Response to the Financial Conduct Authority's Discussion Paper 18/8 on Climate Change and Green Finance

by

THE TRANSPARENCY TASK FORCE

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About the Transparency Task Force

The Transparency Task Force (TTF) is the collaborative, campaigning community, dedicated to driving up levels of transparency in financial services, right around the world. We believe that higher levels of transparency are a pre-requisite for fairer, safer and more efficient markets that will deliver better value for money and better outcomes to the consumer.

Our overall purpose is to help reform the financial services sector such that it better serves the consumer.

For further information about the Transparency Task Force see Appendix A and refer www.transparencytaskforce.org

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…all of whom kindly provided valuable input on a voluntary basis.

Note that not all the participants necessarily agree with every point we make in this response; the views expressed represent the general consensus that has been formed for the purpose of this response.

We do not regard any part of this response as confidential and are happy for the FCA to share it with other parties.

1. Introduction

Consistent with our response to previous related consultations (2017 EU HLEG consultation on Sustainable Finance; 2018 DWP consultation on Clarifying Trustee Duties; and PRA's consultation 23/18 on climate change), The Transparency Task Force ('TTF'), sees an urgent need to align way the financial ecosystem operates with the need to protect the planet.

However, this is a paradigm shift for a financial services industry which has largely been trained and rewarded to consider financial outcomes only, often over a short timescale, meaning significant regulatory intervention will almost certainly be required to accelerate this shift.

We therefore welcome the FCA's Discussion Paper 18/8 on Climate Change and Green Finance.

We have previously stated that it is appropriate to call out climate change as a particular example of a material risk. A failure to mitigate climate change will significantly increase the challenge of dealing with almost all of the other systemic issues due to the interconnectedness of risks[1] and as many recognise we are now in a perilous situation with regards to climate[2]. However, very few understand the potentially severe impacts of an extra degree of global warming and still fewer understand the probabilistic nature of the Paris goals (i.e. that the global carbon budgets only give a 2/3 chance of meeting temperature goals).

Climate Breakdown – What everyone should know

The key problem to be addressed is how to best galvanise support for the urgent need for reform; and part of that challenge is ensuring everybody understands just how drastic and desperate the situation now is.

For example, please consider these points; all of which come from peer-reviewed science journal publications:

- The Earth's atmosphere now contains more carbon than at any time in the last 15 million years; arguably the last 55 million years
- Our world is almost certainly warming faster than at any time in the last 55 million years
- 55 million years ago – a time known as the PETM (Paleaocene-Eocene Thermal Maximum) – crocodiles lived in the Arctic, there were palm trees in Siberia and sea level was 40m higher
- According to the IPCC, we have just 12 years to prevent the global average temperature rise topping 1.5ºC. The UK Met Office, however, suggests that a combination of natural variability and anthropogenic emissions could take us beyond this figure in 5 years
- Methane and additional carbon dioxide added to the atmosphere from thawing permafrost may mean that we cannot avoid at least a 1.5ºC global average temperature rise
- Melting rate of the Greenland Ice Sheet (GIS) has increased fourfold since 2003. On average, between 2002 and 2016, the GIS lost 280 billion tonnes of ice a year. Now, this figure is close

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[1] World Economic Forum, Global Risks Interconnection Map 2018 http://reports.weforum.org/global-risks-2018/global-risks-landscape-2018/#risks

[2] IPCC, Special report on Global Warming of 1.5°C https://www.ipcc.ch/sr15/

to 400 billion tonnes.

- Between 2012 and 2017, the rate of ice loss from Antarctica trebled from 76 to 219 billion tonnes a year (mostly from the West Antarctic Ice Sheet). If this rate of increase in melting is maintained, by the 2040s it will add around 5cm to sea level EVERY YEAR

- The East Antarctic Ice Sheet, previously thought to be stable, is now breaking up. Several colossal glaciers making up one eighth of the East Antarctic coastline are now starting to melt. Loss of just one – the Spain-sized Totten Glacier, would raise global sea level by 3m

- Rather than the one metre or so sea-level rise by 2100, still touted by the IPCC, sea levels could be from 2 – 5m higher by the end of the century

- It is highly likely that – whatever we do – we are already locked into a sea-level rise of 5m and perhaps as much as 20m

- Probably within the next decade, parts of the world will experience unprecedented humid heat-waves, during which the wet-bulb thermometer temperature reaches 35°C. Such conditions are not survivable by human physiologies for more than six hours

- By 2070, humid heat-waves will threaten billions of lives, particularly across the Middle East, South and South East Asia and China

