

Pensions Committee

30 March 2022

Report title	Responsible Investment Activities	
Originating service	Pension Services	
Accountable employee	Rachael Lem Tel Email	Responsible Investment Officer 01902 554764 Rachael.Lem@wolverhampton.gov.uk
Report to be/has been considered by	Rachel Brothwood Tel Email	Director of Pensions 01902 551715 Rachel.Brothwood@wolverhampton.gov.uk

Recommendations for noting:

The Pensions Committee is asked to note:

1. The Fund's draft Voting Principles 2022 [Appendix A].
2. The Fund's engagement and voting activity for the three months ending 31 December 2021 [Appendices B and C].
3. The issues discussed by LAPFF are set out in the Quarterly Engagement Report, which is available on the LAPFF website: https://lapfforum.org/wp-content/uploads/2022/01/LAPFF_QER04_2022_Final.pdf.
4. The research and engagement activity undertaken by EOS at Federated Hermes as set out in the 2021 Annual Engagement Report, which is available on the EOS website: [EOS 2021 Annual Review | UK Institutional \(hermes-investment.com\)](https://www.hermes-investment.com/2021-annual-review).

1.0 Purpose

- 1.1 To update the Pensions Committee on the work undertaken in relation to responsible investment activities since the last Pensions Committee meeting.

2.0 Background

- 2.1 The Fund has a longstanding policy of supporting good corporate governance in the companies in which it invests. The Fund will also challenge companies who do not meet either the standards set by their peers or reasonable expectations as measured by best practice. The Fund's approach is part of its overall investment management arrangements and its active responsible investment framework. There are three main pillars to the framework: selection (of assets), stewardship (of assets), and transparency & disclosure.

3.0 Responsible Investment Activities

Engagement through Partnerships

- 3.1 The Fund's strategy is to engage with its investee companies and other key stakeholders through partnerships and on its own. The Fund aims to protect and increase shareholder value by engaging on a range of financially material ESG investment factors. A significant part of the Fund's engagement programme is implemented through partnerships including the Local Authority Pension Fund Forum (LAPFF), EOS at Federated Hermes ('EOS' - via a contract held by LGPS Central Ltd, the Fund's investment pool operator), the Institutional Investors Group on Climate Change (IIGCC), Climate Action 100+ (CA 100+), the Transition Pathway Initiative (TPI), and the Principles for Responsible Investment (PRI).
- 3.2 Through LAPFF, the Fund engaged 82 companies during the quarter¹, addressing human rights, climate change and governance issues. Most engagements were conducted through letter writing; five company engagements are currently categorised as change in process, whilst substantial and moderate improvements were documented in four engagements.
- 3.3 This quarter LGPS Central undertook 823² engagements with 252 companies on behalf of the Fund, the majority of which were carried out by EOS. Most engagements were conducted through letter issuance or remote company meetings, where LGPS Central, collaborative engagement partners or EOS in a majority of cases met or wrote to the Chair, a Board member, or a member of senior management.
- 3.4 The engagement examples considered in this paper are predominately taken from LAPFF's Q4 2021 Quarterly Engagement Report and EOS's 2021 Voting and Engagement Highlights Annual Review. Following the request of the Financial Reporting Council (FRC) for investors, asset managers and service providers to submit Annual Stewardship Reports for review at the end of April or October each calendar year, some companies, such as LGPS Central and EOS, are choosing to produce an Annual Stewardship report in place of a Q4 2021 quarterly report. The Fund's 2022 Annual Stewardship Report will be

¹ This is a consolidated figure representing the number of companies engaged, not the number of engagements.

² There can be more than one engagement issue per company, for example board diversity and climate change.

submitted to the FRC for review at the end of April and will be presented to Pensions Committee at the June 2022 meeting.

