Responsible investment in 15 pension companies

Report on investigation and case stories about sound practices in the due diligence process

Prepared for

The Danish National Contact Point to the OECD

by

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Background and purpose

On behalf of the Danish National Contact Point to the OECD (the NCP), Carve Consulting has prepared five cases that describe good practices in pension companies working with responsible investment.

The purpose is to show practical examples from the pension companies' due diligence processes relating to responsible investment that can inspire and show investors how they can work with due diligence processes and the OECD guidelines.

The case stories provide an overview of the different steps in the due diligence process and illustrate the methods described in *the Danish Business Authority's Guidance on Responsible Investment (2018).* They describe how responsible investment can be managed in practice and what a number of Danish institutional investors take into account in their work with responsible investment.

Whereas the Guidance to Responsible Investment is written with managers in mind, the selected cases target the people who actually work with responsible investment on a day-to-day basis in both pension companies and other types of companies. They can serve as inspiration both for planning a new approach to investment and for improving existing practices.

The case stories and the underlying investigations were carried out in the period from 8 April to 21 December 2018 by a team of consultants from Carve Consulting.

Focus and content

Each of the five cases focuses on a specific step in the due diligence process. The first case thus focuses on the pension company's policies and how they have been embedded in the organisation; the second focuses on screening, risk analysis and prioritisation of potential adverse impact; the third focuses on how an actual adverse impact is handled; the fourth focuses on communication and reporting, and the last case focuses on complaints procedures and the role of the NCP in the handling of complaints about the adverse impact of investments caused by internal and external players.

Each case is thus a practical example of how a company can work with due diligence in the different steps of the process.

Methodology

Based on the NCP's wish to communicate good practice from Danish companies, primarily pension companies making responsible investments, has Carve Consulting carried out a survey of 15 pension companies' work with responsible investment.

On the basis of this survey, Carve Consulting selected eight companies for further investigation to find out if the way they handled responsible investment reflected good practice. Among these pension companies, Carve Consulting carried out interviews with five companies, which then formed the basis for the case stories. All companies have had the opportunity to read their case stories to ensure that their practices are correctly described.

The investigated pension companies

The pension companies were selected on the basis of their market share. The chosen cut-off point was a 2% market share in 2017 thus, all the investigated companies had a market share of 2% or more. Extracts from the list of pension companies with activities in Denmark published by Insurance and Pension Denmark were used to make the selection.[1]

The following pension companies were surveyed:

- AP Pension
- Danica
- Industriens Pension
- Lærernes Pension
- MP Pension
- Pensam Pension
- PensionDenmark
- PFA Pension
- PKA
- P+
- Sampension
- SEB Pension
- Skandia
- Topdanmark Pension
- Velliv[2]

Criteria applied

The due diligence processes of the 15 companies in relation to responsible investment were assessed on the basis of 12 criteria. The criteria reflect the four steps in a risk-based due diligence process described in the Danish Business Authority's Guidance on Responsible Investment (2018). They cover policies on responsible investment, identification and prioritisation of potential adverse impact, the handling of actual adverse impact and communication and reporting about activities and the results of the work with responsible investment.

An additional criterion is complaints procedures for internal and external stakeholders who become aware of breaches of the OECD Guidelines for Multinational Enterprises or disregard for other standards for responsible investment. This criterion was inspired by the OECD's complaints mechanism for violations of the OECD Guidelines for Multinational Enterprises, of which the NCP is a part, and the UN Guiding Principles for Business and Human Rights,

[1] Pension companies – market shares, Insurance and Pension Denmark, published 28 August 2018. http://admin.forsikringogpension.dk/presse/Statistik_og_Analyse/statistik/pension/markedsandele/Sider/Pensionsselskaber-markedsandelse.aspx

[2] Velliv is the result of an acquisition by Nordea Liv & Pension during the period 2017-18. In the screening process, Velliv was treated as an independent entity, unrelated to the former Nordea Liv & Pension or the Nordea Group. Velliv was therefore assessed entirely on the basis of its own policy for responsible investment.

which require that companies must establish complaints mechanisms for reporting of human rights violations.

The investigation of whether the 15 pension companies comply with the mentioned criteria was based on material available about the companies' responsible investments, including in their annual and interim reports, reports on good governance, annual CSR reports, COP reports to the UN Global Compact, PRI reports and other material available on the companies' websites, including policies and other internal regulations as well as communication about the work carried out and the results achieved.

The criteria applied were formulated as questions that could only be answered with a yes or no. The purpose of this was to make it possible to quantify the degree of compliance. The assessment reflects the conclusions of the individual Carve consultant. The assessment was supported by detailed explanations of the 12 criteria and information about relevant Danish recommendations and international standards. All assessments have been subject to quality assurance by one or two other consultants and have been discussed at project team meetings.

The assessment is pragmatic and based on whether the available material about the company describes in sufficient detail how the work is carried out in practice.

Case stories

Based on the investigation, five companies were selected to illustrate how the mentioned five steps in the due diligence process for responsible investment can be carried out in practice. The five companies were selected on the basis of a number of criteria for good practice.[3]

Transferable: The company's due diligence processes are relevant to other financial companies and can inspire other industries to apply responsible investment processes.

Accurate: Communication and reporting are clear and accurate. Superfluous information is limited to a minimum, and the report gives the reader a good understanding of the company's impact on humans, the environment and the economy.

Cost-effective: The company uses transparent and easily accessible standards and criteria such as OECD, UNGP, GRI or International ESG standards.

Robust: The due diligence processes are embedded in the organisation by means of policies, procedures, controls and documentation and are integrated into the strategic portfolio planning and day-to-day operations.

