



LGPS Central Limited

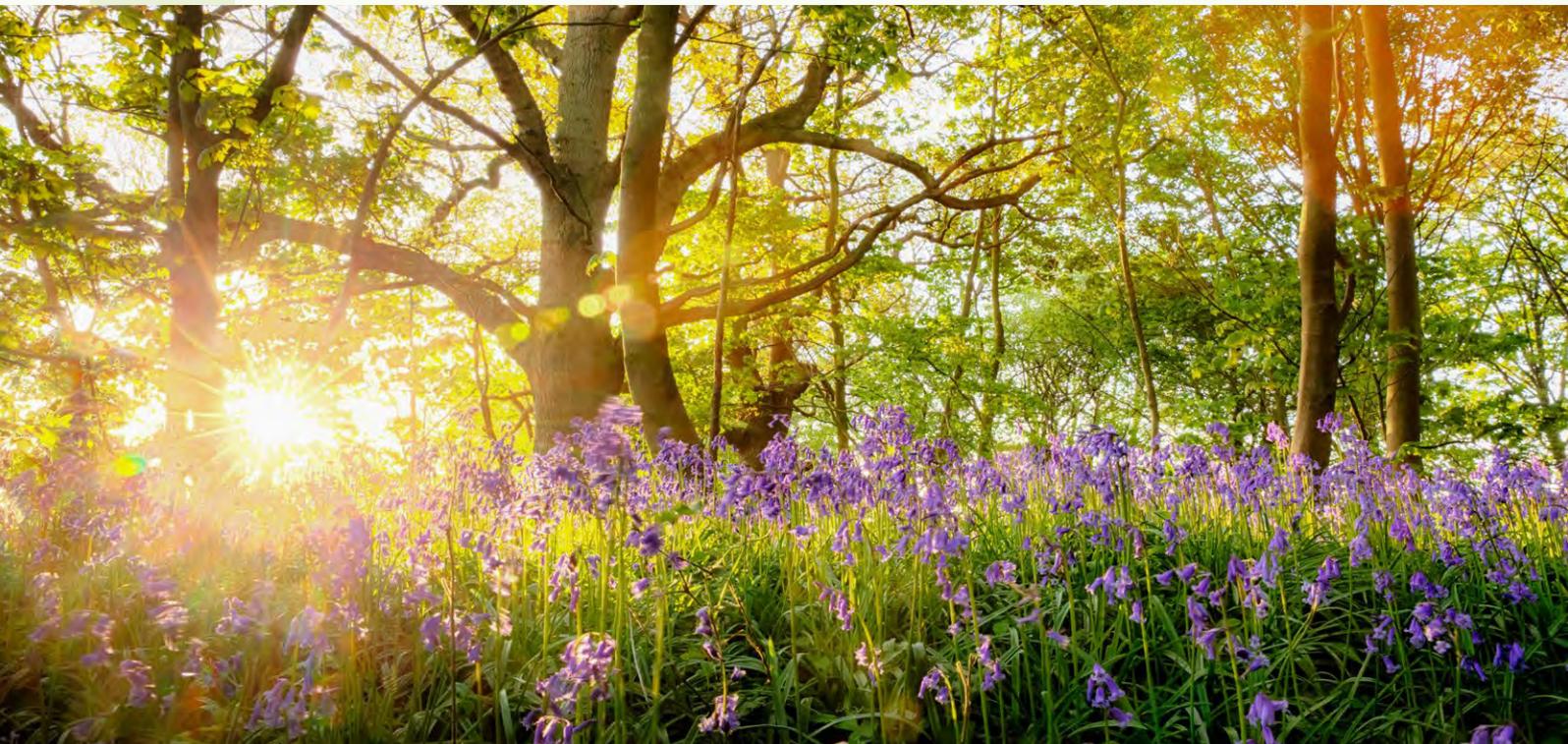
# Annual Stewardship Report 2021



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# 01 Foreword



FOREWORD BY:



**Joanne Segars**  
Chair



**Mike Weston**  
CEO

**Responsible Investment continues to be at the heart of everything we do. We remain convinced that our Partner Funds’ best interests are served through a combination of comprehensive ESG integration and robust stewardship.**



While the health pandemic understandably took centre stage in 2020 and to a degree overshadowed the climate crisis, the latter clearly came to the fore in 2021. The 2021 voting season saw a new development in climate transparency and dialogue with shareholders through votes on climate transition across various sectors mostly in the European market. While all these climate plans passed at respective AGMs there was also notable opposition from shareholders to some plans. We expect more companies to follow suit during 2022 and we also expect investors to scrutinise these plans at a more detailed level against evolving climate risk management standards such as the Climate Action 100+ (CA100+) Benchmark assessment. See further detail on LGPS Central’s

involvement in CA100+ below under table 2.4.2.1 and in Section 4.1.2 below). In the US shareholders expressed a clear desire for better climate risk management at Exxon where three climate-savvy directors were appointed to Exxon’s board against management advice, and at Chevron, with 61% support for a proposal requiring Scope 3 targets. See further detail in Section 5 below.

In the lead-up to COP26<sup>1</sup> LGPS Central co-signed letters to 68 banks asking for Paris-alignment and protection of biodiversity. Going forward, we aim to strengthen expectations on companies across sectors to protect nature and biodiversity as part of their ongoing climate transition efforts. We also take it upon ourselves to actively engage high-risk commodity sectors to, over time, work towards

<sup>1</sup> The COP26 (Conference of the Parties’ 26th meeting) event is a global United Nations summit about climate change and how countries are planning to tackle it.



portfolios that are free from commodity-driven deforestation. Alongside climate change, we have identified three other core Stewardship Themes that we prioritise for corporate and policy engagement. These are plastic pollution, responsible tax behaviour and tech sector risks. We see a greater focus and clarity around what a “plastic transition” entails across key sectors and welcome the announcement of negotiations for a UN treaty on plastic pollution, advocated by businesses and investors including LGPS Central. While tax transparency remains low, we have seen some progress among companies LGPS Central has engaged who are ready to provide greater transparency on tax payments at country-by-country level. Our dialogue with tech sector companies on social media content control has seen companies take critical steps to assess and remove objectionable content. Going into 2022, we will broaden the focus of the latter theme to a human rights risk theme allowing greater attention to companies’ human and labour rights risk mitigation and management across sectors. There is increasing acceptance in society of companies’ responsibility to respect human rights in supply chains and other business relationships. This responsibility is clearly captured in the UN Guiding Principles for Business and Human Rights, which also apply to investors.

We actively monitor engagements undertaken by our external managers. Topics covered in 2021 include, amongst others, environmental management and climate change, energy transition, greater focus and disclosure of health and safety within ESG priorities, data protection and information security risk, and forced labour issues in supply chains.

During 2021, LGPS Central continued in-depth climate risk assessments for each individual Partner Fund and provided a second iteration of Climate Risk Reports (CRR) bespoke to each of them. We made several enhancements to the climate monitoring service, which has run since end of 2019, to ensure it remains aligned to the latest industry developments (see further detail in Table 2.4.1.1 below). The findings in these reports are directly integrated into our climate engagement prioritisation. We released our second stand-alone TCFD Report in 2021 and supported our Partner Funds in producing their own TCFD-compliant reports.

We were pleased to announce in January 2022, a commitment to transition our investment portfolios to net zero greenhouse gas emissions in accordance with the Institutional Investor Group on Climate Change Net Zero Framework (see further detail under Section 2.1.4 below).

We continue to implement our RI Integrated Status approach as we expand our fund offering for Partner Funds, which has involved RI due diligence across a suite of equity, private debt, private equity, infrastructure, property and targeted return investment solutions. We are proud to have developed a Global Sustainable Equity Investment solution throughout the course of 2021, in direct response to increased appetite from Partner Funds. The funds are now expected to launch in Q2 2022 (see Section 3.2 below). Going into 2022, we have grown our Responsible Investment & Engagement Team to total five employees. We will also tender for an ESG data tool to enhance our ability to provide robust challenge to our external managers and help us to understand the ESG risks embedded in our investment portfolios (see further detail in Section 2.1.4 below).

