



Legal Services

FINANCIAL SERVICES



ON THE SCALES 10 OF 2019

PFA Guidance Notice 1 of 2019 & PFA Communication 1 of 2019 – sustainability of investments and assets in the context of a retirement fund’s investment policy statement

The FSCA issued a draft directive in March 2018 on this issue and now the FSCA has issued a final Guidance Notice in June 2019, taking into account feedback received.

A Directive (now called a Conduct Standard) is binding on funds, but an Information Circular (now called a Guidance Notice) is not binding on funds. So, albeit the draft would have been binding on funds, the final version is not binding on funds.

Summary

- Communication 1 of 2019, issued with the Guidance Notice, sets out the context and factors taken into account by the FSCA in issuing Guidance Notice 1 of 2019.
- Guidance Notice 1 of 2019 sets out the FSCA’s intention of giving funds guidance on how a fund’s investment philosophy should ensure the sustainability of the fund’s investments and assets.
- The Guidance Notice also covers the FSCA expectations as to fund reporting and disclosure on issues of sustainability.
- The Guidance Notice includes definitions of ‘active ownership’, ‘broad-based black economic empowerment’, ‘discretionary asset manager’, ‘ESG factors’, ‘sustainable reporting’ and ‘sustainability’.

- A fund's investment policy statement (IPS) should cover how the fund intends to ensure the sustainability of its assets.
- Members should be entitled to a copy of the IPS or an abridged version of it, at no cost.
- Funds have been requested to report on how their IPS complies with the Guidance Notice.

Communication 1 of 2019

In issuing Guidance Notice 1 of 2019, the FSCA has taken into account:

- international and local developments in sustainable finance and investments; and
- that regulation 28 promotes the responsible investing of fund assets and requires funds to have an IPS and consider Environmental Social Governance ("ESG") aspects in their investment strategy.

The FSCA wants to provide guidance to funds on essential aspects of including ESG in their IPS and how funds disclose and report on ESG.

The Guidance Notice encourages funds to make certain disclosures and reporting, in the interests of transparency, accountability and fair treatment of members.

Guidance Notice 1 of 2019

This Guidance Notice was published on 14 June 2019 by the Regulatory Policy department of the FSCA.

The FSCA has released this note with the intention of giving funds guidance on how a fund's investment philosophy should ensure the sustainability of the fund's investments and assets. The Guidance Notice also covers the FSCA expectations as to fund reporting and disclosure on issues of sustainability.

The Guidance Notice includes definitions of:

- *active ownership* –the prudent fulfilment of responsibilities relating to the ownership of, or interest in, an asset, including identifying sustainability concerns, mechanisms to intervene and engage on the investments and shareholder voting.
- *ESG factors* – environmental, social and governance factors, which in the South African context includes broad-based black economic empowerment.
- *sustainable reporting* – report issued to inform stakeholders about a company's policies, programmes and performance on ESG factors.
- *sustainability* – the ability of a company to conduct its business without compromising on future generations to meet their needs and working for a better long-term outcome. When a fund evaluates a company, it must consider economic and ESG factors in relation to that company.

Regulation 28 of the Pension Funds Act calls on funds to promote the responsible investing of fund assets, based on sustainable, long-term, risk-aligned and liability-driven investment.

Sustainability of investments and assets in the context of a fund's IPS

A fund's IPS should cover how the fund's investment strategy and philosophy seeks to ensure the sustainability of its assets including:

- when the IPS was approved and by whom;
- how often the IPS is reviewed;
- how the fund intends monitoring and evaluating the ongoing sustainability of its investments;
- the extent to which ESG factors have been considered; and
- its active ownership policy.

If a fund invests in assets that limit the application of ESG, active ownership or sustainability, the IPS should say:

- why this limitation is in the best interest of the fund and its members; or
- what remedial action is being taken to rectify the position.

Disclosure

In the interest of transparency, accountability and fair treatment of members, funds are encouraged to:

- make a copy of the IPS or an abridged version of it available to members at no cost;
- put the IPS on the fund's website (if it has one); and
- annually inform stakeholders of the contents of the IPS and changes to it.

Reporting

The FSCA has requested funds to report on how their IPS complies with the Guidance Notice.

Funds are encouraged to include feedback on the IPS in the fund's annual financial statements. That feedback should include:

- confirmation that members who asked for a copy of the IPS received it;
- any changes in the last year to the IPS; and
- assets held in compliance with Guidance Notice and their value.

Comment: the FSCA is required to release draft Conduct Standards for public comment and they must go through a Parliamentary process before Conduct Standards are released and are binding on funds. There is no requirement for the FSCA to get public feedback on a Guidance Notice.

If you need more information, please contact your consultant.
