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| Investment |
| Climate and investment reporting |
| Setting expectations and empowering savers |

# About us

Nest was established in 2010 as part of the auto enrolment programme to help people save for retirement. Unlike any other pension scheme in the UK, Nest has a legal obligation to accept any employer that wishes to use us to discharge their auto enrolment obligations. Over 900,000 employers have signed up to use Nest.

Over the last decade, Nest has grown to be one of the largest pension schemes in the UK. We are operating at scale as a high quality, low cost pension scheme helping over 10 million members save for their retirement. Many are low to moderate earners who may be saving into a pension for the first time. A typical Nest member earns around £20,300 per year and nearly half our members are under 35 years old.

Nest is built around the needs and behaviours of our members, from our approach to responsible investment to our focus on customer service. We now occupy a place in the market as a major Master Trust, helping to drive up standards and best practice across the industry. Nest has great potential for delivering pensions to mass market consumers for many years to come, leveraging our scale to deliver value through the combination of low costs, our market leading investment strategy and modernised services all overseen by strong trustee governance.

# Response

We welcome the opportunity to respond to DWP’s consultation on Paris alignment reporting and Stewardship guidance. In particular, it is helpful that the Department have allowed 11 weeks for responses, to accommodate the Christmas period. Although Nest makes every effort to respond to relevant consultations, we hear the concerns – particularly expressed by other occupational pension schemes - over the resourcing of responses. Longer consultation windows support the opportunity to provide the high-quality feedback necessary to deliver well informed regulations which meet Government’s policy goals.

We support the concept of a forward-looking alignment measure, but it’s important to note that we are still some way off from an agreed methodology and industry standard. Paris alignment was left out of DWP’s consultation on TCFD as methodologies were not considered to be advanced enough. Whilst we have seen an increase in investor activity in working towards developing Paris alignment tools, we would argue this is still the case. We make some proposals below over how Paris alignment could be taken forward given the industry’s current position and how the regime could become more targeted.

We also support stronger stewardship efforts by occupational pension schemes, but we recognise the difficulty of effectively legislating over such policy areas without requirements being met through box ticking or boilerplate disclosures. Therefore, we think the Department’s proposal to take a guidance-led approach in the first instance is appropriate, and we broadly welcome the proposals. However, there are a number of areas in which the detail is not completely clear. We identify areas of confusion and suggest how these might be resolved below.

# Chapter 1 – Measuring and Reporting Paris Alignment

## Q1. We propose to amend the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021 to require trustees of schemes in scope to measure and report their scheme’s Paris alignment by adding a requirement for them to select and calculate a portfolio alignment metric and to report on that metric in their TCFD report. Do you agree with this policy proposal?

Under regulations in force schemes will be required to report total emissions and their emissions intensity, which are ultimately backward-looking measures, and only a proxy for the level of climate risk in a portfolio. Such measures do not distinguish between high emissions in sectors which are currently harder to decarbonise (cement, steel, aviation), and those in sectors where emissions are high but opportunities for decarbonisation are higher, such as power and some extractive industries. Within the latter category, it does not distinguish between firms who are on a net zero journey by making forward-looking decarbonisation commitments and undertaking the necessary capital expenditure, and those who have no such plans. With this in mind we therefore support the idea, in principle, of a portfolio alignment metric.

However, we believe that the concerns around lack of a standardised methodology, accuracy and decision-usefulness that are cited in the consultation paper regarding the decision not to consult in 2020, have not yet been addressed to an extent where we feel wholly comfortable with making such a metric a mandatory requirement.

Nest recently issued a request for proposal for portfolio alignment metrics. We decided not to proceed with this due to the significant cost, which was in excess of £10,000 for each implied temperature rise (ITR) and benchmark divergence proposal we received. There was also concern on the lack of coverage and the robustness of methodologies.