We have written this report in alignment with the UK Stewardship Code 2020 and the content reflects feedback received from the FRC on our report for calendar year 2020. This year’s report has been reviewed by the LGPS Central Executive Committee and Board. The report has also been reviewed by relevant heads of department to ensure the accuracy of process descriptions and content. In 2021 our Responsible Investment function was audited by KPMG, with a particular focus on the governance of RI at LGPS Central. This review and challenge have given us confidence that our reporting is fair, accurate and balanced and most importantly informative in that it imparts critical information on our approach to stewardship to our stakeholders.



**Joanne Segars**  
Chair



**Mike Weston**  
CEO

## Key achievements and progress across our stewardship activities in 2021

### Responsible Investment Integration



All product launches and existing products have RI-Integrated Status.

### Climate Risk Monitoring Service



All Partner Funds have received a second iteration of a detailed Climate Risk Report.  
TCFD Reports delivered to Partner Funds in parallel.

### Stewardship Theme Activity & Progress

#### CLIMATE CHANGE



CA100+ Benchmark assessment of March 2021 shows that 52% of the world's largest emitters have net zero goals.

Ongoing engagement with 68 banks on Paris-alignment and protection of biodiversity. 50 banks have responded and 19 confirmed they will publish targets.

Investor expectations on Paris-aligned accounting were communicated to 17 European energy, material and transportation companies.

#### RESPONSIBLE TAX BEHAVIOUR



Engagement with six companies across technology, telecommunications, finance sees progress by two companies on enhanced tax transparency.

Co-signed a letter to the European Parliament supporting a draft directive on public country-by-country reporting (CBCR) in the EU.

#### PLASTIC POLLUTION



Two-year engagement with seven packaging companies that have high exposure to risks/opportunities stemming from plastic transition sees high level of receptiveness to investor concerns.

Collaborative engagement to help combat microplastics pollution is seeing some progress.

Co-sponsored launch of first industry specification to prevent plastic pellet pollution.

#### TECHNOLOGY & DISRUPTIVE INDUSTRIES



102 investor-strong collaboration on social media content control received Stewardship Initiative of the Year award at the UN PRI 2021 Awards for its success in engaging three multinational giants.

Human rights risks engagement initiative is building momentum after [Investor Expectations](#) were published, including engagement with Facebook on their newly launched Human Rights Policy, and Amazon on their recent Human Rights Impact assessment.

### Broader Engagement

#### DEFORESTATION

LGPS is a member of the investor coalition "Investor Policy Dialogue on Deforestation" (IPDD) established in mid-2020.

Dialogue with the Brazilian government (Vice President, Central Bank Governor and Congress).

Co-signing of statement at COP26 committing to tackle agricultural commodity-driven deforestation through active ownership.

#### MODERN SLAVERY

Investor group has engaged 61 laggard FTSE 350 companies that had failed to meet the reporting requirements of Section 54 of the UK Modern Slavery Act 2015.

High success rate: All 61 companies have become compliant with the Modern Slavery Act in the course of 2021.

A phase III of this project (following on from engagement in 2020 and 2021) has begun in 2022 to engage a further 46 FTSE 350 companies.

This report covers each of the **12 principles of the UK Stewardship Code 2020** in numerical order under four main headlines as follows:

PRINCIPLES

1-5

## Purpose and governance

- Purpose, investment beliefs, strategy and culture
- Governance, resources and incentives to support stewardship
- Conflict of Interest
- Identification and response to market-wide systemic risks to promote a well-functioning financial system
- Review of policies, assurance of processes and assessment of the effectiveness of activities

PRINCIPLES

6-8

## Investment approach

- Client communication on activities and outcomes of stewardship efforts
- Integration of material ESG issues including climate change
- Signatories monitor and hold to account managers and/or service providers

PRINCIPLES

9-11

## Engagement

- Engagement with issuers
- Participation in collaborative engagement to influence issuers
- Escalation of stewardship activities to influence issuers

PRINCIPLE

12

## Exercising rights and responsibilities

# 02 Purpose and governance



**PRINCIPLE 1 2.1 Purpose, investment beliefs, strategy and culture**

**2.1.1 Purpose and values**

LGPS Central Limited (LGPSC) is an FCA regulated institutional investment manager responsible for the pooled assets of eight Local Government Pension Funds in Central England. LGPSC was formed in April 2018 and is owned equally by all eight of its Partner Funds and is dedicated solely to the management of local government pension scheme assets.

The aim of the Company is to use the combined scale of its Partner Fund assets to reduce costs, improve investment returns, strengthen governance and widen the range of available asset classes for investment – for the benefit of local government pensioners, employees and employers. LGPSC Partner Funds have combined pooled assets of approximately c.£49 billion. At the end of the reporting year (2021), LGPSC had c.£23 billion in

assets under management and advice invested in listed equities (active and passive), fixed income, private equity, private debt, and infrastructure. The majority of pooled assets are invested in listed equities and fixed income under an Authorised Contractual Scheme (ACS) fund structure.

The pooling endeavour is dependent on continuous dialogue and collaboration; hence we refer to our clients as Partner Funds. All LGPSC Partner Funds view RI&E as a “must have” and we build on a proud tradition of RI which has been spearheaded over many years by individual Partner Funds. We also seek to espouse values as a Company that mirror expectations that we have of investee companies and the wider investment value chain.

Our values and behaviours are:

**We put our clients first**

-  Working in partnership to deliver our Clients’ and Shareholders’ long-term needs
-  Always acting with integrity, transparency and professionalism
-  Doing the right thing

**We are ambitious**

-  Constructively challenging the status quo to continuously improve how we operate
-  Combining a public service ethos with a commercial business focus
-  Celebrate excellence

**We are inclusive**

-  Collegiate and collaborative, delivering more as one team
-  Valuing and treating everyone equally
-  Listening to everyone’s ideas and using their experiences to support growth

**We are a great place to work**

-  Staff are encouraged to be open, learn from mistakes and grow in confidence
-  Individual trust and empowerment combined with personal accountability and responsibility
-  Friendly, honest and supportive in everything we do



As an example, LGPSC Limited is a member of the 30% Club, as well as the Investor Chapter of the 30% Club. We view diversity as integral to sound decision making and we believe that the most effective Boards of companies

include a diversity of skills, experiences and perspectives. This view is reflected both in our RI&E Framework and in our Voting Principles. LGPSC’s Board has 50% female representation, and our Executive Committee has 20% female and ethnic minority representation. LGPSC’s own BAME (black, Asian and minority ethnic) population is 41%, the female ratio is currently 41% and we have 16 different nationalities/cultures across our work force.

Our Company is a member of the Employers Network for Equality & Inclusion, and we participate in a number of work streams of the Diversity Project promoting good practice on flexible working, ethnicity, working families and an early careers programme (mentoring potential graduates from socially disadvantaged communities). When selecting external managers for LGPSC investment mandates, we expect both good in-house diversity across the organisation, and we expect that the manager integrates diversity in their ESG assessments of companies they invest in. Diversity is one element of our broader assessment of a given manager’s culture and ethos and we view strong diversity across gender, culture and ethnicity as indicative of overall strong

governance. We support the newly established Asset Owner Diversity Charter and will use the toolkit provided through the charter to assess managers’ approach and processes to enable diversity and inclusion throughout their organisations and value chains.