The criteria were used as guidelines and not to rate the work of the investigated companies. The reason for this is that the companies are reluctant to describe their own work as good practice. Instead, they point out that due diligence in responsible investment is an ongoing process in most companies and still being developed.

[3] The chosen criteria for good practice are based on evaluation criteria recommended by the OECD (DAC OECD 2010) and the EU's guidelines for non-financial reporting (DG FISMA 2017).

The case stories are therefore both examples of good practice where the work has become an established procedure which is carried out systematically, for example by the use of policies, screening and communication, and examples of how risks and complaints are handled in a more informal manner as and when they arise.

The pension companies selected for the case stories include PFA (policy), MP Pension (potential adverse impact), Skandia (actual adverse impact), P+(DIP/JØP) (communication) and Sampension (complaints procedures).

Assessments and results

The criteria applied include five main groups, each consisting of 2 or 3 questions. The questions are shown below accompanied by the explanatory text, the total overall assessment of the work of the pension companies as well as a result summary.

POLICY

1a) Does the pension company have a policy for responsible investment?

Explanatory text: It can be either a stand-alone policy for responsible investment or a section about responsible investment in a general CSR policy.

The policy should:

- Describe the expectations to conduct both internally and in portfolio companies
- Describe due diligence processes
- Describe requirements to active ownership
- Have been adopted by the top management level
- Have been published
- Be integrated into relevant management systems
- Be embedded in procedures
- Be complied with on a daily basis by the pension company as well as its portfolio companies.

In order for the company to be given a “yes”, the report must include information about all the above points.

Assessment: A “yes” was primarily given to companies with a stand-alone policy. Some were given a “yes” despite not having a stand-alone policy, as their guidelines or principles were described in detail on their website or in a report.

Results: Almost two thirds of the investigated companies (73% corresponding to 11 companies) have adopted a policy for responsible investment.

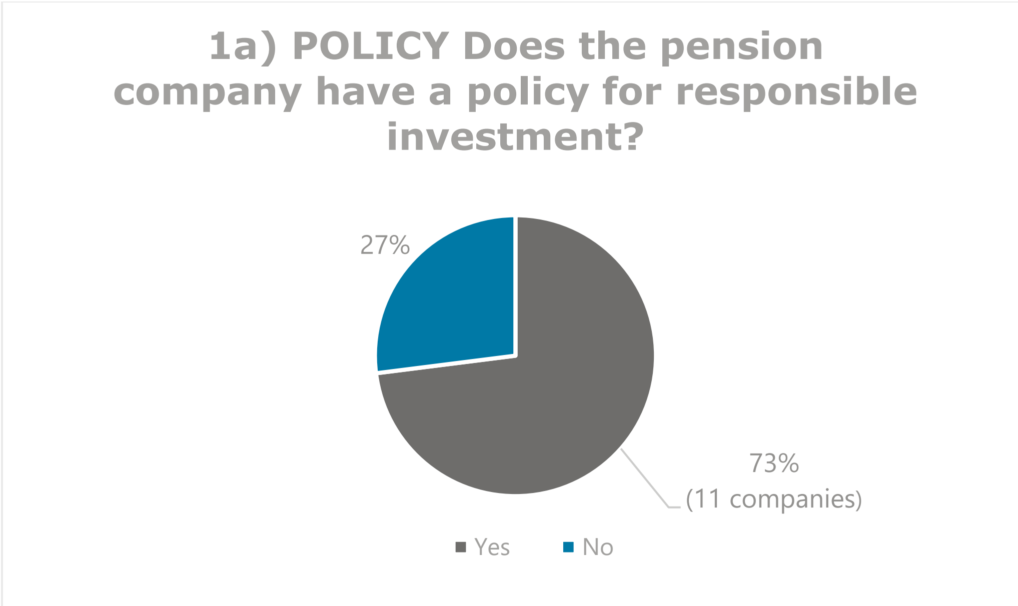

Figure 1 Policy – result 1a)

1b) Does the policy cover the four CSR themes or the three ESG themes?

Explanatory text: The policy must cover adverse impact on:

The following four CSR areas:

- Environment and climate
- Social and working conditions
- Human rights
- Anti-corruption

Or

The following three ESG areas:

- Environmental factors
- Social factors
- Governance factors

If the pension company does not publish information about its work with the four CSR themes or the three ESG themes in connection with its responsible investments, the answer to this question is "no".

Assessment: All companies with a policy were given a "yes", as they all focus on either CSR or ESG themes.

Results: Among the investigated companies, 80% (12 companies) informed that their work was based on either CSR or ESG themes.

