15 July 2019

John Reynolds
Financial Conduct Authority
12 Endeavour Square London E20 1JN
By email to cp19-15@fca.org.uk

Dear Mr. Reynolds,

CFA UK response to the FCA's consultation paper (CP19/15) "IGCs: Extension of Remit".

The CFA Society of the UK (CFA UK) welcomes the opportunity to share its views on the above consultation paper issued by the FCA.

CFA UK consider both ESG investing and Value for Money to be fundamentally important issues for the investment profession today. We applaud the FCA's proposed ruling to extend the remit for IGCs to include and embed further duties in respect of these two important concepts.

CFA UK have written fairly extensively on both issues in recent months (see Appendix 2). And would wish to highlight of particular relevance to these topics both:

- The launch of a new certificate in ESG investment in September when the first cohort of some 500 investment professionals will sit the new exam paper; and
- The position paper "Value for Money: A Framework for Assessment" published last November.

We believe that it is important that consistent governance arrangements exist between consumers of private savings or pension products and members of occupational pension funds. As such believe that the FCA should look to the work done by the DWP in 'Clarifying and Strengthening Trustees' Investment Duties'.

High Level Points

In Summary CFA UK believes:
- IGCs **should** manage and report on financially material ESG risks
- IGCs **may** still incorporate non financial ethical concerns into strategies, if appropriate to client demand and fund objectives;
- IGCs **should not be beholden** to incorporate non-financial ethical concerns, given their broader duties and product strategy, nor should an undue burden fall on them to handle consumer challenge on non-financial ethical concerns (unless incoporated in fund objectives);
- IGCs **should** of course report on ethical concerns where they are incorporated in fund objectives;
- As far as possible, governance arrangements for both consumers of private savings or pension products and members of occupational pension funds should be consistent.

Responses to Questions

Q1: Do you agree that IGCs should report on the adequacy and quality of their firm's policies on (i) ESG issues, (ii) member concerns and (iii) stewardship?

Yes.

i) With effect from October 2019, occupational pension scheme trustees will be required to set out in their Statement of Investment Principles:

-How they take account of financially materially considerations, including (but not limited to) those arising from Environmental, Social and Governance consideration, including climate change;

- Their policies in relation to the stewardship of investments, including engagement with investee firms and the exercise of the voting rights associated with the investments;

We believe the same onus should be placed on IGCs.

It is now widely recognised that "ESG issues" may have a material impact on the financial success of a company. Consultation Paper CP19/15 recognises that "ESG issues" may be 'financial', but that there may be ethical issues that are "non-financial" – we would caution that, with the focus now on ESG, there are few Environmental or Social issues that can easily be dismissed as purely "non-financial" ethical issues. We do agree that fund providers should be considering "ESG issues" to determine their financial materiality and that ICG's should be reporting on the quality and adequacy of their firm's policies and activities for doing this.

We recognise that there will necessarily be judgement as to whether an "ESG issue" is deemed financially material or even "non-financial" (a matter as yet without an expected financial impact). We support the ability for firms to include "non-financial" risks where appropriate to the fund objectives, and this should also be reported on by the IGC. However, we caution that it may not always be appropriate for the IGC to consider or respond to member concerns surrounding "non-financial" ESG issues. Such concerns may solely reflect a member's own ethical beliefs and may not be concerns that in any way relate to the stated objective of the underlying product. We believe that in such instances there should be no onus on the IGC to respond to such matters; dealing with member queries based on their own particular ethics and beliefs could not only be an unnecessary distraction for IGCs, but also limit their capacity to effectively carry out their role.

To the extent that consumers want products that potentially place ESG criteria over and above financial criteria, IGCs should perhaps comment in their annual statement on whether (or not) they consider it appropriate to provide such products to the market and how they have taken member views into account in determining their product offering. From 1 October 2019 occupational pension trustees will be required to prepare a 'statement of member views', setting out how they will take account of the views which, in their opinion, members hold, in relation to the matters covered in the Statement of Investment Principles. At a conceptual level IGC's could produce a similar statement without being drawn into dealing with individual member challenges.

Consultation Paper CP19/15 does not refer to this, but the potential importance of "Impact Investing" should not be overlooked. Impact investing is no longer an activity of simply investing in companies that are directly making an impact, such as renewable energy companies, but can extend to investing with the intention of making an impact through influence as a shareholder (i.e. investing in a company that traditionally may have failed an ESG screen, with the intention of exercising stewardship and/or positive activism to improve that company's ESG credentials).

Where consumers are invested in a product with non-financial objectives (whether a more traditional ESG fund or an impact fund, and whether these objectives be ethically focussed or otherwise) CFA UK believes it is important for the IGC to address member concerns over whether the fund is appropriately reflecting its stated philosophy in its holdings. For impact funds, holdings that at first glance appear at odds with the fund's ESG objective actually may be in line with the firm's policy once the firm's stewardship is considered.

