



Open Report on behalf of Andrew Crookham, Executive Director - Resources

Report to:	Pensions Committee
Date:	16 March 2023
Subject:	Responsible Investment Update Report

Summary:

This paper provides the Committee with an update on Responsible Investment activity during the third quarter of the financial year 2022/23 (October to December inclusive).

Recommendation(s):

The Committee consider the report and discuss the Responsible Investment activity undertaken during the quarter.

Background

1.1 This report provides a summary of various Responsible Investment (RI) activities that have been undertaken on behalf of the Fund during the quarter, and updates the Committee on any new initiatives relating to good stewardship. This includes work by Local Authority Pension Fund Forum (LAPFF), Border to Coast Pensions Partnership (BCPP), Robeco, who are appointed by Border to Coast to provide voting and engagement services, and Legal and General Investment Management.

2.0 Local Authority Pension Fund Forum – RI Activity

2.1 The Fund participates in the Local Authority Pension Fund Forum. LAPFF acts to promote the highest standards of corporate governance to protect the long-term value of local authority pension fund assets. The Forum's current engagement themes include: climate risk, social risk, governance risk and reliable accounting risk. They also act by collaborating with other investors and by responding to governance and industry consultations.

Outcomes Achieved through LAPFF Engagement

2.2 The latest LAPFF engagement report can be found on their website at www.lapfforum.org. Some highlights from the quarter include:

- The annual conference was held in December, this focused on human rights and climate, and covered:
 - Company presentations were given by: Total Energies on their decision to withdraw from Myanmar; and from the Vale Chair about his company's efforts to move on from the 2015 and 2019 tailings dam disasters in Brazil.
 - Topical presentations covered: engaging with non-executive directors on sustainability, executive pay, and racial equity audits. As well as presentations on electric vehicles and the necessary infrastructure and sustainable water use by companies.
 - The conference also considered the growing importance of 'S' in Environment, Social and Governance (ESG) and how the governments 'levelling up' agenda could impact on the LGPS.
- LAPFF engaged with 26 companies on issues ranging from climate change and environmental risk to human rights and supply chain management. Including:
 - Chipotle, the US restaurant chain, on their approach to water stewardship over the last three years. The focus of the engagement has been to encourage the company to undertake a full value chain water risk assessment. During the quarter LAPFF held a follow-up call to measure progress. The company has now completed a materiality assessment covering ingredients, its supply chain and restaurants and has a better understanding of the water related risks facing the business. The next phase of the stewardship plan is to develop context-based targets for specific areas of its operations.
 - A meeting was held with Board Chair at Rolls Royce, covering aspects of business strategy, targets, governance and disclosure. The LAPFF Chair pressed for the board to put the transition plan to the AGM for shareholder approval at a future meeting.
- Other work by LAPFF during the quarter included:
 - Collaborative engagements with Climate Action 100+ members with Lyondell Bassell, the multinational chemicals company, on their decarbonisation strategy and with the steel company ArcelorMittal on implementing Zero-carbon technologies;
 - Supporting fringe events at the political party conferences in the autumn. This year these focused on investing in a just transition following the launch of the All-Party Parliamentary Group for Local Authority Pension Funds Final report from the APPG for Local Authority on 'Responsible Investment in a just transition'; and

- Responding to the LGPS Climate Governance and Reporting consultation. LAPFF welcome the move and have been long time supporters of Task Force on Climate-related Financial Disclosures (TCFD).
- 2.3 Further details on their work during the quarter can be found in the quarterly engagement report. Members of the Committee should contact the author of this report if they would like further information on the Forum's activities.
- 2.4 Annually LAPFF reviews it's workplan for the coming financial year. The workplan for 2023/24 will focus on:
- Responsible Investment, including: Climate and Strategic Resilience, Environmental Protection, and Fair and Just Transition; Human Rights and Employment Practices; and Leadership: Emerging and Developing Initiatives;
 - Promoting Good Governance. Necessary governance practices include adequate board diversity, good practice on anti-bribery and corruption, effective governance of technological development and implementation of this technology, and reliable company accounts. They will undertake engagement activity, attend AGM's and take part in policy engagements;
 - Positioning the Forum, including communication and member services. LAPFF will maintain regular communication with members on engagement objectives, activities, and outcomes, as well as other pension fund-specific collaborations to drive greater momentum and avoid duplication; and
 - Supporting the All-Party Parliamentary Group as a forum to discuss LGPS issues with policymakers and stakeholders.

