

**SUPERANNUATION FUND COMMITTEE**

**Friday, 7 February, 2020**

**10.00 am**

**Council Chamber, Sessions House, County Hall,  
Maidstone**







## AGENDA

### SUPERANNUATION FUND COMMITTEE

**Friday, 7 February, 2020 at 10.00 am**  
**Council Chamber, Sessions House,**  
**County Hall, Maidstone**

Ask for: **Theresa Grayell**  
Telephone: **03000 416172**

#### Membership

Conservative (8):	Mr C Simkins (Chairman), Mr P V Barrington-King, Mr P J Homewood, Mr J P McInroy and Mr J Wright	Mr N J D Chard (Vice-Chairman), Mr P Bartlett, Mr P C Cooper,
Liberal Democrat (1)	Mr D S Daley	
District Council (3)	Cllr J Burden, Cllr P Clokie and Cllr N Eden-Green	
Medway Council (1)	Cllr S Tranter	
Kent Active Retirement Fellowship (2)	Mrs M Wiggins and Mr D Coupland	
UNISON (1)	Mr J Parsons	
Staff Representative (1)	Vacancy	

Please note that the unrestricted part of this meeting may be filmed by any member of the public or press present.

By entering the meeting room, you are consenting to being filmed. If you do not wish to have your image captured, please let the Clerk know immediately.

#### **UNRESTRICTED ITEMS**

*(During these items the meeting is likely to be open to the public)*

- 1 Apologies and Substitutes
- 2 Declarations of interest by Members in items on the agenda for this meeting.
- 3 Future meeting dates - 2020/21

The committee is asked to note that the following dates have been reserved for its meetings in 2020/21:

13 March 2020 (already in the calendar)  
19 June 2020  
4 September 2020  
13 November 2020  
5 February 2021  
12 March 2021  
18 June 2021

All meetings will commence at 10.00 am at County Hall, Maidstone

- 4 Minutes of the meeting held on 15 November 2019 (Pages 1 - 6)
- 5 Verbal Update on Audit Review Action Plan

**Motion to exclude the press and public for exempt business**

That under Section 100A of the Local Government Act 1972 the press and public be excluded from the meeting for the following business on the grounds that it involves the likely disclosure of exempt information as defined in paragraph 3 of part 1 of Schedule 12A of the Act.

Paragraph 3 – Information relating to the financial or business affairs of any particular person (including the authority holding that information)

**EXEMPT ITEMS**

*(During these items the meeting is likely NOT to be open to the press and public)*

- 6 Woodford investment update (Pages 7 - 20)
- 7 Sarasin - presentation

**UNRESTRICTED ITEMS**

*(meeting open to the public)*

- 8 Responsible Investment (RI) / Environmental Social and Governance (ESG) policy (Pages 21 - 68)
- 9 Date of next meeting

The next meeting of the committee will be held on Friday 13 March 2020, commencing at 10.00 am at Sessions House, Maidstone.

**EXEMPT ITEMS**

*(At the time of preparing the agenda the only exempt items were 6 and 7. During these and any other such items which may arise the meeting is likely NOT to be open to the public)*

Benjamin Watts  
General Counsel  
03000 416814

**Thursday, 30 January 2020**

*In accordance with the current arrangements for meetings, representatives of the Managers have been given notice of the meeting and will be in attendance for their items.*

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## KENT COUNTY COUNCIL

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### SUPERANNUATION FUND COMMITTEE

MINUTES of a meeting of the Superannuation Fund Committee held in the Medway Room, Sessions House, County Hall, Maidstone on Friday, 15 November 2019.

PRESENT: Mr C Simkins (Chairman), Mr N J D Chard (Vice-Chairman), Mr P V Barrington-King, Mr P Bartlett, Cllr J Burden, Cllr P Clokie, OBE, Mr P C Cooper, Mr D Coupland, Mr D S Daley, Mr P J Homewood, Mr J P McInroy, Mr J Parsons, Cllr S Tranter and Mr J Wright.

ALSO PRESENT: Mr P J Oakford and Mrs M E Crabtree

IN ATTENDANCE: Ms Z Cooke (Corporate Director of Finance), Mr N Vickers (Business Partner (Pension Fund)) and Miss T A Grayell (Democratic Services Officer).

### UNRESTRICTED ITEMS

#### **157. Membership**

*(Item 1)*

The committee noted that Cllr Stuart Tranter had replaced Cllr Mrs Josie Iles as the Medway Council representative on the committee. Cllr Tranter was welcomed to the meeting.

#### **158. Apologies**

Apologies for absence had been received from Cllr Nick Eden-Green and Mrs Mary Wiggins.

There were no substitutes

#### **159. Declarations of interest by Members in items on the agenda for this meeting.**

*(Item 3)*

Mrs M Crabtree declared that she had recently discovered that a small part of her personal pension fund was invested with a Woodford fund.

Mr P J Bartlett declared that he was an employee of Bank of New York Mellon (BNYM). One of the fund managers listed in an appendix to agenda item 6, covering equity protection, was a BNYM affiliate. Mr Bartlett advised the committee that he had no activity in that part of BNYM's business so would remain in the room during discussion but would not take part in any vote relating to that item.

**160. Minutes of 6 September 2019** (and exempt minute of part of the meeting held on 21 June 2019, which was omitted from the previous agenda but which needs to be approved and signed)

*(Item 4)*

It was RESOLVED that the minutes of the meeting held on 6 September 2019 and the restricted minute of the closed part of the meeting held on 21 June 2019 are correctly recorded and that both be signed by the Chairman.

There were no matters arising from either.

### **161. Motion to exclude the press and public for restricted items**

It was RESOLVED that, under Section 100A of the Local Government Act 1972, the press and public be excluded from the meeting for the following business on the grounds that it involves the likely disclosure of exempt information as defined in paragraph 3 of part 1 of Schedule 12A of the Act.

#### **EXEMPT ITEMS**

(Open access to minutes)

### **162. 31 March 2019 Actuarial Valuation results**

*(Item 5)*

*Graeme Muir, Partner, Barnett Waddingham, was in attendance for this item at the invitation of the committee.*

1. The Chairman welcomed Mr Muir to the meeting and thanked him for attending.
2. Mr Muir presented the valuation results and set out the legal framework and timetable for the valuation process and the methodology used, including the need to take account of the McCloud judgement. He responded to questions of detail from the committee, including the impact of the McCloud judgement, the method used to calculate and compare the values of existing and future pensions, deferred benefits and the impact of the residue of employees with final-salary pensions.
3. The Chairman thanked Mr Muir and Mr Tagg, Senior Accountant, for the fullness of the report which the committee had been given and the explanations and clarifications Mr Muir had given the committee in response to their questions.
4. It was RESOLVED that the assumptions set out in the report and the initial results of the 31 March 2019 actuarial valuation be agreed.

### **163. Investment Strategy**

*(Item 6)*

*Catrina Arbuckle, Director, and Nick Page, Senior Investment Consultant, from Mercer Ltd were in attendance for this and the following item at the invitation of the committee.*

1. Mr Vickers introduced the report and updated the committee on developments in respect of the Woodford Extra Income Fund since the committee's 6 September meeting, including the latest valuation of the County Council's investment. He and Ms Arbuckle answered questions of detail from the committee, including the risk to the County Council's investment compared to the risk in other areas and types of investment in the Woodford Extra Income Fund, the ongoing situation regarding fees payable and the legal advice given by the General Counsel.



2. Mr Vickers drew the attention of the committee to the letter from Link dated 15 October 2019, announcing that the Woodford Extra Income Fund would be wound up and Mr Woodford removed as the fund manager. He outlined the new arrangements for the management of the fund's assets, which are that, as from 15 October, BlackRock Advisors (UK) Limited had been appointed to prepare the listed assets (Portfolio A) for the winding up of the Fund. BlackRock will seek to sell the assets in Portfolio A and use the proceeds to purchase money market funds and FTSE 100 index instruments to enable Link to return part of investors' cash as soon as possible. Meanwhile PJT Partners(UK) Limited had been appointed as a specialist broker to assist in selling the unlisted assets (Portfolio B).

3. The committee commented on the negative media coverage which had been given to the issue and acknowledged the support given to the committee by the County Council's press office in communicating information to scheme members and the public. It was suggested that the 'Open Lines' magazine be used to communicate future news to pensioners and dependent pensioners.

4. Mr Page and Ms Arbuckle then set out and updated the committee on other aspects of the County Council's investment strategy and answered questions of detail from the committee, including options for moving investment between different types of asset, and equity protection. The committee agreed that it needed to have more information on, and examples of, the investment options set out and requested a briefing session with Mercer Ltd and fund managers in the near future to help them to understand fully the options available.

5. The committee then addressed the report's recommendations and it was RESOLVED that:-

- a) the latest position on the Woodford Extra Income Fund be noted;
- b) the investment in multi-asset credit funds with the companies set out in recommendation (2) of the report be agreed;
- c) the committee seek more information on the investment options set out and hold a briefing session with Mercer Ltd and fund managers in the near future to help them to understand fully the options available;
- d) reports from Mercer Ltd be received on a quarterly basis;
- e) the progress made on ACCESS be noted; and
- f) the intention to focus on Environmental, Social and Government (ESG) issues at the February meeting be noted.

#### **164. Competition and Markets Authority (CMA) Order** (Item 7)

1. Mr Vickers and Ms Surana introduced the report and explained the new statutory requirement for local authorities to set strategic objectives against which their investment advisors' performance could be measured. The deadline for this compliance was 10 December 2019. Ms Arbuckle added that there was a sanction of a financial penalty for any authority not complying by the deadline, that the objectives agreed could be reviewed at any time in the future and should be reviewed at least every three years.

2. The committee discussed the four overall objectives set out in the appendix to the report and agreed a number of changes to the wording, which Ms Arbuckle accepted on behalf of Mercer Ltd.

3. It was RESOLVED that:-

- (a) the requirements of the Competition and Markets Authority order and the deadline of 10 December 2019 for the Kent Fund to set its investment advisors strategic objectives be noted;
- (b) the objectives for the investment consultancy provider to the Kent Fund be approved, subject to the changes to the wording discussed and agreed by the committee in the meeting; and
- (c) authority be delegated to the Corporate Director of Finance to agree these objectives with Mercer Ltd.

**UNRESTRICTED ITEMS**  
*(meeting re-opens to the public)*

**165. Fund position statement**  
*(Item 8)*

*Ms Arbuckle and Mr Page from Mercer Ltd remained in the meeting for this item at the invitation of the committee.*

1. Mr Vickers introduced the report and Ms Arbuckle responded to comments and questions from the committee, including the following:-

- a) asked about the possibility of reallocating some funds to boost investment in multi-asset credit, Ms Arbuckle advised that it would be a good idea to grow multi-asset credit and fixed income funds to their optimum size, as set out in the committee's investment strategy; and
- b) one speaker suggested moving more funds into property, using a reputable firm, as the property market may enjoy a further boom in the future.

2. Arising from the advice given at paragraph 1.a) above, the Chairman proposed and Mr J Wright seconded that £100m be transferred from the Baillie Gifford fund and directed into multi-asset credit. This would allow the County Council to further diversify its portfolio, as set out in its strategy for 2020. The committee discussed whether or not this should be delayed until after the General Election on 12 December but were in agreement that the transfer should be made as soon as possible.

*Agreed without a vote.*

- c) asked how this would affect the ability of the Baillie Gifford fund to perform well, Ms Arbuckle advised that investments in fixed-income funds would have more protection.