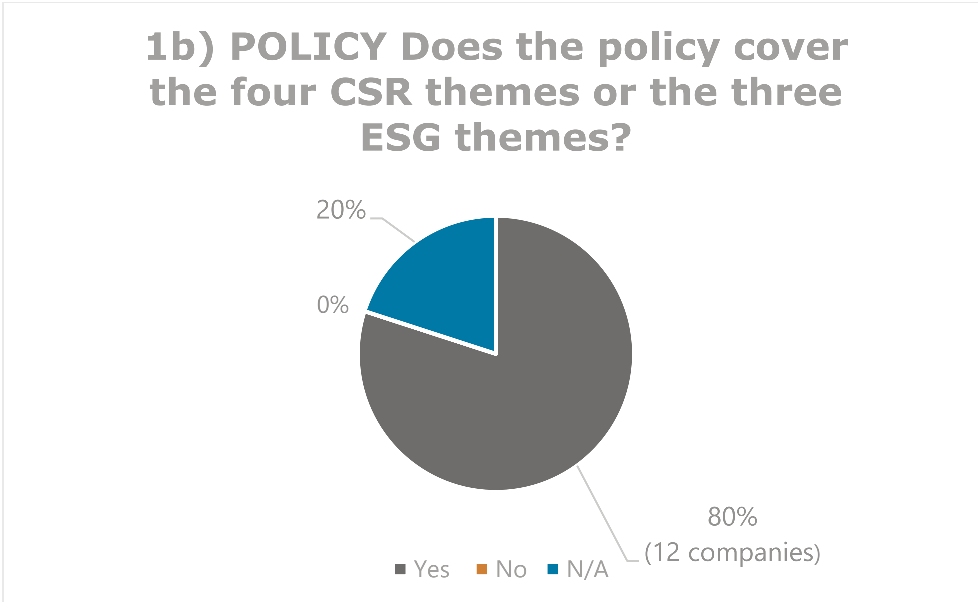

Figure 2 Policy – result 1b)

1c) Has the pension company adopted a policy for active ownership?

Explanatory text: It can be either a stand-alone policy on active ownership or a section in a policy on responsible investment.

Assessment: For the answer to be "yes", the pension company must give explicit information about active ownership. A "yes" was only given to companies with a stand-alone policy where the information was not merely an explanation or part of the policy on responsible investment.

Results: About half of the 15 companies (47% corresponding to 7 companies) have adopted a stand-alone policy for active ownership.

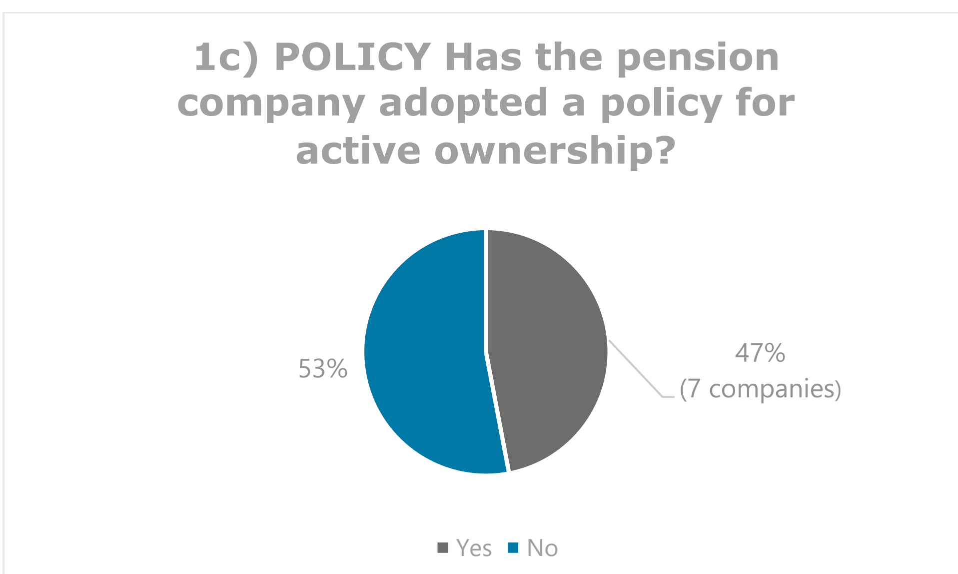

Figure 3 Policy – result 1c)

POTENTIAL ADVERSE IMPACT

2a) Does the pension company use and describe processes for due diligence in relation to adverse impact?

Explanatory text: The pension company must describe the process used to identify and prioritise potential adverse impact.

The description must explain how to plan the process to ensure that:

- It is risk-based
- It maps the areas (geographically, sector, company), where the risk of adverse impact on society is highest
- It gives top priority to high-risk areas

Assessment: The answer was "yes" for all companies that describe the process in full or in part, regardless of the degree of detail. One important factor in the assessment was whether the companies have a process for identifying sector-specific or geographically determined risks, for screening the portfolios for adverse impact, and for prioritising the work, if necessary with the help of external agencies or asset managers.

Results: The vast majority of the companies (87% corresponding to 13 companies) describe their due diligence processes and how they are applied.

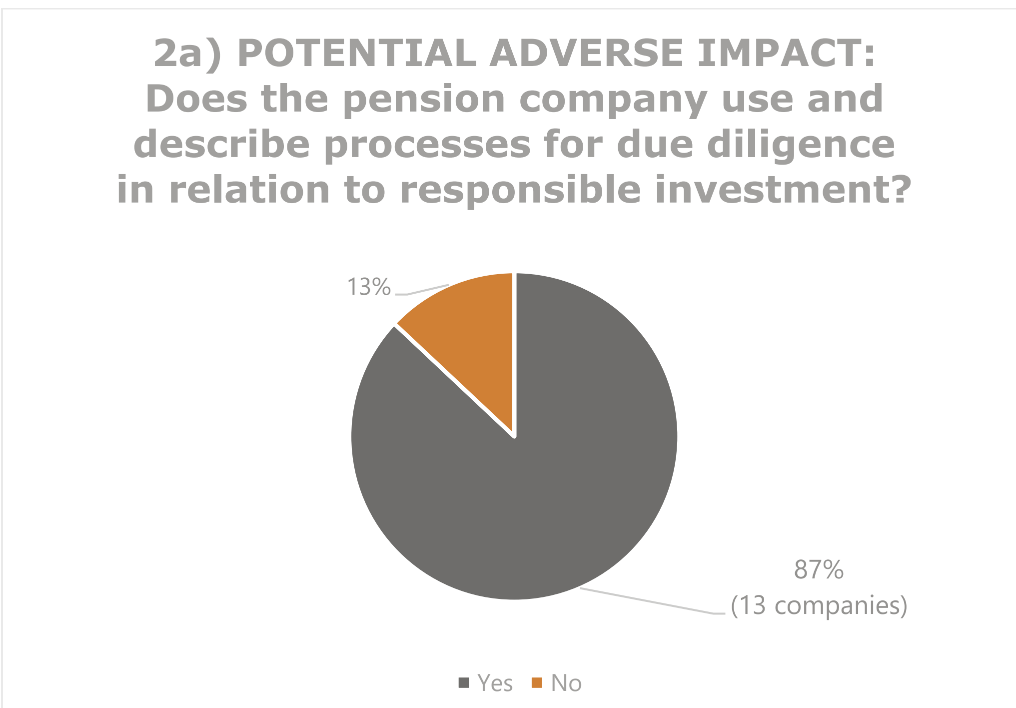

Figure 4 Potential adverse impact – result 2a)

