

Hon Maryan Street
Minister for ACC



9 April, 2008

Speech

The Challenge of Socially Responsible Investment

Notes for speech delivered by ACC Minister Maryan Street to the Council for Socially Responsible Investment annual conference at AUT University

I'm delighted to address your annual conference today, particularly since, as some of you may be aware, I have taken an active interest in this subject for some time.

As an MP I announced in 2006 that I planned to introduce a member's bill providing a framework for socially responsible investment mandates for the government's Crown Financial Institutions, of which there are five.

That bill went into the ballot, but was withdrawn when I was appointed to Cabinet last year and was given, among other jobs, the ACC portfolio.

ACC is of course one of the organisations which the bill was relevant to and it therefore would have been inappropriate to continue to promote socially responsible investment through a member's bill.

I can assure you that I take the matter seriously wearing my new hat, as do my Cabinet colleagues, and that we are continuing to chart a pathway forward. I'm pleased with the progress being made by ACC and would like to talk about this today.

I would also like to talk a little about KiwiSaver and the good news announced by the New Zealand Superannuation Fund just last week in relation to cluster munitions.

The ACC scheme is funded by the collection of levies. All taxpayers, employers, self-employed people and motor vehicle owners contribute to the ACC scheme. The government also funds part of the scheme in lieu of contributions from people who are non-earners, such as children and the elderly.

Each year ACC collects enough in levies to cover the lifetime costs of the claims it expects to receive that year. Many injuries require ongoing rehabilitation, medical care or earnings replacement for several years or decades after the injury is incurred. The amount collected each year therefore contains a portion intended to cover future costs, and it is this portion that is invested until it is needed.

This process enables ACC to limit the amount of future levies charged and to still maintain a sustainable fund. Investment returns also contribute to levy stability by enabling the organisation to smooth out the ACC levy rates.

Investment returns are a key factor in achieving the goal of a fully funded scheme. The Act requires that by 2014, the Residual Claims Account and the residual claims component of the Motor Vehicle and the Earners' Accounts, be self-funding. ACC is currently managing reserves of \$9.5 billion.

ACC's legal obligations

By law, ACC is obliged to manage its funds as if it were an independent trustee. According to Section 275(1) of the Injury Prevention, Rehabilitation, and Compensation Act 2001:

- "...the Corporation must invest, in the same manner as if it were a trustee, all money received by it in respect of any Account that is not immediately required for expenditure."

At the same time ACC must make a statement relating to ethical investment. Section 272(2)(i) of the same Act requires an investment statement (as part of the statement of intent):

- "... being a statement of policies, standards, and procedures that must include a statement relating to ethical investment for avoiding prejudice to New Zealand's reputation as a responsible member of the world community".

ACC's commitment to ethical investment

ACC has a policy of conducting investment activities in an ethical manner, which avoids prejudice to New Zealand's reputation as a responsible member of the world community.

In particular, ACC aims to ensure its purchase and sale of investments are transacted in an ethical manner, its funds are not invested in activities repugnant to the laws of New Zealand or regarded as unethical by a vast majority of the New Zealand public, and ensure it does not cast proxy votes in favour of such activities.

In keeping with this policy, ACC has resolved to avoid investing in companies whose primary business is to produce, sell or distribute tobacco products.

Current ethical investment policy

ACC's current ethical investment policy was largely formalised in 2001. Since then it has been incorporated in the Investment Manual and Statements of Intent.

The current Ethical Investing Policy ensures:

ACC will conduct its investment activities in an ethical manner which avoids prejudice to New Zealand's reputation as a responsible member of the world community. ACC also has a fiduciary responsibility to maximise the long-term risk-adjusted net return on reserves (relative to the change in value of the funding account liabilities).

High standards of corporate governance and consideration of a company's impact on the community and environment have the potential to protect and enhance long-term investment returns. Consequently, ACC encourages internal and external managers to take environmental, social and governance (ESG) issues into account provided they do not have a material negative impact on either investment risk or return.

In particular, ACC will:

- a) Not invest in activities which it believes are repugnant to the laws of New Zealand or regarded as unethical by a vast majority of the New Zealand public;
- b) Require all internal and external fund managers to transact purchases and sales of investments in an ethical manner;
- c) Instruct internal and external fund managers to avoid investing in companies which:
 - undertake activities which are illegal in the jurisdictions in which the company operates, or which are in contravention of UN sanctions;
 - have a culture of disregard for laws, regulations, good governance procedures or interest of shareholders, unless the manager believes that direct contacts with the management of the company and/or proxy voting will result in improvements to this culture;
 - have been identified by ACC as being contrary to its ethical policy (these companies will be specified in writing);
- d) Encourage internal and external managers to cast proxy votes consistent with the above;
- e) Report on implementation of this policy in the Annual Report.

ACC has resolved to avoid investing in companies whose primary business is to produce, sell or distribute tobacco products.

Responsible investment

Like ACC, other Crown Financial Institutions have statutory requirements for 'ethical investing' and 'avoiding prejudice to New Zealand's reputation'. These are the very basic of requirements in my view. Crown Financial Institutions have, however, actively been responding to government signals about ethical investing in recent years.

In addition, in early 2007, the NZ Superannuation Fund, Government Superannuation Fund and Earthquake Commission were asked by the Minister of Finance to review their approach to responsible investment.

The Minister considers 'responsible investment' as a commitment to supporting good corporate governance practices and to understanding the impact on long-term returns of a company's environmental, social and governance policies. He encouraged those institutions to contribute to the public debate by disclosing their responsible investment policies and by including reporting on implementation as part of their regular reporting.

