidance would place significant additional responsibility on trustees and will in turn require their professional services providers – both investment consultants and asset managers – to request, supply, and interpret the information necessary for trustees to discharge their obligations, and to demonstrate how they have done so. There is therefore a risk that services providers take different views on and / or approaches to the definitions and data relating to concepts or metrics included in the guidance, leading to a proliferation in reporting methods ultimately leading to a lack of consensus or comparability, limiting the ability of trustees and the end consumer to monitor and choose between different service providers.

To take the example of portfolio alignment measurement and reporting: while we agree with the DWP that the three models identified by the TCFD PAT are each useful and valid, leaving the choice of model to individual trustees or service providers creates the scope for divergent approaches that will ultimately hamper consistency and comparability – at

[1] BlackRock is one of the world's leading asset management firms. We manage assets on behalf of institutional and individual clients worldwide, across equity, fixed income, liquidity, real estate, alternatives, and multi-asset strategies. Our client base includes pension plans, endowments, foundations, charities, official institutions, insurers and other financial institutions, as well as individuals around the world.

odds with one of the main objectives of the TCFD framework. This problem is compounded by the lack of methodological standardisation for each model, recognised by the DWP in this consultation document.

Similarly, the draft guidance gives scope for divergent policies and criteria for what is deemed a 'significant vote'. In general, where trustees have delegated responsibility for stewardship and voting to asset managers, we believe transparency, including information on significant votes with respect to asset managers' stewardship policies, is the most suitable means by which they should be monitored and held to account for alignment of our policies and activities to those of the pension scheme. While we support the motivation behind requiring trustees to indicate how the 'most significant' votes carried out on their behalf align with the scheme's stewardship policies, in practice, where voting decisions are delegated to asset managers, the latter will be required to supply (often via reporting sought by investment consultants) the information needed to explain which votes are deemed significant. This would represent a departure from the current approach to vote reporting.

To ensure that trustees and end-savers enjoy the full benefits of the enhanced reporting that this guidance will entail, we see the need for working groups comprised of all constituencies in the UK pensions ecosystem – including trustees, investment consultants, and asset managers – to develop coherent reporting processes for both the climate and stewardship aspects of the proposed guidance that make the most effective use of each constituency's role and resources. Such cross-industry processes have been helpful in the past: for TCFD reporting the Investment Association, Pensions and Lifetime Savings Association (PLSA), and Association of British Insurers have worked alongside consultants to develop reporting; while for stewardship reporting, the PLSA voting template has been widely adopted across the pensions market. We strongly believe that industry standards should be agreed before the proposed guidance takes effect to mitigate the risk of reporting proliferation.

Measuring and reporting Paris alignment

We welcome the DWP's intention to require these disclosures on a 'best efforts' basis, and recognition of data limitations through the 'as far as they are able' principle. This is consistent with the approach set out by the FCA in its proposals to enhance climate-related disclosures by asset managers, life insurers, and FCA-regulated pension providers, and DWP rightly recognises that disclosure by asset managers at product or portfolio level are a necessary pre-cursor to pension schemes being able to make these disclosures.

As we highlighted in our response to FCA CP21/17, data coverage for listed equity and fixed income is strong, particularly in developed markets – although there are challenges for currency, short-term instruments, or derivative products where look through of data and associated 'climate risk' attached to them require more analysis. In other asset classes, including government bonds, private markets, and alternative investment such as private equity, private credit, and real assets, there continue to be significant data challenges: coverage issues mean any disclosures will not be reliable or consistent for end-investors. Over time, we expect data coverage and consistency in all areas to improve and encourage further industry-wide collaboration to set standards.

Similarly, as the DWP recognises in the consultation paper, the market has not yet coalesced around a single portfolio alignment metric, and there is little methodological standardisation. This is also the case for some of the 'additional metrics' outlined by the DWP in the proposed guidance. Indeed, while we support the intention around forward-looking metrics such as Climate VAR and implied temperature rise, they are still relatively new, not feasible for some asset classes, and will require third party data providers to provide consistency.

Taken alongside DWP's intention to provide trustees with methodological flexibility for portfolio alignment metrics, we see a risk that implementing the guidance as written without giving industry time to coalesce around reporting standards will lead to divergent approaches to reporting, including for metrics that are nominally the same. This would create significant operational burdens for pension scheme services providers who will ultimately have to supply and interpret the information – but more importantly, it will lead to a lack of consistency and comparability across the market, creating significant difficulties for schemes who may need to 'aggregate up' metrics provided by different service providers; or to compare progress or outcomes between different service providers. Policymakers will encounter a similar problem if they intend to use these disclosures to track pension schemes' progress towards net zero or temperature-alignment targets. Ultimately, this lack of consistency and comparability will be detrimental to trustees and the end-savers they represent.

We therefore see the need to build some degree of consensus across the pensions ecosystem on which metric, or metrics, are most appropriate, and the methodology underpinning them. We believe a working group comprised of trustee representatives, consultants, asset managers, and other relevant service providers should be convened to reach this consensus before the guidance takes effect. The Investment Association has conducted a similar exercise for the first phase of TCFD reporting, in conjunction with the PLSA, Association of British Insurers, and investment consultants. We recommend a similar process be given time to run ahead of the proposed guidance taking effect. We do not believe this would preclude the measurements or disclosures by schemes evolving over time as more data becomes available and modelling becomes more sophisticated, but we do believe it is crucial that there is consistency and comparability across the pensions sector.

