Pension Protection Fund (PPF) response to UK Stewardship Code consultation

About the PPF

The Pension Protection Fund (PPF) is a public corporation, set up by the Pensions Act 2004, and has been protecting members of eligible defined benefit (DB) pension schemes across the UK since 2005. The PPF is run by an independent Board and is accountable to Parliament through the Secretary of State for the Department for Work and Pensions. It protects close to 9 million members belonging to around 5,000 pension schemes. If an employer collapses and its DB pension scheme cannot pay members what they were promised, the PPF pays compensation for their lost pensions. The PPF is funded by a levy charged to eligible schemes, the return on its investments, assets from pension schemes transferred into the PPF, and recoveries from insolvent employers.

The PPF is one of the UK's largest asset owners with £32.1 billion of assets under management. Separate and additionally to the PPF, it also administers the Fraud Compensation Fund (FCF) and the Government's Financial Assistance Scheme (FAS). The PPF looks after over 430,000 members across the PPF and FAS.

Responsible investment is an important part of our overall strategic plan and our core investment principles and strategy.

The goal of our Responsible Investment strategy is to enhance the long-term value of our investments by managing environmental, social and governance (ESG) risks and exploiting opportunities. We are a signatory of the UK Stewardship Code ('the code').

Executive Summary

The Pension Protection Fund (PPF) warmly welcomes the opportunity to provide input to the FRC in relation to the UK's Stewardship Code. As an organisation, we recognise the value of good stewardship in relation to the investment process and have been a signatory to the Code since 2022.

The UK Stewardship Code has long-been regarded as a flagship document when considering investment stewardship globally. This consultation offers the opportunity to future-proof the Code, particularly considering the focus on alternative asset classes in the market. Below is a summary of our responses to the set questions:

Question 1 – Whilst recognising the drivers for amending the existing definition of stewardship, we would welcome further consideration of the options available. As a long-term investor, we believe that there are systemic risks in the wider economy, environment, and society which in the long term may have a direct impact on members and the financial returns we are responsible for delivering. Given this position, we consider the retention of the reference to the wider economy, environment and society are justified.

Question 2 – We are supportive of the proposed disclosure streamlining. We consider this has the potential to create a significant reduction in reporting burden, if implemented effectively.

Question 3 - We welcome the consideration of introducing 'how to report' commentary in the guidance.

Question 4 - We support the importance of recognising the distinct roles market participants have in exercising stewardship. The PPF supports the 10% threshold for applying the principles. Whilst supportive, we encourage the FRC to ensure that flexibility remains for Asset Owners to apply all principles of the code if they wish.

Question 5 - We consider the proposed structure to be an improvement. We believe that the focus on specific roles in the investment chain will lead to higher quality reporting under the relevant Principles.

Question 6 – We have not submitted a response for this question.

Question 7 - We are generally supportive of the streamlined principles. We have offered several suggestions for consideration which primarily focus on ensuring the quality of stewardship disclosed is being implemented consistently within an organisation.

Question 8 – We are supportive of the ability to cross-reference publicly available information. Cross-referencing existing publicly available external information can play a significant part in streamlining reporting, avoiding duplication, and reducing the reporting burden. However, consideration should be given to the accessibility of the documents online.

Question 9 - We have no concerns with the proposed schedule for implementation. We would suggest consideration is given to allow additional signatory engagement in the lead up to the first submissions.

Question 1: Do you support the revised definition of stewardship

Having considered the existing and proposed definitions of stewardship set out in the consultation, we would welcome further consideration of the options available in terms of an amended definition. Since inception, the UK Stewardship Code has been a guiding light for many other markets around the world. Whilst we recognise the varying definitions of stewardship adopted by markets around the world, we appreciate the leading position taken by the FRC historically and consider the removal of reference to the wider economy, environment, and society to be a softening of this position.

As a long-term investor, we believe that there are systemic risks in the wider economy, environment and society which in the long term may have a direct impact on members and the financial returns we are responsible for delivering. Given this position, we consider the retention of the reference to the wider economy, environment and society are justified.

Recognising wider sensitivities in the market in relation to the existing wording, we are supportive of the slightly amended definition noted below:

"Stewardship is the responsible allocation, management and oversight of capital, having regard to dependencies and impacts on the economy, the environment and society, to create long-term sustainable value for clients and beneficiaries."

The proposed definition aligns with director duties under Section 172 of the UK Companies Act, and offers an opportunity for clear director and investor alignment.

Question 2: Do you support the proposed approach to have disclosures related to policies and contextual information reported less frequently than annually? If yes, do you support the approach set out above?

We are supportive of the proposed disclosure streamlining. We consider this has the potential to create a significant reduction in reporting burden, if implemented effectively.

The aim of completeness in the current format of stewardship reporting has, in many cases, led to the reports becoming unwieldy for the wider user group, particularly the general public. We have seen a number of organisations producing significantly shorter, supplementary documents for wider consumption. When considering the annual actions and outcomes reporting content requirements, we encourage the FRC to make clear that the reporting is primarily designed to serve wider stakeholders' needs, rather than function as a regulatory reporting document.