3. It was RESOLVED that:-

- a) the information set out in the report and given in response to comments and questions be noted; and

- b) £100m be transferred from the Baillie Gifford fund and directed into multi-asset credit, as soon as possible.

## **166. ACCESS pooling update**

*(Item 9)*

It was RESOLVED that the information set out in the report be noted.

## **167. Training**

*(Item 10)*

It was RESOLVED that the revised training strategy be approved and the need to complete an assessment of the committee's training needs be noted.

## **168. Pensions Administration**

*(Item 11)*

*Barbara Cheatle, Pensions Manager, was in attendance for this item.*

1. Mrs Cheatle introduced the report and highlighted the reduction in the number of enquiries from scheme members, partly due to the new format of pensions illustrations and partly due to more scheme members using the online calculation facility. Work to address the backlog of cases was continuing, and more staff could instead be deployed on new work, but there was still a challenge around the recruitment and retention of permanent staff. To 'future-proof' the service and establish a more robust career path, a new staffing structure had been introduced.

2. The Charman thanked Mrs Cheatle and her team for the work they undertook, the accuracy and quality of which was vital to the County Council's good reputation as a pension provider and the confidence of scheme members that their pensions were being well managed. This was endorsed by the committee.

3. Mrs Cheatle responded to comments and questions from the committee, including the following:-

- a) concern was expressed about the value for money represented by the cost of the temporary assistance bought in – approximately £350,000 - to clear the backlog of cases. Asked if the new staffing structure would avoid the need for this expense in the future, Mrs Cheatle advised that this would be easier to assess once full staffing had been achieved; and
- b) a view was expressed that the level of resourcing and the effectiveness of the new structure would need to be appraised honestly.

4. It was RESOLVED that:-

- a) the information set out in the report be noted and the Pensions team be thanked for their work, which was vital to the County Council's good reputation as a pension provider; and
- b) a call-off from the Norfolk Framework be undertaken to engage a company to help clear backlog cases.

## **169. Fund Employer Matters**

*(Item 12)*

*Steve Tagg, Senior Accountant, was in attendance for this item.*

1. Mr Tagg introduced the report and responded to comments and questions from the committee, including the following:-

a) asked if there were any employers who consistently paid their contributions to the scheme late, Mr Tagg advised that one, a local authority trading company, had made payment slightly late due to changes in the staff dealing with the work. He assured the committee that any late payment would always be promptly followed up in a monthly meeting, and any persistent late payers reported to the Pensions Regulator. There had been only one such case to report, and some employers consistently paid their contributions early.

2. It was RESOLVED that the employer report be noted and it be agreed that:-

a) the Amey Community Ltd admission agreement may be opened for the two staff transferring to them from Kier Facility Services Ltd;

b) any surplus may be returned by officers to Canterbury Archaeological Trust;

c) any surplus may be returned by officers to Invicta Telecare trading as Centra Pulse;

d) the Chairman may sign the minutes relating to recommendations a) to c) at the end of today's meeting; and

e) once legal agreements have been prepared for the Amey matter, the Kent County Council seal can be affixed to the legal document.

## **170. Date of next meeting**

*(Item 13)*

It was noted that the next meeting of the committee would be held on Friday 7 February 2020, commencing at 10.00 am.

By virtue of paragraph(s) 3 of Part 1 of Schedule 12A  
of the Local Government Act 1972.

Agenda Item 6

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By virtue of paragraph(s) 3 of Part 1 of Schedule 12A  
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By: Chairman Superannuation Fund Committee  
Corporate Director of Finance

To: Superannuation Fund Committee – 7 February 2020

Subject: **Responsible Investment (RI) / Environmental Social and Governance (ESG) policy**

Classification: Unrestricted

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Summary: To review the Kent Fund's RI / ESG policy

## **FOR DECISION**

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### **INTRODUCTION**

1. As the extra meeting on the Committee's annual meeting schedule today's meeting provides an opportunity for members to review the Fund's approach to Responsible Investment (RI).
2. This is a very important and topical issue and its important that the Fund's RI policy is appropriate and fit for purpose.
3. The purpose of today's review is to consider whether the Kent Fund's Responsible Ownership policy and the Corporate Governance section of the Investment Strategy Statement's should be updated.

### **BACKGROUND**

4. In accordance with LGPS regulations the Kent Fund is required to publish its policy on how social, environmental or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments, as well as their policy on the exercise of rights (including voting rights) attaching to investments.
5. Copies of the Kent Fund's current Responsible Ownership Statement and Investment Strategy Statement (ISS) and attached at appendices A and B. The responsible ownership statement describes the Fund's approach to environmental, social and governance issues and the ISS includes a section describing the Fund's commitment to promoting good corporate governance.
6. The Committee last reviewed the Responsible Ownership Statement some time ago and the ISS at its meeting in September 2019.

### **SCHEME ADVISORY BOARD (SAB) CONSULTATION**

7. The local scheme advisory board has recently issued for consultation part 1 of their proposed guidance on the duties of Investment Decision Makers in LGPS funds with regard to developing and maintaining a RI policy. The deadline for

responses to the consultation is 31 January and Kent will with other ACCESS authorities be sending a joint response and a copy of the response will be shared with members at the March meeting.

## **WORKSHOP**

8. To support members with the review of the Fund's RI policy Mercer have been asked to host a workshop and a copy of their slides are attached at appendix C.
9. Officers and Mr Simkins felt it would be helpful for members to have a look at another LGPS fund's RI policy and given that the Hampshire fund though bigger, shares similar characteristics with the Kent fund theirs seemed to be an appropriate policy to consider. A copy of the current policy is attached at appendix D and Andrew Boutflower an officer with the Hampshire Fund has been invited to present to the Committee.

## **RECOMMENDATIONS**

10. Members are asked to consider whether the Kent Fund's policy on Responsible Ownership and the Corporate Governance section of the Investment Strategy Statement's should be updated and to agree next steps.

Alison Mings  
Treasury and Investments Manager  
[Alison.mings@kent.gov.uk](mailto:Alison.mings@kent.gov.uk)

## **Statement of responsible ownership**

The Superannuation Fund Committee is fully aware of its fiduciary responsibility to obtain the best possible financial return on the investments of the Pension Fund (the Fund) for acceptable levels of risk. This responsibility is to keep down as far as possible increases in the cost of the scheme to scheme employers and ultimately to dampen the cost of the scheme to council tax payers in Kent.

The Fund also seeks through good management of Environmental, Social and Governance (ESG) issues to help the financial performance and improve shareholder investment returns in the companies in which it invests.

## **Fiduciary responsibility**

As a consequence of the Fund's fiduciary responsibility to the taxpayer it will not impose restrictions upon the external investment managers on specific stocks or countries which they can or cannot invest in.

The Fund is not positioned either to impose blanket restrictions or to adjudicate which stocks or countries the Fund should invest in and is aware that:

- restrictions will reduce the accountability of the investment managers
- it is very difficult to determine what activities should be prohibited. This is an issue of individual conscience
- it is only possible for investment managers to influence company behaviour if they are a shareholder.

The Committee retains the right to intervene with an investment manager if they undertake investments which are not acceptable for example illegal activities, major fraud.

## **UK Stewardship Code**

The Committee expects the investment managers who hold shares on its behalf to fully comply with the [Financial Reporting Council's \(FRC\) UK Stewardship Code](#) and to fully participate in voting at company annual general meetings. Investment managers provide feedback information on voting decisions on a quarterly basis.

## **Environmental, Social and Governance (ESG) issues**

The Committee expects the investment managers to engage with companies to monitor and develop their management of ESG issues in order to enhance the value of the Fund's investments. The Committee also expects feedback from the investment managers on the activities they undertake.

The Fund would engage directly with a company in which it is invested, in exceptional circumstances.

## **UN principles for responsible investment**

The Fund supports and has signed up to the [UN principles for responsible investment](#). The 6 principles are, we will:

1. incorporate ESG issues into investment analysis and decision making
2. be active owners and incorporate ESG issues into our ownership policies and practices
3. seek appropriate disclosures on ESG issues by entities we invest in
4. promote acceptance and implementation of the principles within the investment industry
5. work together to enhance our effectiveness in implementing the principles
6. each report on our activities and progress towards implementing the principles.

### **Climate change**

As a member of [The Institutional Investors Group on Climate Change \(IIGCC\)](#) we will monitor developments on climate change and use the research undertaken to monitor and challenge our investment managers.

### **Shareholder litigation**

The Fund will actively participate in class actions in the USA and UK where it is of clear financial benefit to it.

### **Policy amended October 2019**



# Kent County Council Superannuation Fund Investment Strategy Statement 2019



# Investment Strategy Statement 2019

## Introduction

1. Regulation 7(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 requires administering authorities to formulate and to publish a statement of their investment strategy, in accordance with guidance issued from time to time by the Secretary of State.
2. Kent County Council is responsible for administering the Kent County Council Superannuation Fund under the Local Government Pension Scheme (LGPS) Regulations. The Council has a duty to ensure that scheme funds not immediately required to pay pension benefits are suitably invested and to take proper advice in the execution of this function. It has delegated these responsibilities to the Superannuation Fund Committee.
3. The Committee has prepared the Investment Strategy Statement (ISS) in accordance with the Guidance on Preparing and Maintaining an Investment Strategy Statement.
4. In September 2016 the Department for Communities and Local Government (DCLG) published Guidance on Preparing and Maintaining an Investment Strategy Statement (ISS). This replaces the previous requirement for a Statement of Investment Principles.

The ISS required by Regulation 7 must include:

- A requirement to invest money in a wide range of investments;
  - The authority's assessment of the suitability of particular investments and types of investments;
  - The authority's approach to risk, including the ways in which risks are to be measured and managed;
  - The authority's approach to pooling investments, including the use of collective investment vehicles and shared services;
  - The authority's policy on how social, environmental or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and
  - The authority's policy on the exercise of rights (including voting rights) attaching to investments.
5. As set out in the Regulations the ISS will be reviewed at least every three years.

## Investment Strategy

6. The Kent Fund's primary objective is to ensure that over the long term it will have sufficient assets to meet pension liabilities as they fall due.
7. In order to achieve this objective the investment strategy seeks to:
  - Maximise returns for a given level of risk;
  - Ensure liquidity requirements are met at all times;
  - Achieve and maintain a 100% funding level;
  - Maintain stable employer contribution rates.

# Investment Strategy Statement 2019

8. The Fund has had a customised asset allocation for a number of years and has regularly reviewed this in light of valuation results, changes in liabilities and investment cycles.
9. In 2018 the Superannuation Fund Committee approved a revised asset allocation for the Pension Fund based on a review of its investments strategy that it carried out with the assistance of its investment advisor, Mercer. The Fund's investments are allocated across a range of asset classes with the largest allocation being to equities which also accounts for the majority of the investment risk taken by the Fund.
10. The Fund's current strategic asset allocation is shown in the table below:

**Table 1: Asset allocation**

Asset class	Allocation %
UK Equities	23.5
Overseas Equities	32.0
Fixed Income	15.0
Property	13.0
Private Equity	4.0
Infrastructure	3.5
Absolute Return	8.0
Cash	1.0
<b>Total</b>	<b>100.0</b>

11. The Fund has an 84% allocation to growth assets (equities, property, absolute return and infrastructure) in order to meet the long-term funding assumptions set out in the 2016 actuarial valuation and a 16% allocation to defensive assets (bonds and cash) to help manage overall levels of funding volatility.
12. Over the long term, equities are expected to outperform other liquid asset classes, particularly bonds. Allocations to asset classes other than equities and bonds allow the Fund to gain exposure to other forms of risk premium and can reduce the overall volatility of portfolios. These assets are expected to generate returns broadly similar to equities over the long term and so allocations to these can maintain the expected return and assist in the management of volatility.

