FCA
Smaller Business Practitioner Panel

Mark Manning
Strategy and Competition Division
Financial Conduct Authority
25 The North Colonnade
London E14 5HS

30 April 2019

Dear Mark,

DP19/1: Building a regulatory framework for effective stewardship

The Smaller Business Practitioner Panel is pleased to respond to the FCA and FRC's joint discussion paper on effective stewardship.

In question 2 you ask if there are any particular areas which we consider that investors' effective stewardship should focus on to help improve outcomes for the benefit of beneficiaries, the economy and society. The Panel has noted recently that there has been a welcome increase in regulatory focus on Environmental, Social and Governance (ESG) activity, which is an area which is currently very actively marketed, and believes this is an important focus for stewardship activity.

There are, however, currently some obstacles to effective stewardship in this area. Many firms are emphasising their ESG credentials, and there is a very real danger of 'greenwashing' if it is not clear what processes and standards support their activity. The work required for genuine investment in a responsible manner is very substantial. There are three aspects to this approach:

1. Responsible share ownership (including stewardship) which involves engagement with investee companies as an asset owner on ESG issues. Responsible investors will take into account how a company is managed, including its culture and behaviour. This can lead to companies being excluded from the investment universe.
2. Positive screening which involves actively looking for and selecting shares to invest in based on their ability to meet certain criteria (such as reporting on, for example, emissions or employee welfare policy). For some investors, positive criteria may rule out certain industries, such as mining and oils, and can reduce the potential universe of shares in which to invest;
3. Negative screening which involves avoiding shares in companies whose activities include for instance pornography, weapons, gambling etc.

Most well established ethical funds carry out all three activities, but we believe that effective stewardship would extend point 1 to investment funds irrespective of whether there is also positive or negative screening present.

Development of clear metrics, taxonomy and monitoring will be necessary to ensure that firms' ESG position is clear to consumers. It is not necessary, or even desirable, for all firms to meet the same ESG standards, but if firms articulate their policies in clear language this will enable consumers to make informed choices. Efforts to agree a taxonomy on sustainable finance at EU level are welcome as a basis for this, but there is still a risk that customers will be misled into buying products which are presented as 'ethical' by firms which do not have rigorous standards to encourage investment in a responsible manner if there is not a coordinated approach at international level.

Yours sincerely,

[signed]

Craig Errington
Chair, FCA Smaller Business Practitioner Panel