

Pensions Committee

20 June 2018

Report title	Responsible Investment Activities	
Originating service	Pension Services	
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Recommendations for noting:

The Committee is asked to note:

1. The Fund's voting and the Local Authority Pension Fund Forum's (LAPFF's) engagement activity for the three months ending 31 March 2018, including Appendix 1.
2. The issues discussed by LAPFF are set in the Quarterly Engagement Report which is available on the LAPFF website:
<http://www.lapfforum.org/publications/qrtly-engagement-reports/>
3. Progress against the Fund's 2018 stewardship themes
4. The Fund's response to the Environmental Audit Committee and initial "more engaged" rating given to the Fund.
5. Other activity undertaken to ensure the Fund continues to develop and support its approach to Responsible Investment.

1.0 Purpose

- 1.1 To update the Pensions Committee on the work undertaken by the investment team regarding their 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 policy. There are three pillars of responsible investment that we focus on: **Selection** of our assets, **Stewardship** of our assets and **Transparency & Disclosure**.

3.0 Responsible Investment Activities

Stewardship

- 3.1 The Fund's strategy is to engage with its investee companies and other key stakeholders through partnerships and directly. 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 program is implemented through partnerships including the Principles for Responsible Investment (PRI), the Local Authority Pension Fund Forum (LAPFF), Institutional Investors Group on Climate Change (IIGCC) and the UK Pension Fund Roundtable.
- 3.2 Through LAPFF, the Fund engaged with 21 companies during the quarter. Most engagements concerned climate change, employment standards, human rights and general corporate governance. Four engagements led to a small or moderate improvement or a change in process. Most engagements were conducted by meetings or by writing letters to the company Chair. A summary of LAPFF's engagement activities for the quarter are provided alongside the voting activity report in Appendix 1. The issues are set out in the Quarterly Engagement Report which is available on LAPFF's website: <http://www.lapfforum.org/publications/qrtly-engagement-reports/>
- 3.3 Through the United Nations' Principles for Responsible Investment (PRI), the Fund is currently a support investor to two engagement topics – cyber security and climate change risk – each of which concerns a number of holdings. As previously reported the Fund is a participant in engagement concerning cyber security risk management in a joint effort with approximately 50 other global institutional investors. WMPF has recently joined an engagement on climate change risk which will be based upon the framework created by the Transition Pathway Initiative (TPI), of which the Fund is a founding member. This engagement will also be channelled through the PRI. The Fund is a participant in Climate Action 100+ (CA100+), which is jointly coordinated by a number of international organisations including the PRI and the IIGCC. As its name suggests, the

initiative covers more than 100 global companies and the Fund is focussing its own efforts on two UK companies.

Stewardship Themes

- 3.4 The Fund's stewardship themes for 2018 are climate change, cyber security and diversity. These themes have been selected because they have both financial relevance and resonance with the Fund's stakeholders. The Fund will, primarily through partnerships, engage with companies, fund managers and other relevant organisations, and will use its voting rights to drive change and signal the importance of these issues to institutional investors. Progress on each theme is reported to the Pensions Committee on a quarterly basis.

Climate Change

- 3.5 The Fund is leveraging its partnership arrangements with the TPI and CA100+, and LGPS Central's internal RI resources. During the period in review, engagements with two UK stocks were progressed through meetings, conference calls and AGM attendance. These companies are those for which the Fund is leading the engagement, and are in addition to the c100 other companies in the collaborative engagement initiative. The Fund has voted against the Chairs of all companies scoring a rating of zero on the TPI's climate change governance framework. As the person most accountable for company strategy, the Fund does not think it acceptable to vote in support of a Chair of a high impact company scoring so poorly on climate change governance. The Fund will seek to engage laggards on the TPI's scoring framework in partnership with like-minded investors. The Fund was pleased to respond to the Environmental Audit Committee's (EAC) request for information on the Fund's management of climate change risk. The Fund's position is that the management of climate risk falls squarely with the Fund's fiduciary duty, and is a risk factor that ought to be managed through investment stewardship. The EAC published the responses from the UK's 25 largest pension funds on 25th May, noting WMPF as "more engaged" and highlighting the steps already taken by the fund to disclose in its 2017 Annual Report, in line with Taskforce on Climate-related Financial Disclosures (TCFD) recommendations.

Cyber Security

- 3.6 Within the PRI's collaborative engagement on cyber security, which includes c50 listed companies, the Fund has co-led on two UK-based companies. These engagements were progressed during the quarter in review with company meetings at each engagement target. In both cases, the Chief Information Security Officer demonstrated to us that cyber risk is being managed to a best-practice standard. We have shared these findings with our engagement collaborators. Following US, UK and France-led airstrikes in Syria, the Russian state was alleged to have sponsored cyber attacks on UK infrastructure and major UK companies. To our knowledge, our engagement target companies were resilient to these alleged attacks.