Stewardship and the Implementation Statement

We agree with the DWP that stewardship is key to delivering value for members of pension schemes, and that trustees should exercise strong ownership and oversight of stewardship activities. We recognise that the money we and other asset managers manage is not our own – it belongs to our clients; and those that wish to play a more proactive role should, where possible, have more choice as to how to exercise voting rights for the assets they own.

Much like asset allocation and portfolio construction, where some clients take an active role while others outsource these decisions to us, some of our clients are interested in having a say in how their index holdings are voted. We want to provide choice to these clients while continuing to support those who have elected to have our investment stewardship team vote on their behalf.

The steps BlackRock is taking in relation to proxy voting choice demonstrate how we believe this might work in practice. From 2022 BlackRock is taking the first in a series of steps to expand the opportunity for clients to participate in proxy voting decisions where legally and operationally viable. To do this, we have been developing new technology and working with industry partners over the past several years to enable a significant expansion in proxy voting choices for more clients.

These voting choice options will first be available to institutional clients invested in index strategies – within institutional separate accounts globally and certain pooled funds managed by BlackRock in the U.S. and UK. We expect the trustees representing 7 million UK pension savers invested in our pooled funds to be eligible for voting choice. This is a first step to expand voting choice in the UK, and we hope to make further progress. The coverage of voting choice beginning in 2022 is based on client demand as well as the legal and operational complexities associated with offering voting choice in specific fund ranges. We plan to continue evaluating demand for and feasibility of expanding voting choice to additional fund ranges.

Where options such as voting choice (or other proxy voting mechanisms identified in the consultation document) are not operationally feasible, trustees of schemes using such investment options will continue to be reliant on the advice and services of professional services providers – both consultants and asset managers – to both guide and execute stewardship policies on their behalf.

And, importantly, while we expect some clients to make use of the discretion offered by voting choice, our conversations with clients indicate this will not universally be the case: trustees who assess and conclude that their providers are well-placed to undertake stewardship on their behalf in alignment with their schemes' stewardship policies should have the opportunity to request that their providers do so – and we will continue to support clients who wish BlackRock to exercise stewardship on their behalf.

Where clients continue to delegate stewardship and voting to asset managers, it will naturally require the various parties involved to take steps to ensure that the approach to stewardship undertaken on the schemes' behalf does in fact align with the schemes' stewardship policies, and for schemes' reporting to properly demonstrate how and why this is the case.

This requires dialogue between end-investors, their advisors and services providers, and asset managers to help shape the latter's stewardship priorities; and full transparency throughout the investment chain that allows trustees to draw on reporting produced by asset managers – which should set out clearly how those asset managers have exercised stewardship in accordance with the approach communicated to clients, thus allowing trustees in turn to explain how the activities of their asset managers align with beneficiaries' expectations.

Each year BlackRock Investment Stewardship (BIS), our independent investment stewardship team reviews, updates, and makes public our investment stewardship policies, including our Global Principles, market-level voting guidelines, and Engagement Priorities. Dialogue with our clients helps shape our policies. In 2020, BIS held over 200 meetings with clients to understand their perspectives on stewardship and better understand the issues that are important to them – including the priorities that they believe should guide our stewardship activities.

We have also been working to increase transparency around our stewardship work. As well as regularly updating and disclosing the policies outlined above, we publish annual stewardship reports that give an overview of our investment stewardship activities throughout the year – including engagement voting, and promoting thought leadership – and case studies on engagement. We also publish quarterly engagement summaries naming all companies we engaged with each quarter across a range of environmental, social, and governance topics; and publish our voting record quarterly for each of the shareholder meetings that have taken place globally – detailing our voting rationales for key items on the ballot. We also publish Vote Bulletins for high profile or significant votes, explaining our decisions, and the engagement and analysis underpinning them.

In cases where trustees have delegated responsibility for stewardship and voting to asset managers, we believe this type of dialogue and transparency is the most suitable means by which we should be monitored and held to account for alignment of our policies and activities those of the pension scheme.

For UK-based clients, this transparency is supplemented by disclosure of our voting record in line with the Pensions and Lifetime Savings Association (PLSA) vote reporting template, which includes details of 'most significant' votes cast. Which votes are deemed ‘significant’ is determined in accordance with our overall stewardship policy, rather than at portfolio- or fund-level.

The draft statutory guidance now being consulted on proposes that where an asset manager votes on schemes’ behalf, trustees should decide which votes are significant, and include them in the Implementation Statement. This would be a departure from the current approach to schemes’ reporting of ‘significant votes’, and in practice, any supplementary information needed to explain this will be supplied by asset managers (often through reporting sought by investment consultants). This, in our view, creates the potential for a proliferation of different reporting standards – a problem the current PLSA template was developed to solve via cross-sectoral consultation and consensus building.

If it is the case that trustees require disclosure of voting activity, including most significant votes, to be developed further, we believe it is critical that a similar process is again followed. Our overarching recommendation that working groups be set up to develop this reporting recognises the need to ensure that transparency does indeed facilitate improved reporting on the alignment between activities undertaken on behalf of schemes and their stewardship policies – and avoids confusion and reporting proliferation. It is also intended to recognise, though, that effective stewardship relies on a clear assessment of the needs and resources each constituency in the UK pensions ecosystem, and that a sustainable solution will be one that reflects these needs and resources in its design.

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We welcome the opportunity to comment on the issues raised by this consultation paper and will continue to contribute to the thinking of the DWP on any issues that may assist in the final outcome.

We welcome further discussion on any of the points that we have raised.

Yours faithfully,

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