We are also supportive of the planned assessment timeframe of annual activities and outcomes reports coupled with triennial policy and content disclosure. Apart from when significant changes are made during the three-year period, we believe it will be more efficient to ensure up to date links are provided in the activities and outcomes report to the policy and context disclosure on the website without having to submit the documents to the FRC. The annual submission of these documents may lead to the need for a legal and compliance review being considered appropriate, even though the FRC will not formally assess the documents. If significant changes are made during the three-year period, then the organisation should re-submit the policy and content disclosure to the FRC in the reporting cycle the changes were made. Clear description in the 'how to report' commentary can ensure organisations know when to resubmit in-cycle due to material changes.

Question 3: Do you agree that the Code should offer 'how to report' prompts, supported by further guidance?

We welcome the consideration of introducing 'how to report' commentary in the guidance. Stewardship is most effective integrated into investor's own processes and philosophy. The addition of 'how to' prompts should "encourage signatories to explain their individual approach to stewardship."

However, we consider the following points worthy of consideration:

- Investor Consultation: Given the importance of content provided in both the 'how to report' section and further guidance to be released, we believe the FRC should consider either a market consultation on guidance produced or establish external working groups to provide a practitioner's view on the draft documents.
- Additional Guidance: We also encourage the FRC to ensure that any guidance documents published maintain the level of ambition in disclosure supported by the current Stewardship Code. We do not wish to see the guidance providing a baseline level of disclosure that then

serves as an acceptable minimum. We place value on the fact that the current stewardship Code is challenging and would not like to see the devaluation of signatory status take place.

- Alternative Investments: The proposed guidance documents for other asset classes (non-listed) are particularly needed in the marketplace. We welcome future focus by the FRC on stewardship guidance in these diverse asset classes.
- One-to-one Advice: In addition to the guidance and 'how to' commentary noted, we also see value in the FRC providing feedback to signatories or potential signatories to address specific issues. Whilst we recognise the potential resource requirements of this service, it could lead to significantly better outcomes for the market, particularly where signatories are looking to innovate.

Question 4: Do you agree that the updated Code for Asset Owners and Asset Managers should have some Principles that are applied only by those who manage assets directly, and some that are only applied by those who invest through external managers?

We support the importance of recognising the distinct roles market participants have in exercising stewardship. The PPF supports the 10% threshold for applying the principles. Whilst supportive, we encourage the FRC to ensure that flexibility remains for Asset Owners to apply all principles of the code if they wish. We acknowledge that there are many Asset Owners with no internally managed assets but that manage meaningful direct engagement strategies. For those organisations, applying all guidelines should be welcomed.

There is increasing evidence available to show that some managers are not aligned with their asset owner's stewardship philosophies. We welcome developments in reporting that encourage asset owners to focus on asset owner/asset manager alignment when applicable.

Regarding duplication of case studies between an investment manager and asset owner, we consider the use of case studies from an investment manager to be an effective way of bringing the investments and work undertaken by the managers to life. Investment managers should work with asset owner clients to ensure suitable case studies are available for its specific portfolio.

Question 5: Do the Principles of the updated Code better reflect the different ways that stewardship is exercised between those who invest directly, and those who invest through third parties?

We consider the proposed structure to be an improvement. We believe that the focus on specific roles in the investment chain will lead to higher quality reporting under the relevant Principles.

We encourage the FRC to engage with the Department for Work and Pensions (DWP), given that many asset owners reporting under the stewardship code are also required to report on how they are implementing their Statement of Investment Principles (SIP) under the DWP's regulations. Harmonisation of these two reporting structures could achieve further efficiencies.

Question 6: Do you agree that the updated Service Providers' Code should have some Principles that are applied only by proxy advisors, and some that are only applied by investment consultants?

The PPF is not providing a response to this question.

Question 7: Do the streamlined Principles capture relevant activities for effective stewardship for all signatories to the Code?

We are generally supportive of the streamlined principles. Below we have highlighted areas of the proposals that we believe warrant additional consideration:

Policy and Context Disclosure:

Policy and Context Disclosure B (formerly Principle 2):

We believe the current code provisions relating to financial incentives offered by signatories should be retained. We consider it relevant whether a firm's performance management approach aligns to its stewardship aims.

Policy and Context Disclosure C (formerly Principle 5):

We would welcome the inclusion of disclosure focusing on assurance received in relation to stewardship integration and/or reporting. Whilst obtaining assurance should not be a requirement of the code, it is useful to understand where an organisation has chosen to seek additional assurance to better understand its internal commitment to stewardship. The 'how to' section of additional guidance could be a suitable place to reference this.

Policy and Context Disclosure D (formerly Principle 3):

Examples of potential conflicts of interest and how an organisation managed them in practice, supporting the description of their process for dealing with conflicts of interest, would be welcomed. The 'how to' section of additional guidance could be a suitable place to reference this.

