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.

<u>Responsible Investment Sub-Committee</u>
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.

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.

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.