2b) Does the process include risk analyses, screening and prioritisation?

Explanatory text: The pension company must describe how they carry out their risk analysis and how they identify any potential adverse impact caused by the company. The company must inform how it uses the risk analysis to screen its portfolios and how it subsequently prioritises its work.

If the description comprises the three steps but without a specific description of the content of each step, the pension company is given a "yes".

Assessment: All companies describing their work have been given a "yes", provided the description is sufficiently detailed and regardless of whether the procedure or work process is described in an annual report, a policy or on the company's website.

Results: Of the companies, 80%, corresponding to 12 companies, describe how they analyse, screen and prioritise potential adverse impact. Of the remaining, one company (7%) does not describe its processes clearly in the company's policies, and two companies (13%) cannot be assessed as they have no policy in this area.

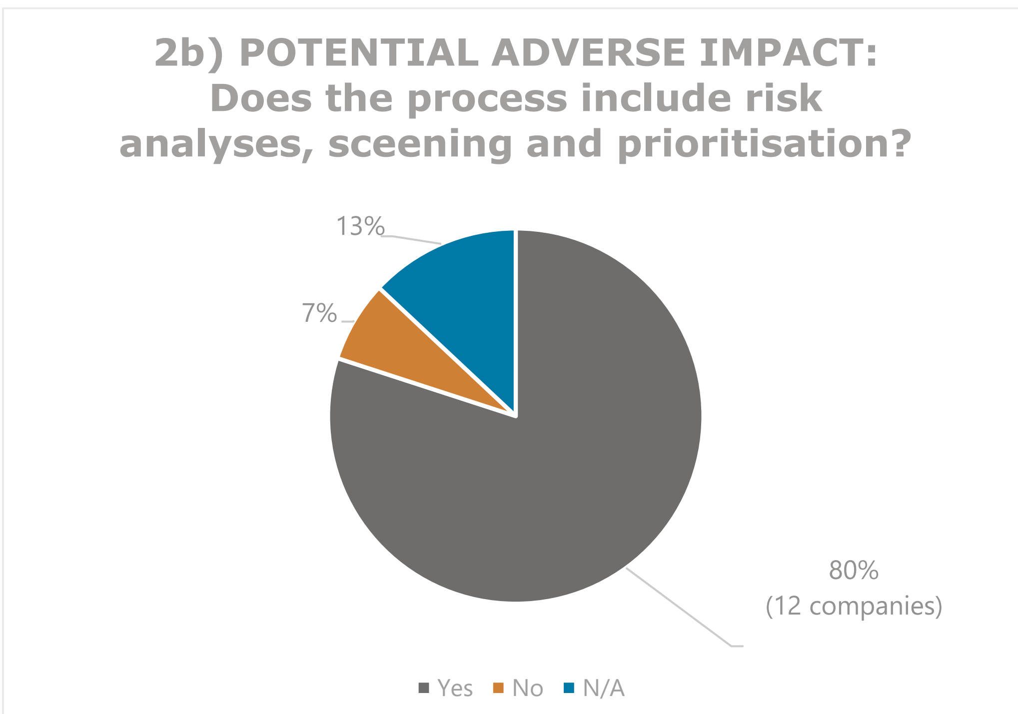

Figure 5 Potential adverse impact – result 2b)

2c) ADVERSE IMPACT: Does the pension company distinguish between potential and actual adverse impact?

Explanatory text: The methods and actions used to handle potential and actual adverse impact vary. The pension company should report separately on the two types of impact and have specific due diligence processes to identify each type.

If the distinction between potential and actual impact is described explicitly or is implicit in the pension company's reports, the answer is "yes".

Assessment: The answer was "no" for all companies except two, because they have failed to make a clear distinction. Several describe "potential and actual" impact in one breath, and the vast majority does not indicate what action is associated with the two types of adverse impact. The answer was "yes" for two companies, because they describe their use of watch lists and focus lists, which indicates that they pay more attention to both potential and actual impact.

Results: Only two companies distinguish between potential and actual adverse impact. The remaining companies do not distinguish (73%) and 13.5% (2 companies) have insufficient information for an assessment.