## Investment management arrangements

13. All investment management activities are carried out externally and there is no internal management other than of cash flow. The Fund has a policy of appointing specialist managers who are expert in managing specific investment strategies which should help the Fund deliver over different investment cycles.
14. The current manager structure and the rationale for this is set out in the table overleaf:

# Investment Strategy Statement 2019

**Table 2: Investment Manager Structure**

Asset Class/Manager	Performance target	Style
<b>UK Equities</b>		
Schroders	Customised UK equity + 1.5%	High concentration
Woodford	FTSE All Share	Unconstrained
UBS	FTSE All Share	Tracking
<b>Global Equities</b>		
Baillie Gifford	Customised regional equity + 1.5%	Fixed weight regional equity
Sarasin	MSCI AC World + 2.5%	Thematic
M&G	MSCI AC World + 3%	Dividend growth
Schroders	MSCI AC World + 3-4%	Quantitative value
Impax	MSCI AC World + 2%	Environmental themed
UBS	FTSE World Ex UK	Tracking
UBS	FTSE Emerging Markets	Tracking
<b>Fixed Income</b>		
Schroders	3 months Sterling Libor + 4%	Total return
Goldman Sachs	+3.5-6%	Target return long term hold
<b>Property</b>		
DTZ	IPD Customised Pension Fund Index	Direct UK property
Fidelity	IPD UK PF All Balanced Property Fund Index	Pooled UK property fund open ended
Kames	IPD UK PF All Balanced Property Fund Index	Pooled UK property fund close ended
M&G	IPD UK PF All Balanced Property Fund Index	UK residential property fund
<b>Absolute Return</b>		
Pyrford	RPI + 5%	Low risk equities/fixed income/cash
Ruffer	RPI	Low risk equities/fixed income/cash
<b>Alternatives</b>		
Private Equity - YFM	GBP 7 Day LIBID	Small value direct UK
Private Equity - HarbourVest	GBP 7 Day LBID	Global fund of funds
Infrastructure - Partners Group	GBP 7 Day LBID	Global fund of funds

# Investment Strategy Statement 2019

## Risk Measurement and Management

15. At four of the Committee's five planned meetings during the year it reviews the actual investment allocation relative to the agreed asset allocation benchmark as well as individual manager performance and related risks. The Committee has to make its assessment in the context of how it will achieve the required investment return of 5.4% per annum assumed by the Fund actuary.
16. The Committee engages Mercer to assist it with its review and receives reports from Officers based on their discussions with investment managers and examination of relevant information.
17. The Fund maintains a full Risk Register which is reported annually to the Committee. This covers the full range of risks faced not just investment risks.
18. The principal investment risks faced are:

**Table 3: Investment Risks**

Risk	Mitigation
Equity allocation risk	The Fund holds equities in order to achieve higher investment returns however in line with its review of the Fund's asset allocation it is now reducing its exposure to traditional equities to reduce the impact of a material fall in equity markets. The Fund invests in managers with a variety of investment styles.
Asset class concentration risk	The Fund is reducing its allocation to UK equities to reduce concentration risk. It is also seeking to diversify its bond allocation.
Active manager risk	The Committee believes that good active managers will add value to the Fund and it aims to establish long term relationships with managers. Managers of the larger mandates annually attend Committee meetings and others have regular meetings with officers.
Inflation risk	Current inflation remains low. The fund invests in equities and property and is increasing its investment in infrastructure to achieve inflation protection.

# Investment Strategy Statement 2019

Risk	Mitigation
Exchange rate risk	The Fund is a long-term investor and can withstand short term currency fluctuations. The Fund monitors its overseas investments' currency exposure but has not made arrangements to hedge this risk.
Alternative asset classes risk	The Fund is increasing its investments in non-property alternative investments following its review of the strategic asset allocation in 2018. It is monitoring the illiquidity risk arising.
Liquidity risk	The Fund actively manages its cash flows over the short and longer term to ensure liquidity.
Custody risk	The Fund must maintain its beneficial ownership of Fund assets when held in custody or trading and it does this through its global custodian. Counterparty risk is mitigated through a robust selection and legal contracting process. Custody risk is reducing as the Fund moves its investments into pooled funds.
Transition risk	The risk of incurring additional costs in relation to the transitioning of assets between external managers is managed through the use of professional advisers and experienced in house staff.
Stock lending risk	The Fund has agreed a stock lending policy for its segregated mandates as well as for its investments in the ACCESS pool. This is a limited programme of stock lending and risk is mitigated by lending to approved counterparties against non-cash collateral mainly comprising of Sovereigns, Treasury Bonds and Treasury Notes.
Regulatory risk	Regulatory risk is predominantly transferred to the externally appointed investment managers who have to meet regulatory requirements. The Fund only manages cash internally and complies with CIPFA and MHCLG requirements in relation to that.

# Investment Strategy Statement 2019

Risk	Mitigation
Investment advice risk	The Fund has engaged Mercer as its investment consultant. The Committee regularly considers the effectiveness of the advice given.
Unmatched liability risk	The Fund is diversifying its investment in fixed income strategies which should more closely match the characteristics of the Fund's liabilities.

## Asset Pooling

19. The Fund is part of the ACCESS (A Collaboration of Central, Eastern and Southern Shires) pool. This is a group of like-minded funds valued at £44bn who came together to meet the Government criteria for pooling set out in November 2015. The ACCESS funds emphasise retaining as much decision making as possible locally in the exercise of their fiduciary responsibility.
20. In 2018 Link Fund Solutions contracted with the 11 ACCESS authorities to provide a pooled operator service. Link is responsible for operating an Authorised Contractual Scheme (ACS) along with the creation of investment sub-funds to meet the needs of the ACCESS funds.
21. The Kent Fund has made a commitment to pool its investments other than its direct property holdings but will rigorously apply the value for money test before moving assets into the pool.
22. During 2018-19 the Kent Pension Fund invested in 3 sub-funds managed by Baillie Gifford, Schroder and M&G. As at 31 March 2019 the total pooled was £2.6bn, being 42% of the total assets of the Fund. Further sub funds are being launched for equity and fixed income asset classes. The ACCESS pool is also making progress in establishing the appropriate structures for pooling alternative asset classes.
23. In February 2018 the Kent Fund also invested in pooled life funds managed by UBS. As at 31 March 2019 the value of this investment was £654m, 11% of the Fund's investments.

## Corporate Governance

24. The Committee has a fiduciary responsibility to scheme members and employers to maximise the investment returns it can achieve for a given level of risk. It therefore does not seek to impose ethically based screens which restrict investment managers from investing in certain companies.
25. The Committee is also committed to promoting good corporate governance in the firms which it invests in. It is expected that investment managers will have their own policies on voting on shareholder issues and on environmental, social and governance issues. The Committee expects the investment managers who hold shares on its behalf to fully comply with the Financial Reporting Council's (FRC) UK Stewardship Code and to fully participate in voting at company Annual General

# Investment Strategy Statement 2019

Meetings. Engagement with companies is taken very seriously and this is regularly discussed with investment managers. The investment managers report to the Committee quarterly on corporate governance issues including voting.

## Advice

26. The Committee takes advice and information from:

- The Council's Section 151 Officer and their staff;
- Barnett Waddingham, the Fund's actuary;
- Mercer, the Fund's investment consultant;
- Investment managers;
- Discussions with other LGPS funds;
- Attendance at seminars and conferences, and
- Financial press and media.

August 2019

### Kent County Council Pension Section

#### Fund benefits and contributions

Sessions House  
County Hall  
Maidstone  
Kent ME14 1XQ



03000 413 488



pensions@kent.gov.uk

### Kent County Council Treasury and Investments

#### Fund accounting and employer governance

Room 3.17  
Sessions House  
County Hall  
Maidstone  
Kent ME14 1XQ



03000 416 747



investments.team@kent.gov.uk





# RESPONSIBLE INVESTMENT / ENVIRONMENTAL, SOCIAL & GOVERNANCE (ESG) UPDATE

KENT COUNTY COUNCIL  
SUPERANNUATION COMMITTEE

February 2020

Page 33



# IMPORTANT NOTICES

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# AGENDA

These slides are addressed to the Superannuation Committee (the “Committee”) of the Kent County Council Superannuation Fund (the “Fund”).

They provide refresher training on Responsible Investment and consider how the Committee might wish to develop their current “Statement of Responsible Ownership” and take account of Environmental, Social and Governance (ESG) considerations in the Fund’s investment arrangements.

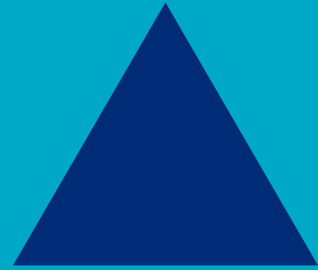
Page 35



- **What is ESG / Responsible Investment?**
  - **Why is it important?**
- **What has the Fund done to date?**
- **What next?**
  - Options for implementing Responsible Investment Considerations?
  - Options for developing the Fund’s policy.
- **Suggested Next Steps for discussion**

# WHAT IS RESPONSIBLE INVESTMENT AND WHY IS IT IMPORTANT

Page 36



# WHAT RESPONSIBLE INVESTMENT IS NOT....

**RI ≠ only investing in  
“nice” companies**

**RI ≠ excluding  
companies or sectors  
which are “bad”**

**RI ≠ accepting poor or  
volatile returns to make  
the world a better place**

**RI ≠ climate change  
alone**



# WHAT DOES ESG MEAN?

What is missing from current finance / investment processes?  
How might the future be different to the past?



# MORE DEFINITIONS

## RESPONSIBLE INVESTMENT (RI)

An investment approach that includes environmental, social and corporate governance (ESG) issues and broader systemic issues — for example, climate change and sustainable development — along with active ownership (stewardship).

### ESG

ESG refers to environmental, social, and corporate governance issues that investors are considering in the context of their investment portfolios.

### STEWARDSHIP

Voting and engagement with underlying companies and/or investment managers and engagement with policymakers for risk/return reasons.

### CLIMATE CHANGE

The risks and opportunities that stem from the transition to a low-carbon economy and the physical impacts of climate change.

## SUSTAINABILITY

In its simplest form, sustainability is “the ability to sustain.” The most widely accepted definition is “that which meets the needs of current generations without compromising the ability of future generations to meet their own needs.”

## RI ≠ SRI ≠ Ethical

### SOCIALLY RESPONSIBLE INVESTMENT (SRI)

Intended to balance an investor’s values with performance considerations, and typically seeks to achieve a trade-off between social and financial objectives.

### ETHICAL INVESTING

An investment philosophy guided by moral values, ethical codes or religious beliefs and originally rooted in negative screening of investments in sensitive sectors.

### IMPACT INVESTING

Investments made into companies, organisations and funds with the intention to generate measurable social and environmental impact alongside a financial return.

← FINANCIAL →

← NON-FINANCIAL →

# WHAT DOES STEWARDSHIP MEAN?



Stewardship aims to promote the **long term success of companies** in such a way that the **ultimate providers** of capital also **prosper**. Effective stewardship **benefits** companies, investors and the economy as a whole.