Climate Change

- 3.5 This is a critical year for both corporate and policy makers in accelerating action towards the goals of the Paris Agreement - to limit global warming to well below 2, preferably to 1.5 degrees Celsius, compared to pre-industrial levels. The focus is now on the UK and the contribution that local authority pension funds and other institutional investors can make to help decarbonise the economy in a way that protects beneficiaries and secures just transition to net zero.
- 3.6 During the quarter LAPFF undertook approximately 420 climate change engagements, the majority of which saw correspondence with the FTSE all-share (excluding investment trusts) pressing for an annual 'Say on Climate' vote. The 'Say on Climate' initiative asks companies to set out their strategy to manage the transition to a net zero emissions business with investors asking for emission disclosure consistent with the Task Force on Climate-related Financial Disclosure, a five-year plan to get onto a net zero emissions pathway and annual provision for shareholders to vote on such plans. In October 2021, the LAPFF chair, together with TCI Fund Management and Sarasin and Partners, wrote to the FTSE All-share (excluding investment trusts and companies that had already made a commitment to annual vote for shareholders) to ask that boards set out their strategy to manage the transition to a net zero emissions business and to provide annual provision for shareholders to vote on such plans. As at end December 2021, 64 responses had been received.
- 3.7 Following correspondence with companies in November 2020, LAPFF joined in further communications with companies to share feedback on climate-related financial disclosures in the most recent set of company financial accounts. Correspondence aimed to encourage the companies to address outstanding concerns in audited accounts issued in 2022. Copies were also provided to the lead audit partner to emphasise the expectation that they alert shareholders where the accounts are not consistent with a 1.5°C outcome.
- 3.8 Alongside LAPFF and LGPS Central, the Fund continues to participate in regular calls with IIGCC and its investor members, receiving and providing updates on EU constituents of the CA100+ initiative. Results of the CA100+ benchmarking process are being discussed with companies following the review period ending in December 2021. Sector meetings are proving helpful in providing peer best practice examples as 'pointers' for other companies in the sector.
- 3.9 The LAPFF-supported "All-Party Parliamentary Group (APPG) for local authority pension funds" inquiry report into a Just Transition was published during the quarter. The APPG had undertaken an inquiry during 2021 examining the role investors can play, with the support of government, in ensuring the transition to net zero considers the social implications for employees, consumers, communities and supply chains. The APPG, chaired by Clive Betts MP, heard evidence from LAPFF members, investors, companies, trade unions and from the Climate Change Committee. The inquiry found that just transition

presented investors with financial risks and covered actions investors can individually and collectively undertake and also set out how Governments can support investors. A copy of the report can be found on the LAPFF Website³.

Sustainable Food Systems

- 3.10 During the quarter, one of the Fund's Sustainable Equities Managers produced an insight piece addressing biodiversity loss and the role of investors. The manager writes that failure to address biodiversity loss carries enormous risks to human health and prosperity, given our dependence on nature. Addressing the crisis is especially challenging, given its complexity, diverse drivers, and our limited understanding of natural processes. We can learn valuable lessons from confronting other environmental issues, including climate change. To respond effectively, the asset manager states that we need to break biodiversity loss down into a set of specific sub-issues (or 'Biodiversity Imperatives') and address them using tailored solutions based on a 'multi-local' approach. Investors can not only contribute significantly to these efforts but also benefit from new business opportunities linked to the sustainable management of biodiversity.
- 3.11 Biodiversity loss was further recognised by EOS at Federated Hermes as an urgent challenge in 2021 given the importance of ecosystems for sustaining global food supplies, providing clean water and air, and absorbing harmful carbon dioxide to help mitigate global heating. In EOS's 2022-2024 Engagement Plan⁴, EOS outline that they will engage with companies, especially those that are involved in the production and sale of food, on halting and reversing biodiversity loss. Depending on the specific company context, engagement will cover various issues including deforestation, regenerative agriculture, sustainable proteins and chemical run-off management.

Human Rights

- 3.12 During the quarter LAPFF engaged companies on approximately twenty human rights issues on behalf of the Fund. In the same time period, the Investor Alliance on Human Rights (IAHR) circulated an investor letter calling for the UK and the EU to implement mandatory human rights and environmental due diligence (mHREDD). It followed with another letter asking that stakeholder engagement be placed at the heart of this legislation. On behalf of WMPF, LAPFF signed both letters.
- 3.13 Over the last couple of years, LAPFF has engaged intensively with mining companies on their human rights practices. The engagement has focused on the participation of affected stakeholders in mining company activities and decision-making. Based on these engagements with mining companies and affected stakeholders, LAPFF has produced five reports on its views regarding mining companies and human rights. The reports are currently being consolidated into a single draft report that LAPFF has circulated for comment to the five companies addressed and to the affected communities whose accounts have been included in the report. After the comments have been received, they will be assessed and integrated as appropriate before the report is released publicly.