We agreed with much of the feedback given over the summer to the TCFD’s June consultation on portfolio alignment metrics that ITR measures may give a false sense of precision. Additionally, by condensing a complex set of sector and company level risks into a single portfolio level measure, trustees and others can focus unduly on of the importance of lowering the headline implied temperature rise – potentially driving divestment decisions which are not in members’ interests - and make less use of the metric as an engagement and asset allocation tool – using the tool to, in the words of the draft regulations “identify and assess the climate-related risks and opportunities which are relevant to the scheme”. Furthermore, most ITR tools are also proprietary, expensive and inconsistent, making it difficult for stakeholders and members to compare and contrast performance between schemes. We note that the TCFD in its final guidance acknowledged the challenges to implementing portfolio alignment methodologies, including the resources involved, and encourages organisations to disclose qualitative and quantitative information given existing data and methodologies.

Whilst a benchmark divergence measure allows for greater unpacking of the extent to which investee firms are aligned with a net zero target, there are still challenges. Free-to-use tools such as the Transition Pathway Initiative (TPI) have relatively low coverage, whilst paid for products with wider coverage will have similar challenges to ITR in relation to inconsistent methodologies. There are also reported issues associated with potential over-reporting of alignment by TPI, [as highlighted by Reclaim Finance](https://reclaimfinance.org/site/en/2021/12/06/the-tpi-benchmark-misleading-approach-dangerous-conclusion/).

A binary measure, based on the proportion of assets that have set a Paris-Aligned target, is the most straightforward measure. There are nevertheless challenges too with the binary measure - it is an incomplete guide to the forward-looking climate risk of the overall portfolio. One might have a portfolio where 20% of the assets under measurement in the fund are net zero aligned, superficially superior to another where only 10% is aligned, whilst the degree of misalignment for the remaining 80% of the first portfolio is considered to be worse.

All of the different types of tools therefore have their own challenges and benefits. We agree with DWP’s viewpoint that no one tool is better, especially as there is not yet a best practice measure and that schemes should not see the different options as a hierarchy or a progression, especially when the landscape is evolving very quickly.

If DWP were minded to proceed, we suggest that the most effective approach may be to set the initial expectation in statutory guidance of a binary alignment measure *only*, reflecting Science Based Targets. The use of Science Based Targets – a robust and widely-used framework which captures not only scope 1 and 2 but also significant scope 3 emissions, requires interim targets of 15 years or less, and restricts the uses of offsets and avoided emissions[[1]](#footnote-1) - would provide a clear, comparable and consistent basis to undertake the first year’s reporting.

DWP could then consider the results of that first wave of reporting in the second half of 2023 alongside the possible emergence of more consistent approaches, with a view to moving to more sophisticated measures over time as methodological standardisation continues to develop.

This would be an ambitious but reasonable way of phasing in (and phasing up) expectations as agreed consistent approaches emerge. Low cost or free-to-use implied temperature rise metrics, which are sufficiently robust to meet the standards set out in the Portfolio Alignment Team’s report, should emerge. Binary measures may themselves improve or could alternatively become obsolete. This development could be accommodated by building out further extensions to the statutory guidance over time, with the removal of redundant measures.

Without this phased approach, there is a risk of schemes committing significant time and funds early to mutually inconsistent implementations of benchmark divergence and implied temperature rise which for reasons of practical implementation they may feel subsequently tied to. Abandoning these reporting models later on for new more standardised measures as these emerge will likely be associated with significant movements in reported alignment, which will be difficult to explain to engaged savers.

Finally we would flag a mismatch between DWP regulations and FCA rules. The final draft FCA rules set out in PS21/24 touch on portfolio alignment metrics in a number of areas but each reference is far from specific.

* ESG 2.1.6 requires that asset managers ‘must take reasonable steps to ensure its climate-related financial disclosures also reflect the following materials, to the extent they are relevant to the firm’s climate-related reports…. part 4, section D of the TCFD Annex, entitled “Asset Managers”’.
* ESG 2.1.7 refers only to the TCFD Guidance on Metrics, Targets, and Transition Plans being “relevant” in assessing whether climate-related financial disclosures are consistent with the TCFD Recommendations and Recommended Disclosures, and the TCFD guidance itself does not favour any one measure.
* Finally ESG 2.3.13 suggests only that asset managers “must, as far as reasonably practicable, also include the following calculations for each TCFD product… metrics that show the climate warming scenario with which a TCFD product is aligned, such as using an implied temperature rise metric.’

