



Legal 'certainty' needed over schemes' ESG duty - 30 May 2008 11:00

IPE.com 30 May 2008 11:00:

EUROPE/GERMANY – Pension funds are calling for "legal certainty" over how sustainable development affects their fiduciary duty along with improvements to the quality of long-term sustainability information provided in company reports, a study commissioned by ASSET4 and the German government has revealed.



The study, entitled '*Long-term and sustainable pension investments: a study of leading European pension funds*', was conducted by Dr Axel Hesse, and highlights evidence suggesting while pension funds are clearly long-term investors, they are making "insufficient use" of long-term research into sustainable development.

That said, the respondents – from 10 of Europe's largest pension funds and asset managers with more than €460bn assets under management – claimed while long-term information supplied by companies was slightly better than from specialist research companies, there was a "strong need for catching-up" in relation to providing investors with "materially important sustainability information".

The interviewees – which included representatives from ABP, AP1, AP4, USS, MetallRente, BT Pension Scheme, Ethos, FRR, ERAFP and PGGM Investments – rated information found in company management reports the worst at 4.39 out of 6, while separate sustainability reports ranked only slightly better at 3.95, where 1 is good and 6 is bad.

Findings from the study suggested although these reports have been published for some time "they frequently lack brief and well-prepared, materially important information".

As a result, the respondents claimed the best practice to integrate long-term sustainable research into the mainstream is to focus on the most important, industry-specific, Sustainable Development Key Performance Indicators (SD-KPI).

The study, sponsored by [ASSET4](#) – a provider of Environmental, Social and Governance (ESG) information - and the [German Federal Environment Ministry](#), claimed the interviewees see a "high potential for generating above-average returns in SD-KPIs" as these would "most likely lead to long-term, risk-adjusted outperformance, whereas approaches that are too broad are more likely to lead to underperformance".

In addition, the report revealed pension funds believe there should be more legal certainty regarding whether pension funds need to take sustainability goals into consideration as part of their "fiduciary duty", while legal frameworks which restrict long-term sustainable investment – such as annual guaranteed rates for traditional insurance-linked pension funds in Germany and Switzerland – ought to be eliminated.

The research showed pension funds are already "increasingly campaigning for generally better frameworks", both politically and from companies, with a current focus on a more stringent climate

protection policy.

Although the report admits the interviewees are already "sustainability pioneers", it argued the positive impact on revenues from stricter frameworks "could become one of the most dynamic drivers of politics for sustainable development overall", particularly if "all pension funds in the developed world behaved in a similar manner".

Findings from the research showed the respondents pretty much all agreed pension funds should "define goals with regard to corporate citizenship of investee companies", one such example being ABP's demand in March 2008 requiring companies it invests in to operate in compliance with the UN Global Compact Principles.

However, interviewees also agreed "a clarification by legislators whether sustainability targets have to be considered by the pension funds regarding their fiduciary duty is desirable for legal certainty", particularly in countries where there has not yet been any "explicit clarification".

That said, the respondents said while legislators should prescribe that sustainability goals be taken into account with investments, "the 'how' and the specific design should continue to be decided by the pension fund".

In addition, the study revealed that if pension funds were able to increase their long-term investment horizon – which in theory could be as long as 23 years – the average asset allocation of pension funds could see a reduction in liquid funds, short and medium-term bonds and hedge funds, offset by an increase in private equity, real estate, infrastructure, commodities and shares.

The full report can be found on the ASSET 4 website [here](#).

If you have any comments you would like to add to this or any other story, contact Nyree Stewart on + 44 (0)20 7261 4618 or email nyree.stewart@ipe.com

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