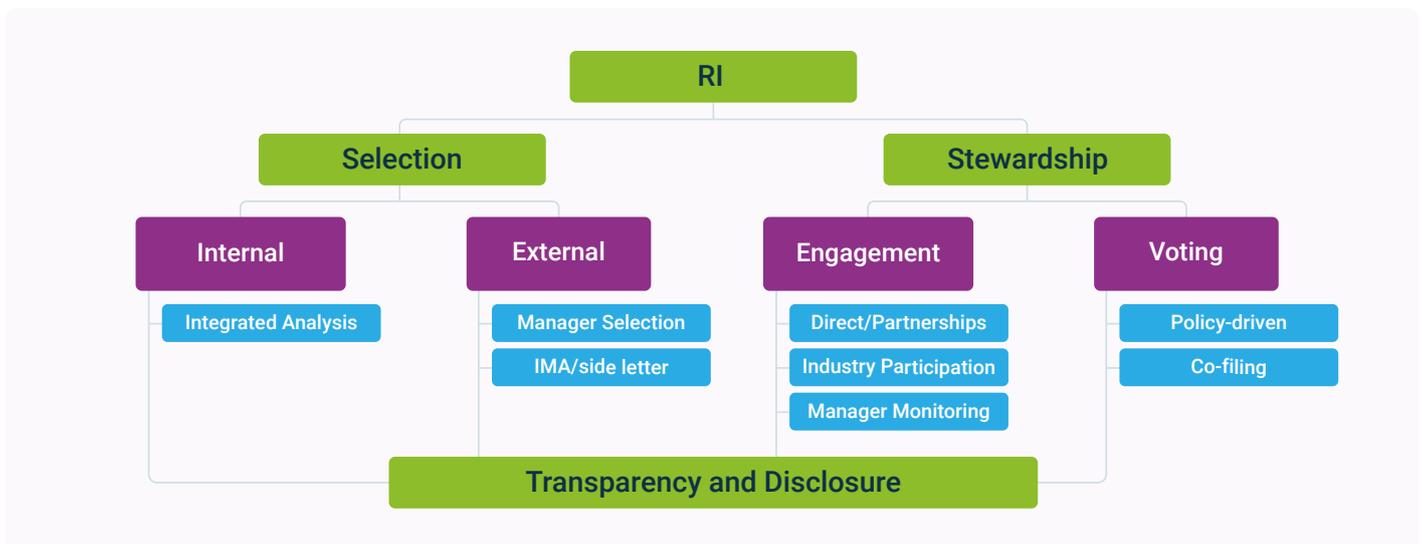
We have decided to develop a Modern Slavery Statement for LGPSC, not as a legal requirement, but with a view to applying leading practice, as a Company, as an investor engaging companies and in our procurements. We currently assess external managers’ compliance with the Modern Slavery Act in the selection process. The procurements follow the Official Journal of the EU (OJEU) process that is adopted by all English public sector entities, but dates from the time the UK was part of the EU. We continue to be a part of an investor collaboration engaging FTSE 350 companies on Modern Slavery Act compliance (see Section 4.1.3 below). We do not currently ask investee companies to voluntarily comply with the Modern Slavery Act if they fall below the revenue threshold. However, we still view it as appropriate to set a high standard for ourselves as a Company as well as to protect our stakeholders from any reputational risk. We perceive the level of modern slavery related risk to our business as low from the outset and will develop a proportionate approach to this which covers all parts of the business.

## 2.1.2 Responsible Investment integral to our asset management operations

At inception of LGPSC in April 2018, we established a Framework for RI&E which builds on the investment beliefs of the Company’s eight Partner Funds. The Framework establishes two high-level objectives for all LGPSC RI-related efforts. These are:

- 1 Primarily, to support investment objectives;
- 2 Secondly, to be an exemplar for RI within the financial services industry, promote collaboration, and raise standards across the marketplace.

The RI&E Framework is applied in a manner that promotes these objectives both before the investment decision (which we refer to as the **Selection** of investments) and after the investment decision (the **Stewardship** of investments). Furthermore, we aim to be **Transparent** to all stakeholders and accountable to our Partner Funds through regular **Disclosure** of RI activities.



We take the view that strong RI policy and action increases our ability to protect and grow stakeholder value. Against this premise, key targets of our RI efforts are to:

- 1 Integrate material environmental, social and governance factors into investment decisions both pre and post investment
- 2 Influence corporate behaviour at company and sector levels through engagement, voting and other means of influence outside of listed equities
- 3 Participate in and contribute to industry-wide best corporate and investor practices
- 4 Enhance trust with our stakeholders through ongoing dialogue and a high level of transparency

The strategy to meet the key objectives and the way we aim to measure success against them, is described in the Sections below of this document. Table 2.1.2.1 shows, at high level, our objectives and how we measure achievement against them.

**TABLE 2.1.2.1: SUMMARY OF TARGETS, STRATEGIES AND MEASURES OF SUCCESS**

TARGETS	STRATEGY	MEASURES OF SUCCESS (MOS)
<b>Integrate material ESG factors into investment decisions</b>	Define an RI Integrated Status approach for each fund prior to launch and through its lifecycle	100% of relevant products achieve and maintain RI Integrated Status RIIS is approved by the Investment Committee and maintenance is checked quarterly by the Quarterly Portfolio Review Committees See Section 3.2 below
<b>Influence corporate behaviour</b>	Engagement and voting at company and sector levels	Achieve the majority of MoS listed in Section 4.1.2 below (Stewardship Themes)
<b>Participate in and contribute to industry standards</b>	Engagement at industry and policy levels	Active contribution to theme-relevant industry initiatives and broader initiatives of relevance to LGPS Funds Contribution to a minimum of three public consultations or policy initiatives on standards/regulation with market-wide application and/or theme-relevant application See Section 2.4 below
<b>Enhance trust with stakeholders</b>	Transparency and disclosure	<u>Regular Stewardship Updates</u> three times per year, in addition to an <u>Annual Stewardship Report</u> in line with UK Stewardship Code 2020 Quarterly RI meetings with Partner Funds Annual RI event for Partner Funds to allow dialogue on key themes and to build knowledge – RI Summit held on 13 October 2021 PRI report in line with PRI (Principles for Responsible Investing) Framework, achieving a high score. LGPSC received an A+ rating for its 2019 report, and are still awaiting the outcome of 2020 report AAF report including testing of the accuracy of RI data and implementation of RI processes See Section 3.1 below for more detail

During 2021, we have achieved the majority of these measures of success as is evidenced in the relevant sections of this report (see references in the right-hand column of the above table).

### 2.1.3 A “One-for-eight” model

Since inception, LGPSC’s RI&E function has implemented a “one for eight” model. This means that we operate one framework, one service offering, one approach, that delivers the same service to our eight Partner Funds. This aligns well with the overarching goal of the pool, which is to reduce costs, improve investment returns, strengthen governance and widen the range of available asset classes for investment while implementing high quality RI services. We label this “Mandate Services”. One of the core functions of the pool is to provide Partner Funds with investment opportunities suited to their investment needs as these evolve. As part of our Mandate Services, we apply an all-encompassing *RI Integrated Status* (RIIS) approach to any fund at launch and through the lifespan of that fund. Through RIIS we ensure that RI objectives are reflected at inception of new funds through

to deployment/selection of asset managers and their ongoing monitoring. RIIS is described in more detail in Section 3.2 below.

While still in a phase where Partner Fund assets are transferring to LGPSC, we also offer some customisation of client-specific deliverables; “Call-off Services”. These include assistance with RI&E policy design/update, RI-specific training for boards and pension committees, and ad-hoc queries from beneficiaries on RI-related matters. We have continued our Climate Risk Monitoring Service (CRMS) which is bespoke to each Partner Fund and tailored to their strategy and asset allocation. CRMS and how this has evolved in the last year is described in further detail in Section 2.4. below.

### 2.1.4 Looking ahead

Looking ahead, LGPSC recognises the growing importance of sustainability to the investment process and the evolving demands of our stakeholders. Signals from government and consumers are becoming clearer and analytical tools and the outputs they produce are becoming more sophisticated. Key areas of focus during 2021, and going into 2022, is to action LGPSC’s commitment on net zero and Paris alignment as well as extend climate risk analysis at portfolio level to a broader set of ESG risks. We are committed to ensuring that our climate analysis and broader ESG analysis remain fit for purpose and in step with industry developments in this area.

#### Net zero commitment

In January 2022 we announced a commitment to transition LGPSC’s investment portfolios to net zero greenhouse gas emissions (GHG). This commitment will provide additional focus and transparency to our response to the current climate emergency. It will help frame our conversations with external managers and with our investee companies, reinforcing our expectations around climate risk management and establishing parameters around the decarbonisation of our investment portfolios. We will utilise the Institutional Investor Group on Climate Change’s (IIGCC) Net Zero Investment Framework to achieve net zero emissions across our internally and externally managed portfolios by 2050 (or sooner), focusing initially on Listed Equities, Corporate Bonds, Sovereign Bonds and Real Estate. In addition, we will have an interim target where we will aim to achieve a 50% reduction in GHG emissions by 2030 across our equity and fixed income portfolios. We are committed to extending our focus to include other asset classes as reliable data become available and to provide attractive investment opportunities in the renewable energy and green tech sectors to match our Partner Funds’ demands.