- The Gulf Stream has slowed by 15 – 20 percent since the middle of the 20th century, and is now at its slowest since at least 1600 years

- The Gulf Stream has a tipping point, beyond which it can shutdown in a couple of years, perhaps even a few months. We don't know what the tipping point is, nor if or when shutdown will happen again

- Beneath the submarine permafrost of the East Siberian Continental Shelf sits an estimated 1400 billion tonnes of carbon, in the form of methane (86 times more potent as a greenhouse gas than carbon dioxide)

- A single methane 'burp' could release 50 billion tonnes of methane, increasing its level in the atmosphere 12-fold and advancing global warming 30 years, almost overnight

- If we burn most (not even all) fossil fuel reserves, the global average temperature rise is estimated to be 16°C. This will take the planet's average temperature from about 14°C to around 30°C. For human-kind this would be close to an extinction-level event

Despite an increasing awareness of both the changing physical risk environment and the transition risks associated with climate change, relatively few organisations appear to be adopting a strategic approach. The reasons for this include a lack of awareness of relevant techniques, a lack of knowledge of this area, a lack of accountability, a perception that this is low priority; and simple wilful blindness.

We therefore see the urgent need to driving climate risk rapidly up the corporate agenda within the financial services sector.

Furthermore, given the inherent difficulties in galvanising support for urgent reform (despite the obvious severity of the problem) we believe that all the financial regulators around the world must adopt a strong leadership position.

For the UK market it is mission-critical that the FCA plays a full part in driving forward what must now happen. Anything less would be a needlessly high-risk strategy, when the stakes are as high as they could be imagined.

As one of our community once stated: “We don’t have a spare planet up our sleeve”

2. Our responses to the main questions

Q1: What, if any, difficulties do issuers face in determining materiality? We are also interested in exploring how investors consider materiality in this context.

Quantifying the materiality of climate risk remains an imperfect science for both investors and issuers. The risks are, however, clearly significant and some might say existential. As such, the fact that this area is still evolving should not be allowed to delay efforts to bring climate risk into investment analysis. In fact, it is likely to impact both the language, and the form, of any regulatory recommendations. It is also important to recognise that opinions on materiality are likely to vary even within the same sector.

Existing national and international industry-led initiatives and frameworks should be leveraged, wherever feasible, to avoid duplication of effort and costs in terms of both time and money.

Listed below are a few issues and ideas which need to be further developed/discussed:

1. Progress EU taxonomy – i.e. industry experts working with regulators.
2. Produce transparent, consistent low-carbon and positive-carbon benchmarks across each of the eight sector categories outlined in the TCFD status report (09/18). Progress EU Action plan Number 5: Develop sustainability benchmarks.
3. Performance measurement against carbon benchmarks is also required. Consider working with primary and secondary information agencies and data firms such as Bloomberg, Reuters, MSCI, FTSE and ISS-Ethix. The FCA should also liaise with CFA Institute (which has a strong track record having developed GIPS compliance standards) and who are also currently developing performance measurement in the Fiduciary Management industry.
4. Asset owners should engage with companies to promote the performance measurement of Board executives against low-carbon/positive-carbon benchmarks. By aligning the bonus structures of executives to climate-related risks (e.g. as per Unilever), investors can be confident that climate change will be fully embedded into the company’s strategy, approach to governance, risk processes and metrics. Transparent benchmark and goal setting, for example, using Science Based Targets, coupled with independent performance monitoring by a third party provides decision-useful information on materiality for capital allocation. JB: Add: This should extend to the remuneration of asset managers often delegated by asset owners to engage companies on their remuneration.
5. Scenario analysis gives investors insight into the company’s climate-related risks and opportunities. Clear detail on the methodology and models used is essential to ensure full disclosure of the financial impacts from each scenario (e.g. B2D, 4D etc). Further work is required including leveraging existing initiatives e.g. IIGCC’s newly formed ‘Investor Practices Programme’, ‘IEA scenario analysis’ and the UN’s SDGs etc.