It is therefore perfectly possible to envisage that managers providing services to schemes will adopt a range of measures including the percentage of holdings with science-based targets, a TPI or a PACTA based measure, and one or more ITR measures. As these will not be consistent or comparable, it is highly likely that schemes will have no choice but to obtain raw holdings data and carry out the analysis themselves. This provides an additional argument for favouring a relatively simple approach which can be carried out in house, such as a binary alignment measure.

## Q2. We propose that: (a) trustees who are subject to the requirements in Part 1 of the Schedule to the Climate Change Governance and Reporting Regulations on or after 1 October 2022 (including trustees to whom the requirements are re-applied in accordance with regulation 3(4), 4(4) or 5(4)) will be required to select, calculate and report on a portfolio-alignment metric and to publish the findings in their TCFD report within 7 months of the relevant scheme year end date in the same way as they are for other metrics. This will apply to: trustees of a trust scheme which had relevant assets equal to, or exceeding, £5 billion on their first scheme year end date which falls on or after 1st March 2020, and who remain subject to the requirements in Part 1 of the Schedule on 1 October 2022 trustees of a trust scheme which has relevant assets equal to, or exceeding, £1 billion on a scheme year end date which falls on or after 1st March 2021 trustees of all authorised master trusts and authorised collective defined contribution schemes

## After 1 October 2022 (b) trustees will cease to be subject to the requirements to select, calculate and report on a portfolio alignment metric in accordance with regulations 3(4), 4(3), 4(5), 5(3) and 5(5) of the Climate Change Governance and Reporting Regulations: trustees of a scheme with relevant assets of less than £500 million on a scheme year end date which falls after 1 October 2022 will cease to be subject to the requirements to select and calculate a portfolio alignment metric with immediate effect, but must still report on their selected portfolio alignment metric in their TCFD report for the scheme year which has just ended, unless the relevant assets on the scheme year end date were zero trustees of an authorised scheme which ceases to be authorised after 1 October 2022 (a “formerly authorised scheme”) and which had relevant assets of less than £500 million on the scheme year end date immediately preceding the scheme year in which authorisation ceased, will cease to be subject to the requirements to select, calculate and report on a portfolio alignment metric with immediate effect trustees of a formerly authorised scheme which has relevant assets of less than £500 million on a scheme year end date after authorisation ceased, will cease to be subject to the requirements to select and calculate a portfolio alignment metric with immediate effect, but must still report on their selected portfolio alignment metric in their TCFD report for the scheme year which has just ended, unless the relevant assets on the scheme year end date were zero

## Do you agree with these policy proposals?

Our understanding of the implications of the proposals are that the requirement for the 4th (portfolio alignment) metric would apply to authorised master trusts and corporate schemes with effect from the scheme year which is underway on 1 October 2022.

Whilst this is a relatively rapid introduction, in practice it means that the earliest date on which schemes might need to report a portfolio warming metric is 31 July 2023, for schemes with a scheme year cycle of 1 January to 31 December. Given the urgency of action on climate change risk, and the flexibility in the initial range of portfolio warming metrics, we support this proposal in principle.

Given the number of savers, schemes and assets at risk of climate change in corporate schemes with between £1bn and £5bn, we believe they should be brought into scope at the same time as larger schemes.

If DWP were to limit the first year’s reporting to a binary measure only, in line with our response to Q1, then we support the timing as drafted.

If however DWP were keen to proceed with including more complex measures such as benchmark divergence or implied temperature rise, we suggest that – given the volume of other compliance activity to which pension schemes are currently exposed – schemes might be given longer in the first year of application to calculate their portfolio alignment metric.

Such schemes might be permitted in the first year to use some or all of the time after year end before the reporting deadline to carry out calculation and analysis. This would still mean disclosures take place to the same timescales – within 7 months of scheme year end – but gives schemes slightly more time to get the process right. This might also be especially helpful where schemes are undertaking procurement of service providers to carry out the analysis on their behalf through a public tendering process.

## Q3. We propose to incorporate the requirements to measure and report a portfolio-alignment metric into the existing Climate Change Governance and Reporting Regulations so that the requirements are subject to the same disclosure and enforcement provisions as the other metrics requirements. Do you agree with this policy proposal?