#### ESG data tool

We have identified a need for access to broad ESG research and data going beyond climate risk metrics and will procure this during Q2/Q3 of 2022. This will help identify ESG risks and opportunities of investments, at a stock level and portfolio level. The service is expected to cover, at a minimum, investment in listed equities and corporate fixed income. The data and analysis are expected to include ESG stock ratings, comparative scoring on material ESG risks and opportunities, a portfolio level tool, as well as qualitative ESG research to provide underlying context. The tool will be used for proactive monitoring and reporting on the ESG characteristics of LGPSC funds, with the potential to create an annual in-depth ESG reporting service, akin to that of the CRMS. Furthermore, the tool will help us challenge external managers on their stewardship and engagement activities and prioritisation of stewardship resource. It can also be used to enrich our voting and engagement prioritisation in-house, helping to uncover which companies are exposed to risks beyond climate change, such as modern slavery, human rights, responsible tax behaviour and circular economy.

At the start of 2021, we undertook annual reviews of our RI&E Framework and Voting Policies to reflect the UK Stewardship Code 2020 and to strengthen our position on diversity and climate change performance. We expect UK companies to have at least 33% female representation on their boards and to be reporting ethnic minority representation at board level. We review these expectations annually so that they remain both realistic and demanding. We have also re-set our expectations of investee companies in terms of climate change management quality score against Transition Pathway Initiative assessments, expecting a score of 4 (highest available). This reflects both the urgency with which companies need to address climate change risks and the progress that has already been made.

We undertook a review at the start of 2021 of resourcing within the LGPSC RI&E Team to make sure that both people and systems resourcing is in line with the Team business plan and associated deliverables. As a result of this review and through discussion with our Partner Funds, we have – during Q1 of 2022 – strengthened the resource for the RI&E Team with a Senior Stewardship Analyst, taking the RI&E Team to five people.





## 2.2.2 Board oversight and ownership across the organisation

LGPSC’s Board is responsible for approving and monitoring implementation of the RI&E Policy (RI&EP). We have established a Board-level KPI that 100% of relevant products achieve and maintain RI Integrated Status, and regular updates on progress are provided to the Board. The Board meets at least six times a year. RI&E, including climate change, is a regular item on the Board’s agenda.

During 2021, the RI&E Team provided LGPSC’s Board with an overview of the Company’s latest TCFD report as well as regular updates on the Company’s stewardship effort and the Climate Risk Monitoring Service. Alongside on-going oversight and knowledge building, Board members sometimes get involved in our broader RI effort e.g., through speaker assignments or in ongoing engagements. During Q1 of 2021, the Chair of the Board, Joanne Segars, took part in a meeting with the Vice President of Brazil, representing LGPSC as a member of the investor coalition “Investor Policy Dialogue on Deforestation” (see further detail under Section 4.1.3 below). LGPSC Board members were involved in LGPSC’s International Women’s Day event in March 2021 and also took part in LGPSC’s RI Summit later in the year. Our Chair, Joanne Segars, represents LGPS Central on the newly established Occupational Pensions Stewardship Council.

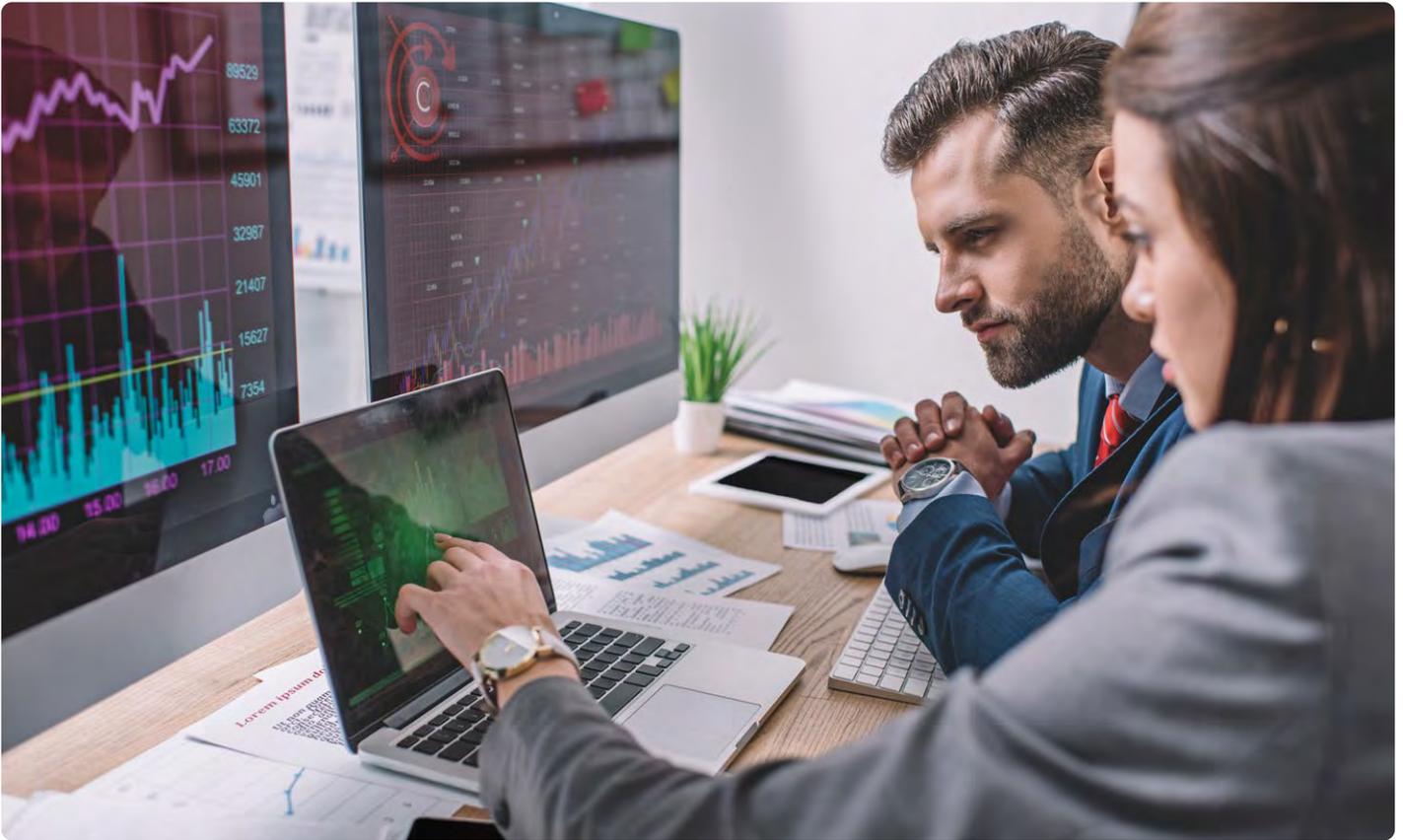
We believe it is critical that RI is owned and practiced across LGPSC. As such, the RI&E Team performs a coordinating function relying on regular interaction with colleagues in asset class teams, in the broader Investment Team and across back-office functions including Operations, Legal, HR and Compliance. The RI&E Team reports to the Chief Investment Officer (CIO). The Director of RI&E is a member of the Investment Committee, the Private Markets Investment Committee and the Senior Management Team. RI&E related matters are regularly brought to the LGPSC Executive Committee for discussion and approval. During 2021 this has

included for example review of LGPSC RI&E related policies, becoming a founding member and Board member of TPI Ltd (established October 2021), and ongoing discussions on LGPSC’s net zero commitment (see Section 2.1.4 above).

LGPSC’s RI Integrated Status (RIIS) approach inherently requires and allows detailed dialogue between the RI&E Team and the relevant Asset Class Team from inception of a fund and throughout its lifespan. This approach also ensures that the RI approach taken for a given fund or asset is co-sponsored by the Director of RI&E and the relevant Investment Director, reinforcing a shared ownership to RI integration. RIIS could be viewed as an in-house form of “RI certification” which covers the following key elements: Beliefs, Documentation, Process, Reporting and Review. See further detail on RIIS under Section 3.2 below.

