PRI | Principles for Responsible Investment

CONSULTATION RESPONSE

CRISA CODE FOR RESPONSIBLE INVESTMENT IN SOUTH AFRICA

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PRI Association

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INTRODUCTION

The United Nations-supported Principles for Responsible Investment (PRI) is the world's leading initiative on responsible investment. The PRI has over 3,000 signatories (pension funds, insurers, investment managers and service providers) globally with approximately US $100 trillion in assets under management.[1]

The PRI works with its international network of signatories to put the six Principles for Responsible Investment into practice. Its goals are to understand the investment implications of environmental, social and governance (ESG) issues and to support signatories in integrating these issues into investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society. The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a menu of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system.

This consultation response represents the view of the PRI Association and not necessarily the views of its individual members.

More information: www.unpri.org

ABOUT THIS CONSULTATION

The Code for Responsible Investing South Africa (CRISA) Code was first issued in 2011 and aimed at providing guidance to institutional investors on the execution of investment analysis and investment activities, and the exercise of rights to promote sound governance. Recognising the development in stewardship and responsible investment in years since, the CRISA Committee have issued a revised Code for feedback, such that the CRISA Code can be used by investors to support corporate governance in South Africa as well as the evolution of stewardship and responsible investment for a more inclusive and equitable economy.

SUMMARY OF PRI'S RESPONSE TO THE DRAFT CODE

We strongly support contents of the revised draft code, including but not limited to; an outcomes-based approach that encourages pursuit of positive outcomes across impact, inclusion, innovation and resilience,[2] and an "apply and explain" disclosure standard that allows sufficient flexibility to be applied proportionately across different assets and types of organisations. The revised CRISA code rightly recognises and reflects significant developments of the last decade on sustainable finance.

The central recommendation of the PRI's response is that the CRISA Committee should establish more robust oversight of the Code for greater effectiveness by formalising the process to become a signatory to the Code. We acknowledge the ongoing organisational structure review and believe this could be used as an opportunity to strengthen oversight of the Code. We also provide some recommendations for amendments to the Code wording on stewardship.

Our more detailed answers and recommendations below are in response to selected questions from the consultation that draw on specific expertise and evidence from the PRI's work.

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[1] See https://www.unpri.org/signatory-directory/

[2] CRISA Code for Responsible Investment in South Africa Revision Consultation Draft November 2020, page 10.

PRI'S RESPONSE TO SELECTED QUESTIONS

Question 2: Application of the revised Code

a) Do you agree with the flexible and universal approach to application and adoption?

We agree with the proposed approach for application of the Code on a proportionate basis. It is important that factors such as the size and type of organisation and its investment philosophy and style, should not limit application of the Code. We agree with the "apply and explain" approach.

We recommend that there should be increased oversight of the Code and the introduction of a mechanism for organisations to formally become approved signatories to the Code. Without this the Code will be limited in its effectiveness. The objectives of the revised Code address some of the most important issues for the future of sustainable finance and economic development in South Africa. We believe that voluntary tools like the CRISA Code are critical to ensure the finance sector delivers for beneficiaries, supports sustainable development and the wider economy. Measures will only drive capital flows to the extent that these investments are incentivised or rewarded. In this context, we believe it is appropriate to ensure the Code has adequate oversight. Increased oversight and establishing a formalised list of approved CRISA Code signatories will better enable the CRISA committee to ensure quality application of the Code, monitor Code effectiveness, and encourage transparency of the activities of investors, which in turn also strengthens scrutiny on corporate governance, and encourages high standards among investors.

b) Should the Code contain targeted recommendations for different investment categories or types of investment organisations, or should these be dealt with in separate guidance?

We recommend that the Code principles set clear and ambitious expectations on stewardship activities across the investment chain without being too prescriptive, that will enable organisations' application of the principles to evolve. Stewardship practices should be a source of competitive differentiation, particularly among investment managers. It is important that signing the Code is a meaningful activity, and that high quality reporting against it enables stewardship practices to be clearly understood and assessed. We believe that the implementation and reporting notes under the principles do support that aim. We have no strong view on whether separate guidance is issued but note that in response to feedback on guidance for the UK Code, the Financial Reporting Council opted to remove separate guidance in issuance of the UK Stewardship Code 2020, instead providing supporting text alongside the principles.[3] The CRISA Committee should determine what will be most effective in the South African context and for organisations applying the Code.

c) Is the approach to application on a proportionate basis sufficiently clear?

The PRI recommends that signatories should be required to apply all principles of the Code and that this can be done in a manner appropriate to the organisations' size and operations, taking a proportionate approach across asset classes, which can be determined by the organisation applying the Code. We recommend that those applying the Code are required to provide transparent disclosure about how and to what proportion of assets the Code is applied. This could be included in the reporting segment of Principle 4.

Question 4: Principle 1 Integrating sustainable finance

Do you have any comments on Principle 1 and the practice recommendations for implementation and reporting?

[3] FRC Feedback Statement, October 2019, page 5.

The PRI strongly supports the Code requirement for systematic and explicit integration of ESG and broader sustainable development considerations, and the inclusion of issues that have market-wide or systemic impacts.