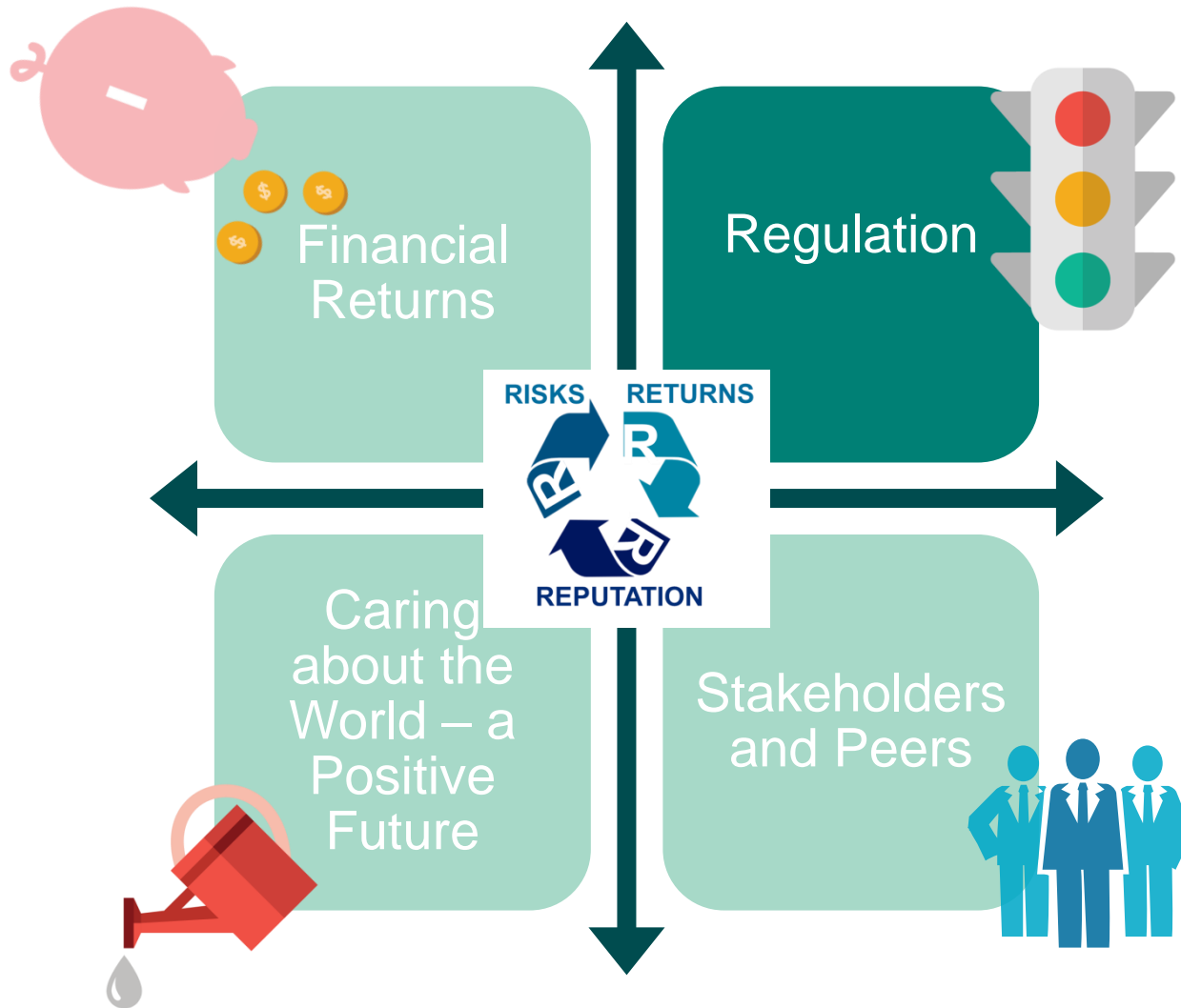
For investors, stewardship is **more than just voting**. Activities may include **monitoring and engaging with companies** on matters such as strategy, performance, risk, capital structure, and corporate governance, including culture and remuneration. **Engagement is purposeful dialogue with companies on these matters as well as on issues that are the immediate subject of votes at general meetings.**

Source: FRC

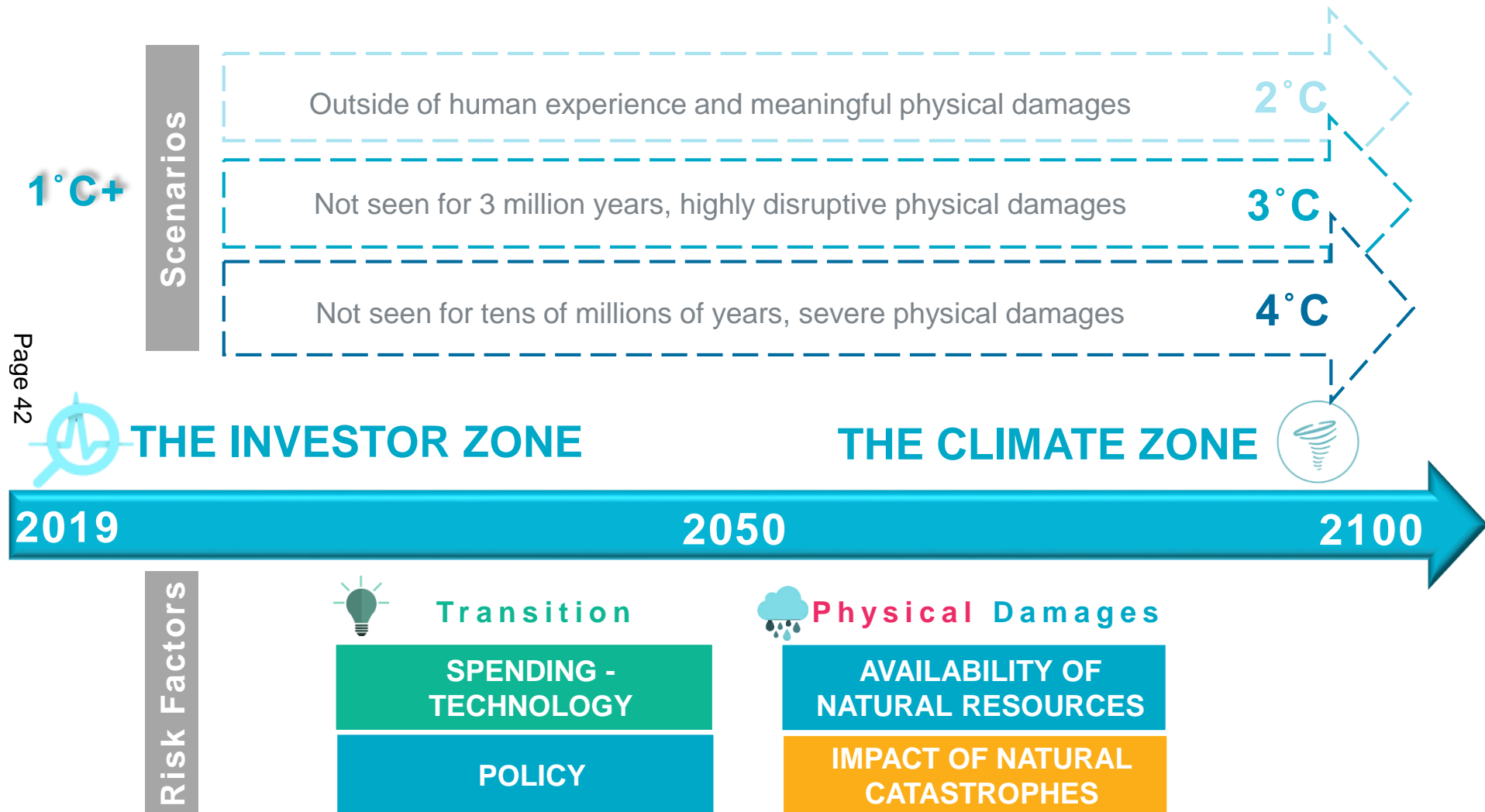
Good stewardship should help to both create and preserve value over the long-term for companies and markets



# WHY DOES ESG MATTER?



# WHY DOES CLIMATE RISK MATTER?



Page 42

# WHAT DOES ESG MATTER – GOVERNMENT CONSULTATION

- The Scheme Advisory Board has prepared and is currently consulting on Responsible Investment guidance.
- As such, the draft guidance seeks to consolidate and clarify Responsible Investment duties and obligations within the LGPS - regardless of investment beliefs and views on the “Spectrum of Capital” shown to the right.

Page 43

The Guidance sets out:

- Responsible Investment definitions;
  - Statutory duties and responsibilities;
  - Non-Statutory duties; and
  - Details of recent strengthening of RI requirements and reporting in trust based pensions.
- Mercer don’t believe the guidance is saying much new and are hopeful that part 2, which we understand will follow in due course, will expand on expectations and provide more concrete detail.

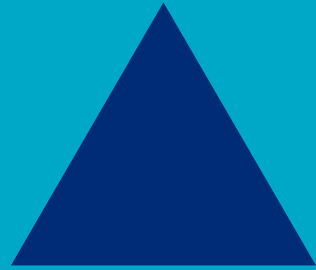
The spectrum of capital



\* This integration of sustainable practices across an organisation’s core business may also be termed Corporate Social Responsibility (CSR), although many organisations have a separate (often philanthropic) CSR ‘carve-out’ that is distinct from their approach to sustainability  
Source: GB Social Impact Investment Taskforce, Asset Allocation Working Group (2014)

# WHAT HAS THE BEEN DONE TO DATE?

Page 44



## WHAT HAS BEEN DONE TO DATE?

- The Committee has prepared a Statement of Responsible Ownership setting out its high level views on RI.
- The Fund's Investment Strategy Statement also includes a Corporate Governance statement commenting briefly on the Committee's RI views.
  - Are these still fit for purpose or do they require review?
- The Fund has become a signatory to the PRI, "Principles for Responsible Investment" the world's leading investor body for responsible investment.

Page 45

The Fund has signed up to ACCESS's voting policy providing managers with clarity on its expectations around exercising the voting rights attached to the Fund's investments

- The Committee receives quarterly manager updates from Mercer which include "ESG ratings" for its investment managers (where Mercer maintain coverage).
  - ESG rating information has been included in the manager selection advice provided to the Committee as part of the Absolute Return and MAC selection undertaken in recent years.
- The Fund invests a small portion of its equities with Impax, who Mercer regards as a market leader in environmental equity investment, in their Environmental Markets Fund.

# MERCER'S ESG RATING SCALE

ESG ratings are undertaken by Mercer's global manager research team. They are on a scale from 1 (highest) to 4 (lowest) and assess how well managers integrate ESG factors into investment processes.

ACTIVE

## ESG 1

Leader in the integration of ESG factors and active ownership into core processes.

## ESG 2

Less advanced than ESG1 investors but with moderate integration of ESG factors and active ownership.

## ESG 3

Limited progress with respect to ESG integration and active ownership, albeit with signs of potential improvement.

## ESG 4

Little or no integration of ESG factors or active ownership into core processes and no indication of future change.

Ratings for passive equity strategies differentiate how well firms undertake their stewardship activities such as voting, engagement, industry collaboration and reporting.