There is no variable pay at LGPSC. LGPSC staff are incentivised to integrate stewardship and investment through the following means:

- Investment Directors have RI and ESG integration objectives included in their semi-annual Personal Development Reviews
- Training and knowledge sharing: As an example, during Q4 of 2021 the RI&E Team provided a training session to all LGPSC staff on net zero and divestment vs engagement, which had very high attendance and inspired a lot of questions and discussion
- All staff are being asked to think about RI&E and sustainability initiatives as part of smarter working as we have moved into a new office working arrangement mid-2021
- Going forward, all job descriptions for staff at LGPSC will reflect RI integration



### 2.2.3 Dedicated in-house stewardship resources

Going into 2021, the RI&E Team consisted of an Investment Director, Stewardship Manager and two IMC qualified analysts, both of whom are working toward their CFA certificate in ESG. Considering increasing expectations from Partner Funds in terms of breadth and depth of the RI service, and to deliver key strategic projects while covering for key person risk, we decided to expand the Team to five. Recruitment took place during H2 2021 and as of February 2022 we have expanded the Team with a Senior Stewardship Analyst.

Team members come from diverse academic backgrounds and specialisms across fund management, RI policy development, ESG integration in public and private markets, stewardship and engagement across the value chain and climate expertise. We welcome this diversity and breadth of perspectives. The Team leverages a strong network among peer investors both in the UK and globally, as well as investee companies, industry associations and relevant regulatory bodies.

### 2.2.4 External stewardship resources

With limited in-house resources we have contracted an external Stewardship Provider, EOS at Federated Hermes, to provide global voting and engagement services. Following a comprehensive due diligence process EOS were selected as their beliefs align well with LGPSC's and Partner Funds' beliefs. We share a view that dialogue with companies on ESG factors is essential to build a global financial system that delivers improved long-term returns for investors, as well as more sustainable outcomes for society.

EOS reports on voting and engagement activity across relevant ACS funds on a quarterly and annual basis. Outside of reporting, we regularly interact with EOS both one-to-one, for instance through voting season on contentious votes, and together with

other EOS' clients at Client Advisory Councils hosted twice a year. Through this regular dialogue, we can ensure that our values remain aligned (see Section 3.3.2 below with a detailed review of EOS' services during 2021). EOS also engages with regulators, industry bodies and other standard setters on our behalf to shape capital markets and the environment in which companies and investors can operate more sustainably.

We expect our external managers to engage investee companies on our behalf on material issues including ESG factors. We receive quarterly data from external fund managers on the number of engagements undertaken and the weight in portfolio. See further detail under Section 3.3. below.



## PRINCIPLE 3 2.3 Conflict of Interest

LGPS's approach to managing and mitigating risks associated with conflicts of interest is outlined in the LGPSC conflicts of interest policy. This is made available to all staff and Partner Funds of LGPSC. The policy is designed to ensure fair outcomes for Partner Funds and to ensure that LGPSC fulfils its stewardship responsibilities to its pool partners in terms of how their assets are managed.

The policy was signed off by the LGPSC Investment Committee, Executive Committee and Board when implemented. The policy is reviewed annually and changes to the policy are approved through the same governance process.

LGPSC employees, including senior management and members of the executive committee are required to complete conflicts management training on an annual basis and confirm their adherence to its standards. This training includes guidance on what constitutes a conflict of interest. The conflicts policy is also contained within the LGPSC Compliance Manual. It is readily available to all staff whether working from home or office based.

When LGPSC appoints external managers, a thorough due diligence process is undertaken. This includes consideration of the external managers process and procedures around the Management of Conflicts of Interest. We expect our managers to have robust controls and procedures in place around conflict management and to demonstrate commitment to managing conflicts fairly.

LGPSC only manages Partner Fund assets, and all our active portfolios are managed externally. LGPSC staff are not remunerated through a bonus scheme. These two factors are key mitigants in terms of conflict risk.

### Examples of Conflicts of Interest

#### Avoidance of conflict in the process of hiring managers to Sustainable Equities Fund

A member of the RI&E Team serves on the Sustainable Investment Advisory committee of a well-known Sustainable Investment Manager. This relationship was always considered to be symbiotic, as it provides a development opportunity for the member of staff which benefits LGPSC, and it allows the local government pension perspective to be heard in the wider asset manager industry. Potential conflicts were considered from the outset, and it was agreed that should a situation arise whereby the manager in question applied for an LGPSC mandate, the RI&E team member would not be involved in the selection process. Unsurprisingly this manager put forward a mandate proposal when LGPSC was selecting managers for its Global Sustainable Equity Fund. LGPSC managed this potential conflict by ensuring that the employee in question was not involved in the selection process; neither the formulation of mandate requirements nor the manager assessment and scoring process. The selection



process was established with precise and clear selection criteria and each manager was selected on their application alone. Furthermore, the process was constructed and executed by the Active Equities Team at LGPSC with input from the Director of RI&E. The application of this robust and independent process resulted in the asset manager in question being selected to manage one of the mandates within the fund structure. The employee in question will not have any involvement in the ongoing assessment of the manager post appointment in respect of ESG integration or stewardship. We consider that this process was managed in the best interests of our Partner Funds and their beneficiaries. The selection process ensured that the managers that matched the mandate criteria most closely and had a clear and demonstrable process delivered by an experienced and stable team, were selected.

### **Appointment of Transition Manager for the Global Sustainable Equities fund**

All colleagues involved in the appointment process were required to complete a conflicts of interest declaration. The declaration asks colleagues to provide details of any conflicts with any of the potential transition managers for assessment by the compliance Team. The approach taken is that conflicts will inevitably arise particularly in the form of existing business relationships and previous periods of employment with the investment managers on the shortlist. As long as these conflicts are declared and recorded, they can be managed.

### **Voting**

Conflicts of interest can arise during the voting season. This can for instance be the case where a proxy voting provider also provides other services to corporates or possibly in some circumstances where they engage with and provide voting recommendations in relation to a pension scheme's sponsor company.

We expect our proxy voting providers to be transparent about conflicts of interest and to implement measures to ensure they manage these conflicts such as Chinese walls, conflicts management policies and conflicts registers. As from Q1 of 2021, EOS at Federated Hermes – LGPSC's external stewardship provider – applies an enhancement to its service to further improve transparency by informing voting clients of potential significant conflicts of interest when EOS provides voting recommendations. One such conflict would be when EOS recommends a vote in relation to clients' sponsor companies, and specific assurance of EOS' independence in assessing this stock is needed.

EOS has a publicly available [Stewardship conflicts of interest policy](#). EOS conflicts are maintained in a group conflicts of interest policy and conflicts of interest register. As part of the policy, staff report any potential conflicts to the compliance team to be assessed and, when necessary, the register is updated. The conflicts of interest register is reviewed by senior management on a regular basis.

### **Fairness in the provision of RI&E Services from LGPSC to Partner Funds**

LGPSC operates a one for eight service model. This ensures that we deliver a consistent level of service to all eight partner funds ensuring that no conflicts arise in terms of the level of support they get from the RI&E Team.

During 2020, LGPSC provided Climate Risk Reports to all eight Partner Funds, as part of a Climate Risk Monitoring Service that we have made available to them. For the 2021 provision of the same service, we followed the same delivery order as last year. This is to ensure consistency and fairness among Partner Funds and to avoid some receiving reports six months apart or others 14 months apart.