6. Developing quantitative financial measures to assess materiality would be decision-useful for investors. For example, percentage impact (upside or downside) to earnings over a one, five, and ten-year outlook e.g. EBIT and percentage impact to asset values (tangible and intangible).
7. Tools and analytics should be accessible to all investors so that they can readily and cost-effectively assess materiality concerns. For example, the TCFD 'Knowledge Hub' built by the CDSB (Carbon Disclosure Standards Board) is a useful online aggregator for publicly available resources, events and case studies on climate-related disclosures in alignment with the TCFD recommendations.
8. Work is further required re understanding climate-related risks and materiality concerns associated with investing in derivatives/ETFs, index products and, in particular, synthetic instruments, which are increasingly being used in many portfolios.
9. Within asset managers' disclosure/reporting, the focus is still too much on equity market-cap-weighted approaches. There is a distinct lack of reporting for other asset classes or strategies that are not benchmark-orientated. There needs to be increased activity in other asset classes (e.g. Bonds) and early innovators in SmartBeta and actively managed strategies.
10. The downstream element is still under-represented (e.g. materiality of climate risks and opportunities for products and services, especially within finance – bank loans, insurance, financing etc).
11. There is not enough consideration for location-specific risks due to the ongoing lack of asset-level data. This is relevant when considering transition risk but is especially relevant for physical risks
12. There is merit in the FCA exploring how to work with the Cambridge Institute for Sustainability Leadership regarding their new Impact Performance Measurement Tool which is both practical and measurable.
13. There is merit in the FCA exploring how to work with the SASB regarding their developing quarterly non-financial reporting on each stock, sector etc. in terms of ESG actual financial impact.

In addition, guidance for issuers on materiality should be provided to remove some of the subjectivity and enable capital allocation decision-makers to opine on the validity and resulting impact to their financial expectations. The more quantitative this can be, the better.

These could consider:

- % impact (upside or downside) to earnings over a one, five, and ten-year outlook e.g. EBIT
- % impact to asset values (tangible and intangible)
- Qualitative statements on impact to supply chain, employees and customer base that result in change in earnings or asset values and tie into the above two metrics

Additional difficulties identified by the Transparency Task Force include:

- Cultural inertia - firms wanting to simply continue doing what they have done before
- Governance barriers - layers of Committees leading to slow change
- Lack of dedicated resources ('side of desk' approach)
- Lack of training
- Lack of training at senior levels, executives lack vital knowledge, insight and expertise
- On-paper Executive champions are often paying lip-service to 'manage' the situation
- Marketing can disguise a lack of progress
- There has in the past been a lack of direct guidance from regulators; this needs to change
- Lack of confidence around metrics
- Poor customer engagement on ESG issues misinterpreted as 'apathy'

- Malaise of materiality; ESG has to compete with other 'Risks'
- Excessive focus on short term metrics - leading to a failure to recognise material long term issues
- Divergence of information from companies in financial reports and narrative reports
- Significant accountability gap as investors have limited ability to seek information directly and company disclosures are inconsistent; the landscape is far too opaque

We also believe that:

- The industry struggles with materiality, which inevitably comes down to a question around past returns and stock/sector performance.
- Non-financial metrics are quickly subordinated to financial indicators and KPIs. This stems from both 'convention' and a lack of clarity on materiality which filters down from issuers to asset managers into the asset owners.
- Asset owners rarely review issuer disclosures and rely on their asset managers to aggregate and assess; this is an unreliable approach as there is insufficient alignment of interests.
- Fund investors and asset owners can observe a lack of consistency in terms of a disparate range of studies in support of, or against, integration of ESG and/or climate risk factors.
- Executives and investment committees often relegate ESG and climate reports as 'for noting' rather than 'for action'. That inconsistency is perpetuated by a lack of consistency between asset managers reporting on their own integration.
- Evidence in support of incorporating ESG and sustainability are often discounted in favour of studies that support the status quo. Large meta studies are often depicted as too abstract to allow practical implementation or address specific measures.
- Whilst FCA consulting on guidance to issuers is very welcome, guidance on materiality determinations and more robust and transparent enforcement of existing legal requirements is also needed.
- Disclosure requirements should cater for the needs of all users of this information (asset owners, asset managers, trustees, individual investors.)
- Financial markets need clear guidance in order to ensure consistent disclosure and to enable transparent, efficient pricing mechanisms to evolve rapidly - allowing for an accurate assessment of the risks and opportunities within the security being issued. As such, decision-useful information will help investors to make responsible and informed capital allocations.

Q2: We are interested in understanding whether greater comparability of disclosures would help investors in their decision-making more generally. If so, what framework would be most useful?

- Greater comparability of disclosures would help investors make informed, responsible decisions.
- We recommend building on the existing and widely accepted TCFD framework and leveraging industry-wide expertise, initiatives and innovative solutions as they evolve.
- Greater comparability of disclosures would enable better decision-making by investors and their agents. **The inaccuracy and inconsistency of climate-related disclosure is a fundamental obstacle to the growth of Green Finance.**
- Ideally, a standardised international framework of disclosure is required. Realistically, the UK should develop its own disclosure framework while working with international partners.
- The imperfections of this market are such that this will require a balance to be struck between demanding too little or too much information from issuers.

