



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

Report to:	Pensions Committee
Date:	21 September 2023
Subject:	Responsible Investment Update Report

Summary:

This paper provides the Committee with an update on Responsible Investment activity during the first quarter of the financial year 2023/24 (April to June 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:

- Peak voting season: It has been a busy voting season for LAPFF. Representatives attended six AGMs. LAPFF also issued a record number of voting alerts, including over 50 climate-related shareholder resolutions, 55 voting recommendations for environmental, social and governance (ESG) resolutions at mining companies and technology companies. Oil and gas companies and banks were a further area of focus for LAPFF this AGM season, with LAPFF supporting the 'Follow This' resolutions at BP and Shell. It was interesting to note that many ESG resolutions gained traction this year, while the so-called 'anti-ESG' resolutions aimed at questioning the value of ESG issues in relation to financial performance, appeared to lose ground. LAPFF will continue to issue voting alerts throughout the year as appropriate.

Voting alerts focused around:

- Climate: Due to the scale of the investment risks and as part of a continued focus on mitigating climate risks, this area has been a focus for LAPFF, and they have issued a series of dedicated climate change voting alerts. These alerts recommend voting positions on climate-related shareholder resolutions with the aim of ensuring companies properly address the climate risks they face. The alerts covered companies in different sectors and centred on climate topics that LAPFF engages on, including transition plans, adequate targets, lobbying, and a just transition.
 - Mining: LAPFF issued voting alerts this quarter for Rio Tinto, Anglo American, Glencore, and Vale. The aim of these voting alerts was to draw attention to both the companies and investors that there is still significant work to do on both human rights and decarbonisation in respect of creating shareholder value for investors.
 - Technology: LAPFF issued voting alerts largely supporting ESG shareholder resolutions filed at technology companies over the last few years and did so again this year. These are part of an engagement escalation strategy where LAPFF issues voting alerts as an initial point of engagement with US companies, with which it deems there are ESG or financial concerns. LAPFF continues to have concerns about corporate governance and social practices at large US technology companies.
- LAPFF engaged with 84 companies over the quarter, on issues ranging from climate change and environmental risk to human rights and supply chain management. Including:
 - Kingfisher, who were cited in a Financial Times article as providing above inflation wage increases for its lowest paid staff, in contrast to the vast

majority of FTSE100 companies. LAPFF sought a meeting to understand the company's approach to remuneration and employee engagement, particularly in the context of a cost-of-living crisis.

- Next and Adidas about their continued operations in Myanmar. Myanmar has been under an extended state of emergency and fraught with a variety of human rights issues since the military coup in February 2021. The Ethical Trading Initiative posted guidance last September for companies in the country's garment sector, with many choosing to exit the country having exhausted efforts to leverage positive human rights outcomes.
- Other work by LAPFF during the quarter included:
 - Stakeholder engagement: LAPFF presented at a side event of the OECD Forum on Responsible Supply Chains. The aim of the presentation was to share LAPFF's learning from its visit to Brazil and, more broadly, its engagement with stakeholders affected by mining operations.
 - Consultation responses: The UN Working Group on Business and Human Rights ran a consultation this quarter on extractives, human rights, and the just transition. LAPFF submitted a consultation response that expressed support for good human rights and environmental due diligence legislation, and emphasised the need for improved stakeholder engagement by extractive companies.
 - Webinars: LAPFF partnered with IndustriALL to host a webinar on the importance of concluding negotiated, binding agreements rather than relying on voluntary, business-driven standards to reduce both human rights risk and business risk.

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.

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 Q2 2023](#)). 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; as well as an update on the significant activities of the team. During the quarter, Border to Coast were the subject of an Accounting for Sustainability (A4S) [case study](#) showcasing how they have implemented the Task Force for Climate Related Financial Disclosures (TCFD) recommendations ahead of its mandatory reporting, which is required by June 2024. The case study sets out the work that has been completed to understand the risks and opportunities, and established more informed policies and processes for stewardship, including engagement and voting.
- The industry update provides details of:
 - The Financial Conduct Authority's (FCA) primary market effectiveness review.
 - The Institutional Investors Group Climate Change (IIGCC) new net zero standards for oil and gas companies and for banks. The Group also made further enhancements to the Net Zero Investment Framework, publishing guidance for bondholder climate stewardship and net zero in private equity.
 - The International Sustainability Standards Board (ISSB) issued inaugural standards with the aim to create a common language for disclosing the effect of climate-related risks and opportunities on a company's future prospects.
 - The European Central Bank (ECB) released its third review on banks' climate-related risk disclosures practices and trends.
 - Climate Change 100+, the largest investor-led climate change initiative, has entered its next phase to drive increased corporate climate action over the next decade.
- High level information on voting activity for the quarter across all Border to Coast funds. Border to Coast voted at 579 meetings during the quarter, covering 9,027 agenda items. In 72% of meetings Border to Coast cast at least one vote against the recommendations of management. The report also includes voting case studies relating to: Nextera Energy, Glencore, Amazon and Total Energies.

