SOCIAL FINANCE

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Stephen Haddrill
Chief Executive
Financial Reporting Council
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2nd March 2018

Dear Mr Haddrill,

I write in response to your consultation on the Proposed Revisions to the UK Corporate Governance Code and the FRS's Consultation on Strategy 2018/21.

Social Finance (www.socialfinance.org.uk) is a not for profit organisation established over ten years ago and regulated by the FCA. We seek to establish new ways of tackling entrenched social problems that are scalable and sustainable. On occasion, this involves raising investment from institutional and retail investors for whom the wider social purpose of an investment is an important motivation to the decision to invest alongside the expected financial return.

In our work, we are aware of a growing appetite from investors, and advisers and fund managers on their behalf, to invest for a wider purpose than purely a financial return. As part of this, investors are keen to identify companies that measure and report on their wider impact on society, and have articulated a strategy for delivering and increasing their positive impact and hold themselves accountable for delivering on this strategy. It is important that companies provide robust information to enable investors to form these judgements and there is therefore a growing need for the better reporting of non-financial outcomes.

I led the product development working group in the recent Government initiaitve to support the emergence of a culture of impact investment. As part of my work, it was clear that high quality non-financial information of this kind will be critical to enable asset manager to create social impact product which adequately reflects the trust vested in them by the investor. Absence of this information risks stifling the growth of large liquid funds which are critical if this type of investment is to flourish in a responsible way.

The need for this information goes further than responding to investors explicity looking to invest for positive social impact. There is increasing demand from all investors for better reporting of non-financial outcomes as a way of better understanding risk. There is a growing appreciation that companies with a developed awareness of their broader impact on all stakeholders, including the communities in which they operate and the resources they consume, deliver financial returns which are more sustainable and therefore lower risk. As Larry Fink, the CEO of Blackrock wrote in his recent 2018 letter to CEOs: "To prosper over time, every company must not only deliver financial performance, but also show how it makes a positive contribution to society. Companies must benefit all of their stakeholders including shareholders, employees, customers and the communities in which they operate." To fail to do so runs the risk that "companies will ultimately lose the license to operate from key stakeholders".

We therefore welcome Principle A of the revised code which clarifies that "the function of a board is to promote the longer term sustainable success of the company, generate value for shareholders and contribute to wider society". We also note the commitment in the FRC Strategy 2018/21 to developing how non-financial reporting is best implemented and that you will monitor emerging practice in this area. We believe that the appropriate reporting should enable investors to understand the social and environmental impact of an enterprise in a much deeper way than simply to fulfil the requirement of ESG screening.

We believe that the United Nations Sustainable Development Goals provide a starting point for an integrated approach to impact reporting. By requiring an enterprise to reflect on all areas of potential impact, it is possible to mitigate the risk that focus is unduly placed on the most positive metrics. While the framework was originally developed to assist governments rather than private sector entities, it is a very helpful starting point and already widely used and acknowledged as coherent. There are a number of tools being developed which aid companies to use the SDGs to guide their own strategic thinking and measurement. (I draw your attention to SDG Compass (https://sdgcompass.org/) and Future Fit (http://futurefitbusiness.org/) in particular).

We note and support the FRC's 'future of corporate reporting' project as key to driving change in the area of non-financial reporting and providing a focal point for collaboration and harmonisation. In the early stages of developing market standards of disclosure, the FRC's leadership in this way is likely to be crucial.

Active engagement by investors with reporting companies - and increased use of non-financial information - is critical to accelerating best practice in this area and should be encouraged, and explicitly referenced, in any revision to the Stewardship Code.

I trust that these responses are of some help to the FRC as they develop their guidance in this important area

[redacted]

David Hutchison
Chief Executive

cc. Catherine Horton, FRC