- In order for this comparability of value it must translate into common aggregations and reporting standards by asset managers
- The FCA should consider that existing reporting requirements (if applied properly and enforced) already provide a sound basis for incorporating climate change-related information into existing disclosures. Use should therefore be made of existing provisions in order to create a sound base which the TCFD could then be built on.

Q3: Would exploring a 'comply or explain' approach (or other avenues to encourage more consistent disclosures) be an effective way of facilitating more effective markets?

Overall, we are driven by a collective desire to increase transparency; improve consistency and comparability and an imperative to act sooner to address climate change.

We believe that:

- The purpose of facilitating 'more effective markets' is to address the financial services community's failure to respond effectively to climate change and the risks it presents to investors and to wider society.
- The regulatory focus should therefore be on improving the operation of the market rapidly.
- In order for markets to function properly, reliable and comparable information must be available. As such, consistent disclosure is therefore key.
- Although 'comply or explain' would represent progress, the experience indicates that this may not be ambitious enough. The industry is notoriously slow to adapt to important themes particularly when short-term commercial interests of market participants often seem to take priority over the real concerns of asset owners
- The whole industry needs to move on the disclosures at the same time to remove the opportunity to arbitrage between those complying, with those who do not. (we have witnessed this with MiFID II).
- Climate-related risks require urgent attention and need to be prioritised to ensure compliance and rapid uptake; plus the evolution of a standardised practice to promote efficient markets.
- Widespread adoption of disclosure requirements will help to make climate-related risks and opportunities become an integral part of a company's risk management and strategic planning processes. Over time, companies' and investor understanding of the financial implications associated with climate change will grow, information will become more useful for decision making, and risks and opportunities will be more accurately priced, allowing for the more efficient and responsible allocation of capital.
- Some form of supervisory 'reward' (such as a reduced risk-weighting for securities with higher standards of disclosure) could act as a powerful 'nudge' to better disclosure and greater transparency.
- Careful attention would need to be made to not encourage false disclosures /compliance. For issuers this would need to be integral to listing rules and, in turn, fed through asset managers to asset owners via a common framework such as TCFD. The means to validate data accuracy is key
- As mentioned previously, material climate related disclosure should already be disclosed under existing laws and is therefore not voluntary. However, this needs to be properly enforced in order to be effective.

Responses to the further questions relating to Climate Risk Reporting:

Q1: Do you think that a requirement for firms to report on climate risks would be a valuable measure?

Firms should report publicly on how they manage both physical and decarbonisation climate risks:

- This should be mandatory and apply to all regulated firms
- Reports should include both transition and physical risks
- This should be at the Board or ExCo (for private firms) level as per guidance from TCFD.
- This should also include Fund Boards; it will ultimately be relevant for all Pension Trustees, Insurance companies and Banks.
- This would also help both the financial services firms and their clients as it would aid alignment of key issues.

Furthermore, we believe that it would be prudent and pragmatic to make a special provision for small firms.. Smaller firms below a reasonable threshold could benefit from a standard regulated estimate and reporting methodology. The aim being to not overload smaller firms with a higher proportional cost of meeting the new disclosure requirements.

Q2: Do you have any suggestions for what information could be included in a 'climate risks' report?

- It should follow TCFD's guidance across the four pillars and supplementary guidance for key sectors (especially the financial participants).
- It needs to include both transition and physical risks and should be at the asset/operations level not just headquarters.
- It needs to distinguish between reporting on how they manage their 'own firm' climate risks (i.e. internal governance matters) and how they manage climate risks on behalf of their clients (i.e. investment processes).
- It should make it clear when and where they rely on third parties such as delegated investment managers, commercial research providers, sustainability ratings providers, etc.
- It should include impact to liquidity of assets held over set time periods that align to investment outlooks of investors e.g. one, five and ten-year outlook
- It must set out how oversight and monitoring is managed and deal with variations between different asset classes.

- The report could include:
    - Progress against Climate change target COP23
    - ISO 14001 Compliance
    - Agreed Scope 1-2 Carbon intensity; both CO2E emission and reserves
    - Broader GHG and Pollutant metrics statement
    - Carbon reduction metric
    - Positive impact projects invested
    - Green infrastructure projects invested
    - Non-compliance
    - Presence of controversies
    - Operating Resources dedicated to climate change
    - Chief Climate/ESG Officer summary
    - Carbon intensity of funds (with explanations)

- Exposure to assets deemed at risk of becoming stranded.

