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Governance of Sustainability Dialogue - *From Climate Change to Social Change*

23-24 June 2021
Hosted by UNCTAD World Investment Forum

Plenary 5: Investor Duties and Sustainability Related Disclosure

- Anne-Marie Jourdan, Chief Legal Officer, Fonds de Reserve Pour Les Retraites, France
- Wim Bartels, Co-Chair, Impact Measurement, Reporting & Assurance Services, KPMG IMPACT & Partner, KPMG, Netherlands
- Takeo Omori, Responsible Investment Group, Asset Management One Co., Ltd., Japan
- Paul Lee, Head of Stewardship & Sustainable Investment Strategy, Redington, UK
- Chair, Bastian Buck, Chief of Standards, GRI, Netherlands

Bastian Buck:
This panel was designed to bring different global, national, and regional perspectives on the current status of sustainability related disclosure expectations and what the future holds. We're joined by Takeo Omori from Asset Management One, Japan, Anne-Marie Jourdan, of Fonds de Reserves Pour Les Retraites, France, Paul Lee, from Redington, and Wim Bartels, Co-Chair, IMPACT Measurement, Reporting & Assurance Services, KPMG, and Partner of KPMG in Netherlands.

The panellists will give their perspectives, focused on their own roles. Takeo, what is the Japanese perspective?

Takeo Omori:
We are one of the leading Asset Managers in Japan, with around US$510 billion in AUM. Regarding climate related disclosure by Japanese companies, Japan has the largest number of TCFD supporters worldwide. The most recent TCFD status report confirms 310 supporting companies, compared to 219 in UK and US. European countries have the highest disclosure rate of all 11 items in TCFD, with Asia-Pacific

second in eight of 11. Asia-Pacific is the largest region, with most support from Japanese companies.

Engagement of Asset Managers is a reason for this. They're encouraged to support TCFD, initially, before moving forward. The TCFD Consortium is a unique initiative incorporating various industries, companies and financial institutions, e.g., Asset Managers, big banks, academia and government agencies, like METI. Asset Management One is a member of the Steering Committee.

TCFD disclosure is a good framework, with some implementation difficulties. The consortium is useful for investee companies and investors to collaborate and share concerns. Based on their discussion, we published guidance for investee companies and investors.

A worldwide initiative aiming to achieve Net Zero GHG emissions by 2050, Net Zero Asset Managers Initiative, was launched in December 2020. Asset Management One was the only Japanese Asset Manager to join at launch. A further 30 joined globally, with 57 more added in January, totalling 87, representing US$37 trillion in AUM, around 40% of total global AUM. As one of six members of the Advisory Group, I work closely with the Steering Committee and other Asset Managers.
The commitment of the initiative includes setting interim targets before COP26, a percentage of AUM aligning with the Net Zero scenario in 2030. We need to define our portfolio, consistent with our 1.5° scenario. The Assets Managers will carefully examine the disclosure of investee companies, including GHG emissions, setting of short or midterm targets or long-term goals and decarbonisation strategies to support these targets. We then determine the investee companies aligned with the scenario.

Moving towards COP26 and beyond, we'll see huge increase in investor demand for investee companies' efforts and disclosure on climate change. It's early stages, but soon, hopefully, disclosure requirements will converge and become standardised, to some extent. We wish to play a key role in moving the world towards a Net Zero society.

Bastian Buck:
The interplay between investee companies and institutions like yours in driving climate disclosure and availability of information is very interesting. The Japanese Corporate Governance Code was revised recently and is recommended. Will this give a further push to Japanese disclosure?

Takeo Omori:
It was revised this month, to say companies should disclose climate-related information, based on TCFD recommendation. Solely for companies listed on the Prime Market, the top tier. Tokyo Stock Exchange is restructuring into three new markets in April 2022, with companies required to comply with a new Corporate Governance Code to remain in the top tier. It isn't mandatory, but FSA officials state comply or explain is mandatory in Japan, so this code should have a significant impact there.

Bastian Buck:
It's a development we'll see in other countries, as well. For a Continental European, and specifically French, perspective, Anne-Marie, what is your view on developments and your outlook in this area?

Anne-Marie Jourdan:
In 2015 France had a regulatory framework for extra financial transparency for investors, particularly on climate. Article 173 of the Energy Transition Law for Green Growth already required systematic publication of procedures for integrating ESG criteria in investment policies and risk management procedures, whilst encouraging integrating climatic risk.