We agree that, in the context of a 'mainstream' product, it is appropriate that ESG be recognised as only one particular category of financial risk and not given such a prominence that it overshadows other equally material financial risks. Likewise, policy-makers must guard against encouraging current ESG trends to overshadow other ESG issues which also have financial significance. The clear potential for ESG to be a significant contributor to future performance must be recognised such that these issues are not downplayed and also to ensure each of them is properly considered and weighted according to its relative importance.

ii) It is widely recognised that members of work-place pension schemes engage rarely if at all with their scheme providers. Therefore, where members have gone to the trouble of raising valid concerns, it is important that IGCs hold the scheme to account for effectively addressing these concerns.

iii) CFA UK responded to DP19/01 and CP19/07 as well as the FRC's consultation on proposals for revisions to the stewardship code earlier this year. CFA UK broadly agreed with the proposals from the FCA and FRC in relation to stewardship and in particular the increased focus on outcomes and the requirement for firms to publish an outcomes activity report. This in turn should provide IGCs with the transparency they require to properly assess the strength of stewardship exercised by the fund provider(s) and allow them to report effectively and efficiently to members on this.

Q2: Do you agree that IGCs should report on how the firm has implemented its policies on ESG issues, member concerns and stewardship?

- If a firm has a policy it should be expected that that policy is implemented, however providing details of activities that demonstrate how a policy has been implemented in practice may both help the consumer understand what the policy means in practice and focus the IGC's attention on apporiately monitoring the policy. This is consistent with the DWP conclusion requiring schemes of 100 or more members with DC sections to produce a report on how they implemented their investment stratgey, and to publish it alongside other material.

- We are confident that in reporting on the implementation of an ESG policy, the IGC's should be pointing to different activities each reporting period and therefore have no concerns that such an additional reporting requirement would take the form of boiler-plate language.
- We would also wish to underline that environmental, social and governance issues all deserve firms' attention and CFA UK is concerned that in some cases governance risks seem to be given far more prominence than environmental and social risks.

Q3: Do you agree that IGCs should report on the firm's policies on these issues for both pathway solutions and workplace personal pensions?

Yes.

- We believe scheme members do require some additional protection and transparency. We expect the average scheme member's attention to, and understanding of, these technical products to be insufficient to protect them from potential harm.

Q4: Do you agree that firms should make the IGC's annual report publicly and prominently available, with 2 prior year reports for comparison?

Yes.

- This would be an important step in engendering trust in the firm and ensuring accountability of the members of the IGC. Three years should be a minimum requirement in our view, and some firms may find that publishing a longer time-series enhances the communication of their value for money proposition to members.
- CFA UK believes furthermore that IGCs should also highlight in their annual report if policies and their adequacy and quality have changed over the year.

Q5: Do you agree that the proposed guidance should apply more widely, to all firms that provide pension products and all life insurers that provide investment-based life insurance products?

Yes.

- CFA UK believes it is important that these requirements are seen as "standard" across the long-term savings market.

Q6: Do you agree that we should focus our requirement for an IGC on firms offering pathway solutions to consumers?

Yes.

- It is primarily at the point of interface with the consumer that one has the entire picture on which to assess cost and appropriateness. Bringing the distributor IGC (rather than the manufacturer IGC) focus to this area should be important in helping to protect those ultimately using drawdown solutions.

- While both manufacturer and distributor having an equal responsibility may seem intuitively appealing, we worry that a regime where both the manufacturer IGC "signed off" the pathway solution's "integrity" and the distributer IGC approved its "appropriateness" for the target market may undermine the accountability to be attached to each sign-off, as each IGC might be encouraged to rely on the sign-off of the other.

- A dual-sign-off regime also would increase the cost of oversight which would ultimately be borne by the scheme's members.

Manufacturer firms are of course required to provide full information regarding their pathway solutions to distributer firms and to provide it in as transparent and clear a way as possible.

Q7: Do you agree with our proposed approach for providers with smaller numbers of non-advised consumers entering drawdown?

- CFA UK believes that that all pathway solutions offered to non advised customers should have been approved by a competent independent oversight body. Whether it is an IGC, GAA or third-party GAA that performs this independent oversight is not so relevant providing it is competent oversight.
- CFA UK supports the use of GAAs - for the firms in question a GAA is likely to provide the appropriate level of skill and experience that may otherwise be lacking, and at a cost that given economies of scale should not be disproportionate to benefits gained.

- We are not adequately conversant with the drawdown comparison tool to be offered by the Money & Pension Service and refered to in clause 4.40. We recognise the important role that this tool could play in opening up competition in the market for drawdown products (and are supportive of this). However, we are currently wary to comment on it as an alternative to advice until it has been proven to be an adequate substitute for traditional financial advice and capable of effectively dealing with the complexity of the full range of different financial circumstances that individuals retirees will have. At this stage we question whether there should be any choice for firms other than (i) to use an IGC, (ii) to use a GAA or (iii) to refuse to provide pathway solutions to non-advised customers.

Q8: Do you agree that IGCs must be in place in time to assess the initial designs of pathway solutions?

Yes.

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Q9: Do you agree that we should be more prescriptive in our rules and guidance for firms and/or IGCs on how value for money should be assessed?

No.

- At this stage we believe that the FCA should take a route where they establish a framework of principles to be followed, which look rather like headings and sub-headings, rather than prescriptive rules which could stifle innovation. The principles could be augmented by voluntary guidance, but we would advocate against hard rules.