Q3: Do you have any views on which regulated firms should be required to compile a climate risks report?

- All regulated firms should be required to compile a climate risk report, including those with e-Money licences
- Climate change will affect everyone and every investment business in some form (not just the specific investor groups targeted by certain financial services firms). It is therefore incumbent on the entire financial services system to address climate risk.

This should include the following:

- Authorised Fund Managers, Unit Trust Managers and UCITS Man Cos.
- Asset owners
- General insurers
- Master Trust pension scheme
- DB Scheme trustees
- Workplace pension providers
- ISA providers
- ETF providers
- Multi-managers
- Index manufacturers
- Platform providers

3. Our responses to the additional questions

Q1: How can authorities, including the FCA, most effectively work with industry to meet investor demand for green investment opportunities and encourage those raising capital and investing in it to pursue sustainable outcomes?

There is a need to focus on the role of intermediaries to ensure messages are clearly communicated to end investors - including adviser fact finding processes.

We believe that:

- The length and complexity of this 'value chain' has many undesirable effects. One is that – even if clear standards of climate related disclosure could be devised and applied – it could be extremely hard for the ultimate investor to 'look through' these intermediaries and identify the climate-related risks and returns to which they are exposed.
- The FCA should work with other regulators and policy makers to create more consistency in measures, reporting methods and disclosures in order to aid better understanding and more rapid progress.
- Education and professional qualification syllabuses need to move much faster to embed this at a much earlier point in the financial services industry; it should represent a key component of core knowledge moving forward
- Investment managers should be obligated to explain their climate risk strategies to end investors succinctly, in plain English, supported by links to further information where required.

- It is worth considering adding FCA-endorsed scenarios to set out clearly the estimated material effects from climate risk on assets; thereby resolving the current discord among asset owners.
- It is worth considering providing asset owners with tools to assess issuers and asset managers.
- Clear 'pathways' that can be communicated to clients should be set for
  - Integrating climate risk into different product areas (e.g. default pension funds, OEICs etc.)
  - 'Best Practice' stewardship reporting guidelines
  - The assignation of clear responsibilities to boards across all product areas

Q2 Do you agree with the extent of the FCA's proposed interventions on climate change-related financial disclosures? Is there a specific need for us to intervene further in the interests of market integrity or consumer interests?

The Transparency Task Force agree with the proposed interventions but feels that the FCA needs to act rapidly as a softly/softly approach is liable to be 'too little too late'. This needs to include removing scope for regulatory arbitrage and reminding regulated business of their fiduciary duties and their role in the global economy.

Industry skill levels and awareness of climate risk should also be considered with a view to ensuring the financial services community recognises the seriousness and urgency of climate risk and is equipped to respond to it. (The results of the recent PRA study on this topic indicate why this is important.)

FCA interventions should, where possible, be aligned to – and not competing with – existing widely used standards and regulatory requirements e.g. SASB, GRI, IR, IASB/FASB – as well as the work of the FRC, DWP and PRA. The aim should be to create a level and consistent playing field that is able to respond to future developments as they emerge.

Q3: In light of the EU work on taxonomy, what are your views on the form common standards and metrics for measuring and reporting against green financial services products should take?

The EU taxonomy work is yet to be finalised and although potentially very useful we cannot as yet predict its final iterations or whether it will gain universal support (Brexit notwithstanding). At present there remain open concerns relating to parts of the proposed methodology - see below.

- The EU approach seems pragmatic and should deliver a significant step forward. However, a key element of the EU approach is the development of technical screening criteria, such as a test as to whether the product "contributes substantially" to one or more of the six environmental objectives.
  (see:https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/sustainable-finance-teg-frequently-asked-questions_en.pdf)

- This is likely to be difficult to prove or test in practice as climate change represents the sum of a range of behaviours from multiple parties. Therefore, a particular financial product is unlikely to be able to demonstrate that it "contributes substantially". It is potentially more practically feasible therefore, to focus on criteria such as "do no significant harm" though this is not a legitimate definition of sustainability, especially when it refers to an issue such as climate change which requires positive contributory change, not a net neutral impact.

- Therefore, criteria should also be able to articulate, measure and verify positive contribution/harm reduction, capacity expansion or an otherwise manifest contribution to the abundance, vitality and productive capacity of natural capital; and society worldwide

In order to reduce costs and maximise efficiency the FCA should look to adopt (or as a minimum reference) this work and potentially that of others. An appropriate system would need to be dynamic (able to respond to new developments) and able to be used alongside other frameworks and goals such as the Sustainable Development Goals and TCFD framework.