PASSIVE

## ESG p 1

Leaders in Voting & Engagement across ESG topics, with active ownership activities and ESG initiatives undertaken consistently at a global level

## ESG p 2

Strong approach to Voting & Engagement across ESG topics, and initiatives at a regional level, with progress made at a global level

## ESG p 3

Focus tends to be on Voting & Engagement on governance topics only, more regionally focused with less evidence of other internal ESG initiatives

## ESG p 4

Little or no initiatives taken on developing a Voting & Engagement capability, with little progress made on other ESG initiatives

# MANAGER ESG RATINGS FOR THE FUND

Manager	Mandate	Mercer Research Rating*	Mercer ESG Rating**	Rating Change Over Period?
Baillie Gifford	Active Global Equity	A	ESG2	-
Schroders	Active UK Equity	N	N	-
	Active Global Equity - QEP Value	A	ESG3	-
UBS	Passive UK, Global and EM Equities	A	ESGp3	-
M&G	Active Global Dividend Equity	N	N	-
Sarasin	Active Global Thematic Equity	B	ESG2	-
Impax	Global Environmental Markets Equity	A (T)	ESG1	-
Woodford	UK Equity Income	C (T)	ESG4	-
Goldman Sachs	Buy and Maintain Global Credit	N/A***	N/A***	-
Schroders	ISF Strategic Bond	B+	ESG3	-
Pyrrford	Global Absolute Return	R	R	-
Truffer	Global Long only Absolute Return	A	ESG2	-
HarbourVest	Private Equity	B+	ESG3	-
YFM	Private Equity	N	N	-
Partners Group	Infrastructure	B+	ESG2	-
DTZ	Segregated UK Direct	A	ESG2	-
Fidelity	UK Real Estate	A	ESG3	-
Kames	Active Value Property	B+	ESG3	-
M&G	UK Residential Property Fund	A(W)	ESG2	-
A	ESG1 or ESG2	✓		
B+	ESG3	-		
B or C	ESG4	*		

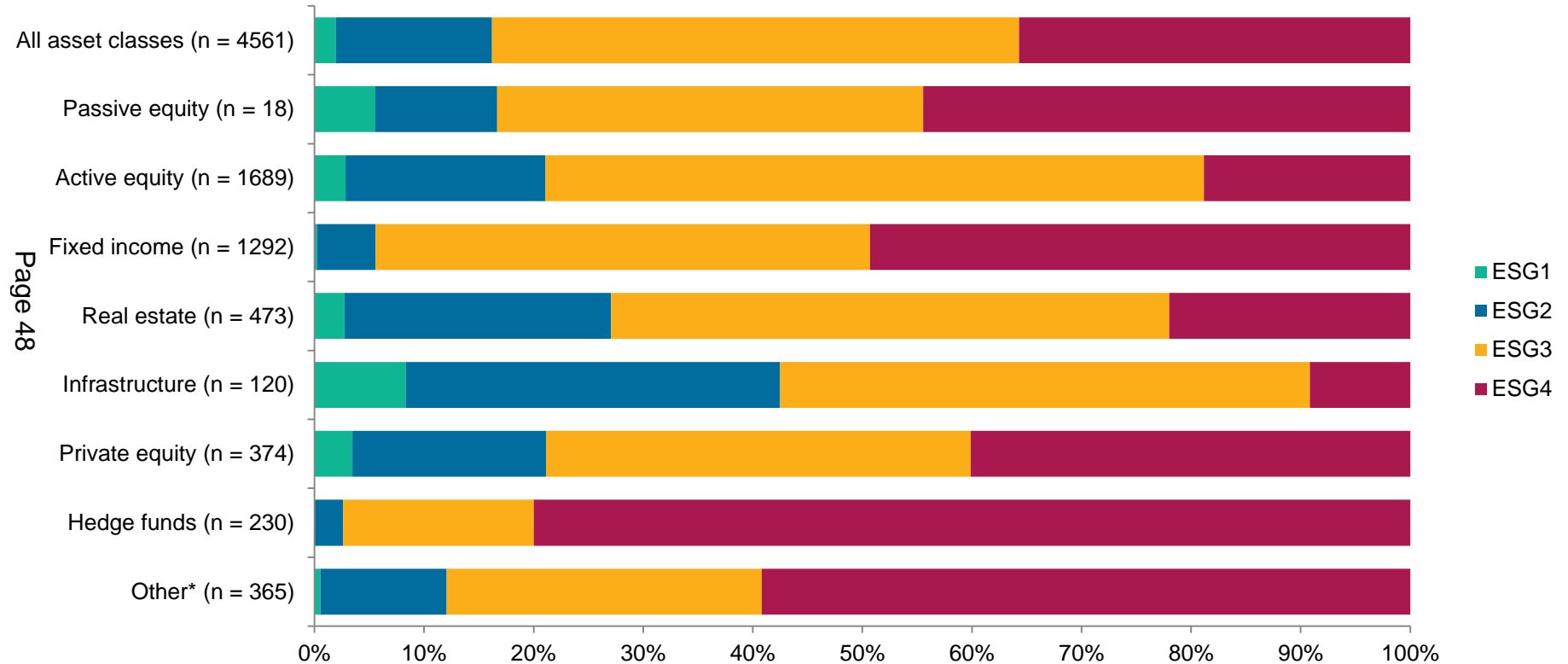
\*For an explanation of Mercer's ratings see the Appendix

\*\*ESG/ESGp = Environmental, Social and Governance.

\*\*\* Mercer do not maintain a rating for the specific GSAM strategy which the Fund invests in but we do rate their Global Buy and Maintain Credit capabilities "A".

# WHAT CAN BE DONE VARIES BY ASSET CLASS

Distribution of 4,500+ Mercer ESG ratings\*\*



Page 48

Over 4,500 strategies rated currently – ratings began in 2008



Less than 17% achieve an ESG1 or ESG2



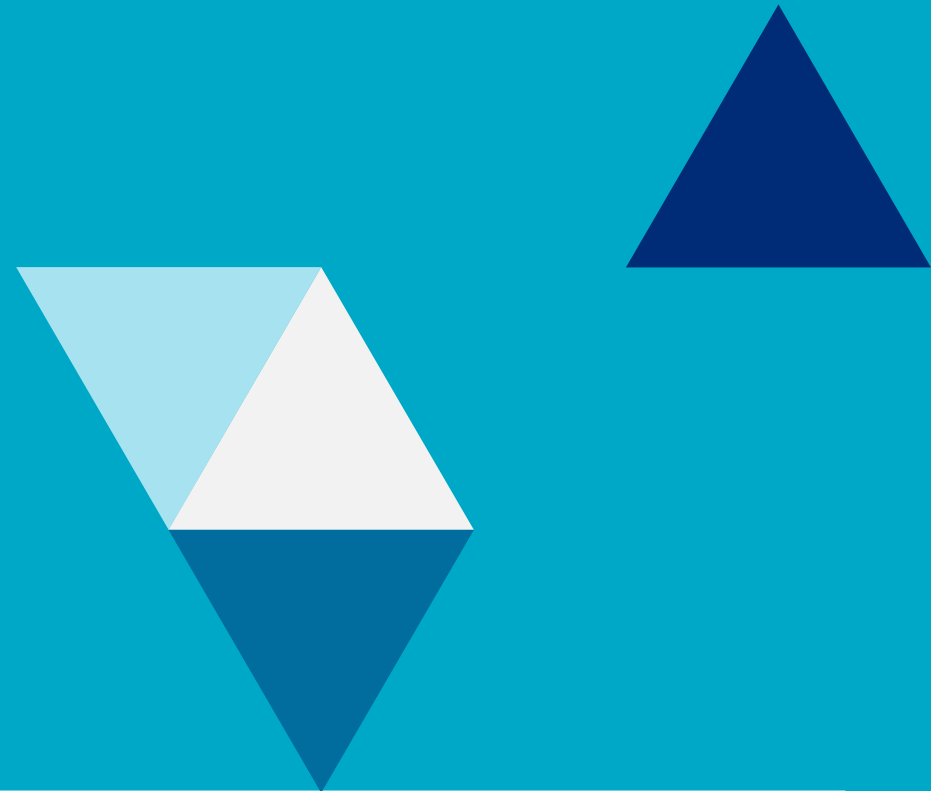
ESG ratings for passive equity introduced in 2014



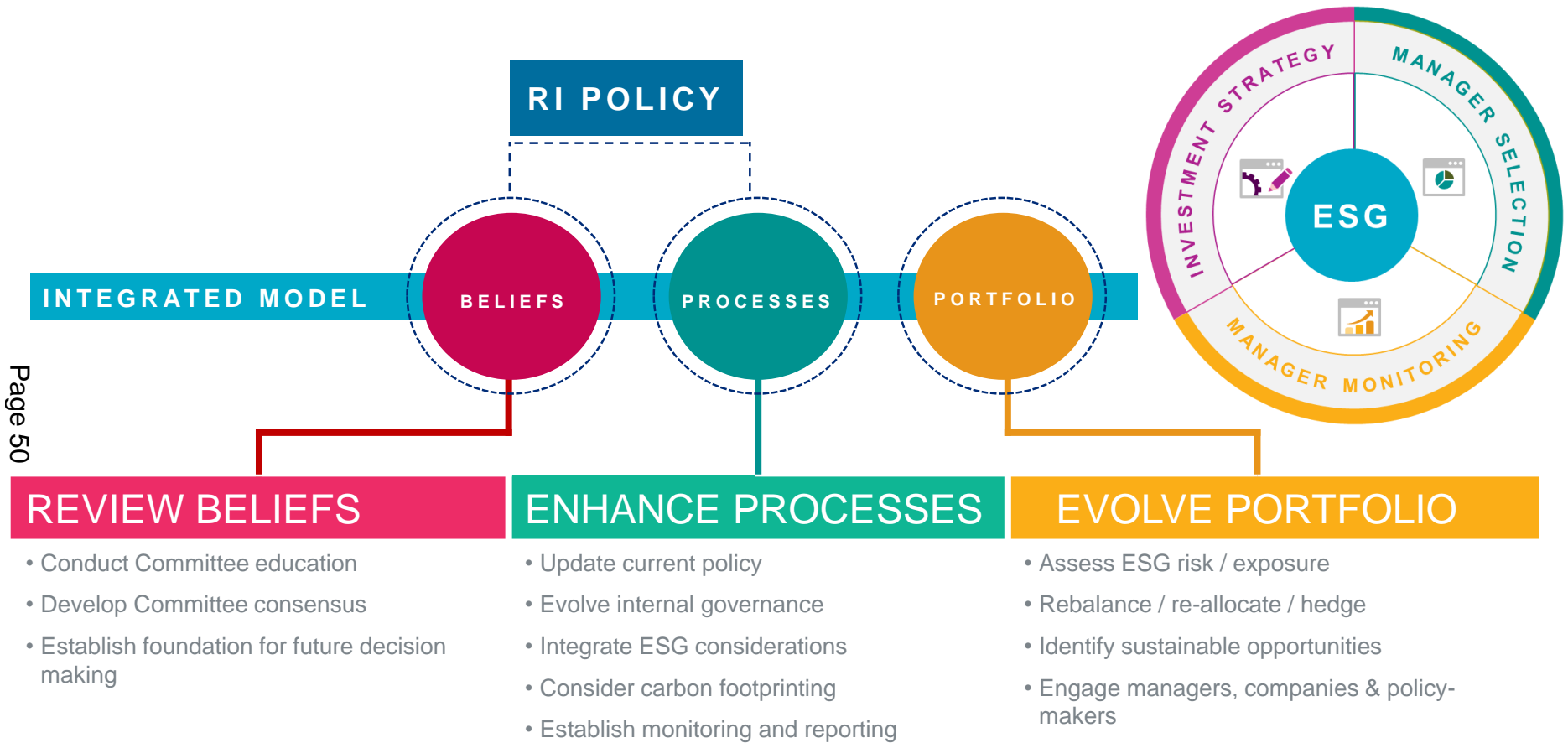


# WHAT NEXT?

Page 49



# GOVERNANCE – BELIEFS TO PORTFOLIO



Page 50

**Developments in the Fund's Responsible Investment policy don't need to happen overnight or be revolutionary**

# KEY STRATEGIES FOR IMPLEMENTATION OF RI CONSIDERATIONS



Page 51

## Integration

Include ESG factors in investment analysis/decisions to assess materiality



**OBJECTIVE:**  
Financial objectives + risk management improvement

## Stewardship

Actively engage with companies failing to address ESG risks through voting and engagement