France's Experience with Application Report, published in June 2019, strongly influenced the European system, including disclosure regulation, a pillar of the development of European Sustainable Finance. Article 29 of the Energy Climate Law of 8th November 2019 fits into this context, articulating French and European requirements with a triple objective: retain and clarify the provision resulting from Article 173, strengthen this to meet Energy Climate Law requirements, with emphasis on publication of risk linked to climate change and biodiversity erosion, learned from more than five years' extra financial reporting experience, particularly with clear structure of information published on TCFD disclosure pillars on strategy, governance, risk management and use of specific metrics and targets. Following this, a decree was published on 28th May 2021 for application of this law, providing institutional investors with more readable and operational text than Article 173.

Improving companies' extra-financial reporting, especially available data quality, is an important challenge for better integrating biodiversity into strategy investment. This is new; in Article 173 we are not focused on biodiversity. The decree covers risk from biodiversity erosion and the alignment strategy with international objectives of preserving biodiversity. Institutions and Asset Managers must integrate into analysis the main impact on biodiversity, negative investment policy.

The publication of Strategy for Aligning Portfolio with International Long-term Biodiversity Conservation Objectives, by the financial institution, seems particularly important. The decree requests details on scope of the value chain selected, measurement of alignment with objectives of current International Treaty of the Convention of Biological Diversity, analysis of the contribution to reduction of main pressures and impacts on biodiversity, mention of support for a biodiversity footprint indicator and, if applicable, how it measures alignment with international objectives relating to biodiversity, and request for a specific publication on risks associated with biodiversity. It's not easy to read, with much for investors to take into account.
The French Reserve Fund has not submitted to Article 173, but has continued to incorporate these measures since 2001.

Bastian Buck:
It's interesting that scope of sustainability or ESG consideration has widened through regulatory initiatives, and French legislation will lead the way for European, but also global, ambitions. Biodiversity is described as the next high profile ESG or

sustainability issue. Maybe in the future, many more issues will be looked at with the same rigour we aspire to today for climate. How do you confront the sustainability obligations at the French Reserve Fund? What do you consider?

Anne-Marie Jourdan:
It's a long story. The fund was created in 2001. The French Parliament incorporated rules requiring the fund's general investment policy orientation to take into account social, environment and ethical considerations. Since then, we've tried to implement this commitment, as a responsible investor, by formalised five-year ESG strategies, characterised by growing ambitions in responsibility and desire to progress and support progress of players in our ecosystem: management companies, index providers, non-financial analysis providers. We combined these principles, created general principles, concrete objectives, which the Management Board present to the fund's Supervisory Board for approval. We have a Responsible Investment Committee from the Supervisory Board, overseeing guideline implementation, defined by the board and Extra-Financial Committee.

Our strategy has two pillars: protect our reputation by exclusions in accordance with international agreements, e.g., anti-personnel mines, cluster bombs, tobacco and coal exclusion in 10% of companies, and restricted investment in securities under serious allegation. The second is protecting the value of investments by assessing and considering potential risk of loss of value linked to current and future cost of non-exemplary management of companies: environment, social and governance.

We sign different initiatives, the last, in 2019, being the Net Zero Asset Owner Alliance. We work closely and delegate the management of assets to Asset Managers. Management mandates, after a strong selection process, giving increasing place to ESG, require Managers to take into account ESG investment strategy, particularly in indices of voting rights dialogue. As we join the NZAOA, we'll shortly publish interim targets, having already put reduction objectives to achieve carbon neutrality in our last RFP in credit sure bonds. We also launched RFP on indexes replication linked to the Paris Agreement, with objectives to achieve carbon neutrality.

Bastian Buck:
It's great that ESG or sustainability considerations are systemically part of your institution and work with Asset Managers. Paul, in context of our colleagues' contributions, what is the UK position?

Paul Lee:
The UK has two developments worth highlighting, steps forward in demands and requirements on asset owners, particularly pension funds, which are impacting through the investment chain, and potentially, corporate.

Implementation statements are about implementation of the Pension Scheme Statement of Investment Principles (SIP). Under new regulations, this must encompass discussion of ESG considerations of schemes, with particular specification to include considerations of climate change. A statement must be made, the implementation statement being a new requirement, to be implemented over the next year, requiring pension schemes to explain their implementation of the SIP, including ESG.

The SIP must focus on how the scheme is effective in delivering its key aims and what it's delivered and changed over the reporting period. DC pensions should be across the whole SIP, DB pensions require only disclosures around voting and engagement. Hopefully, DBs will report more broadly, which many are, but DB focus on voting and engagement tends to mean focus of implementation statement discussions have been on the voting and engagement side. Most debate is on voting, because of tension between asset owners and Fund Managers on the implications of requirements. The implication statement expects disclosure of most significant votes, which is not defined, but should scheme focused and less broad.