One TTF member explained: *"In the past five years we have analysed around 60 ESG frameworks and global regulations looking for the common threads. The danger of rigid frameworks set by regulators is that they are difficult to change. Politicians like quick and easy fixes and then move on. Again, what have we learned from the past 20 years is that principles that evolve are better than rigid top-down rules which can be gamed".*

Q4: How could regulators and industry best work together as part of the 'Climate Financial Risk Forum'?

This forum should aim to draw on broad expertise from across the range of financial services companies and other stakeholders (including the PRA and NGOs) with a view to improving knowledge transfer.

This topic needs to be made a higher priority on their governance and oversight agendas of financial services firms if it is to be addressed effectively. Priority should be given to encouraging firm's CEO's and Boards (including Fund Boards) to engage more proactively i.e. with Dear CEO letters, forum attendance, etc.

Q5: What are your biggest concerns and commercial priorities regarding climate change?

- The slow speed with which industry firms are addressing climate change impacts for their investors (i.e. the 'too little too late' risk)
- The costs of unnecessary divergence between jurisdictions, policies and regulation
- Ongoing focus on transition risks at the expense of also considering physical risks (physical risks are barely mentioned in the paper, despite being referenced as important in the TCFD recommendations).
- Too great a focus on companies (and therefore, only equity/corporate fixed income asset classes), and too little focus on other asset classes e.g. sovereigns, commodities, real assets/infrastructure.
- The risk of major investors 'greenwashing' in order to reduce costs
- Insufficient action from investors in areas where there is a complex investment chain and lines of responsibility (e.g. Malaysian rainforest being destroyed in part as a result of food demand from wealthier nations.)
- Poor communication leading to growing 'end client' scepticism

- Resistance (and *in extremis* perhaps even sabotage) by investment organisations and individuals in senior positions that prefer to retain the status quo.

Q6: What are the biggest barriers to the growth of green financial services in the UK?

- Lack of regulatory pressure - many investment organisations will not focus seriously on this area unless they are directed to do so. The FCA has a wonderful opportunity to shake things up, for the benefit of all
- Inconsistent and narrow interpretations of fiduciary responsibility - including ultimately counter-productive short termism.
- Focus upon voluntary approaches - with pressure on costs, significant risks such as climate change need to be mandated.
- Lack of consumer awareness of options, largely resulting from poor financial awareness and the low regulatory interest there has previously been in this area.
- Clarity on what constitutes ‘green finance’ (and a poor understanding of the role finance plays in addressing climate risk.)
- The gap between marginal improvements (e.g. better than the norm) and the requirements of adequately responding to climate change (radically different from the norm).
- Outdated regulation and regulatory systems
- Individual investors are generally unable to robustly or effectively challenge asset managers and issuers on their claims of “green” or climate-aware investments.
- Short-term pressure to generate returns versus the need to invest in R&D for the future
- Insufficient collaboration throughout the investment chain
- Poor communication between asset managers and asset owners (for example, pension fund members or life assurance policyholders)
- Existing green, ethical, responsible and ESG funds being difficult to compare because of their diverse strategies
- Challenges posed by the fact different investment products (e.g. collective investment funds) have emerged to meet different client needs
- Lack of widespread sustainability skills/competencies within financial services and the currently limited opportunities for entities at earlier stages of development to learn from peers. (Initiatives relating to standards development - including ISO/BSI/GFI - should serve to address this and help develop wider confidence in the market).
- Education. The CFA has recently incorporated an ESG module into its certification scheme. We propose that ESG should be a required module for all financial services qualifications. However, educational standards should be monitored to ensure risks and opportunities are explained appropriately.
- Entrenched ‘Risk’ conventions, the packaging of products and cost ceilings (e.g. as it relates to auto-enrolment) directing people away from integrating ESG and climate risk.
- Regulatory and political uncertainty arising from and relating to Brexit.

4. Further considerations

We believe there is a significant disconnect between the proportion of people that research suggests would like to invest in a climate-change-aware manner and those that actually do. Why is the “demand side” so weak? There are many reasons for this but as indicated earlier we believe the quality of fact-finding by intermediaries when assessing the suitability of investment options for an investor is wholly inadequate.

Put simply, most financial advisers do not apply the "know your client" tenet of regulated financial advice in a sufficiently broad manner. We believe they should interpret "know your client" to cover whether the client has any views that are relevent to investment solution selection; including whether the client would prefer to invest in a climate-change-aware manner, be that because they are considering the possible financial impact of investing in assets that could become stranded; and/or whether their values are such that regardless of the potential financial consequences they simply do not want to invest in assets that are harmful to the planet.