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## 2.4 Identification and response to market-wide and systemic risks to promote a well-functioning financial system

### 2.4.1 Stewardship Themes

In close collaboration with its Partner Funds, LGPSC has identified four core Stewardship Themes that guide the pool's engagement and voting efforts. These are climate change, plastic pollution, responsible tax behaviour and 'tech sector' risks. These themes have been chosen based on the following parameters:

- Economic relevance
- Ability to leverage collaboration
- Stakeholder interest

Identifying core themes that are material to the Partner Funds' investment objectives and time horizon, that are likely to have broader market impact, and that are perceived to be of relevance to stakeholders, helps us prioritise and direct engagement. We fully acknowledge that the spectrum of ESG risks is broad and constantly evolving. However, and in agreement with our LGPSC pool partners, we consider it appropriate to pursue these themes over a three-year horizon, at a minimum, while conducting annual reviews to allow for necessary adjustments or changes. This helps us build strong knowledge on each theme, seek or build collaborations with like-minded investors, identify and express consistent expectations to companies on theme-relevant risks and opportunities, and to measure the progress of engagements. Furthermore, we take the view that engagement on a theme needs to happen at multiple levels in parallel: company-level, industry-level, and policy-level. With our long-term investment horizon, we take a whole-of-market outlook and changing the "rules of the game" through industry and policy dialogue is as important, if not more important, than individual company behaviour. In Section 4.1.2 below, we give a detailed overview of engagement activity and progress for each Stewardship Theme. In Section 2.5, we provide information on the annual review of Stewardship Themes that was carried out during Q4 of 2021.

### 2.4.2 Climate Risk Monitoring Service

Climate action failure is the stand-out, long-term risk the world faces in likelihood and impact according to recent reports from the Intergovernmental Panel on Climate Change. If 'business as usual' continues, the world could heat up by about 5 degrees by 2100 which would have catastrophic environmental impacts and cause profound societal damage and significant human harm. A Paris-aligned transition to a low-carbon economy would lead to lower economic damage and for long-term investors is preferable to alternative climate scenarios. We believe investors can best encourage this transition through a combination of a) understanding the risks to their portfolios at a granular level, b) stress-testing portfolios against various temperature scenarios, c) identifying tools and actions that can be taken to address and minimise risk. In January 2022, we announced a commitment to achieve net zero across our assets under stewardship by 2050 (see Section 2.1.4 above). Our climate risk monitoring service is a key building block in ongoing work toward this goal.

Since 2020 LGPSC has conducted in-depth climate risk assessments for each individual Partner Fund and provided an annual Climate Risk Report (CRR) bespoke to each of them. The CRR is designed to allow each Partner Fund a view of the climate risk held through their entire asset portfolio accompanied by proposed actions each could take to manage and reduce that risk. To facilitate disclosure in line with the Task Force on Climate-Related Financial Disclosures (TCFD), the CRR is deliberately structured to align with the four TCFD disclosure pillars.

2021, was our second edition of the CRRs to Partner Funds. We made several enhancements to the climate monitoring service to ensure it remains aligned to the latest industry developments and therefore the best assessment on climate-related risk we can provide to our clients. We particularly wanted to emphasise progress made against the findings of the first report to give our Partner Funds a view on their direction of travel. Table 2.4.2.1 provides a summary of the methods we use to assess financially material climate-related risks and opportunities, alongside outlining the improvements we made to the service in 2021.

TABLE 2.4.2.1: METHODS OF ASSESSING CLIMATE-RELATED RISKS AND OPPORTUNITIES

SECTION	ANALYSIS	2021 ENHANCEMENT
<p><b>Governance</b></p>	<p>The purpose of this section is to identify areas in which the Fund’s governance and policies can further embed and normalise the management of climate risk. We provide a review of the Fund’s documentation from the perspective of climate strategy setting and issue recommendations on how the Fund could improve its governance of climate-related risk.</p>	<p>We provide a progress update against the recommendations and considerations issued in the first report and suggest further policy extensions the Fund could consider.</p>
<p><b>Strategy</b></p>	<p>We assess the extent to which the Fund’s risk and return characteristics could be affected by a set of plausible climate scenarios. This includes an estimation of the annual climate-related impact on returns (at fund and asset-class level), and climate stress tests (to explore the potential impact of a sudden climate-related price movement). An external consultant provides analytical support for this section.</p>	<p>We did not utilise Climate Scenario Analysis in the 2021 reports. As a top-down method of analysis it is more suited to a biennial review. We intend to revisit Climate Scenario Analysis in 2022. In lieu, we conducted a literature review on the techniques that the Fund could consider enacting to further manage climate risks within alternative asset classes.</p>
<p><b>Risk Management</b></p>	<p>Based on the report findings we provide a Climate Stewardship Plan which identifies the areas in which stewardship techniques could be leveraged to further understand and manage climate-related risks within the portfolio. The plan includes plans to engage both individual companies and fund managers.</p>	<p>We provide a bespoke engagement update for each of the companies included in the Climate Stewardship Plan. The section identifies the rationale, objectives and strategy of the engagement, alongside issuing a progress update. We make use of the TPI and CA100+ benchmark as key tools to monitor company activity.</p>
<p><b>Metrics &amp; Targets</b></p>	<p>We conduct a bottom-up carbon risk metrics analysis at the company and portfolio level. For the most part, four types of carbon risk metric are utilised: portfolio carbon footprint, fossil fuel exposure, weight in clean technology and climate risk management (via the Transition Pathway Initiative).</p>	<p>The chapter provides a comparative analysis, examining the metrics from the first report against the updated metrics of the second report.</p>

Having recently completed the 2021 reporting cycle, LGPSC has conducted a review to identify further improvements to the service. Enhancements that we aim to make to the 2022 reports include:

- Inclusion of a 1.5°C scenario into the Climate Scenario Analysis
- Enhance the company progress updates to demonstrate a more robust link between engagement and outcomes
- New additions to the suite of carbon risk metrics, reflecting the shift towards measuring alignment with net zero, such as % of portfolio with net zero targets, % of portfolio revenue derived from fossil fuels, % of portfolio revenue derived from clean technology and absolute carbon emissions/financed emissions

Our Partner Funds have used the findings of their CRRs to develop individual Climate Strategies covering governance, beliefs, objectives, strategic actions and reviews in relation to their climate-related risk. To date, seven of our Partner Funds have published Climate Strategies, with one more upcoming in 2022. Aside from strategy setting, the CRRs have also been used to facilitate TCFD disclosure (which seven of our Partner Funds have achieved to date); formulate Climate Stewardship Plans; conduct training sessions on climate change; initiate governance and policy reviews; and for exploring potential investments in sustainable asset classes.

In 2021, we continued to explore areas of convergence and commonality across each of the eight bespoke CRRs to facilitate collective action as a pool. We identified a number of recommendations that featured in all of the CRRs and worked

in collaboration with our Partner Funds to crystallise these into specific pool-level workstreams. Examples of actions we have taken include holding a joint Partner Fund Responsible Investment Day, releasing an updated 2021 TCFD Report, and issuing a Net Zero Statement for LGPSC made with the full support of all eight Partner Funds. Furthermore, the CRRs identify companies that face a high level of climate risk and are of particular significance to certain portfolios. This information is fed into our engagement prioritisation and as a result, we are enhancing our involvement in ongoing CA100+ engagements to cover as many, if not all, such “red flag” companies. The same companies will be automatically included in LGPSC’s Voting Watch List of companies that are given particular scrutiny ahead of AGM (see Section 5.2 below).

### 2.4.3 Attendance and contributions to industry dialogue, partnerships and building of standards

LGPSC is an active participant in the debate on good corporate and investor practice. We value collaboration with peer investors and with industry initiatives, which gives a stronger voice and more leverage in engagement. Taking part allows us to access data, research and tools available to members – and at the same time influence further development of these initiatives.

Table 2.4.2 below is a list of organisations and initiatives that LGPSC is an active member of and includes a brief assessment of the efficiency of the initiative and outcomes during 2021.