Question 5: Principle 2 Diligent stewardship

Do you have any comments on Principle 2 and the practice recommendations for implementation and reporting?

The PRI strongly supports the Code's recommendations for signatories to demonstrate how they are discharging their stewardship duties when seeking to identify and address material ESG issues and broader sustainable development considerations. Stewardship is one of the most effective mechanisms that investors have to address material ESG risks, whilst also driving real-world outcomes that create long-term value for clients and beneficiaries.

We support the recommendation that organisations applying the Code disclose policies regarding how they exercise and discharge their stewardship responsibilities in the form of engagement and voting. Important aspects of institutional investors' engagement and voting policies include how they set objectives for their engagement activities with issuers, what tools they use to achieve these objectives, and how they assess whether these objectives are met. The PRI report "A practical guide to active ownership in listed equity" provides guidance on what institutional investors should include in their engagement and voting policies.

We also strongly support the revised Code's recommendations that organisations report on how these policies were implemented, as well as on the outcomes of stewardship activities, during the reporting period. To ensure that stewardship activities support the Code's focus on outcomes, it is important that this is included in organisations' engagement and voting policies. Good quality and regular reporting on the outcomes of stewardship activities is vital to enable asset owners/institutional investors to monitor their managers/service providers to ensure that these activities are aligned with beneficiaries' interests.

We recommend that Principle 2 includes investors' disclosure on both how they intend to escalate engagement efforts, should they fail to see progress towards meeting the engagement objectives, and how stewardship is linked to investment decision-making activities.

In addition, we recommend either removing or amending Lines 220 and 221/Paragraph 2.7 to explicitly emphasise the quality of engagement. We believe that high quality engagement, well-considered voting, and well-informed investors will be more effective in creating value for clients and beneficiaries than a focus on the quantity of stewardship. This should help to reduce the risk of incentivising focus on the quantity of engagement, over the quality and effectiveness of stewardship in achieving the stated outcomes.

Lastly, we recommend that the revised CRISA code make explicit reference to engagement with policymakers and standard setters. This recognises that in some circumstances institutional investors' engagement with these non-issuer stakeholders can be a more effective, if not necessary, way of addressing material ESG issues and broader sustainable development considerations to create long-term value. In this sense, PRI uses a broader definition of stewardship than is presented in the revised the Code.

Question 6: Principle 3 Capacity building and collaboration

Do you have any comments on Principle 3 and the practice recommendations for implementation and reporting?

We support the revised Code's recognition of collaboration, and particularly the role that collaboration amongst investors can play in enhancing the impact and weight of engagement dialogue. Collaborative engagement is one of the most effective ways of engaging with issuers, this has a number of benefits including: sharing the costs of engagement amongst a wider number of investors, enhancing the legitimacy and influence of investors with the issuer, and pooling knowledge and resources. It is also a more effective mechanism for issuers to engage with a range of their investors and shareholders, enabling them to gain clarity on investors' expectations around material ESG issues and reducing the number of meetings they undertake with investors on the same issues. Successful collaborative engagement has positive effects on financial performance (Dimson et al. 2021 Coordinated engagements). Collaborative engagement is also vital for investors to engage in addressing systemic risks which affect the overall market, this is particularly important in the South African context given the disproportionate impacts of climate change and inequality.

As the revised Code rightly highlights, investors involved in collaborative engagement should be aware of potential regulatory requirements under aspects of both securities and antitrust law, particularly issues around acting in concert. However, with reference to legal guidance commissioned by PRI and conducted by Bowman's Acting in concert and collaborative shareholder engagement: South Africa we highlight that in many cases, collaborative engagement on ESG issues by shareholders is unlikely to trigger regulatory requirements.

Question 9: General comments

We note that the Code provides a general disclaimer that where there is conflict between the Code and applicable legislative provisions, the legislation will prevail. We recommend the Committee to engage with legislators and policymakers to ensure that the Code is embedded in legal requirements that will take precedent, and to as far as possible eliminate any potential conflicts with legislation.

To date, most stewardship codes have been established as voluntary instruments, although they are increasingly referred to in legislation. We believe that it will be important that the Code’s legal ‘underpinning’ and alignment with legislation is clarified.

We recommend the committee consider and make clear how the Code can support the South African National Framework for Sustainable Development. We believe that stewardship, disclosures, investors duties, taxonomies of sustainable economic activities and national sustainable finance strategies are all important and mutually reinforcing elements of sustainable investment policy and regulation to enable sustainable development.[4] Decisions on the allocation of capital – whether investment capital or capital that supports and enables the functioning of a country’s economic and financial system – are ultimately driven by the views of companies and the finance sector on the risks and opportunities presented by different investments. National frameworks and tools like the CRISA Code are critical to bridge this gap between the finance sector and the wider economy.

We recommend that the Committee might also require organisations to provide sign-off by a member of the C-suite to demonstrate the importance of the revised CRISA Code and the application of its contents for the organisation.

[4] See PRI and World Bank “How Policymakers can Implement Reform for a Sustainable Financial System. Part I: A toolkit for Sustainable Investment Policy and Regulation.”