Many Fund Managers have difficulty meeting the challenge of the new requirement, not recognising asset owners' requests are driven by the regulatory disclosure requirements they face. Focus on voting is, unfortunately, leading to neglect of reporting on engagement, or considerations of reporting, much less reporting on SIP delivery, more generally. Fund Manager and asset owner tension is interesting, with one element of the statement expected to be asset owners explaining how they held Fund Managers, and other advisors or providers, to account for delivery. We all must move forward on this.

Some asset owners regard this as a compliance matter. Hopefully, most will see the opportunity for communication. We must invite interest of scheme members and beneficiaries, and responsible investment, sustainability, is a great way to engage individuals in the investment process. It's alien to most people, but ESG is about relating investment to real-world impacts and communicating on this will engage people much more.

The 2020 Stewardship Code, which was published at end of 2019, is an update of the existing UK Stewardship Code. The first reports have recently been submitted to the FRC, the Code's regulator, which are the 2020 calendar year activities. FRC is reviewing those over the summer and a statement will be made in early autumn to announce who reached the threshold, qualifying as a signatory of the new Code.

The new Code is interesting, a major step forward. Signatories were previously simply required to explain their stewardship policy. It's no longer enough to express policy or say what the scheme has done on stewardship, but all signatories must explain outcomes, what's been delivered through the work. Outcome is mentioned more than 30 times in the Code. It's requires practical delivery and changing companies' processes.

The Code is not just strictly discussing engagement and stewardship, it's very broad. One principle is on voting, three on engagement and eight covering the organisation's philosophy, approach and mindset towards ESG, generally, with a substantial principle on ESG integration in the investment process. 40 asset owners sought to sign to it, initially, which is more than I expected. We'll see what happens.

Bastian Buck:
These types of developments in UK inform international debates. Do you think the UK will lead the way with this Stewardship Code?

Paul Lee:
Geopolitically, the UK is leading less than previously. Specifically with the Code, hopefully, but it will probably be slower. The new Code is very demanding, going much further than the preceding Code. Other nations may be slow in moving towards this mindset. The Japanese code is the one I'm aware of having been updated since ours and Japan makes only one discreet mention of outcome.

Bastian Buck:
A perfect indicator for progress, counting the number of mentions of outcome in codes. Wim, you've been asked to reflect on global status quo and developments, linking into sustainability related disclosure for Asset Managers and owners, and corporate reporting.

Wim Bartels:
I'll discuss what is happening globally in terms of regulations and initiatives, the quality of disclosures and what it means for asset owners and Asset Managers. Internationally, we see significant development towards further convergence, especially the IFRS Foundation initiative, which brings together at least five current non-financial reporting frameworks into standardised disclosures. Simultaneously, the EU are developing an updated Sustainability Reporting Directive and further standards in 2022 and 2023. In the US, the SEC is exploring climate related disclosures. The Chinese Government recently mandated listed companies report on ESG.

SEC and IFRS have particular perspective on investors. I'm a member of TCFD and we welcome our voluntary initiative being translated and incorporated into a mandatory regulation, which is also happening in UK. The EU will follow, with IFRS tackling climate change and climate risk, initially.

This is all welcomed, but sustainability is much more than climate, so, importantly, the IFRS is asked to explore the wider ESG agenda and set it fairly quickly. We tend to focus on risk, driven by TCFD, but we mustn't forget impact. A concern is the focus of the next two years is financial risk from climate change, and subsequently, from ESG, and we may forget the impact companies have, and Asset Managers and owners have in their investment chain. Bastian, the GRI standards focus on companies' impacts on environment. Concentrating only on climate change, what we saw as impact only, is now a financial risk, which applies to many more sustainability developments, including social.
The convergence drive is critical. Asset Managers and owners will be helped with standardisation, starting with corporates, then used by Asset Managers and owners for portfolio reporting.

A couple of points require attention in relation to current Asset Manager and owner disclosures. There's, understandably, a heavy focus on carbon emissions with climate change and climate risk. We have data for it, but the risk is much more than carbon emissions and we need a shift in focus in risk analysis and portfolio impact. When setting Net Zero targets, we need underlying plans on how to achieve them. EU requirements include due diligence, looking at adverse impacts in investment chains. It's difficult, but it's an area needing attention.

Investors shouldn't wait for the regulation. IFRS is moving at a high pace. They can't set standards in four months. They must take due process, which takes over a year for each standard. Investors should look into impacts and think of impacts in investment chains and pilot models assessing impacts. Don't wait for corporates, model the impacts, it provides relevant insights.

Conduct a sector analysis for risk. Many Asset Managers are doing exclusion, but ESG is more than climate and exclusion. Examine sector characteristics and requirements. Due diligence is critical for Asset Managers and owners. From my experience with Dutch insurance companies/asset owners, this is an area to work on.