We agree that this metric should form part of the same TCFD report. There are already a number of existing disclosure requirements for schemes, including the Statement of Investment Principles (SIP), Chair’s Statement, SIP implementation report and TCFD report, in addition to voluntary disclosures such as those required of the PRI and the FRC Stewardship code.

As with the Sustainability Disclosure Requirements announced in October, it would be confusing for regulators, trustee bodies, civil society bodies and engaged members alike to mandate a new report. We support new disclosure requirements being merged into existing disclosure duties, and we would welcome a Government commitment to review sustainable investment reporting requirements in the round in 2023 to identify duplication and unnecessary complexity which can be stripped out, whilst maintaining a strong and effective overall regime.

We agree with the other disclosure requirements, and we agree that the penalty regime should be the same for the rest of TCFD. However, given the lack of standardisation and significant variation in tools and data availability, we would welcome greater clarity on how this metric will be considered by TPR in the penalty regime.

## Q4. (a) Do you have any comments on the draft amendments to the Regulations?

We have no comments – other than our comments on the definition of a portfolio alignment metric, which we cover in our answer to 4(b)

## (b) Do you have any comments on the draft amendments to the statutory guidance? Please include in your answer any comments you have on whether you consider that they meet the policy intent stated in this chapter. We particularly welcome comments on the definition of a portfolio alignment metric and whether respondents think it reflects the policy intent?

We are in broad agreement with the draft definition in regulations of “a metric which gives the alignment of the scheme’s assets with the climate change goal of limiting the increase in the global average temperature to 1.5 degrees Celsius above pre-industrial levels”. A concern, if the definition were to be loosened to allow alignment with say “well below 2 degrees” or “2 degrees”, is that disclosures become still less consistent. Even with the same methodology an engaged stakeholder or saver is going to struggle to make effective comparisons between 3 schemes, one of which reports 10% of their portfolio being aligned with 1.5 degrees, a second reporting 15% aligned with well below 2 degrees, and a third reporting 20% aligned with 2 degrees.

As with our response to Q1, we would encourage DWP to keep the definition under review and update it as appropriate in the light of any new international agreements, changing understanding of the science, and the transparency, standardisation and robustness of the models available.

We agree with most of the statutory guidance.

However, on paragraph 161 we suggest strengthening this.

Where currently the text reads “Trustees should, where possible, choose a tool which includes consideration of Scope 3 emissions for sectors where these are significant”, this might be strengthened to read “trustees should choose a tool which includes consideration of Scope 3 emissions in relation to all sectors for which these are significant”.

The caveat of “where possible” is unnecessary, because this is only an expectation in statutory guidance, so the scheme can take a different approach if they can justify it – and the legislative requirement is “as far as they are able”. The second change is suggested to make clear that it is the developers of the tool’s judgment as to whether the scope 3 emissions for a given sector are significant, rather than whether the scope 3 emissions are significant for the scheme. We believe scope 3 emissions will be significant for all schemes, although the level of significance will depend on sector and asset allocations.

We would be grateful for confirmation of our interpretation of paragraphs 162-164. If DWP is minded to permit a benchmark divergence measure, we or other schemes may wish to present our portfolio alignment at a sectoral level by showing the proportion of our holdings in a given sector which are aligned with 1.5 degrees, with 2 degrees or below, with between 2 and 3 degrees and so on.

It is not clear that the guidance permits this – however, we believe such reporting gives savers more granular and meaningful information than a portfolio-wide aggregated benchmark divergence or implied temperature rise number. It also helps knit the reported climate risk measures together with the trustees’ stewardship activities and reporting, by identifying the firms on whom to focus engagement and voting efforts, and providing a framework for reporting this. If it’s DWP’s view to permit this approach, it may be helpful to amend paragraph 162 to indicate that there is not an expectation that trustees must report a single metric for each category, and that they may instead report the proportions of their portfolio meeting a range of alignment thresholds (for example, 1.5oC or below, above 1.5 but below 2, 2 to 3, and above 3), as long as this is clearly explained.