³ [Responsible-Investment-for-a-Just-Transition-Report.pdf \(lapfforum.org\)](#)

⁴ [EOS Engagement Plan 2022-2024 | UK Institutional \(hermes-investment.com\)](#)

- 3.14 The LAPFF Vice Chair, was appointed in 2021 to the City of London's Taskforce on Socioeconomic Diversity Advisory Board and during the quarter, the Vice Chair attended an in-person event to discuss a number of issues that both the advisory board and working groups are looking to overcome. Questions of whether mandatory reporting by government or regulators were asked, and what role sector bodies can play. The role of membership bodies seeking to progress change in this area was discussed as well as what members of the taskforce believed would convince senior leadership to improve socio-economic diversity. LAPFF's work on diversity will continue in 2022 and will incorporate aspects of socio-economic diversity alongside other aspects.
- 3.15 For the third consecutive year, the Fund has joined 122 investors with £9.6 trillion in assets under management, to become signatory to the Rathbone's Modern Slavery Initiative. Thus far during March 2022, letters have been sent to 44 target companies and Rathbone's have already begun to receive a number of positive responses.

Responsible Financial Management

- 3.16 Executive remuneration pay structures are a critical tool for aligning the activities of management with a company's purpose, strategy and incentivising long-term value creation, including wider social and environmental outcomes. During 2021, EOS opposed 53% of UK remuneration policy proposals versus 50% in 2020. EOS denote that they saw evidence of some good practices, with many companies repaying the money received from the government to furlough their employees or in business rates relief, and it was generally accepted amongst those not able to do so that they should not pay bonuses to executives.
- 3.17 In their 2022-2024 Engagement Plan, EOS have outlined that in some markets they consider that compensation structures and practices are generally not fit for purpose, with some recent practices, such as introducing structures to gear the majority of pay towards performance-based pay, may have been well-intentioned but have proved ineffective with unintended consequences such as escalating quantum and encouraging short-termism or financial engineering. The coronavirus pandemic has served as a reminder of the limitations of pay schemes reliant on stock options or performance-based incentives schemes. EOS therefore wish to see simpler, more transparent pay schemes with the reduction of variable, performance-based elements in pay, replacing these with higher fixed pay, paid primarily in shares held for the long term. The long-term outcomes EOS seek include executives being rewarded for behaviour aligned to the desired corporate culture; simple, understandable pay schemes that incentivise delivery of long-term sustainable value; clear disclosure explaining the nature and appropriateness of awards; and fair levels of pay that clearly align with performance and can be justified to employees, investors and other stakeholders.

Voting Globally

- 3.18 The Fund's Voting Principles are currently executed by EOS via a contract held by LGPS Central Ltd, the Fund's asset pool company. The Fund has contributed to and endorses LGPS Central's Voting Principles, the latest iteration of which is due to be published in April 2022. The Fund has reviewed and updated its Voting Principles noting the important role voting places in the overall engagement strategy and in consultation with appointed investment managers, including LGPS Central Ltd. Key updates to the document include:

strengthening of expectation on board composition to enhance diversity (Section 3.1); enhancement of Auditor Independence and Remuneration practices (Sections 3.2 and 3.4); and inclusion of Section 3.5 '*Sustainable Business Practices*' which sets out enhanced expectations of company climate-related disclosures and transition plans and encourages commitment to biodiversity protection as part of a broader climate transition effort. A draft version of the Fund's updated Voting Principles can be found in Appendix A. This has been developed ahead of the 2022 voting season, with the final version to be presented to Committee for approval in June 2022.

- 3.19 The voting activity for the quarter across markets and issues can be found in Appendix B. During the period, the Fund voted at a total of 316 company meetings (2,424 resolutions) – 59 UK, 46 Europe, 38 North American, 44 Developed Asia, 90 Australasian and 39 in Emerging and Frontier Markets. At 167 meetings we recommended opposing one or more resolutions. The largest number of resolutions that were opposed concerned board structure and remuneration (usually voting against non-independent non-executive directors where the Fund or its advisors do not see sufficient independent oversight on a company board).

Asset Owner Diversity Working Group

- 3.20 This quarter the Fund has continued its involvement in the Asset Owner Diversity Working Group, which in 2022 saw the development of the first Asset Owner Diversity Charter⁵, which aims to tackle diversity bias within the asset management industry. The Charter has now been backed by 20 signatories representing £1.88 trillion in assets under management/consultancy. Preliminary questionnaires were sent to a subset of Asset Managers during Q1 and Q2 2021, which led to the development of the 'Asset Manager Diversity and Inclusion Questionnaire' which is set to be available to all asset managers globally later on in 2022. Simultaneously, the Fund is looking to incorporate diversity and inclusion into its conversation with managers with a view to this becoming a required metric for asset managers to report on in the coming year. Pensions Committee will be kept informed of the progress of both initiatives.