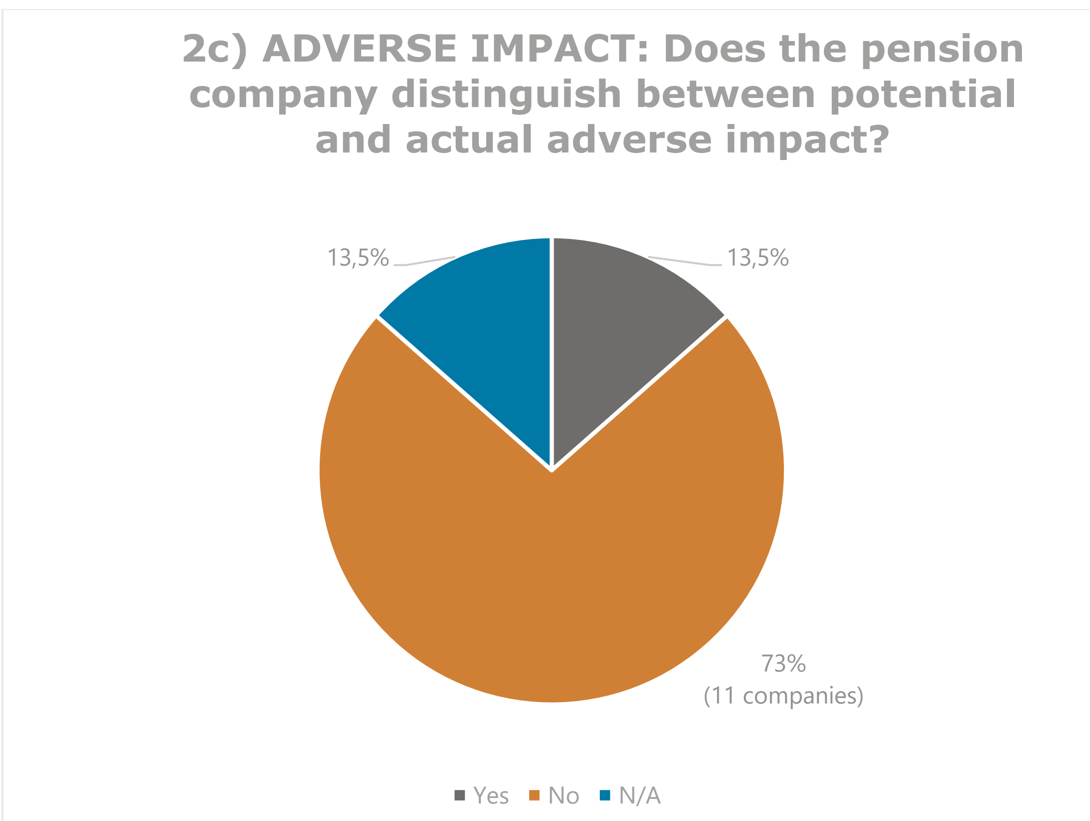

Figure 6 Adverse impact – result 2c)

ACTUAL ADVERSE IMPACT

3a) If the answer to 2a) is YES, is there a connection between the way actual adverse impact is handled and the relationship between the pension company and the portfolio company?

Explanatory text: The relationship between the pension company and the portfolio company may result in the pension company causing actual adverse impact by:

- Being directly connected to the portfolio company through ownership of a minority share
- Contribute, make possible or encourage, e.g. by having considerable influence on the decisions and actions of the portfolio company
- Through own involvement, e.g. through employees, if the pension company has a controlling influence in the portfolio company.

To answer "yes" to the question, the pension company must describe the processes or systems used to assess their own actual adverse impact.

Assessment: The answer was "no" for all companies that do not clearly describe how they handle actual adverse impact and only write about voting at the general meeting.

Results: Only two of the companies specifically address how the relationship between the pension company and the portfolio company works in connection with the handling of actual adverse impact. The remaining companies have either not included sufficient information about the relationship to be given a "yes" (73% or 11 companies), or have not produced relevant information with the effect that an assessment could not be carried out (13.5%).

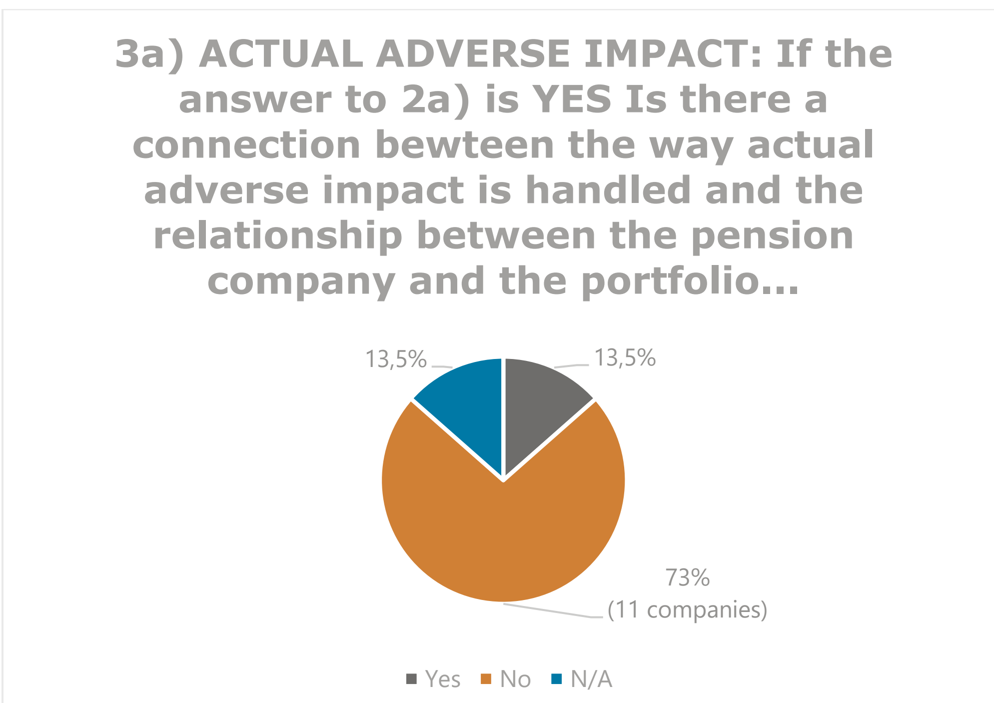

Figure 7 Actual adverse impact – result 3a)

3b) Does the pension company have a plan for preventive and mitigating measures to be taken in the event of actual adverse impact?