If DWP permits a range of metrics, we would suggest – perhaps in paragraph 174, or elsewhere – that schemes are expected to state what methodology they have used to calculate their portfolio warming metric, to discourage false comparisons between schemes, or between sections within schemes.

We suggest that statutory guidance also encourages or expects schemes to set out the percentage of the assets in each section (or, if the reporting is by asset class, sector, geography or on some other characteristic, for each characteristic), on which the scheme is reporting.

We would suggest that useful additions to the statutory guidance on metrics might re-emphasise the desirability of managing climate change as a systemic risk as well as a portfolio risk – for example, by saying something like the following after paragraph 117 or paragraph 118.

In their use of metrics to “identify and assess the climate-related risks and opportunities which are relevant to the scheme”, trustees should however recognise that climate risks are systemic and cannot necessarily be diversified away through asset allocation decisions alone.

It would also be useful to remind trustees via the statutory guidance or perhaps DWP’s consultation response that they can set targets in relation to portfolio alignment metrics as well as total emissions, emissions intensity and additional climate metrics.

Finally – again if DWP continues to permit a range of measures - it would be helpful if this message to reassure schemes that there is no expectation of “progressing” to more complex measures is also mentioned in the statutory guidance itself. This reassurance in the consultation could perhaps be usefully re-iterated in the statutory guidance by redeploying some of the text from paragraph 37 of chapter 1 of the main consultation.

As an aside, we would note that the paragraph between paragraphs 156 and 157 is unnumbered.

## Q5. Do you have any comments on the new regulatory burdens to business and benefits of requiring schemes to measure and report their Paris alignment?

The regulatory burdens will depend on the type of approach taken. Our initial view is that Nest could do an analysis of the percentage of its holdings with a Science-Based Target, or the percentage of holdings with different degrees of Paris alignment under TPI, which would be done in-house, and take only a few hours. However, we would note again the limitations in coverage and the impact on building a comprehensive understanding of whether the scheme is “Paris-aligned”.

If, however there was an expectation that schemes should develop an ITR, or calculate a benchmark divergence figure in relation to a much wider range of firms than allowed by TPI, this would take up considerably more time and incur significant costs. As mentioned in our response to Q1, Nest recently issued a request for proposal on portfolio alignment metrics and were quoted costs in the region of £10K-£30K. Where schemes purchase proprietary ITR or benchmark divergence measures through their consultants, there is the possibility – as with scenario analysis – that data providers will charge consultants licensing fees for the output of the models, and these fees will in turn be passed to pension schemes and ultimately savers.

Subject to DWP being very clear that this is not the expectation however, we believe that DWP’s estimation of the burdens is broadly accurate.

## Q6. Do you have (a) any comments on the impact of our proposals on protected groups and/or how any negative effects may be mitigated? (b) any evidence on existing provision made by trustees in response to requests for information in alternative accessible formats? (c) any other comments about any of our proposals?

We have no comments.

# Chapter 2 – Stewardship and the Implementation Statement

## Q7. Should DWP include a vote reporting template in its implementation statement guidance which trustees are expected to use? If so, should such a template be based on the PLSA’s vote reporting template? What changes, if any, would be needed to the PLSA template if it were to be adopted?

## What are your views on the adoption of an engagement reporting template? Should it be separate from any vote reporting template or integrated with it, so that – in relation to equities – both voting and engagement activities are described for the same set of assets?

Whilst Nest does not use the PLSA vote reporting template or the ICSWG engagement reporting template specifically, we set our own requirements and already include a lot of what those templates promote in our stewardship practices and engagement with fund managers. We do this with the help of our service provider Minerva Analytics, which provides us with comprehensive analysis of our managers’ voting policies and decisions for each AGM period.

We are supportive of efforts to standardise data collection where this is mutually agreed between pension scheme and asset manager, but one form of reporting should not be imposed on pension schemes by their service providers. They should be free to agree their own reporting requirements that are appropriate for their approach. Trustees should not be expected by DWP statutory guidance to use either reporting template on a “comply or explain” basis.