TABLE 2.4.3.1: PARTICIPATION IN INDUSTRY DIALOGUE

ORGANISATION/ INITIATIVE NAME	ABOUT THE ORGANISATION/INITIATIVE	EFFICIENCY AND OUTCOMES
<p>PRI</p> 	<p>Largest RI-related organisation globally. Helps with research, policy influence and collaborative engagement. During 2021, LGPSC Head of Stewardship has been a member of the PRI Plastics Working Group and the PRI Tax Working Group.</p>	<p>PRI is a standard bearer of good practice for RI. LGPSC has been a member of PRI since inception of the pool. We view LGPSC’s active participation in PRI through submission of an annual report and through membership of PRI Working Groups as clearly value-adding to ongoing RI development and pursuit of Stewardship Theme engagements.</p>
<p>IIGCC (Institutional Investor Group on Climate Change)</p> 	<p>Influential asset owner and asset manager group. Useful for climate change research and policy influence. During 2021, LGPSC Head of Stewardship has been a member of the Corporate Programme Advisory Group.</p>	<p>IIGCC’s corporate engagement and policy engagement programmes are both highly value-adding to LGPSC’s work on climate change on behalf of all Partner Funds. It has a clear purpose and seems attentive to member needs and input. IIGCC engages broadly with stakeholders, for example with policy makers in the lead-up to COP26.</p>

<p><b>Cross-Pool RI Group within LGPS</b></p>	<p>Collaboration group across the LGPS pools and funds. Includes funds and pool operators. LGPSC Head of Stewardship was Vice Chair of the group during 2021.</p>	<p>This is a good forum to allow discussion between like-minded investors, who operate in the same regulatory environment and with similar expectations from Partner Funds and beneficiaries, on RI topics of interest and/or urgency, including net zero commitments for investors, human rights risks, biodiversity etc.</p>
<p><b>The Local Government Pension Scheme Advisory Board</b></p>	<p>LGPS Head of Stewardship is a member of an RI Advisory Group to SAB that was formed at the start of 2021. Discussions are held on RI relevant policies and standards that will have direct or indirect implications for LGPS funds and pools.</p>	<p>Discussions during 2021 have centred around themes such as just transition, impact investing and MHCLG’s work to introduce TFCF aligned reporting across LGPS Pools and Funds.</p>
		
<p><b>Transition Pathway Initiative (TPI)</b></p>	<p>Analysis of companies based on their climate risk management quality and their carbon performance. TPI analysis (by research team at LSE Grantham Research Institute on Climate and the Environment) is highly regarded and carries industry influence. LGPSC Head of Stewardship was a member of the TPI Steering Committee during H2 2021, and since October 2021 a member of the Board to the newly formed TPI Limited.</p>	<p>TPI is a highly useful tool that LGPSC uses directly to inform engagement and voting on behalf of Partner Funds. We view very positively TPI’s close collaboration with CA100+ during 2020 and 2021 in the roll-out of the Benchmark Framework which allows evaluation of company progress against Paris alignment on key parameters (targets, actions, disclosures). We support the planned expansion of TPI research through the establishment of a Climate Transition Centre.</p>
		
<p><b>CDP</b></p>	<p>CDP is a not-for-profit charity that runs the global disclosure system for investors, companies, cities, states and regions to manage their environmental impacts.</p>	<p>Our membership of CDP is in support of ongoing work for carbon emissions reporting across companies and sectors, and to tap into analysis and research. We welcome CDP’s work on deforestation, including a “Forest champions programme”, which we aim to tap into for our current and future engagement on deforestation.</p>
		
<p><b>30% Club Investor Group</b></p>	<p>Investor group engaging both UK listed equities and increasingly companies abroad, on gender diversity. LGPSC has been a member since inception of our Company.</p>	<p>This forum has a clear target and allows for discussion, learning and direct engagement with like-minded peers on an ongoing critical governance issue. During 2021, a sub-set of 30% Club Investor Group members, including LGPSC, has engaged in the Japanese market.</p>
		

<p><b>BVCA</b> British Private Equity and Venture Capital Association</p> 	<p>UK trade body for private equity.</p>	<p>This forum is very useful for deal flow information. It also runs discounted training courses which helps build knowledge.</p>
<p><b>LAPFF</b> Local Authority Pension Fund Forum</p> 	<p>Engagement with companies in the UK and abroad, assisting LGPS funds with sustainable and ethical investment challenges.</p>	<p>LAPFF has conducted engagements that is complimentary to LGPSC's stewardship theme engagement effort, for instance in reaching out to companies during 2021 on human rights risks that stem from operating in conflict zones such as Palestinian/Israeli territories.</p>
<p><b>Climate Action 100+</b></p> 	<p>Engagement collaboration of more than 700 investors with a combined \$68 trillion assets under management. Engaging 166 companies on climate risk that are responsible for 80% of global industrial GHG emissions. LGPSC Head of Stewardship is a member of the Mining and Metals Sector Group.</p>	<p>This is a targeted and robust investor collaboration which LGPSC views as highly value adding relative to climate change risk management. The 2020 CA100+ Benchmark Framework, with scores published in March 2021, embeds structure and rigour to assessments of companies against a Paris trajectory.</p>
<p><b>Investor Forum</b></p>  <p>THE INVESTOR FORUM</p>	<p>High quality collaborative engagement platform set up by institutional investors in UK equities. LGPSC has been a member since inception of our Company.</p>	<p>LGPSC co-sponsored an Investor Forum coordinated plastic pellet prevention project during 2020-2021. The overarching goal of this project is to help companies achieve and maintain zero pellet loss across their pellet handling operations.</p> <p>The first industry standard specification for plastic pellet handling was published in July 2021.</p>

## Policy engagements and consultation responses:

Since inception of LGPSC in April 2018, the Company has taken active part in policy dialogue on behalf of Partner Funds across various themes and regulations including on ethnicity pay reporting, tax transparency, modern slavery, climate change and sustainability reporting requirements.

In Q1 2021 we co-signed a **letter to the COP26 President** asking for support to investors by seeking publication of key underlying assumptions and commodity price projections tied to a 1.5C scenario. The International Energy Agency's special report *Net Zero by 2050: a Roadmap for the Global Energy Sector* published in May 2021 provides clarity in this regard. The roadmap highlights the gap between where we are and where the 1.5 scenario says we need to be. The IEA describes the energy transition as an all-hands-on-deck crisis that "hinges on a singular, unwavering focus from all governments—working together with one another, and with businesses, investors and citizens. The Net Zero report from IEA is actively used as a reference point when we engage companies across sectors, for instance through the Climate Action 100+ collaboration.

LGPSC responded to an All-Party Parliamentary Group for Local Authority Pensions Funds consultation on **Just Transition** on 4 May 2021. We are of the opinion that the just transition must be recognised as a global challenge as communities that stand to be impacted the most by climate change are often situated in developing countries. We consider that COVID-19 illustrates that global challenges require global solutions. Government has an important role to play in encouraging supporting innovation by sending strong signals to investors in terms of policies, subsidies, and taxes. For example, decisive carbon pricing and robust regulation around carbon off-setting. Investors also have an important role to play in bringing about a just transition through both engagement with the corporations and assets in which we invest and through financing the transition itself. The element of just transition is being raised with companies that are in scope of Climate Action 100+ engagement and companies will be assessed on this in the 2022 benchmark exercise.

LGPSC expressed support for the Government to mandate **net zero Metrics as part of TCFD reporting** in a response to the Department for Work and Pensions' consultation on Climate and investment reporting. We consider that mandatory reporting will encourage more comprehensive reporting of emissions by corporations and commitments to achieve net zero, particularly if this regulation is supported by complimentary regulations across the economy. The financial cost associated with TCFD reporting in a manner consistent with the regulation proposed by DWP may be underestimated and we recognise that this might be challenging for some investors to achieve. Furthermore, we think the metrics will need to be carefully explained to stakeholders and net zero

alignment does not tell us everything we need to know about the climate risk faced by a portfolio.

Ahead of COP26 in Glasgow, LGPSC signed a statement alongside 586 other investors, managing \$46 trillion in assets, **urging governments to undertake five priority actions to accelerate climate investment** before COP26. These priority actions include:

- Strengthening of NDCs<sup>2</sup> for 2030 before COP26.
- Commitment to a domestic mid-century, net-zero emissions target, and implementation of domestic policies to deliver these targets.
- Incentivising private investments in zero-emissions solutions and ensure ambitious pre-2030 action.
- Ensuring COVID-19 economic recovery plans support the transition to net-zero emissions and enhance resilience.
- Committing to implementing mandatory climate risk disclosure requirements aligned with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations.

LGPSC's stewardship provider, EOS, regularly engages on behalf of clients with a wide range of stakeholders, including government authorities, trade bodies, unions, investors, and NGOs, to identify and respond to market-wide and systemic risks. As an example, EOS co-authored a paper setting out **investor expectations on the alignment of the banking sector with the goals of the Paris Agreement**. The paper focused on three areas: the actions banks should take to align their financing activities with the Paris goals and the achievement of net-zero emissions; steps to strengthen the governance of their climate strategy; and disclosure to demonstrate implementation. The paper was officially launched by the Institutional Investors Group on Climate Change (IIGCC) in April 2021 and a courtesy letter was sent to 27 banks by a group of 35 investors, with a copy of the paper. Subsequently, the group initiated collaborative engagements with these banks. EOS leads or co-leads the dialogue with eight banks and takes an active participating role with five other banks.