Explanatory text: The pension company must describe how they handle their adverse impact using:

- Mitigating measures
- Preventive measures
- Dialogue
- Active ownership (attending general meetings and voting)
- Disinvestment
- Exclusion

For the answer to be "yes", the company must describe action they have taken in response to identified actual impact.

Assessment: The answer was "no" for all companies, because none of them describe more than the possibility of dialogue, escalation, voting and disinvestment. There was thus no description of the process followed in cases where an adverse impact suddenly occurs, or where an identified potential impact is realised and it becomes necessary to mitigate a critical situation.

Results: No companies meet the criterion.

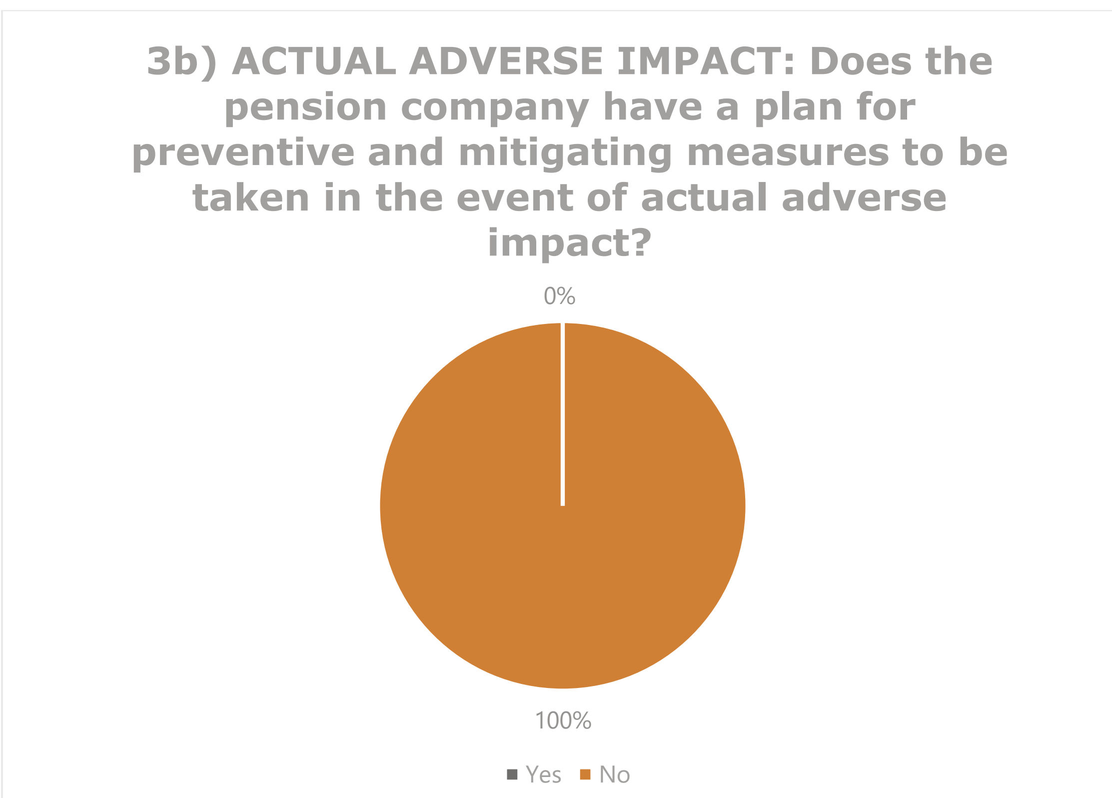

Figure 8 Actual adverse impact – result 3b

COMMUNICATION

4a) Does the pension company inform about responsible investment and active ownership in its annual financial report, CSR report or other annual reports?

Explanatory text: Information about responsible investment must be provided in at least one of the following reports: the financial annual report, CSR report, COP report, PRI report or the report on good governance.

The pension company should not just mention active ownership but describe how it is exercised in the course of the year. This includes:

- Deviations from the policy provisions on active ownership and voting
- The use of advisers to engage in dialogues and to vote

A "yes" requires that this information is published at least once a year in a report or on a website containing information about active ownership, the use of advisers and deviations from the policy.

Assessment: The answer was "yes" for the companies that describe their dialogues and results. The answer was "no" for companies that merely write that a policy exists. None of the investigated pension companies provide financial key figures for their responsible investments.

Results: About two thirds of the companies (67% or 10 companies) provide information about their responsible investments and active ownership in their annual company reports. The remaining 33% (5 companies) do not provide any information about their responsible investment portfolio in their annual reports.