Rather, we agree with the principle and recommendation set out in the Taskforce on Pension Scheme Voting Implementation’s report of September, which indicated that “asset managers and their trade bodies should sign up to the principle of answering all reasonable requests on their voting and stewardship activity. They should not work on the basis that reporting via the PLSA template, abiding by the Stewardship Code and compliance with FCA rules will be sufficient. They should be willing to provide answers to all reasonable requests from clients”.

It would be very helpful if any endorsement by DWP of one or more reporting templates took place alongside the reiteration of that principle.

## Q8. Do you have any comments on our cross-cutting proposals for the draft Guidance on Statements of Investment Principles and Implementation Statements, in particular that:

## (a) they are written for members?

We agree with the principle that these documents should be written for reasonably engaged and informed members, and we already do so.

Nest has not found it problematic to write a SIP Implementation Statement which both demonstrates compliance and is *understandable* to this sub-group of the membership. However, it is rarely possible to make the SIP as *engaging* as we might like, and Nest typically uses its [Responsible Investment Reports](https://www.nestpensions.org.uk/schemeweb/nest/aboutnest/investment-approach/responsible-investment/responsible-investment-reports.html) in preference to statutory disclosures to communicate with our savers, as well as other interested customers (such as employers and their advisers) and stakeholders. This does tend to create a doubling of effort for conscientious schemes which are required to do everything twice – once for statute and once for usefulness. We appreciate the challenges for DWP in producing legislation for a wide range of schemes with different levels of buy-in to responsible investment, but we would welcome further discussion over how current and future legislative requirements might be reshaped to allow well-governed schemes to communicate in a way which works for savers whilst also meeting statutory requirements.

We would also highlight a potential mismatch between DWP policy objectives here and the perceived effect of the regulations more widely. The Annual report and Accounts (ARA), of which the Implementation Statement forms a part is not required to be written for members.

## (b) these are trustees’ statements, not their consultants’?

We strongly agree with this proposal. Schemes should have ownership and control over the content of their SIP not their consultant.

A clear expectation of trustee ownership is helpful in giving scheme governance bodies more confidence to tailor their SIP to their actual investment beliefs and practices.

## (c) Implementation Statements should set out how the approach taken was in savers’ interests?

We agree with this proposal in principle. If an Implementation Statement is to be written with members as one key audience, it is reasonable to expect that the text will make efforts to explain why the approach was appropriate for the membership.

DWP may however wish to consider setting out their expectation in relation to how and when this and other changes are made. Regulation 2(1) of the Investment regulations sets out a triennial review cycle, and regulation 2(2) of the Investment regulations imposes a requirement on single employer schemes to consult with their sponsoring employer, and to “obtain and consider the written advice of a person who is reasonably believed by the trustees to be qualified… and to have the appropriate knowledge and experience”.

It might be the case that where the expectation is for all schemes to update their SIP to embed these principles immediately it could cause a capacity crunch for schemes and their advisers, or result in more boilerplate text from hurried implementation. On the other hand, encouraging schemes to only consider this guidance at the next review point may not lead to changes quickly enough. It may be that some changes – for example on voting – are seen as more urgent; whereas others, such as the explanation of how saver interests had been met, could be fulfilled at a later date if schemes were compliant in other respects.

## (d) trustees should be able to include material from voluntary disclosures, such as Stewardship Code reporting, as long as they meet the requirements in the Regulations?

We strongly support the principle of being able to re-use material from voluntary disclosures.

We believe it would also be helpful for DWP to set out publicly that it is permissible to combine voluntary and statutory disclosures into a single document – so for example, a scheme can produce a single report which meets statutory duties in relation to implementation statements whilst also serving as their Stewardship Code report.

We believe that this is permitted because trustees are free to include or annex other information in their annual report and accounts. As per our response under (a), whilst the annual report and accounts must have existence as a single document, in line with regulation 12 of the Disclosure regulations, mandatory for-publication sections of the report and accounts can be published in whatever form the trustees see fit.

## Q9. (a) Do you have any comments on our proposed Guidance on stewardship policies?

We agree with the broad thrust of these recommendations as best practice. However, there are some places where there is a slight uncertainty about the Department’s proposals, and other parts of the guidance which are more focused on good practice in stewardship itself, rather than stewardship policies, and the movement between the two might cause some confusion.