Q10: We welcome your view on what legacy pension products should be compared with, when assessing value for money.

CFA UK believes that legacy pension products should be treated in the same way as all other pension products. Where the value for money of a legacy pension product compares unfavourably with modern-day equivalents the responsible IGC should be transparent about the situation with the affected customers, explain the reasons for this and still look for ways to improve value for money for members going forward, be it through fee reductions or significant alterations to the structures that may result in exceptional one-off costs but should, in that IGC's judgement, lead to better value for money for members over time.

Q11: Do you agree with the conclusion and analysis set out in our cost benefit analysis?

No comment.

CFA Society United Kingdom

We are grateful for the opportunity to respond to these valuable consultations and would welcome the opportunity to take any questions you may have.

Yours sincerely,

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CFA Society of the UK

With thanks to contributions from:

Natalie Winterfrost, CFA
Alistair Byrne, CFA
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CFA UK Professionalism Steering Committee

Appendix 1: About CFA UK & the CFA Institute

CFA UK: serves nearly 12,000 leading members of the UK investment profession.

- The mission of CFA UK is to build a better investment profession and to do this through the promotion of the highest standards of ethics, education and professional excellence in order to serve society's best interests.

- Founded in 1955, CFA UK is one of the largest member societies of CFA Institute (see below) and provides continuing education, advocacy, information and career support on behalf of its members.

- Most CFA UK members have earned the Chartered Financial Analyst® (CFA®) designation, or are candidates registered in CFA Institute's CFA Program. Both members and candidates attest to adhere to CFA Institute's Code of Ethics and Standards of Professional Conduct.

CFA Institute: is the global association for investment professionals.

- The mission of CFA Institute is to lead the investment profession globally by promoting the highest standards of ethics, education, and professional excellence for the ultimate benefit of society.

- It awards the Chartered Financial Analyst® (CFA), and Certificate in Investment Performance Measurement® (CIPM) designations worldwide; publishes research; conducts professional development programs; and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry.

- As of 1st February, CFA Institute has more than 165,000 members in 162 markets, of which more than 160,000 hold the Chartered Financial Analyst® (CFA) designation.

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Appendix 2: Recent CFA UK Publications on Value for Money & ESG:

A) Position Papers:

- Value for Money: A Framework for Assessment (November 2018):
https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/3-research-and-position-papers/value-for-money--a-framework-for-assessment.pdf

B) Recent Consultation Responses:

i) Value for Money

- Response to the FCA regarding CP18/9: Consultation on Further Remedies – Asset Management Market Study (June 2018):
https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-letter-to-karen-northey.pdf?la=en&hash=D330FBFA4E022E4392EC47A7AE395EEDE44E8EC5

- Response to the FCA regarding MS17/1.2: Investment Platforms Market Study:
https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-letter-to-kate-blatchfordhick-final.pdf?la=en&hash=96A9B1F1AE37C588706DE59377574D38FC8D24CA

ii) ESG

- Response to the FRC and FCA joint discussion paper (DP19/1) "Building a regulatory framework for effective stewardship" (April 2019):
https://www.cfauk.org/-/media/files/pdf/professionalism/cfa-letter-to-fca-on-dp19_01-final.pdf?la=en&hash=9A937D561C3D2451047CBD7A3982C7D242B355E6

- Response to FRC's consultation on the proposed revison to the Stewardship Code (March 2019):
https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-uk-response-to-the-frcs-consultation-on-the-stewardship-code.pdf?la=en&hash=DE129C5EF548A241711060A40B0C1DB56154C82A

- Response to FCA consultation CP19/07 on proposals to improve shareholder engagement (March 2019):
https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-uk-response-to-the-fcas-consultation-on-proposals-to-improve-shareholder-engagement.pdf

- Response to FRC's consultation on proposed revisions to the UK Corporate Governance Code and the future direction of the Stewardship Code (Feb 2018):
https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-letter-to-catherine-horton-28-feb-2018--final.pdf?la=en&hash=CF53FFB72384C08CF5D6D7BC85E310C6EBF4320A

- Response to the Investment Association's consultation on sustainability & responsible investment (March 2019):

https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-letter-to-jess-foulds-at-the-ia_.pdf?la=en&hash=0A01E51C384079642F147E97B58B091EE86382B8

- Response to the FCA regarding Discussion Paper (DP18-08) Climate Change & Green Finance (January 2019):

https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-letter-to-shamamah-deen-31jan19-final.pdf?la=en&hash=1D3FE7C8D43E0FF339F4CCE9FC884BF4FE3D0C37

C) <u>Other:</u>

- CFA UK's Certificate in ESG Investing:

https://www.cfauk.org/esg

- 5 steps to help trustees navigate their ESG responsibilities (May 2019):

https://www.cfauk.org/pi-listing/5-steps-to-help-trustees-navigate-their-esg-responsibilities

- What does ESG mean for investing (May 2019):

https://www.cfauk.org/-/media/files/pdf/pdf/1-study-with-us/esg/certificateinesginvesting_may19.pdf