The last quarter included peak voting season. During this period, Border to Coast enacted their strengthened voting policy on climate change. They voted

against a significant number of board Chairs across oil and gas, mining, and materials holdings. They also publicly pre-declared decisions to vote against the Chairs of Shell and BP and to vote against Glencore's climate report to signal their intent to other investors. The increasing escalation is particularly warranted given recent backsliding on targets seen among some companies on the back of strong profits.

- Engagement activity, which included 409 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. The report also includes engagement case studies relating to: Shell and BP, and a Just Transition to Net Zero.

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 Q2 2023](#)).
- 4.2 During the quarter they have engaged with companies on 109 occasions on topics including: environment, social, and corporate governance matters. This quarter's report provides details on the Robeco's biodiversity engagement theme, human rights due diligence for conflict-affected and high risk areas, and good governance.

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 Q2 2023](#)) detailing their activity during the quarter, across all their investment products. The report covers the key activity from their Investment Stewardship team, details of significant engagement activity and vote during the quarter, and policy update. During the quarter LGIM engaged 167 times with 146 companies on topics including: climate impact pledges, remuneration, board composition and strategy. 56 of their engagements were in North America, 46 in the UK and 29 in Europe (ex-UK).

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. The latest report available covers Q3 2023 ([Future World Fund ESG Report Q3 2023](#)).

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). During the quarter:

- Global Equity Alpha – 3,203 votes were cast, with 492 votes against management, and 197 meetings were attended. In 81% of meeting one or more votes were cast against management recommendations.
- UK Listed Equity – 1,468 votes were cast, with 78 votes against management, and 70 meetings were attended. In 67% of meeting one or more votes were cast against management recommendations.

6.3 Full details of the votes cast during the period April to June 2023 can be found on the Border to Coast website: [Integrated Full Details Voting Report Q2 2023](#).

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 this quarter MSCI have changed their approach to ESG ratings. This raises the requirements for a fund to be assessed as 'AA' or 'AAA'. This has led to over 30,000 fund ESG rating downgrades across the industry, including impacting on the majority of Border to Coast funds. MSCI also moved away from applying an adjustment factor to fund ratings. This is now calculated as a simple weighted average of the ESG scores of the underlying holdings. Border to Coast is supportive of this methodology as it is much more intuitive and representative of a Fund's ESG characteristics, as well as being much less volatile quarter-to-quarter. Although there have been downgrades in the Border to Coast Sub-fund ratings all are rated A or above.

7.3 For the quarter ended 30 June 2023 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.

7.4 *“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.”*

**In accordance with the Licence Agreement between Border to Coast Pensions Partnership Limited and MSCI ESG Research (UK) Limited.*

7.5 In summary:

- Global Equity Alpha – the fund’s overall ESG rating fell during the period from AAA to A, however the fund remains above the benchmark. This is due to a change in methodology at MSCI which is explained in paragraph 7.2 above.

The fund remains materially below the wider index on all carbon metrics (financed emissions, carbon intensity and weighted average carbon intensity – WACI). This is due to the relative underweight allocations to some high emitting sectors including oil and gas.

Heidelberg Materials and Holcim account for around 55% of portfolio financed emissions, down from 62% last quarter. Due to their involvement in cement production, the carbon metrics of the fund are highly sensitive to each of these companies’ emissions, as well as any fluctuations in their investment value and/or allocation.

- UK Listed Equity– the fund’s overall ESG rating fell during the period from AAA to AA, however the fund remains above the benchmark. This is due to a change in methodology at MSCI which is explained in paragraph 7.2 above. However, the fund benefits from holding a higher weighting of companies considered to be ‘leaders’.

The Fund is currently below, or in-line with, the benchmark for financed emissions and carbon intensity. WACI remains slightly above the benchmark, however, the Fund's WACI decreased in the quarter. Financed emissions increased slightly in the quarter but remain below the benchmark.

Sterling Investment Grade Credit – the fund's overall ESG rating fell during the period from AAA to AA. This is due to a change in methodology at MSCI which is explained in paragraph 7.2 above. The benchmark was also revised down to AA from AAA.

The Fund is currently below the benchmark for portfolio financed emissions, carbon intensity and WACI, and has been trending downwards over time. Energy companies Enel and EDF contribute close to half of the Fund's financed emissions.

8.0 Stewardship Code 2022/23

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, and the FRC expects a continuous improvement in stewardship activity undertaken.

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 and remained a signatory after making a successful submission for 2021/22. Attached at appendix F is the draft Stewardship Code submission for 2022/23. This will be submitted to the FRC in October. Feedback from the FRC and notification of whether the Fund has made a successful submission will be received in Spring 2024.

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
Appendix F	Lincolnshire Pension Fund Stewardship Code 2022-23 draft submission

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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