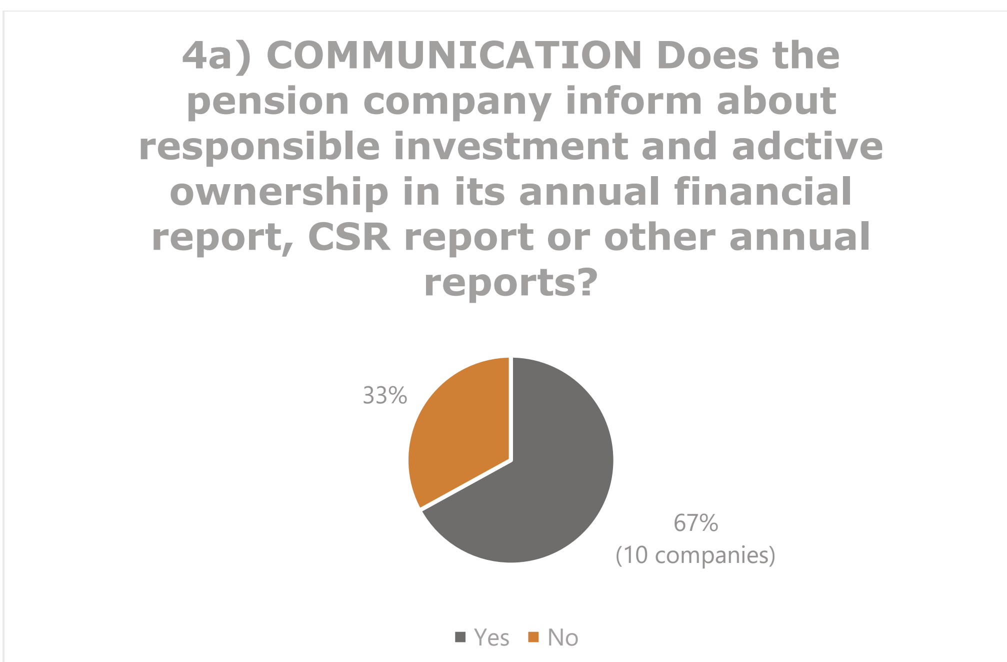

Figure 9 Communication – result 4a)

4b) Does the pension company report more than once a year? For example in an interim report?

Explanatory text: For the answer to be “yes”, the pension company must have published reports on active ownership more than once a year.

Assessment: Almost all the companies’ interim reports follow the same structure. This structure does not include a paradigm for reporting on responsible investment. One company uses the interim report to inform about initiatives and decisions relating to responsible investment.

Results: Most of the companies do not report on their responsible investments in their interim reports (93% corresponding to 14 companies).

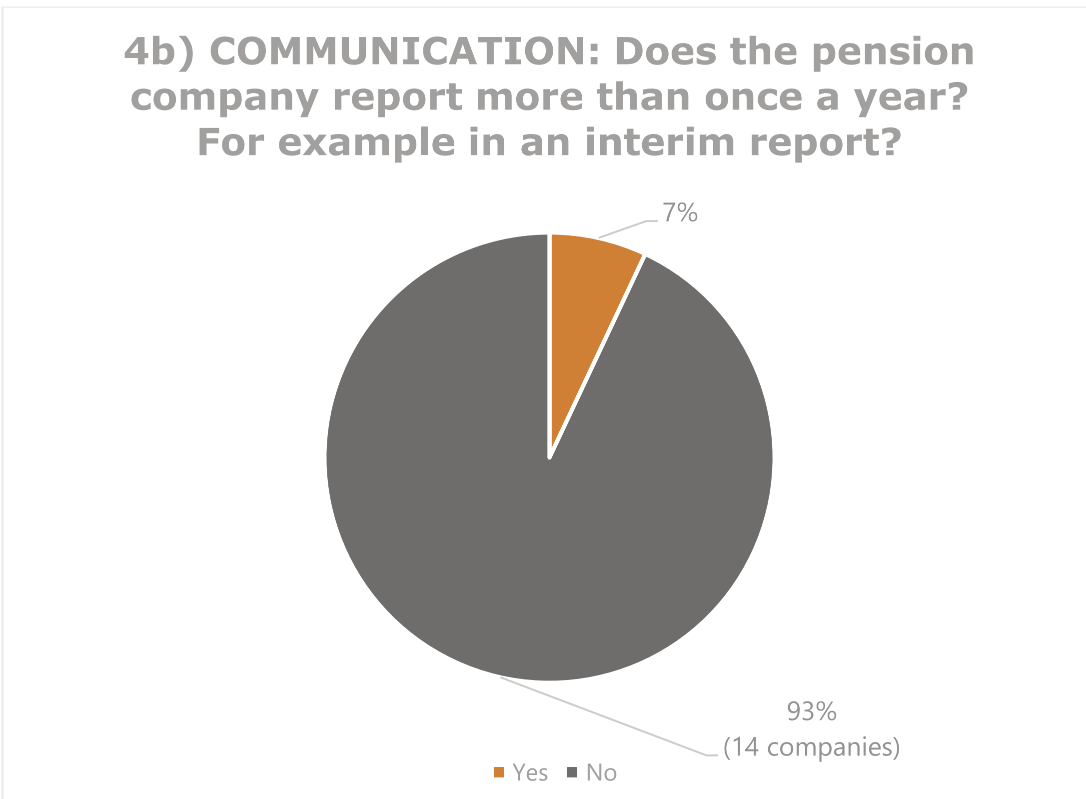

Figure 10 Communication – result 4b)

COMPLAINTS PROCEDURES

5a) Does the pension company have an established procedure for complaints from internal and external stakeholders about responsible investment?

Explanatory text: The pension company should describe how they give internal and external stakeholders an opportunity to complain if standards for responsible investment have been set aside and/or the investment activities have resulted in adverse impact in areas relating to CSR or ESG.

The company can, for example, inform about its procedure for receiving and processing internal claims, e.g. a whistleblower scheme or the use of external legal procedures.

For the answer to this question to be "yes", the company must describe some form of internal complaints procedure or an external complaints procedure in relation to responsible investment in general or more specifically in relation to human rights.

Assessment: Text searches have been carried out for the pension company + complaint, responsible investment + complaint and + whistleblower, but without results. The same keywords were used to search in available reports. These searches reveal that only four companies provide information about their complaints procedures.

Results: Only four of the 15 investigated companies provide information about their complaints procedure for internal and external stakeholders (27%).

