Summary
• Increasing ESG regulations on schemes, such as the Statement of Investment Principles and the Task Force on Climate-related Financial Disclosures, will likely lead to a rise in ESG enquiries from scheme members.
• A clear message, without jargon, is vital when communicating ESG matters to members, by possibly focusing on the engagement part of the story, rather than divestment, to avoid creating complexity around messages.
• With DC self-select options, it is not just about making ESG funds available but also explaining to members why it is important for them to look at the ESG options and what they should consider.

Enticing engagement through ESG action

Stephanie Baxter considers how schemes can, and should, communicate ESG efforts to members

Much has been said and written about why environmental, social and governance (ESG) is a great engagement tool to encourage saving and drive greater interest in pensions. Survey after survey has shown that members increasingly care about where their money is invested and want it to be 'doing some good'.

Apart from the very big pension funds, most schemes' provision of information to members on ESG has been limited. This is expected to

change quite rapidly as they face more stringent regulatory requirements around responsible investment and look to demonstrate to members how they are acting on ESG. But how can schemes and providers best communicate their ESG efforts to savers, and to what level?

Regulations that came into force in 2019 require trustees to demonstrate ESG considerations in their Statements of Investment Principles. Since last October, they have to had to issue 'implementation statements' setting out how these considerations have been followed during the year.

"We haven't had many of those implementation statements yet because the law only came in October 2020, so there hasn't been a lot of open trustee dialogue with members around how they are implementing ESG strategies," says Sackers partner, Stuart O'Brien.

The Pension Schemes Bill will bring in powers to introduce climate change regulations – including requirements for pension schemes to have net-zero carbon emissions by 2050, and to adopt and report against the recommendations of the Task Force on Climate-related Financial Disclosures.

"I hope that trustees will go beyond the black letter of the law in terms of disclosures, and actually think more carefully about what would be good communication with members, not just what meets statutory requirements," says O'Brien.

He predicts that, as the amount of disclosure required from trustees increases, this will probably lead to a rise in the number of enquiries from members. Some of that will be driven by consumer charities and civil society groups, which are increasingly promoting divestment from fossil fuel giants, for example.

"That could prompt a member to scratch beneath the surface and say to the pension scheme, 'You claim to have a weighted average carbon intensity of X and have a target to reduce it to Y, and are reporting that you are moving towards that target – but I've had a look and you're still investing in companies that are mining thermal coal," says O'Brien.

Divestment vs engagement

Trustees should first of all be clear and comfortable about their investment approach to ESG. Then, for the purposes of disclosures and engagement with members, they need to have a really clear message and narrative.

"If schemes have a divestment strategy, they need to make sure they are really clear as to why that financially fits within the overall strategy," says O'Brien.

Some public-sector funds, such as Universities Superannuation Scheme (USS), have experienced lobbying from their membership about divesting from fossil fuels over the years.

LCP investment partner, Ian Gamon, says: "USS looked very carefully at what they could do, and came back last year with quite significant announcements about divesting from thermal coal and tobacco – but they had to be very careful in signposting it as a financial decision.

"One of the dangers of communicating to members is that if you do not position it very carefully, there is a risk that you're then in breach of fiduciary duty and you then face difficult questions about whether you're investing in members' best interests."

In publishing the legal advice it had received, USS was very transparent to its members. Gamon says being transparent and open is a good way forward for schemes.

Quietroom senior writer, Caroline Hopper, suggests focusing on the engagement part of the story rather than divestment to avoid creating complexity around messages.

After working on the Make My Money Matter campaign last year, she says people mistakenly confused the campaign for a divestment campaign. She explains: "It's not that the Make My Money Matter campaign had confusing messages, but because it's just so much for people to understand. This happened to me when I first looked at my pension investments around five years ago."

Quietroom has been trying to help various pension schemes "really tell the story of engagement, why that's really powerful and how using investor influence makes massive companies improve how they tackle the climate crisis", Hopper says.

This involves taking something powerful and emotive, and talking about how the scheme is influencing companies to do something.

As Aon's UK head of responsible investment, Tim Manuel, says: "If the scheme is investing in funds that are thinking about sustainability in a positive way, and if you're communicating about the positive stories that come from it, then the negative aspects of divestment don't become an issue."

Overcoming the challenges

Communicating ESG to members is a challenge because most members are not investment experts. For example, how do you explain factor investing to members and convert it into numbers that will be interesting and exciting for people who are not experienced in investment lingo?

LCP DC partner, Mark Smith, says first of all, it is better to use the term 'responsible investment' rather than ESG which "takes a lot of explaining".

He adds: "From a communications perspective, we look at how we can honestly say something on behalf of trustees in a way that converts it back into what it really means. At the moment, the biggest schemes tend to tilt into ESG slowly – so each year they might move some developed equities into a climate tilt. This is quite a decent amount of real change if you can measure it and then communicate that to members."

Schemes could consider match up messaging about the pension fund's strategy with the employer's messaging, according to Aon investment principal, Christopher Inman.

"There will be messaging from the corporate around sustainability practices, targets and objectives – but then you look at the pension scheme and there's nothing there *[in terms of messaging]*. It's about thinking of the themes that you want to communicate and then linking them up with company communications as far as possible.

"For example, when employees' annual benefits selection comes round, and one of their benefits is being able to lease electric cars as part of their benefits package, we can tie that with the some of the companies and technologies that the pension scheme is invested in."

Self-select options

DC schemes could also use communications to highlight the range of ESG funds that members can self-select. One challenge is that self-select ESG funds are all called different things, which can be confusing for the member, according to Gallagher director of retirement communications, Karen Bolan.

She says: "We always advocate simplicity above everything else, so quite often what we will do with clients is rename the funds. For a member, it's not really that important that they understand all of the underlying things in the fund. It's about simply labelling it something nice, friendly and simple that shows it is an ESG fund."

Gallagher has developed a carbon footprint modelling tool for some clients in Australia to provide a way to engage people, help them to understand what their carbon footprint is, and show them what they can do to positively impact it by, for example, investing in self-select ESG funds.

Bolan says the firm "does not subscribe to the Kevin Costner 'build it and they will come' philosophy for anything".

She explains: "You have to drive people – so using marketing techniques and getting people to interact with the information that's online. You need to do something to drive their interest so they will go and look at it – so it's not just about making ESG funds available. Also, explain why it is important for them to look at the ESG options, what they should consider, and then give them good, simple information."

There are many ways for pension schemes to communicate their ESG efforts to members in an innovative and helpful way. If this encourages members to be more interested in pensions and understand more about them, it can only be a good thing.

Written by Stephanie Baxter, a freelance journalist