Activities and Outcomes Report:

Principle 1 (formerly Principle 7)

We believe that there should be a clearer focus on the integration of stewardship insights into the investment process. Whilst this is clearly reflected in the title, we believe more focus could be added in the 'how to report' section. The 'how to report' section currently only asks for examples, but we believe that a full breakdown of how stewardship is integrated across all asset classes should be included, as is the case with the current code. In addition, this should go beyond explaining priorities in areas of stewardship and how this differs across assets, to also cover how the investment process (both at asset allocation and investment selection levels) utilises stewardship insights, along with variations across asset classes.

We also believe the Code would benefit from emphasising the importance of ESG factors being integrated in a systematic and repeatable manner in investment decisions, regardless of asset class. We appreciate being able to understand how material ESG factors are integrated and ultimately utilised in the investment decision process. Insights into this process would be hugely beneficial to the reader of stewardship publications to ensure that consumers of the information are not only being provided discretionary best-case reporting, which may not provide a true and fair representation of the asset managers investment process.

Principle 2 (formerly Principle 4)

Managing market-wide and systemic risks: The retention of the principle is welcomed, particularly if the wording on the benefits to the economy, society and environment is removed from the definition of stewardship. We believe that the lack of reference to public policy advocacy should be addressed, ensuing that it applies to all signatories or enables them to explain why they do not use it.

Principle 3

The PPF is supportive of the streamlined principles combining the collaborative engagement and escalation principles into an overarching engagement principle. This combination more accurately reflects the realities of stewardship, where escalation and collaboration are part of the investor's engagement toolkit, to be used fluidly. In addition, the proposal is preferred to the FRC's previous clarification that collaborative engagement and escalation need only occur and be reported on "where necessary." We believe that this risked framing both as tools of last resort. We consider it particularly important for the final principles to refer to both escalation and collaborative engagement as potential parts of an integrated stewardship approach.

Regarding collective engagement, to ensure readers can determine the actual level of involvement of an organisation, the FRC should clarify that signatories should state their role in the collaboration. Additional explanation on why an organisation chose to use a particular collaboration or escalation method should be highlighted as useful information to include.

An area that has come under particular focus in the market is how various organisations classify what engagement actually entails. Guidance for the market would be welcomed within the engagement principle of the code.

Principle 4 (formerly Principle 12)

We believe that the language used under 'other asset classes' ensures that signatories are required to explain their general approach and intention in addition to how they exercised these rights during the year. We also believe that the principle would benefit from being explicit that disclosures should cover how rights, responsibilities and escalation differ by type of asset (for example, asset class or geography).

We encourage the FRC to reconsider the reference to fixed income in line with the 2020 Code. Given the FRC's aim for the code to apply across asset classes, keeping references to fixed income and adding key expectations for other asset classes would be beneficial.

The detailed requirements relating to proxy voting in the Code should be retained. Whilst standards of disclosure in relation to voting are well understood in the UK, ensuring this expectation is maintained going forward is particularly useful given the Code's prominence. In addition, the inclusion of how rights and responsibilities are wider than voting (including stock lending, shareholder proposals or attending AGMs for example) should be noted.

Question 8: Should signatories be able to reference publicly available external information as part of their Stewardship Code reporting, recognising this means Stewardship Code reports will no longer operate as a standalone source of information?

The PPF is supportive of the ability to cross-reference publicly available information. Cross-referencing existing publicly available external information can play a significant part in streamlining reporting, avoiding duplication, and reducing the reporting burden. However, consideration should be given to the accessibility of the documents online. Many investment managers have different tiers of information available online depending on whether they are an individual or professional investor depending on their role. Any links to these documents in the organisation's stewardship report should be accessible to all. There will also be significant onus on an organisation to ensure the links work for the year that report is current, as a minimum. We also note the FCA's Sustainability Disclosure Requirements Policy Statement (PS23/16) permits cross referencing from the UK Stewardship Code.

Realistically, links will become corrupted over time and at that point, if a reader wished to review a prior year's report, the report would neither be 'stand-alone' nor give a complete picture, if all of the information intended for use is no longer available. On this basis we suggest a summary of salient aspects of the cross-referenced document be included in the stewardship report. This would also be useful to readers of stewardship report that are content with a summary of a potentially deeper topic. This would also assist in maintaining the 'stand-alone' nature of the reports.

Question 9: Do you agree with the proposed schedule for implementation of the updated Code?

We have no concerns with the proposed schedule for implementation. We would suggest consideration is given to allow additional signatory engagement in the lead up to the first submissions. The market puts significant weight on achieving Stewardship Code status and providing time for additional engagement would increase the quality of submissions and confidence in the process.

Further information The PPF would be happy to discuss the points we have made in our submission in more detail. Please contact Kristy Gaywood, Strategy and Policy Adviser, for general queries regarding the PPF (Kristy.gaywood@ppf.co.uk) or Claire Curtin, Head of ESG and Sustainability, for further information about the above responses (Claire.curtin@ppf.co.uk)