LAPFF 2022-2023 Workplan

- 3.21 As per previous years, the Fund was pleased to have the opportunity to be able to feed comments into the development of the LAPFF 2022–2023 Workplan. Commensurate with the Fund's engagement themes for 2019-2023 and WMPF's newly established climate targets for 2021 – 2026, the Fund asked LAPFF to continue the strong work that it is doing in their climate workstream, which comprises net zero, Paris-aligned accounts, strategic resilience, just transition and electric vehicles. The Fund also asked LAPFF to continue to press for companies operating in the Occupied Palestine Territories to produce credible human rights impact assessments and will seek clarity as to how best approach engagement with these companies.

⁵ [Asset Owner Diversity Charter | Diversity Project](#)

Occupational Pensions Stewardship Council

- 3.22 During the quarter the Fund attended an Occupational Pensions Stewardship Council (OPSC) quarterly meeting. In response to a recommendation by the Department for Work and Pensions, the OPSC was established mid-2021 to promote and facilitate high standards of stewardship of pension assets. The council provides schemes with a forum for sharing experience, best practice and research, and providing practical support. The council also enables opportunities for schemes to collaborate on stewardship activities such as shareholder resolutions, climate change, corporate governance and other topics.

Correspondence

- 3.23 The Fund continues to receive correspondence from individual members of the public, and more established divestment groups in connection with climate change, human rights issues and calls for divestment. During the quarter the Fund received queries and correspondence on responsible investment topics relating to investment in Occupied Palestine Territories (OPT). The Local Authority Pension Fund Forum is continuing a programme of engagement over 2022 on behalf of the Fund and is monitoring both UN activity and the developing political situation in OPT areas. Pensions Committee will be kept abreast of progress.
- 3.24 The Fund is shocked and saddened by the escalating events in Ukraine over the last couple of weeks and our thoughts are with those whose lives are affected by the invasion and ongoing conflict. We are united with many others in our view that war is not the answer, and we are supportive of the actions taken to support the people of Ukraine. The Fund has received a number of queries from members and press outlets on the Fund's investment holdings within Russia. The Fund has reviewed its investment holdings and continues to liaise with Fund Managers to assess actions taken in response to the developing events in Ukraine, together with the increasing sanctions imposed on Russia. Fund investments in this area represent a very small and reducing element of the Fund portfolio, with actions having already been taken to reduce exposure.
- 3.25 The Fund, and its managers, have taken action to limit future investment (as outlined in a separate report to be discussed later in this meeting) and we continue to monitor the situation in line with our Responsible Investment Framework⁶. The economic and investment landscape has fundamentally shifted, with geopolitical risks, and humanitarian impact coming to the fore. The Fund believes this requires a fundamental review of investment strategy and re-evaluation of social and governance risks with this being our focus as we continue to monitor the financial and non-financial implications, short and longer term.
- 3.26 The Fund continues to respond to all correspondents and will continue to monitor progress on the issues outlined, with updates to each quarterly Pensions Committee Meeting.

⁶ [Responsible Investment Framework - March 2021 \(wmpfonline.com\)](https://www.wmpfonline.com)

4.0 Financial implications

- 4.1 The promotion of good corporate governance amongst companies in which the Fund invests is complementary to the Fund's objective of maximising financial returns, as it is widely believed that good corporate governance improves shareholder value in the long term.

5.0 Legal implications

- 5.1 This report contains no direct legal implications.

6.0 Equalities implications

- 6.1 This report contains no equal opportunities implications.

7.0 Other Potential Implications

- 7.1 This report contains no other potential implications

8.0 Schedule of background papers

- 8.1 LAPFF Quarterly Engagement Report: https://lapfforum.org/wp-content/uploads/2022/01/LAPFF_QER04_2022_Final.pdf.
- 8.2 EOS at Federated Hermes Public Engagement Report: [EOS 2021 Annual Review | UK Institutional \(hermes-investment.com\)](https://hermes-investment.com/eos-2021-annual-review-uk-institutional)

9.0 Schedule of appendices

- 9.1 Appendix A – WMPF Draft Voting Principles 2022
- 9.2 Appendix B – WMPF Engagement Activity
- 9.3 Appendix C - WMPF Voting Activity