3.0 Border to Coast Pensions Partnership – RI Activity

- 3.1 Border to Coast is the pooling company chosen by Lincolnshire Pension Fund. Border to Coast is a strong advocate of RI and believe that businesses that are governed well and run in a sustainable way are more resilient, able to survive shocks and have the potential to provide better financial returns for investors. As a representative of asset owners, they practice active ownership by holding companies and asset managers to account on Environmental, Social and Governance (ESG) issues that have the potential to impact corporate value. They also use shareholder rights by voting at company meetings, monitoring companies, carrying out engagement, and litigation.
- 3.2 Their approach to RI and stewardship is set out in their [Responsible Investment Policy](#), [Corporate Governance and Voting Guidelines](#) and [Climate Change Policy](#). These documents can be viewed on the Border to Coast website. They also publish a quarterly stewardship newsletter detailing the activity they have undertaken during the quarter. A copy of the report for the latest quarter can be found at on

their website ([Quarterly Stewardship Report Q4 2022](#)). Highlights from their work during the quarter include:

- An overview of the quarter's RI activity which included: voting and engagement activity during the quarter; the publication of their Responsible Investment Policy, Corporate Governance and Voting Guidelines and Climate Change Policy which all apply from 1 January 2023; confirmation of the continued appointment Robeco to support Border to Coast to meet their active ownership requirements. Border to Coast have also appointed a new Stewardship Manager and were awarded the Best Approach to Responsible Investment at the 2022 LAPF Investments Award.
- An industry update providing details of the UN biodiversity conference (COP15) which took place in Montreal in December. The conference ended with governments reaching a non-binding agreement with the aim of addressing biodiversity loss, restoring ecosystems, and protecting indigenous rights. The Emerging Markets Just Transition Investor Initiative, and RI reporting requirement framework which makes arrangements around investing responsibly more formal.
- High level information on voting activity for the quarter across all Border to Coast funds. Border to Coast voted at 124 meetings during the quarter, covering 1,044 agenda items. In 44% of meetings Border to Coast cast at least one vote against the recommendations of management.
- Engagement activity, which included 279 engagements, carried out by: external managers appointed by Border to Coast; Robeco, as the Pool's engagement and voting manager; internal portfolio managers; and by LAPFF.

4.0 Robeco – RI Activity

- 4.1 In addition to the direct RI work undertaken by Border to Coast, they have appointed Robeco to provide voting and engagement services. A copy of their quarterly activity report can be found on the Border to Coast website ([Robeco Quarterly Active Ownership Report Q4 2022](#)).
- 4.2 During the quarter Robeco have voted at 126 AGM's, the percentage of meetings where they have at least one vote against management is 44%. During the quarter they have engaged with companies on 77 occasions on topics including: the environment, social and corporate governance matters. This quarter's report provides details on the social impact of artificial intelligence, social impact of gaming, biodiversity, and corporate governance in Asia.

5.0 Legal and General Investment Management – RI Activity

- 5.1 Legal and General Investment Management (LGIM) manage 15% of the Fund's portfolio, which is invested in the Future World Fund (global equities). The Future World Fund invests systematically in a globally diversified portfolio of quoted company shares. The index is designed to favour investment in companies which exhibit characteristics that have historically led to higher returns or lower risk than the market as a whole, and companies which are less carbon-intensive or earn green revenues. LGIM also builds ESG factors and responsible investing into all its investment activity. More information on this can be found on their website: [LGIM Responsible Investing](#).
- 5.2 On a quarterly basis they publish an ESG Impact Report ([LGIM Quarterly ESG Impact Report Q4 2022](#)) detailing their activity during the quarter, across all their investment products. The report covers the key activity from their Investment Stewardship team, details of their Climate Impact Pledge, participation in COP27 and COP15, and information on significant votes. During the quarter LGIM engaged 891 times with 665 companies on topics including: climate change, remuneration, gender diversity, board composition and strategy.
- 5.3 LGIM also produce an ESG Report specifically for the Future World Fund. This details key ESG metrics including carbon footprint and weighted average carbon intensity data, as well as voting and engagements statistics for the last 12 months. This report is available on the LGIM website ([Future World Fund ESG Report Q4 2022](#)).

6.0 Voting

- 6.1 To enable the Fund to fulfil its stewardship responsibilities as an active shareholder, the active equity managers are required to report on their voting on a quarterly basis.
- 6.2 Border to Coast has produced summary proxy voting reports, which are attached at appendix A (Global Equity Alpha) and B (UK Listed Equities). Full details of the votes cast during the period October to December 2022 can be found on the Border to Coast website: [Integrated Full Details Voting Report Q4 2022](#).

7.0 Border to Coast Environmental, Social and Governance (ESG) Reporting

- 7.1 Border to Coast have worked with MSCI, the investment research company, to provide quarterly ESG and carbon reports. The reports include an ESG rating, weighted score for the quarter and the direction of travel, as well as information on the best and worse companies in the sub-fund. The report also includes details on carbon emissions and intensity.

7.2 For the quarter ended 31 December 2022 the ESG reports can be found at:

- Appendix C: Global Equity Alpha Sub-fund;
- Appendix D: UK Listed Equity Sub-fund; and
- Appendix E: Sterling Investment Grade Credit Sub-fund.