It would be helpful if paragraph 30 could make clear that DWP specifically encourages trustees to summarise their stewardship priorities. It may be preferable to set the expectation that trustees should both summarise their priorities *and* provide links to their managers’ policies, and that this should be “if applicable”, rather than simply “if available”. For example, a scheme may have its own policies which it uses in preference to its managers’.

We would also suggest that these priorities are set out in a document outside but referenced from the SIP, but explicitly outside the requirement to consult with employers, consultants or others. For reasons set out in our answer to Q8(c), including content in the SIP which then needs to be updated more frequently than every 3 years could involve needless expense which would discourage schemes from keeping their priorities up-to-date.

It would be helpful if the guidance made explicit that the stewardship priorities encompassed both voting and engagement.

Whilst Nest would have no such issues with the current proposals it may also make sense for DWP to consider some kind of *de minimis* in relation to the extent to which schemes should link to or reproduce managers’ voting policies in relation to small sections of the scheme.

For examples, trustees might be encouraged to report on the stewardship policies in relation to any individual fund which made up more than 5% of the scheme’s assets, or for the funds which collectively account for – say – 75% of the scheme’s assets.

The guidance in this section is helpful, but a clearer delineation between regulatory requirements (paras 27, part of para 28, 29, and 38), best practice contents for the SIP (the rest of para 28, 30-34 and possibly para 44) plus wider stewardship best practice (paras 35-37, 39-43) would be welcome.

## (b) Do you have any comments on our proposed Guidance on significant votes?

We agree with the guidance on significant votes. We also provide a response on the other guidance relating to the implementation statement.

In para 47, we suggest it is made clear that the engagement objectives relate to the past year. If for example the scheme has set longer-term engagement objectives, we would expect these to overlap with the stewardship priorities detailed in the previous section of the guidance which the draft guidance encourages schemes to include in the SIP. Requiring schemes to set out their long-term engagement priorities again via the annual report feels like unhelpful duplication. It may also be helpful for the trustees to set out any escalation they undertook with their own asset managers, given the point in paragraph 29.

We have some caution over paragraph 50. Voting statistics will be broken down differently by different managers, making it harder for schemes with more limited resources to aggregate consistently by theme. Whilst we can see that this information is helpful for savers, it may be helpful to frame this more flexibly, for example, by making explicit that more detailed breakdowns are encouraged rather than expected, and suggesting that this is done for the largest funds – again, perhaps those accounting for more than 5% of the assets, or those which in total account for more than 75%.

We would question the practicalities of the approach referred to in the first sentence of para 53. In practice a scheme will compile all information it has been able to obtain at the time the annual report and accounts is finalised. It feels disproportionate to set an expectation that the scheme should go back and update the information later, when in all likelihood this is a consequence of long lead times in fund manager reporting.

We instead suggest that paragraph 54 may set the expectation that where the asset manager is unable to give the trustees timely information on voting, that the trustee should highlight this in their implementation report.

## Q10. Do you have any comments on our proposed Statutory Guidance on the information to be included in the Implementation Statement with regard the requirements under the Disclosure Regulations, Schedule 3, paragraph 30(f)(i)-(iv)?

We agree with this proposal, although we would note that the question contains an error. It should refer to paragraph 30(f)(ii)-(iv).

## Q11. Do you have any comments on our proposed Statutory Guidance on meeting the Implementation Statement requirements in the Disclosure Regulations relating to choosing investments?

We agree with this proposal.

## Q12. Do you have any comments on our proposed Guidance on meeting requirements in the Investment Regulations and Disclosure Regulations relating to investment strategy?

We agree with the proposals in relation to the SIP.

In relation to the IS, we agree with the policy intention here – although see below – and the clarification of DWP’s expectation is helpful. However, we would note that the expectation in paragraph 80 to “state whether these policies have been adhered to and, where this is not the case, the reasons why not, including explaining what action, if any, the trustees propose to take or have taken to remedy the position” appears to duplicate an existing regulatory requirement in paragraph 30(1)(b) of Schedule 3 to the Disclosure regulations. This provision (referred to in the preceding section on choosing investments) sets out that “where investments for the scheme have been made in the year that do not accord with the statement of investment principles governing decisions about investments required under section 35 of the 1995 Act (or were made in a previous year and continued to be held at the end of the year), a statement by the trustees or the fund manager giving the reasons why and explaining what action, if any, it is proposed to take or has already been taken to remedy the position.”