Diversity

- 3.7 The Fund has continued to press for improvements in diversity both at investee companies and at investment managers. With regards to investee companies, the Fund has decided to vote against the Chairs of Nominations Committees that have failed to achieve 25% women on the boards of FTSE 100 companies (the threshold is 20% for FTSE 250 companies). This voting strategy, which will link to the Fund's engagement strategy, aligns with the Fund's membership of the 30% Club Investor Group, as well as its support for the Davies Review, the Hampton-Alexander Review and WMPF's Voting Principles. With regards to investment managers, the Fund has participated in a project to develop monitoring and reporting standards in private markets. As part of its input, the Fund has argued for core disclosure on matters of diversity. It is hoped that these reporting standards will become market practice, thus raising the standard of disclosure on diversity by financial services companies.

Shareholder Voting

- 3.8 The Fund currently has its own bespoke UK voting policy which our voting provider, Pensions and Investments Research Consultants Ltd (PIRC), executes on the Fund's behalf directly and via LGPS Central. The Fund follows the voting advice of PIRC for European, US, Japanese and Pacific region company meetings.
- 3.9 The voting activity for the quarter across markets and issues can be found in Appendix 1. During the period the Fund voted at a total of 408 company meetings – 54 UK, 69 European, 58 North American, 60 Japanese, 136 Asia (excluding Japan), 2 Australasian/South African and 29 in the rest of the world. During this period there were 51 meetings where the Fund supported all the resolutions put forward by companies. Approximately 39% of the resolutions were not supported by the Fund. The largest number of resolutions that were opposed concerned the re-election of directors (usually voting against non-independent non-executive directors where the Fund or its advisors do not see sufficient independent oversight on a company board) and remuneration.
- 3.10 Melrose Plc put its remuneration report to shareholder vote at its AGM on 10 May. The Fund chose to oppose the report owing to the quantum of the awards to senior executives. Whilst the company's remuneration policy has some admirable components – including its alignment with shareholders through basing variable remuneration on the outperformance of the company relative to benchmark, and the policy's simplicity compared with peers – it is in contrast with the spirit of the Fund's Voting Principles because it can lead to excessive rewards. The Fund was joined by 23% of the company's shareholder base in opposing the remuneration report. The Fund welcomes the statements from the company that it will review its variable pay and that engagement with shareholders will commence in the coming months.

LGPS Central

- 3.11 LGPS Central's first sub-funds were launched in April 2018. Ahead of this, LGPS Central signed up to the UK Stewardship Code (receiving Tier 1 status, which is the best practice rating) and issued its *Responsible Investment & Engagement Framework*. Through this framework, LGPS Central is able to implement the Fund's own *Responsible Investment Framework*. LGPS Central intends to issue Quarterly Stewardship Reports, with the first issue covering 2018 Q1, expected publication in August 2018.

Other

- 3.12 Carillion Plc was a FTSE-listed construction & outsourcing company based in Wolverhampton, primarily with UK operations but also operating globally including the Middle East. Shortly before its collapse, Carillion had a market valuation of approximately £1bn and employed c20,000 people in the UK. Carillion was a strategically important service provider to the UK government supplier, with contracts to build HS2, maintenance of Network Rail and homes maintenance for the MoD. In May 2018, the Department for Business, Energy and Industrial Strategy (BEIS) and the Department of Work and Pensions (DWP) issued a joint report on Carillion's collapse. The report focussed on debt, the pension fund, dividend payments and the roles of external auditors and company directors. The Financial Reporting Council (FRC) is conducting a review into various aspects of the company's collapse. The Fund continues to monitor the situation with a view to potential learnings for institutional investors. WMPF has previously voted against re-election of the external auditor and notes this is one area under consideration in the FRC review.

4. 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 Environmental implications

- 7.1 Environmental implications are addressed through the Fund's Responsible Investment Framework.

8.0 Human resources implications

8.1 This report contains no direct human resources implications.

9.0 Corporate landlord implications

9.1 This report contains no direct corporate landlord implications.

10.0 Schedule of background papers

10.1 LAPFF Quarterly Engagement Report:
<http://www.lapfforum.org/publications/qrtly-engagement-reports/>

11.0 Schedule of Appendices

11.1 Appendix 1 (Voting and Engagement Activity)

11.2 Appendix 2 (Environmental Audit Committee summary of the UK's 25 largest pension funds responses and ratings)