Bastian Buck:
Is it premature to ask investors to communicate and integrate information not available at company level? This relates to biodiversity but could be extrapolated to other issues. Wim has alluded to a requirement for action, notwithstanding some information not being available. What do others feel, in view of regulators formulating expectations?

Anne-Marie Jourdan:
When the French Government published Article 173, there was no data or methodology. Giving this requirement to Asset Managers and owners progresses the search for tools. There are now some tools and databases able to provide biodiversity indicators: the Biodiversity Impact Analytics, the Global Biodiversity Score for Financial Institutions, the Corporate Biodiversity Footprint, the Biodiversity Footprint for Financial Institutions. Several works are in progress in many European countries. Central Bank is working on this.
In France, we need laws to implement things. We have the law and must progress. The Asset Managers and owners must work with data providers and companies to obtain the information.

Paul Lee:
I'd hope we didn't need laws or too much detailed definition of disclosure requirements. We can start to pull things through the system by demand and expectations placed on companies by the investment chain. Some issues are ill-defined. Currently, it's difficult to define precise measures and metrics required, but more information is needed. Companies must work on ways of disclosing more to help us understand their footprint and impact. Ultimately, metrics will be clearer and more consistent, but we must start the process to progress.

Wim Bartels:
Agreed. When you start modelling, you realise not only the information you have, but what you don't have. It drives you to ask your investees if they could provide that

missing information. This won't happen within a year, but starting the conversation will drive the quality apart from regulation.

Many companies initially require indicators and assessment of materiality, which is important, but look at adverse impacts in your sector, which can be identified very easily and quickly if you understand your business, using a common sense approach. In agriculture we have an impact on biodiversity, water and potentially social circumstances, three key adverse impacts. What must we know to inform our stakeholders of our actions in this space? Water diversity, what are the social circumstances? Find indicators and start modelling. It starts conversation with companies.

Bastian Buck:
For years, GRI has invited Asset Managers and owners to take corporate disclosure at face value. If there's no disclosure on biodiversity, there's probably very little structured action in that particular corporate on biodiversity. If there is initiative and policy implemented, corporates will talk about it. It's sobering to look at high profile issues of public discourse and how little is disclosed. It can be a first lever for company engagement and asking how, with the prospect of agreeing a new biodiversity convention, so little is reported in a sector with very profound biodiversity impacts. A main driver for further GRI uptake is investor conversations with investor relation functions in companies. Questions are asked about impacts and SDGs, which triggers GRI type reporting.

How far do you think today's regulatory actions cater to investor needs? Are they recognised and understood in the actions described and that you foresee?

Wim Bartels:
With that, we get at least standardised information and, generally, investors like standardisation for modelling. I hesitate, because the question is whether it addresses the real needs of the investors. It provides standardised information, but does it provide the real understanding of the topics? I'm concerned with standardising everything and putting it into an indicator. With TCFD, a level of standardisation has helped to better understand the climate risk topic. As a step, it helps, and IFRS is listening to the investors, so it should address those needs.

Anne-Marie Jourdan:
Article 173 was very vague, and investors had to determine how to answer requirements. After five years, the regulator added clearer investor guidance, because analysis of results revealed that some investors had 100 pages and some three. To compare investors and what they've done, regulators must provide clear guidance.

Paul Lee:
That's true, but we need to take responsibility. If we're involved in regulatory processes, we can ensure they deliver what we need. We shouldn't create new regulatory processes for the sake of it. Regarding Climate Accounting Recommendations under IFRS, we must make better use of existing regulation,

pressing companies to respond more effectively, which is more urgent than creating new regulatory frameworks. Investors must participate in processes to extrapolate the information and disclosures required.

Bastian Buck:
Could you give some guidance in terms of urgent actions for sustainability disclosure? Where would you advise colleagues to focus their attention activities, going forward?

Takeo Omori:
Achieving Net Zero is a huge challenge for everyone. Asset Managers have a role to play in encouraging companies to disclose more information.

Paul Lee:
Don't expect others to solve the problem. Investors must demand more from companies and engage in regulatory processes to shape requirements to our needs. Take on the burden and progress it ourselves.

Wim Bartels:
Look beyond climate change, take sustainability broadly and qualitatively identify adverse impacts, and disclose on that.

Anne-Marie Jourdan:
The key is integration. When we do due diligence with Asset Managers, integration is not completely achieved and sometimes Portfolio Managers aren't completely aware of ESG issues, and it's not fully integrated in their management. Asset owners have more pressure to invest in companies with ESG criteria. We will also put more pressure on our Asset Managers.