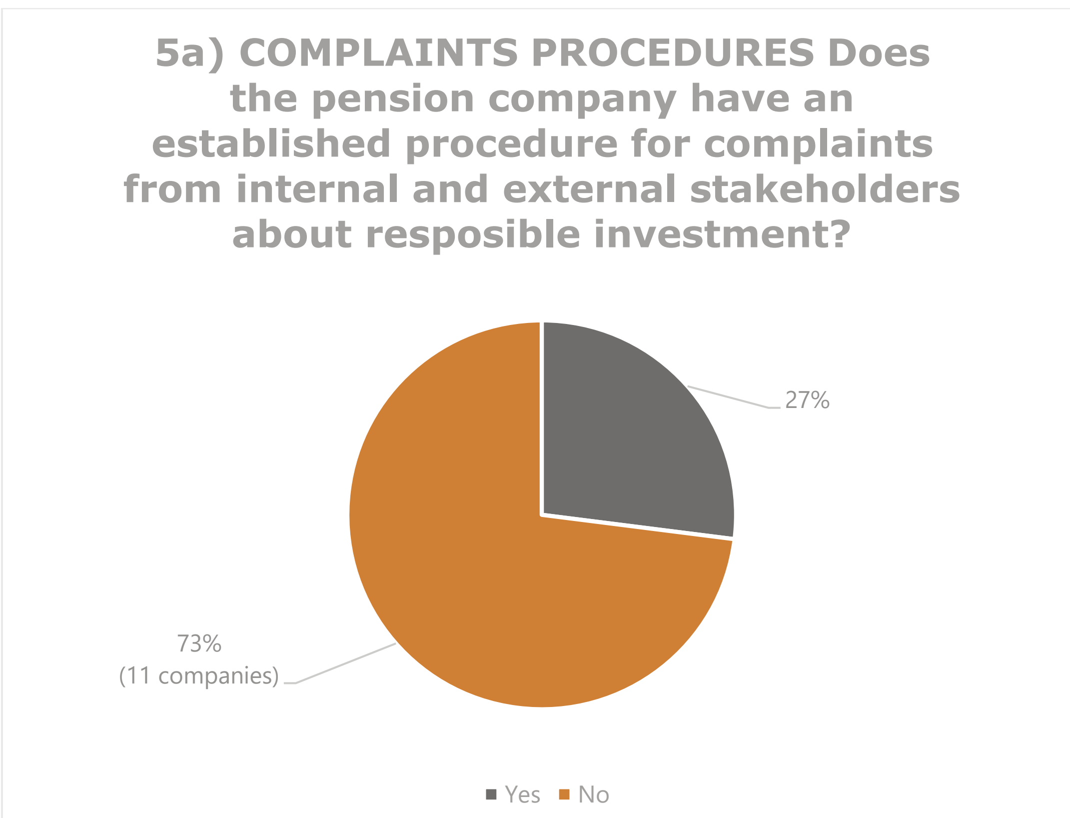

Figure 11 Complaints procedure – result 5a)

5b) Does the pension company provide information about its contact with The NCP?

Explanatory text: The pension company should disclose:

- The number of complaints lodged with the NCP about adverse impact caused by the company's investments
- The scope of the company's dialogue and collaboration with the NCP

The answer is "yes" if the company discloses information about the number of complaints.

The answer is "yes" if the company provides quantitative or qualitative information about complaints and dialogues.

Assessment: Text searches were carried out for the pension company + the NCP and + the Danish National Contact Point. The same keywords were used to search in available reports. The searches show that none of the 15 companies disclose information about their contact with the NCP.

Results: None of the companies inform about current or finalised cases handled by the NCP or about their dialogues and collaboration with the complaints-handling institution.

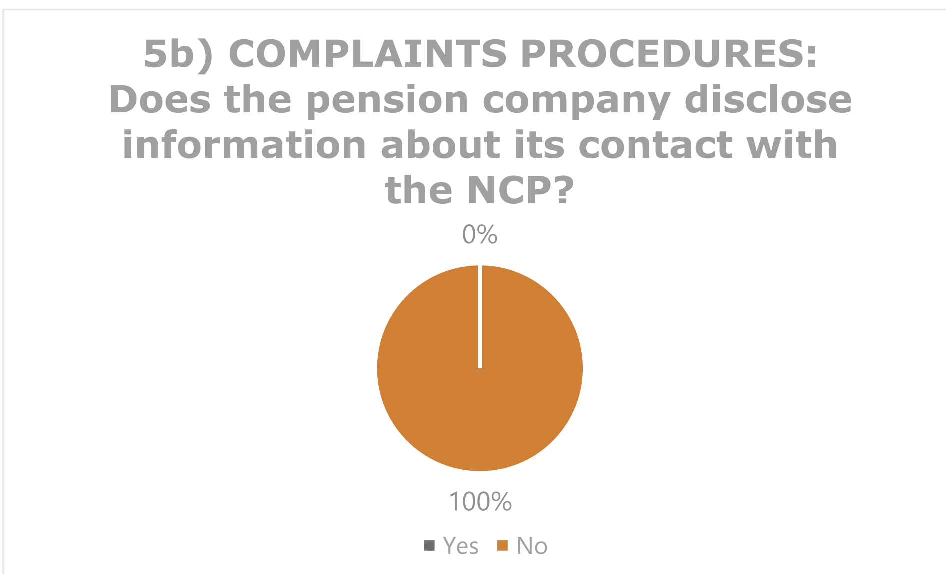

Figure 12 Complaints procedure – result 5b)

Membership of the UN Global Compact and PRI

The investigation of the 15 pension companies included checking whether the pension companies are members of the UN Global Compact and PRI.

Six of the companies are members of the UN Global Compact and eight are members of PRI.

This information was obtained by searching the website of the UN Global Compact and a membership list downloaded from PRI's website.