**OBJECTIVE:**  
Financial objectives + financial system improvement

## Thematic Investment


Allocate to sustain. themes/impact investments, e.g. renewable energy, water, social housing



**OBJECTIVE:**  
Financial objectives + positive social + environmental impact

## Exclusions

Screen out sectors or companies deemed irresponsible or misaligned with values



**OBJECTIVE:**  
Align with values/ reputation/risk management or longer term financial expectations

# OPTIONS FOR DEVELOPING THE FUND'S RESPONSIBLE OWNERSHIP POLICY AND POSITION



## RI Beliefs Survey

**Aim** - Clarify the Committee's views on RI.

**Why?** - Assist in updating the Responsible Ownership Statement and planning future work

Page 52

## ESG Ratings Review

**Aim** – Understand how the Fund's managers compare to their asset class peers.

**Why?** – Improve understanding. Set targets for future manager appointments (no lower than ESG3). Engage laggards and measure future progress.

## Carbon Footprint Analysis

**Aim** – Understand the carbon intensity of the Fund's equity portfolio.

**Why?** – Improve understanding. Set targets for reducing it over time.

## Voting & Engagement review

**Aim** – Assess the level of engagement and voting managers are undertaking on the Fund's behalf.

**Why?** – Allows Fund to engage with managers (ACCESS?) to do better.

## Stewardship review

**Aim** – Understand whether the Fund's managers have reported in line with the new 2020 Stewardship code and how well they comply.

**Why?** – Allows Fund to engage with managers to improve.

## Climate change scenario stress testing

**Aim** – Understand how the Fund will perform in different climate change scenarios.

**Why?** – Improve understanding. Incorporate into strategic decision making.

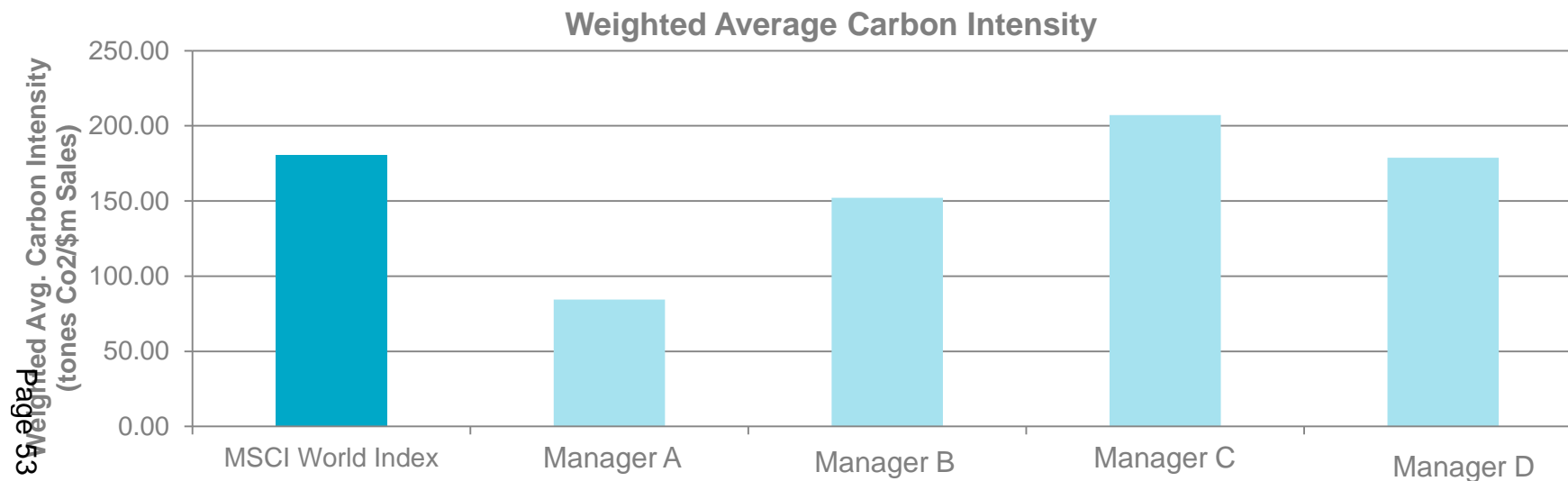
## Consider introducing thematic allocations

**Aim** – Better manage risks or capitalise on the potential returns from a move to a low carbon economy and broader sustainable opportunities.



e.g. through the ACCESS arrangements UBS offer a "Climate Aware Global Equity Fund"

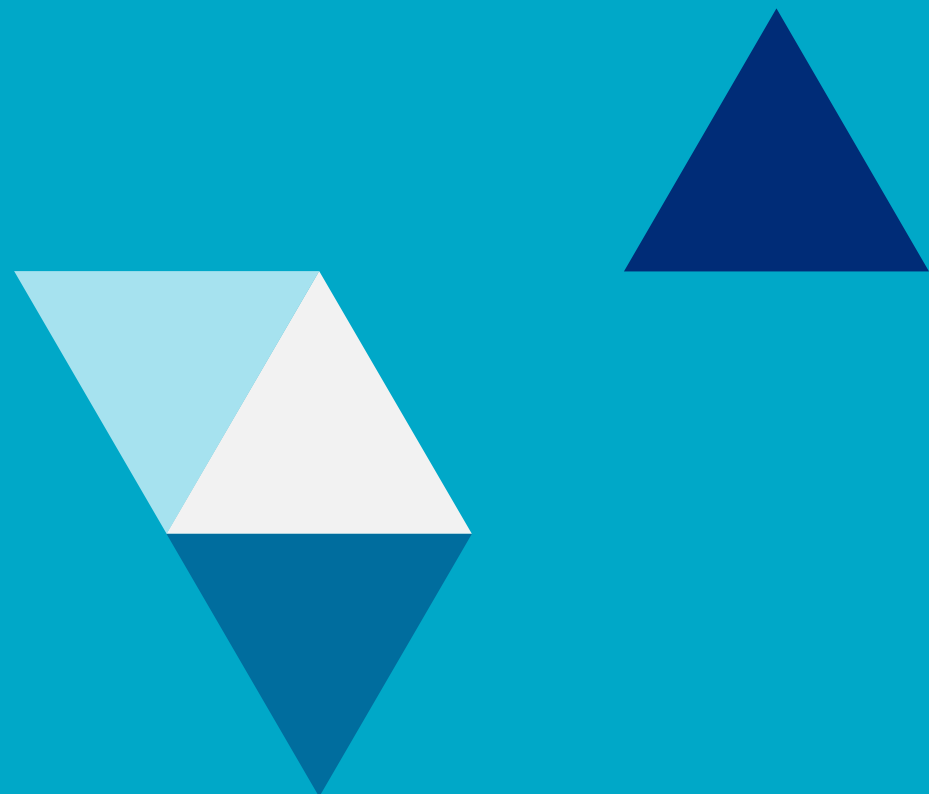
# CARBON FOOTPRINT ANALYSIS



- Relative to the MSCI World benchmark:
  - **Manager A** is 53% less carbon intensive
  - **Manager B** is 16% less carbon intensive
  - **Manager D** is 1% less carbon intensive
  - **Manager C** is 15% more carbon intensive. The carbon intensity is attributable to its overweight exposure to Utilities relative to the benchmark
- **Potential Actions**
  - Engage with higher intensity managers to understand whether they are aware of their carbon footprint and which companies are contributing to it. Do they have plans to see it reduce?
  - Consider appointing a manager with a low carbon approach to reduce the Fund's exposure to climate risk.

# SUGGESTED NEXT STEPS

Page 54



# SUGGESTED NEXT STEPS

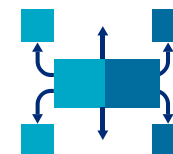


Agree if any action is required to update the Statement of Responsible Ownership

More training? RI belief's survey?

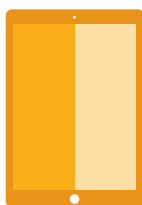


Update Corporate Governance statement in ISS (if applicable) and include ESG risk in risk section



If beliefs have evolved, consider how best to align investments with these

Page 55

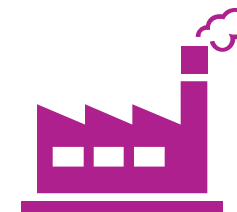


Monitor and assess what the managers are doing on the Committee's behalf

Develop a list of RI questions to use at manager review meetings



Consider whether carbon footprint analysis would be worthwhile

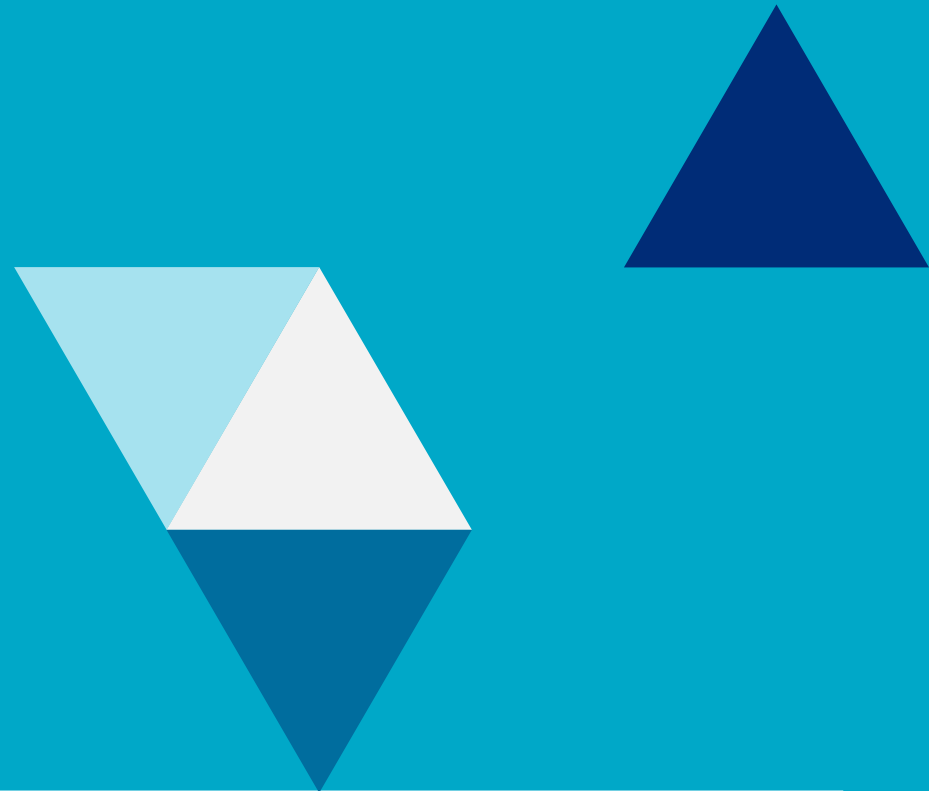


Consider exploring thematic opportunities and low carbon e.g. the UBS Climate Aware fund available through ACCESS

What else do ACCESS plan to offer?

