

PRI RESPONSE TO THE DRAFT REGULATION AMENDING PERU'S PRIVATE PENSION SYSTEM INVESTMENT ADMINISTRATION

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INTRODUCTION

The United Nations-backed Principles for Responsible Investment (PRI)¹ is the world's leading initiative on responsible investment. The PRI has over 3000 signatories (pension funds, insurers, investment managers and service providers) globally with approximately US \$90 trillion assets under management.

Responsible investment explicitly acknowledges the relevance to the investor of environmental, social and governance (ESG) factors in investment decision-making for the long-term health and stability of financial markets.

PRI welcomes the opportunity to respond to the Peruvian Superintendence of Banking, Insurance and Pension Fund Managers (SBS) on amendments of the Compendium of Regulatory Superintendence Standards of the Private Pension Fund Management System that reinforce the concepts of fiduciary responsibility and incorporation of ESG (environmental, social and governance) factors into Pension Fund Managers.²

ABOUT THIS CONSULTATION

Under this proposed regulation SBS aims to introduce for the first time ESG factors into Pension Fund Managers' investment practices. The draft regulation recognises that best market practices have identified ESG factors as influencing investment earnings through their impact on companies' financial performance, and through the risks they pose to economy growth and stability of the financial market. SBS considers therefore that Pension Fund Managers integrate these factors into the investment and risk management of private pension funds.

The draft regulation requires that Pension Fund Managers incorporate ESG in investment and management, and disclose how they do so. The draft regulation states that as of April 1, 2021, Pension Fund Managers must comply with all established provisions for investment management and investment risks in relation to the incorporation of ESG factors.

¹ <https://www.unpri.org/>

² <https://www.sbs.gob.pe/normativa-y-estandares/normativa/prepublicacion-de-proyectos-normativos>

KEY RECOMMENDATIONS

PRI welcomes the proposal to incorporate ESG factors into the investment processes of Pension Fund Managers. This regulatory update will align Peru's pension fund regulatory framework with the modern understanding of investor duties, whereby investors are required to incorporate all value drivers, including environmental, social, and governance (ESG) factors, in investment decision making.³

PRI also welcomes the disclosure requirement for Pension Fund Managers on how they incorporate ESG factors into investment and risk management, as proposed in the draft regulation.

PRI's key recommendation is to clarify in the regulation the scope and definition of investor duties in Peru. The fiduciary duties of institutional investors require them to:

- Incorporate environmental, social and governance (ESG) issues into investment analysis and decision-making processes, consistent with their investment time horizons.
- Encourage high standards of ESG performance in the companies or other entities in which they invest.
- Understand and incorporate beneficiaries' and savers' sustainability-related preferences, regardless of whether these preferences are financially material.
- Support the stability and resilience of the financial system.
- Report on how they have implemented these commitments.

The most common policy reforms on pension fund regulations have been: (a) disclosure requirements, where pension funds are required to disclose their responsible investment commitments and/or how these commitments have been implemented; and (b) regulations that encourage pension funds to adopt responsible investment practices. The Peruvian standard includes ESG factors incorporation, both in investment policies, risk management, stress analysis and within alternative financial instruments. We recommend adding a requirement related to the disclosure of responsible investment policies and practices, and ESG factors materiality in Pension Fund Managers investment practices.

Lastly, we recommend that in addition to this regulation, SBS mandates the disclosures by issuers of comparable, standardised, investment grade ESG data to support Pension Fund Managers' work on ESG incorporation.

DETAILED RESPONSE

The analysis below is specific to the articles that relate to ESG factors set out in this regulation draft.

In Article 100 on "Investment Policies Structure", the regulation draft proposes to incorporate the following text:

"Policy on environmental, social and governance factors:

- **Criteria on the integration of environmental, social and governance factors into the investment process.**
- **Qualitative and quantitative criteria and/or tools used to integrate, evaluate and monitor environmental, social and governance factors in each asset type.**

³ <https://www.unpri.org/policy/fiduciary-duty>

- **Support in the case environmental, social and governance factors that are not integrated, evaluated and monitored in the investment process or in some asset type."**

The PRI recommends to include as part of this article specific definitions aligned with national and international disclosure requirements. Comparable ESG information will support meaningful disclosures for beneficiaries and other market participants.

The PRI also recommends to require the disclosure of this policy and its implementation to beneficiaries and other market participants.

In Article 113 on "Functions of the Investment Risk Unit", the draft regulation proposes to incorporate the following text:

(v) In relation to investment risk management policies and procedure manuals, propose the integration of environmental, social and governance risk, at portfolio, asset type and investment instrument or product level.

w) Periodically assess the impact of environmental, social and governance factors integrations into the portfolio risk profile, in accordance with the policies and procedure manuals defined by the Pension Fund Managers.

As for article 100, we recommend alignment of definitions with national and international ESG disclosure definitions and standards, including with the TCFD framework.

Article 120-A. - Stress test analysis:

The Pension Fund Manager's investment risk unit should conduct, on a monthly basis, a stress test analysis of the investment risks of managed portfolios, including environmental, social and governance factors.

We recommend - as promoted by supervisory guidelines on ESG factors integration into investment and risk management of International Organization of Pension Supervisors- IOPS' guidelines on ESG integration in pension supervision⁴ - to promote that governing bodies of pension funds or asset managers should be encouraged to conduct scenario analysis for each investment strategy. Scenario-based risk analysis should support risk management. Such scenarios should include a variety of factors, including ESG factors (environmental risk scenarios and climate risk in particular) that can cause extraordinary losses or hinder risk control in the investment strategy. The governing bodies of a pension fund or asset managers should use these scenarios to confirm that the particular investment strategy is appropriate, prior to implementation.

Article 171. - General authorisation procedure

d) Alternative instruments for commodities, natural forests or Hedge Funds:

- Type 2 Fund: 2% of Managed Portfolio value.

- Type 3 Fund: 3% of Managed Portfolio value.

⁴ <http://www.iopsweb.org/iops-supervisory-guidelines-esg-factors.htm>

We recommend adding a definition for natural forest and a clarification on which specific investment projects are considered (forest conservation, reforestation, etc.).

This response has been prepared by Arturo Caballero, Programa de Inversión Responsable (PIR)

PRI has experience of public policy on sustainable finance policies and responsible investment across multiple markets, and stands ready to further support the work of SBS to promote sustainable investment in Peru.

Any question or comments can be sent to policy@unpri.org.