7.3 *“This disclosure was developed using information from MSCI ESG Research LLC or its affiliates or information providers. Although Lincolnshire County Council Pension Fund information providers, including without limitation, MSCI ESG Research LLC and its affiliates (the “ESG Parties”), obtain information (the “Information”) from sources they consider reliable, none of the ESG Parties warrants or guarantees the originality, accuracy and/or completeness, of any data herein and expressly disclaim all express or implied warranties, including those of merchantability and fitness for a particular purpose. The Information may only be used for your internal use, may not be reproduced or re-disseminated in any form* and may not be used as a basis for, or a component of, any financial instruments or products or indices. Further, none of the Information can in and of itself be used to determine which securities to buy or sell or when to buy or sell them. None of the ESG Parties shall have any liability for any errors or omissions in connection with any data herein, or any liability for any direct, indirect, special, punitive, consequential or any other damages (including lost profits) even if notified of the possibility of such damages.”*

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7.4 In summary:

- Global Equity Alpha – the fund weighting remains at ‘AAA’, and following the positive impacts associated with the restructure of the Fund and upgrades to key positions held, including Amazon and Mckesson during the period, the weighted ESG score increased and remains above the benchmark.

The increased ESG score, and overall rating occurred despite increased exposure to CCC rated companies. The restructure of the Fund to include a specific allocation to emerging markets means that the Fund now holds companies that are deemed by MSCI to lag global peers on ESG related risk metrics and mitigation strategies. However, the weighting to emerging markets remains underweight versus the benchmark and therefore the impact of the exposure to these laggard companies is marginal.

Carbon metrics once again saw mixed changes over the period. Portfolio carbon emissions fell during the quarter, while Weighted Average Carbon Intensity (WACI) increased marginally. Both metrics were driven by the impact of the Fund restructure and serve to highlight the challenges associated with calculation methodologies and allocation basis of emissions. Exposure to fossil fuel reserves was stable over the period.

- UK Listed Equity – the ESG weighted score remained consistent in the quarter, retaining its ‘AAA’ rating and is slightly above the benchmark. This is due to the fund holding a higher weighting of companies considered to be ‘Leaders’ and no ‘Laggards’. There were several company upgrades in the quarter, including Unilever and Derwent London to ‘AAA’.

The Fund is currently below, or in-line with, the benchmark for carbon emissions, carbon intensity and WACI. All carbon metrics remained level when compared to last quarter.

Sterling Investment Grade Credit – the fund scores below the benchmark on a weighted ESG score basis, driven primarily by an overweight position in UK government bonds (rated A) against an underweight position in European Investment Bank bonds (rated AAA). Despite this, the Fund has increased its overall rating to ‘AAA’.

This quarter sees a material increase in data availability due to the inclusion of subsidiary mapping of issuers to parent companies. This data has been monitored over the past year and can demonstrate that there is no decrease in the quality of data. Inclusion of this additional data is in line with market practice.

8.0 Stewardship Code 2022

8.1 The Financial Reporting Council (FRC) introduced the new UK Stewardship Code in 2020. The Code sets high stewardship standards for those investing money on behalf of UK savers and pensioners, and those who support them. The Code comprises twelve ‘apply and explain’ principles for asset owners, under the headings:

- Purpose and governance;
- Investment approach;
- Engagement; and
- Exercising rights and responsibilities.

8.2 To become a signatory to the Code, organisations must submit a Stewardship Report demonstrating how they have applied the Code’s Principles in the previous 12 months to the FRC. The FRC will assess the report, and if it meets their reporting expectations, the organisation will be listed as a signatory to the Code. Once listed, organisations must report annually to remain a signatory.

8.3 The Fund became one of the first Local Authority Pension Fund signatories to the Code, following submission of a report for 2020/21. The Fund submitted a second annual report in October 2022 for the financial year 2021/22 and was notified in February 2023 that we have successfully remained a signatory of the Code for that

year. The FRC also provided feedback on the submission and areas to be considered when preparing the submission for 2022/23.

Conclusion

9.1 This report brings to the Committee information on the various Responsible Investment (RI) activities that have been undertaken on behalf of the Fund during the quarter.

Consultation

a) Risks and Impact Analysis

The Pension Fund has a risk register which can be obtained by contacting the Head of Pensions.

Appendices

These are listed below and attached at the back of the report	
Appendix A	Border to Coast Global Equity Alpha Voting Activity
Appendix B	Border to Coast UK Listed Equity Voting Activity
Appendix C	Border to Coast Pensions Partnership - ESG Quarterly Report - Global Equity Alpha
Appendix D	Border to Coast Pensions Partnership - ESG Quarterly Report - UK Listed Equity
Appendix E	Border to Coast Pensions Partnership - ESG Quarterly Report - Investment Grade Credit

Background Papers

No background papers within Section 100D of the Local Government Act 1972 were used in the preparation of this report.

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