# APPENDIX

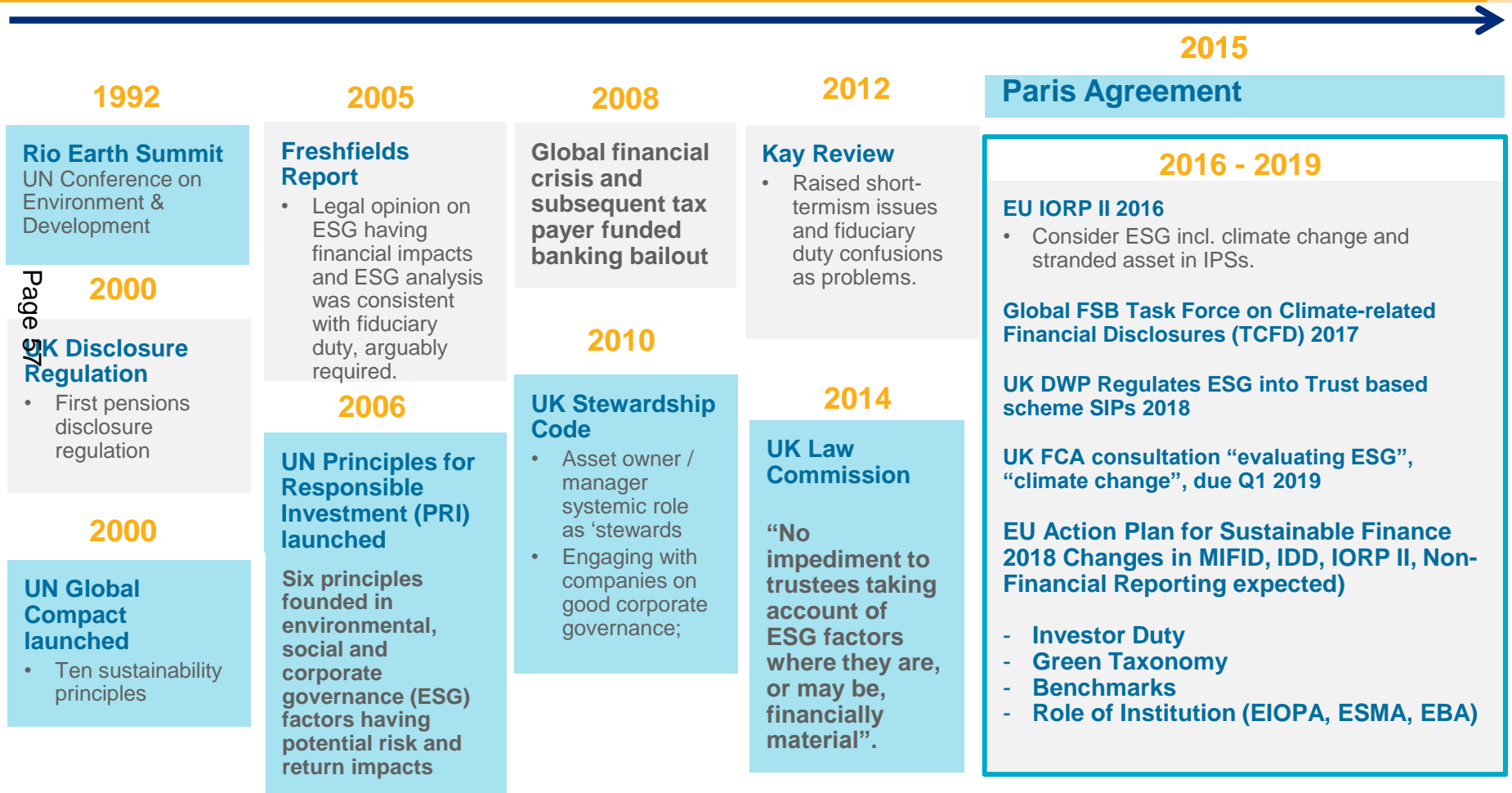
Page 56





# THE INVESTMENT CASE – DUTY

INVESTMENT DECISION MAKERS WITH DISCRETIONARY POWERS HAVE A FIDUCIARY DUTY TO THEIR BENEFICIARIES, WITH INTERPRETATION OF THESE DUTIES EVOLVING OVER TIME



# MERCER'S ESG RATING CRITERIA

## ACTIVE (all asset classes)

### IDEA GENERATION

- ESG factors integrated into active fund positions as a source of value added.
- Identification of material ESG factors - skill of team members, data sourcing

### PORTFOLIO CONSTRUCTION

- Efforts to integrate ESG driven views into the portfolio's construction.

### IMPLEMENTATION

- Engagement and proxy voting activities (if applicable).
- Investment horizon align with ability to effectively implement ESG views?

### BUSINESS MANAGEMENT

- Firm-level support for ESG integration, engagement activities and transparency.



## PASSIVE (equities)

### VOTING & ENGAGEMENT

- Policy, process and prioritisation.
- Quality of engagements.

### RESOURCES & IMPLEMENTATION

- Data analysis to enhance active ownership.

### ESG INTEGRATION

- Skill set of resources.
- Effectiveness of engagement outcomes.

### FIRMWIDE COMMITMENT

- Collaborative initiatives and engagement with regulators and policymakers.

# APPLICATION & OPPORTUNITY BY ASSET CLASS

	Manager Progress on ESG Integration*	Availability of Sustainability Themed Strategies **
Public Equity (Active)	Medium/High	Low/Medium
Fixed Income	Low/Medium	Low
Real Estate	Medium/High	Low
Private Equity and Debt	Medium	Low/Medium
Infrastructure	High	Medium/High
Natural Resources***	Medium	Medium / High
Hedge Funds	Low	Low

Page 59

**Note:** Low: <5%; Low/Medium: 5-10%; Medium: 11-20%; Medium/High: 21-40%; High: >40% (As at April 2018),

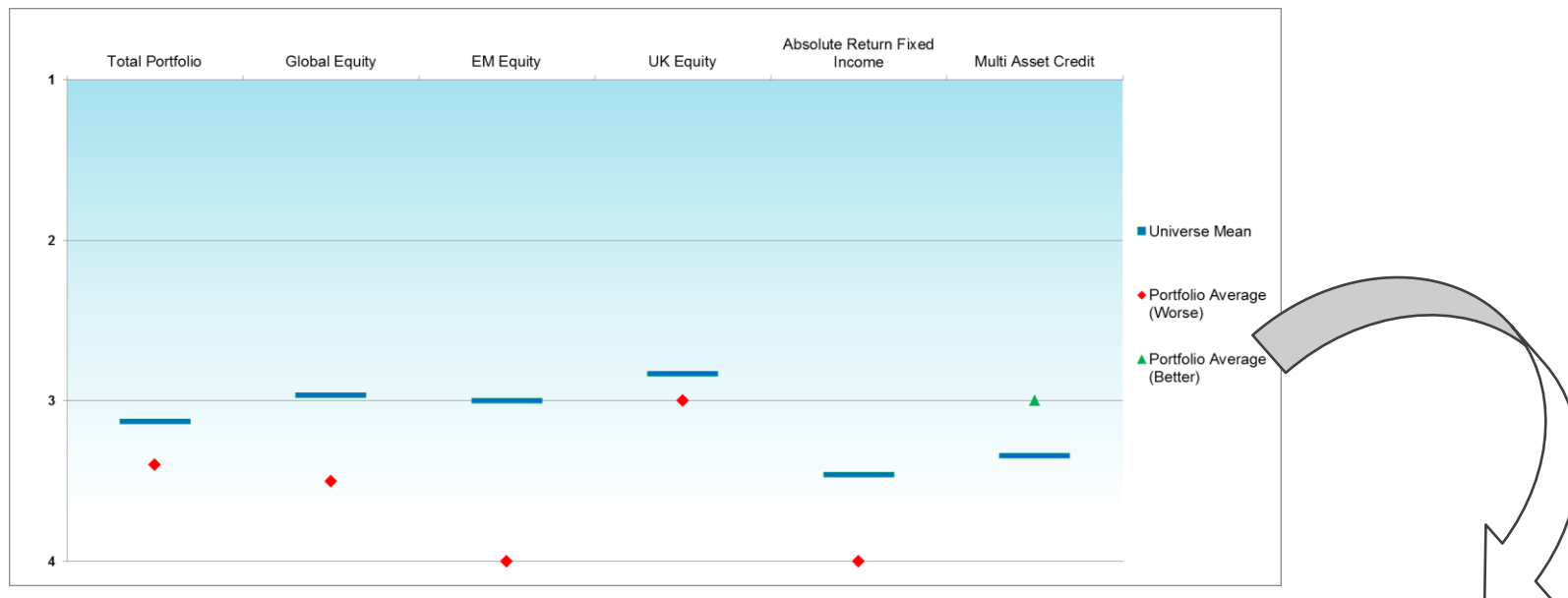
\* Refers to the percent distribution of ESG1 and 2 rated strategies in GIMD, where available.

\*\* Refers to the percent distribution of sustainability themed strategies compared to mainstream by asset class – noting equities is a large universe so the low relative number is not actually a low absolute number.

\*\*\*Conservative view - research updates in this asset class may result in a more favourable view than is currently held.