It is perfectly possible that a straightforward communication from the FCA to all financial intermediaries advising that the regulatory tenet of "know your client" must take into account all relevent information that can be reasonably obtained by asking the client a suitably comprehensive set of questions, including suitable questions about the client's views on the relevance of climate change when selecting an investment.

Interestingly, we believe that financial advisers that fail to ask a suitably comprehensive set of questions prior to making an investment selection recommendation may be exposed to the risk of litigation by the client for failing to sufficiently take into the client's attitudes and beliefs.

Whilst good progress has been made in recent years with regard to ensuring a client's religious beliefs are considered as a matter of routine (for example in relation to those that prefer to use Shariah-complaint funds) it is clear that the intermediary sector is a long way behind the curve when it comes to advisers properly considering the client's views on climate change.

Because of the potential for litigation in this space there may be a material systemic risk in the advisory sector that must be dealt with as quickly as possible. Appropriate and suitably swift action by the FCA may prevent a significant market failure; and like all potential market failures the quicker they are dealt with the better.

We suspect demonstrating the adviser failed to "know the client" may be a relatively easy challenge for the client to deal with – the simple question they need to ask is.

"Did the fact-find form you completed prior to giving me advice capture information about my views on climate change?"

Furthermore, we suggest the FCA seeks dialogue with the professional indemnity insurers that cover financial advisers to establish whether their standard policies cover the risk of claims against advisers that can be shown to have failed to take into account all relevent and reasonable-to-obtain information.

5. Suggested next steps

We sincerely hope that our response has been useful to you. We also hope that the complete lack of resource we have to create a “polished” response is more than made up for by the authentic interest we have in the topics covered.

We also hope the knowledge and insight we have attempted to convey shows that the Transparency Task Force’s valiant volunteers have tremendous potential value to a key regulator making significant strides forward into what is a largely new area to it.

Whilst a written response may be useful we believe a “round table” discussion on the issues and ideas conveyed in our response will create an opportunity for the FCA to take the dialogue to a higher level of understanding. It’s good to talk, so on that basis we wish to propose that a round-table-discussion meeting be held at the FCA to “bring this response to life.”

We arranged something similar with the PRA in the Summer and we believe it was of use to all that participated. Please advise if you may wish to organise a meeting.

Follows: Appendix A

APPENDIX A: Further information about the TTF

The Transformational Power of Transparency

We seek to harness the transformational power of transparency; a power that has been known about and understood for over a century since the seminal work of Justice Louis D. Brandeis and his 1914 book “Other People’s Money and How the Bankers Use It.” This is the work that gave the world the idea that “Sunlight is said to be the best of disinfectants; electric light the most efficient policeman.” ….an idea that is at the very heart of what the TTF is all about.

The transformational power of transparency works because of the correlation between transparency, truthfulness and trustworthiness.

Free of commercial conflicts

The TTF is free to consider what is ultimately best for the consumer without commercial conflicts and we are perhaps unique in being made up of a truly pan-industry cross-section of individuals that includes market participants, researchers, academics, legal professionals and those formally representing trade bodies and professional associations. As such we are well-placed to establish consensus that does not merely reflect the wishes of one particular “tribe” or another. We are therefore able to work to one simple and straightforward guiding principle: “What is best for the consumer?”

Our Special Interest Groups

The TTF seeks to operate in a collaborative, collegiate and consensus-building way; focusing on solutions, not blame. Our solution-orientated approach is made possible because of the work of volunteers. We have over 500 volunteers organised into 18 Special Interest Groups (SIGs), with each group working on a campaign to help drive reform that will improve outcomes for consumers.

Our SIGs are:

- Costs & Charges
- Market Integrity
- Financial Stability Team
- Banking
- Anti-Scams
- Foreign Exchange
- Asset Management
- APAC
- Americas
- EMEA
- Global Transparency Index
- Pensions
- Financial Planning
- FinTech
- Compliance, Legal, Audit, Regulatory, Governance, Custodian, Risk Management, general Counsel

- Investment Consulting & Fiduciary Management
- Communications
- **PISCES**

PISCES is directly relevant to this response. PISCES is made up of members who like the idea of the world's capital markets becoming a 'force for good'. We believe there is tremendous scope for the way the financial services sector influences what happens in our world.

To explain the name of the SIG: the **P** is for Purpose; **I** is for Impact Investing; **S** is for Sustainability; **C** is for Climate Change; **E** is for Environment, Social and Governance; and **S** is for Socially Responsible Investing.