We would welcome clarification as to whether the expectation in statutory guidance could be met by publicly reporting the disclosure in paragraph 30(1)(b), and if not, why not.

However, we would go further and suggest a more rounded view may be taken for the purposes of an implementation statement which seeks to explain how and the extent to which the policy is followed. This would be to look at the outcome of the scheme’s investment policy rather than to merely report that it had been complied with. This more holistic view could be achieved by encouraging schemes to publish the investment report mandated by paragraph 30(1)(c) of Schedule 3 to the Disclosure regulations, which encompasses a review of the investment performance of the scheme's fund during the year, and over 3-5 years, including an assessment of the nature, disposition, marketability, security and valuation of the scheme's assets. The performance, nature, disposition, marketability, security and valuation would seem to map fairly well to the requirements set out in paragraphs (i) to (v) of regulation 2(3)(b) of the Investment regulations.

Finally, we would briefly note that the paragraph after paragraph 79 is unnumbered, and the single bulleted list which follows may be a formatting error.

## Q13. Do you have any comments on our proposed Guidance on meeting requirements in the Investment Regulations and Disclosure Regulations relating to financially material considerations (including ESG and climate change)?

We agree with the proposal that the SIP should explain the trustees’ investment beliefs. Nest already does this, and we believe it provides useful context for the SIP itself, and useful context as to how the scheme consider the ways in which financial markets operate.

In relation to the other suggested best practice in the SIP, we suggest that DWP may wish to consider clarifying whether their proposal is that trustees describe this process “in the round”, or if that is not the intention, to limit the proposals to the asset managers responsible for the majority of their assets or similar. We would prefer to see a proposal of the former.

As set out in our answer to Q9(a), even as a 10-year old scheme with relatively few self-select fund choices, Nest has arrangements with 15 different fund managers, and 24 underlying fund building blocks. As assets under management grow, we expect the number of managers and fund building blocks to also grow. Whilst our reporting duties under this guidance would be manageable, it would perhaps be unhelpful if trustees of less well-resourced schemes were to interpret the best practice as meaning they needed to spell out the precise tendering and monitoring practices in relation to each fund. They might well vary for good reasons, including the asset class and the strategy in question and whether the fund made up a larger or smaller part of the portfolio.

We agree with the proposals in relation to the Implementation Statement.

## Q14. Do you have any comments on our proposed Guidance on meeting requirements in the Investment Regulations and Disclosure Regulations relating to non-financial matters?

In relation to paragraphs 92 and 93, it is unclear whether it is being suggested that it is best practice guidance to include details of this member feedback mechanism in the SIP. We would suggest that guidance might encourage schemes to summarise the arrangements, but to do so briefly.

We agree with the proposals in relations to the implementation statement, in paragraphs 96 and 97. Whilst Nest does not have a policy of acting on non-financial factors expressed by savers in our default fund, we believe that where schemes claim to do so, there should be an expectation of reporting what they actually did as a result.

## Q15. Do you have any comments on our proposed Guidance on meeting requirements in the Investment Regulations and Disclosure Regulations relating to arrangements with asset managers?

We would highlight that regulation 2(3)(d) of the investment regulations, on arrangements with asset managers, is somewhat unclear in relation to expectations of what a good policy ought to look like. Given the lack of public statements on these additions to the regulations, these are areas where further guidance, or indeed in due course simplification of the regulatory requirement may usefully be considered.

It is unclear, where the draft guidance states “The details of the portfolio turnover costs in relation to the main sections and popular defaults can be given via a link to the Chair’s Statement” whether the expectation is that trustees should include this, or whether, in common with the rest of the paragraph, this is something trustees may choose to do. We would support the latter.

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1. https://sciencebasedtargets.org/wp-content/uploads/2019/03/SBTi-criteria.pdf [↑](#footnote-ref-1)