# PORTFOLIO ESG RATING REVIEW ANALYSIS - EXAMPLE

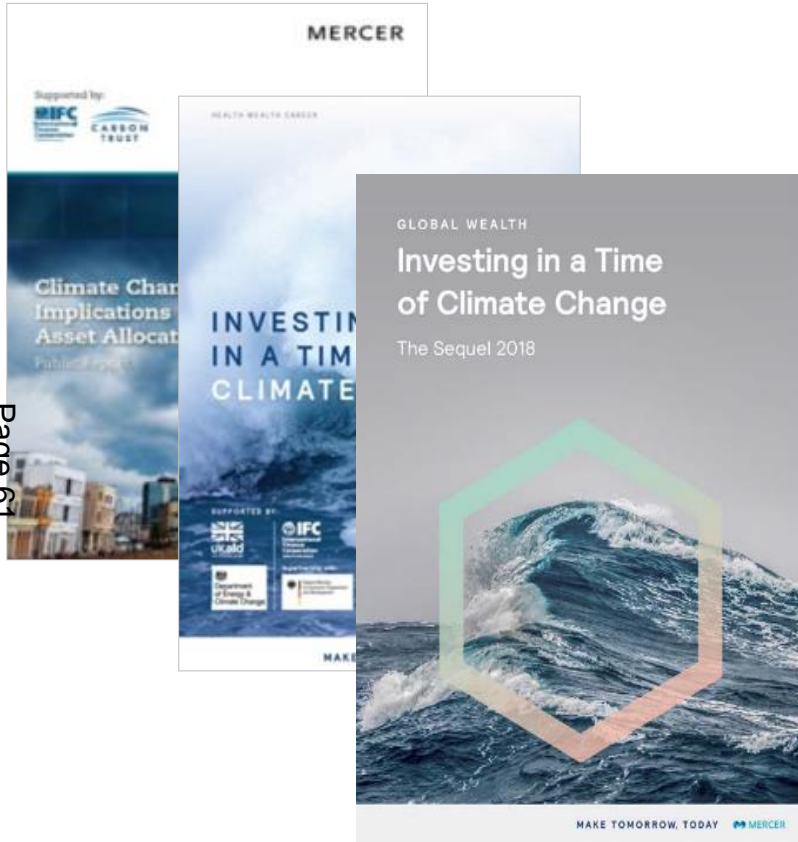
Page 60



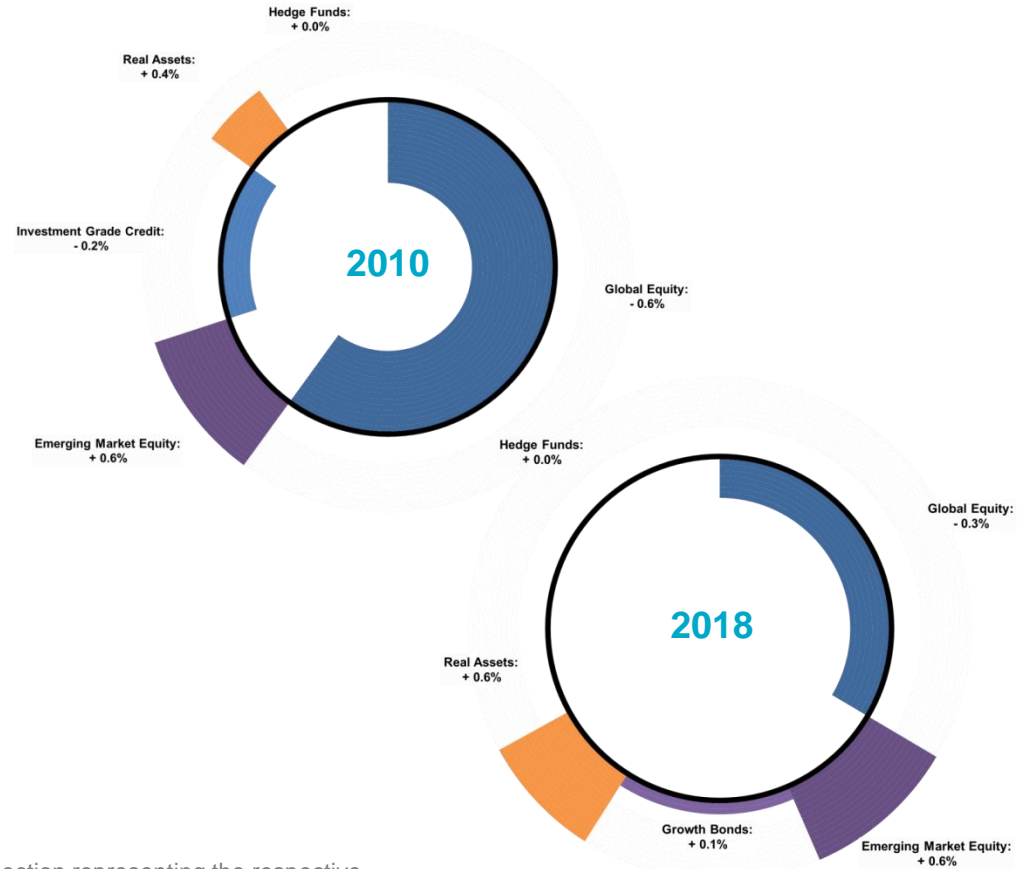
XYZ Pension Fund (Universe)	Underlying Managers	Asset Class and Universe Ratings Distribution Comparison Charts																
Absolute Return	<table border="1"> <tr> <td data-bbox="671 1046 804 1163">Manager 1</td> <td data-bbox="804 1046 937 1163">Good rating</td> </tr> <tr> <td data-bbox="671 1163 804 1273">Manager 2</td> <td data-bbox="804 1163 937 1273">Poor rating</td> </tr> </table>	Manager 1	Good rating	Manager 2	Poor rating	<table border="1"> <caption>ESG Rating Distribution Comparison</caption> <thead> <tr> <th>Entity</th> <th>Good (Blue)</th> <th>Yellow</th> <th>Poor (Red)</th> </tr> </thead> <tbody> <tr> <td>Fund</td> <td>~70%</td> <td>0%</td> <td>~30%</td> </tr> <tr> <td>Mercer Universe</td> <td>~5%</td> <td>~10%</td> <td>~85%</td> </tr> </tbody> </table>	Entity	Good (Blue)	Yellow	Poor (Red)	Fund	~70%	0%	~30%	Mercer Universe	~5%	~10%	~85%
Manager 1	Good rating																	
Manager 2	Poor rating																	
Entity	Good (Blue)	Yellow	Poor (Red)															
Fund	~70%	0%	~30%															
Mercer Universe	~5%	~10%	~85%															

# CLIMATE SCENARIO MODELLING

Page 67



## Annual Additional Return Impact – over 10 Years (2°C Scenario)



The black circle represents the total portfolio, with the width of each asset class section representing the respective percentage weighting. Asset class sections expected to experience a reduction in returns will move towards the circle centre and those expected to experience additional returns will move outwards from the circle.

# THEMATIC INVESTMENT OPPORTUNITIES



## RENEWABLE AND ALTERNATIVE ENERGY

Solar, wind, wave, biofuels, and geothermal technology



## ENERGY EFFICIENCY

Storage plus power network, industry, building, and transport efficiency

Page 62

## WATER INFRASTRUCTURE AND TECHNOLOGIES

Irrigation, storage, treatment, drainage and flood protection



## POLLUTION CONTROL

Pollution control solutions and environmental testing



## WASTE MANAGEMENT AND TECHNOLOGIES

Recycling processing, hazardous and general waste management

## HEALTH AND SOCIAL SERVICES

Positive impacts for social development and poverty or aging population



## SUSTAINABLE CONSUMER GOODS

Meeting shifting consumer demands in sourcing and technology



## RESPONSIBLE FINANCE

Supporting role for real economy

**MAKE**  **MERCER**  
**TOMORROW,**  
**TODAY**

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## Hampshire Pension Fund

### **DRAFT Responsible Investment Policy**

The Pension Fund's investment principles include:

- i) that it has a long term focus, and
- ii) a belief in the importance of Responsible Investment, including consideration of **social, environmental and corporate governance (ESG)**, which can both positively and negatively influence investment returns.

The Pension Fund's approach to Responsible Investment, includes consideration of the UN Principles for Responsible Investment (UNPRI), which provides the following examples of ESG factors:

- **Environmental** - climate change – including physical risk and transition risk, resource depletion, including water, waste and pollution, deforestation,
- **Social** - working conditions, including slavery and child labour, local communities, including indigenous communities, conflict, health and safety, employee relations and diversity
- **Governance** - executive pay, bribery and corruption, political lobbying and donations, board diversity and structure, tax strategy

These factors, whilst not exhaustive, provide a baseline of ESG factors to be taken into account as part of the Pension Funds overall investment strategy.

#### Responsible Investment Sub-Committee

The Pension Fund Panel and Board (PFPB) take their responsibilities for Responsible Investing and the consideration of ESG issues very seriously, and have established a Responsible Investment sub-committee, which meets at least twice a year, to consider emerging ESG issues.

The Terms of Reference of the sub-committee are as follows:

To make recommendations to the PFPB on ESG issues having completed the following activities:

- a. to review regularly the Pension Fund's Responsible Investment Policy (contained in its Investment Strategy Statement), and practices relating to it, to ensure that ESG issues are adequately reflected;
- b. to consider representations on ESG issues.

## **Hampshire Pension Fund**

### Consideration of ESG in Investment Decisions

The Pension Fund delegates its investment decisions to its appointed investment managers, who are a combination of specialist external active investment managers and passive investment managers. The PFPB engages in responsible stewardship with its investment managers and will review and monitor investments in the context of this Policy as follows:

#### **Passive investment managers**

These managers are employed to mirror the stocks in various indices, and the PFPB accept that in making investments for the Pension Fund through an index, passive managers are unable to actively take ESG factors into account.

However, the PFPB does expect its passive investment managers to engage with companies within the index on ESG issues and to also exercise voting rights particularly on ESG issues attached to investments (see separate section below on Exercising Voting rights).

#### **Active investment managers**

The PFPB delegates responsibility for making individual investment decisions (non passive) to its active investment managers.

In delivering their service to the Pension Fund, the PFPB requires its active investment managers to pro-actively consider how all relevant factors, including ESG factors, will influence the long term value of each investment.

To ensure that ESG factors are considered in investment decisions, the PFPB uses the following framework of questions, which it requires its investment managers to be able to answer and uses as a basis to scrutinise them.

For each investment has the investment manager assessed and concluded that the expected long-term financial return is mitigated from the risk of:

- Detrimental social impacts from the company's products/services.
- Negatively contributing to Climate Change or other environmental issues.
- The wider impacts of Climate Change.
- Poor corporate governance and systems of control.
- A senior management pay structure that is biased towards managers making short-term decisions that aren't in the company's and investors long-term interests.
- The treatment of the company's workforce or workers in the company's supply chain.
- Reputational damage to the company, the Pension Fund in relation to its beneficiaries, Hampshire residents, or the general principles of the UK Corporate Governance Code; as a result of its approach to any ESG issue.

## **Hampshire Pension Fund**

If the PFPB do not receive satisfactory responses to these questions they may undertake further engagement with investment managers (and possibly directly with investments) and/or consider directing the investment manager to not invest in the company/sector in question.

### **Stock/Sector Exclusions and Social Impact investments**

The PFPB may also consider disinvestment from a particular stock, the exclusion of a particular type of stock or investment in specific 'social' investments where, based on an evaluation of ESG factors, it believes that the decision would be supported by a significant majority of scheme members and employers; the PFPB may take this approach so long as it does not result in significant financial detriment to the Pension Fund.

### **Exercise of rights attaching to investments**

Each of the Pension Fund's investment managers is asked to work actively with companies they are invested in to ensure they achieve the best possible outcomes for the Pension Fund, including forward-looking social, environmental and corporate governance standards. This includes instructing investment managers to exercise the Fund's responsibility to vote on company resolutions wherever possible.

The Fund believes that if companies comply with the principles of the UK Corporate Governance Code published by the Financial Reporting Council, this can be an important factor in helping them succeed; but the Fund also accepts the need for a flexible approach that is in the common long-term interests of shareholders, company employees and consumers. The Fund's investment managers should cast their votes with this in mind.

In particular, the Fund's investment managers should cast their votes to ensure that:

- executive directors are subject to re-election at least annually
- executive directors' salaries are set by a remuneration committee consisting of a majority of independent non-executive directors, who should make independent reports to shareholders
- arrangements for external audit are under the control of an audit committee consisting of a majority of independent non-executive directors, with clear terms of reference – these should include a duty to ensure that investment managers closely control the level of non-audit work given to auditors, and should not significantly exceed their audit-related fee unless there are, in any investment manager's opinion, special circumstances to justify it
- in the investment managers' opinion, no embarrassment is caused to the Fund in relation to its beneficiaries, Hampshire residents, or the general principles of the UK Corporate Governance Code.

If investment managers do not follow these guidelines, they must report to the Pension Fund explaining why.

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