Since ACC is also committed to the responsible investment of public money and takes a whole-of- government approach towards achieving outcomes, ACC communicates regularly with other Crown Financial Institutions on their investment framework and policies. Similar policies would make it easier to exchange ideas and share resources.

KiwiSaver

So what progress has been made? As of (1 April) last week, providers of KiwiSaver schemes and providers of complying superannuation funds are now required to disclose their approach to responsible investment.

Providers will have to disclose in their investment statements whether or not their investment policies and procedures take into account responsible investment criteria – including environmental, social and governance considerations.

If they do take these considerations into account, they must say where further information can be obtained on the extent to which responsible investment is taken into account in the investment policies and procedures of the fund.

I understand Liam Mason from the Securities Commission is also speaking at this conference to discuss the guidance which is now available to support the industry in meeting its new responsible investment disclosure requirements.

The responsible investment disclosure requirements reflect the fact that growing numbers of investors worldwide want to ensure that their investments support activities or practices that meet their approval.

A similar approach has been taken in a number of other jurisdictions in recent years. For example, in the United Kingdom since 2000, the trustees of occupational and local government pension schemes are required to disclose the extent to which (if at all) they consider social, ethical or environmental issues in their investment process.

The Australian government also requires similar disclosure of all investment product providers, with the addition of labour standards.

A key benefit of disclosure requirements, rather than more onerous restrictions, is that they enable investors to make investment decisions based on their own values, fully informed by a clear understanding of what factors funds take into account when making investments and what companies/industries/sectors/ types of investments they are investing in.

With over 500,000 New Zealanders - across income brackets, age groups and ethnicities – now members of KiwiSaver, this approach enables the diverse range of KiwiSavers to make individual, informed judgements on what type of fund they wish to invest in.

Wearing his Disarmament and Arms Control Minister hat, my colleague Phil Goff last week welcomed the New Zealand Superannuation Fund's announcement that it would divest from companies involved in the production of cluster munitions once a Treaty on the weapons comes into force.

The Treaty, which will be concluded by the end of 2008, stems from the Oslo Process which was started by New Zealand and six other countries last year.

The Board of Guardians, which made the announcement, is by law independent of, and may not be directed by, the government. But the board adheres to a policy of responsible investment and is aware of New Zealand's strong support for a ban on cluster munitions which cause unacceptable harm to civilians.

The Board has already withdrawn investment in companies such as those producing tobacco, whale meat and land mines, on the basis that they do not meet responsible investment standards and it was logical for the board to add cluster munitions to this list because they act like land mines.

Many fail to explode on impact and can remain lethal for decades, triggered off when stumbled upon by civilians long after the conflict in which they were used has ended.

The Dublin Convention next month aims to agree to a treaty which prohibits cluster munitions which cause unacceptable harm to civilians.

ACC initiatives

ACC too has made good progress. In 2006 ACC stopped making investments in tobacco companies. Additionally, in 2007 ACC excluded investments in four companies because of their actual or potential involvement with the production of landmines which was not in compliance with the Ottawa Mine Ban Treaty.

ACC is currently in the process of excluding investments in companies involved with the design, testing, assembly and/or refurbishment of nuclear explosive devices.

In March 2008, ACC became a signatory to the United Nations Principles of Responsible Investing. In doing so, ACC is acting in line with the New Zealand Superannuation Fund (a founding signatory) as well as the Government Superannuation Fund, ASB Community Trust, Earthquake Commission and Trust Waikato (all signatories).

This general framework, released in April 2006, articulates six principles for investors to incorporate environmental, social and governance (ESG) issues into the management of investment portfolios.

The six principles were developed by a group of institutional investors convened by the UN Secretary-General and are familiar to you.

Signing is a public commitment to implementing the principles. Having ESG policies and procedures that are consistent with an internationally accepted standard marks a milestone in the ongoing evolution of ACC's investment policy.

Conclusion

It does need to be acknowledged that decisions on ethical investments can sometimes be complicated by factors such as what to do when one small aspect of a business's operation does not meet the ethical guidelines but the rest do.

As such, the implementation of ethical investment policies will be evolutionary (as opposed to revolutionary) and will require finding the right balance on a number of issues such as:

- What activities do the vast majority of the New Zealand public regard as unethical? Should investments in a company be excluded if the public still actively buys other products of the company?
- Is it better to exclude investments in companies, or invest and engage with the management to try to persuade the company to change?
- How to balance the costs of implementing ethical investing policies (potentially lower returns from exclusions) with the objective of maximising returns (lower returns mean higher future ACC levies)?
- If investments are banned in companies involved with refurbishing nuclear explosive devices on contract to their governments, should investments in bonds issued by those governments also be excluded?

My next step with ACC is to encourage more open reporting on investment policy and practice. More accessible reporting of ACC's investments and disinvestments will help to keep that issue actively in front of both the public and the Government.

Transparency, both in terms of the way financial institutions disclose and report on their investments and in terms of the ability of the public to scrutinise them, is pivotal to ensuring the path towards more socially responsible investment is actually evolutionary.

As I said in the explanatory note to the bill I drafted as an MP, this includes truthful advertising and promotion as well as accurate and accessible financial and performance reporting. It also requires socially responsible consideration of supply and distribution chains, production methods and the impact on local communities.

There is still work to be done and a number of issues to work through before this debate can be said to be resolved in the New Zealand, let alone an international, context. I look forward, as I previously have, to the contributions which will be made through this conference. Keep up the good work!

Media Contact: Ruth Berry: phone (04) 471 9685, 021 833 353