For further information about our Special Interest Groups and to download a spreadsheet showing their members see here:

https://www.transparencytaskforce.org/teams-of-volunteers/

The TTF Strategy for Driving Change

Our Strategy for Driving Change is all about bringing togethor two groups of people:

#1, those with a sense of passion & purpose about what needs to be changed, such as our 350+ volunteers; and

#2, those with the power & position to make change happen i.e. the regulators, senior civil servants, policymakers and Parliamentarians.

We bring these two groups together in many ways, for example through our Transparency Symposia; and through our Special Events. Here's three examples of our Special Events:

1. 12th September 2016 at the Houses of Parliament, Co-chaired with Tom Tugendhat MBE MP, where we held "The first Transparency Strategy Summit in the World," the primary purpose of which was "to begin to build consensus on the best way to protect the interests of the UK's pensions-saving public through full disclosure on all the costs and charges they are paying but not being told about." That special event led to the TTF sending a letter to the Chair of the Work and Pensions Committee asking the Committee to open an inquiry on pensions costs and transparency.

2. 26th June 2017 at the Houses of Parliament, Co-chaired with Lord Cromwell, where we presented TTF Banking Team's White Paper on Current Accounts entitled "Sensible recommendations about the lack of transparency around charges for Free-If-In-Credit personal current accounts."

3. 7th February 2018 at the Houses of Parliament, Co-chaired with Lord Cromwell; a very special meeting where we presented our White Paper entitled "Ideas to help reduce the chance of another Global Financial Crisis" which subsequently initiated the launch of a new All Party Parliamentary Group on Financial Stability. The draft Purpose Statement for the

new APPG is “To respond to the universal shared interest in avoiding another Financial Crisis by providing a helpful forum for parliamentarians to work cross-party, developing fledgling policy initiatives to buttress the resilience of our financial system; supported by participation from industry, academics, experts, think tanks, civil society, campaign groups and regulators.”

Our “North Star” Question

We are guided by our “North Star” question, which is – “What is best for the consumer?” and we think this is an important perspective to take because the inherently lucrative nature of the financial services sector means that there will always be tens of thousands of market participants, trade bodies and professional associations around the world that are extremely adept at representing their commercial interests.

Many of these organisations are very well resourced, with large budgets for campaigning/lobbying/influencing and it is obvious that they have had a great deal of influence over the writing of the rules that are used to regulate and govern the sector.

The overall impact of this reality is that the best interests of the consumer are very often overshadowed by what will enable market participants to continue to flourish and enjoy high profit margins; sometimes at the expense of the consumer because of an attitude of “profit before principle.”

Fortunately, there are some organisations that do not seem to follow the “profit before principle” mindset at all; they are very often characterised by enlightened, values-based leadership that seems to fully understand the importance of the sector reforming how it works; and there are also some market participants that have a not-for-profit or mutual structure and are therefore more predisposed to a customer-centric way of working.

However, in the overall scheme of things there is a very one-sided battle when it comes to the sum total of influences acting on the regulators and policymakers on behalf of market participants compared to those acting exclusively on behalf of the consumer. This can typically be evidenced by the amount of consultation responses representing the commercial interests of market participants (both directly and via their trade bodies) when compared to the amount of responses from organisations that take a wholly pro-consumer stance.

The cumulative effect of powerful lobbying over decades has contributed to a financial services sector that sometimes seems more committed to its commercial self-interests than purposefully serving the customer. We believe this needs to change – not only for the benefit of the consumer but also for the benefit of the sector itself. The last point might seem surprising but we truly believe the financial services sector as a whole is suffering as a consequence of having not been sufficiently careful about looking after the consumer’s interests. This manifests in many ways and a particular concern we have is around the trust deficit.

TTF Governance

The TTF has an Advisory Board, the overall purpose of which is to help set our strategic direction and priorities; and to help deal with the hugely important issue of fund-raising as we are severely limited by a lack of resource.

The Advisory Board Chair is John Howard who presented the BBC Radio 4 pro-consumer programme "You and Yours" for 14 years; and is a former Chair of the Financial Conduct Authority's Financial Services Consumer Panel.

For further details about our Advisory Board see here:
https://www.transparencytaskforce.org/about-1/advisory-board/

The TTF Ambassadors

The issues that the TTF are looking to help fix are not confined to the UK. We are therefore building a global network of Ambassadors such that we can deal with matters on an international basis. For further information about our Ambassadors see here:

https://www.transparencytaskforce.org/ttf-ambassadors/

End.