EOS also engages on market-specific trends and policies and as an example, responded to a consultation by the UK Department for Business, Energy & Industrial Strategy on **mandatory Task Force on Climate-related Financial Disclosures (TCFD) reporting** for listed companies, large private companies and limited liability partnerships. EOS promoted enhanced regulation around climate risk reporting in line with the TCFD recommendations. In the US, EOS welcomed the **decision by Nasdaq mandating that Nasdaq-listed companies should have at least two diverse directors** (including at least one woman and at least one member of an underrepresented community). If companies do not, they must explain why they have failed to do so under a phased transition that started from 6 August 2021.

<sup>2</sup> Nationally Determined Contributions (NDCs). Under the Paris Agreement each Party must prepare, communicate, and maintain successive nationally determined contributions it intends to achieve

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## 2.5 Review of policies, assurance of processes and assessment of the effectiveness of activities

### Review of LGPSC RI&E policies

Prior to the launch of LGPSC in April 2018, LGPSC’s Board approved three RI-related policy documents; LGPS RI&E Framework, LGPS RI&E Policy and LGPS Voting Principles. Each document is subject to annual review by the LGPSC Board which happens at the start of every year. Ahead of each annual review, LGPSC consults its Partner Funds to solicit their views. Revisions will then be taken through LGPSC’s Investment Committee and Executive Committee for discussion and approval before the Board finally assesses and approves them. The Board take an active interest in these policies and often recommend alterations and enhancements. They are familiar with the issues and their perspectives are welcome and add value.

In addition to Partner Fund consultation, we discuss trends and developments in RI with investor peers on a continuous basis, in particular with other LGPS pools (see overview of Initiative memberships in Section 2.4 above). We also discuss voting trends with EOS and with peer investors ahead of revision of our Voting Principles. As an example, we have over the last two years heightened our expectations on companies’ governance of Board and Senior Management diversity (gender and ethnicity), sustainability reporting and climate risk management. We have done this in tandem and close alignment with similar changes to EOS’ voting policies and those of close peers.

At the start of 2021, we compiled an RI Emerging Risk Register. This will help us stay attuned to any regulatory initiatives (hard and soft law) that may impact on our RI approach and policies. We consider this a “live” document that will be updated on a regular basis in close collaboration with LGPSC’s Legal Team. We have shared this document with Cross-pool peers through the Cross-pool RI Working Group. Discussion on upcoming regulation, consultations, other standard developments will be a regular item for discussion within this group.

### Ongoing information-sharing and review of Stewardship Themes

Through our quarterly PAF RIWG meetings (See Section 2.2.1 above), we allow for information-sharing and debate/checks on LGPSC’s provision of RI services against the RI&E Framework. All our Partner Funds take a keen interest in RI and engagement, which is a reflection of their ultimate beneficiaries’ ongoing interest in climate change and broader sustainability issues.

LGPSC undertake an annual review of the effectiveness of the Stewardship Themes in close collaboration with Partner Funds. During 2021, we conducted a review through PAF RIWG discussions which resulted in the following adjustments:

- Climate change remains the number one theme
- Biodiversity and land use should be included alongside

climate change

- The S in ESG should feature more prominently, with a preference for focus on Human Rights

Description of themes in light of discussions with Partner Funds:

### CLIMATE CHANGE

Climate change is regularly among the World Economic Forum’s top five global risks, both in terms of likelihood and impact. Through both physical risks (e.g., increases in extreme weather events) and market risks (e.g., impact of carbon pricing or technology substitution), climate change impacts institutional portfolios. In addition, greater incidence of flooding, wildfires, chronic precipitation, sea level rise are already having profound societal consequences.

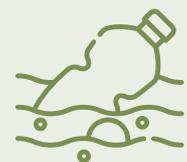


In the UK, campaign groups, governments and regulators are increasingly taking an interest in the extent to which investors are managing climate-related risks. This includes the Environmental Risk Audit Committee, Department of Work and Pensions, Financial Reporting Council, divestment campaign groups, and more. TCFD reporting will become mandatory for LGPS Funds from 2023. Investor best practice on climate change is emerging through the Institutional Investor Group on Climate Change (IIGCC) Net-Zero Investment Framework.

Biodiversity loss could reduce nature’s ability to provide goods and services, including food, clean water and a stable climate. Tropical forests play an important role in tackling climate change, protecting biodiversity and ensuring ecosystem services. Forests alone absorb one-third of the CO2 released from burning fossil fuels every year. During COP26 we have seen governments pledge to halt deforestation by 2030. Financial institutions, including LGPSC, have committed to engage with a view to eliminating commodity-driven deforestation by 2025 through engagement at policy and corporate levels.

### PLASTICS

Plastic pollution is a global problem that is continually growing due to both an increase in consumerism and an increase in the number of plastics used to manufacture the things we use regularly. Some companies are starting



to change the way they use these plastics and are actively taking steps to reduce waste.

As well as the negative effects on the planet, companies that purchase, use, or produce significant amounts of plastic could face regulatory tightening, more plastic taxes, and reputational damage as consumers and policymakers become more aware and mindful of the problem. It will be necessary to look at both shorter-term targets companies should strive for, in line with emerging best practices, as well as a longer-term vision for “zero leakage/waste” by 2050. LGPSC joined a call (on behalf of businesses and financial institutions) on United Nations member states to commit to the development of a global treaty on plastic pollution to commence early 2022. Agreement has since been found to negotiate a treaty (See further detail below in Section 4.2).

Amazon, Apple, Facebook, Microsoft and Twitter) on human rights risks including privacy and data protection; freedom of expression; disinformation and political discourse; and on discrimination and hate speech. We also know that weak labour rights in supply chains (especially in emerging markets), both in the technology sector and across other industries, can cause reputational damage that in turn risk undermining shareholder value over the long term.

We view it as feasible to adjust this theme to a broader Human Rights theme that would allow a greater focus on human and labour rights across companies and sectors. We would take as a starting point the UN Guiding Principles for Business and Human Rights, which also apply to investors. Ongoing engagements on Modern Slavery and related to the Israel/Palestine conflict would continue and would be captured under this theme.

### TAX - TRANSPARENCY AND FAIR TAX PAYMENT

The trust an organisation builds with its stakeholders is of critical (though intangible) value. As a measure of an organisation’s contribution to the economies it operates in, tax is a key dimension in building that trust.



Global corporate tax avoidance is estimated to cost governments \$240 billion globally in foregone revenues each year. Companies with overly aggressive tax strategies could be storing up liabilities and could damage their reputation with key stakeholders. While many countries are providing various forms of tax relief to businesses during the COVID-19 pandemic, it seems reasonable for investors to expect companies to pay their fair share of tax. G20 leaders have recently agreed a corporate tax deal for minimum 15% corporate tax, which adds to the expectations for responsible tax behaviour.

### AAF controls

LGPSC carried out an externally assessed AAF 01/06 – Assurance Reports on Internal Controls of Service Organisations under the guidance issued by the Institute of Chartered Accountants in England and Wales which was issued in May 2021. These internal controls include testing of the accuracy of RI data and implementation of RI processes in relation to LGPSC’s voting policy, voting implementation, and accuracy of voting data. As part of the AAF controls, LGPSC carries out quarterly internal quality controls of engagement and voting data before this is shared with Partner Funds through Regular Stewardship Updates. We also conduct an annual review of EOS’ stewardship services, which is based on multiple interactions with EOS during the year (see Section 3.3 below). This review is shared with our CIO and the LGPSC Investment Committee.

EOS has its voting process independently assured on an annual basis (AAF 01/06).

### Internal audit of RI&E function

In 2021 an internal audit of the Responsible Investment function was conducted by KPMG. The objective of this internal audit was to assess the design and embeddedness of the processes in place surrounding LGPS Central’s RI&E policies and underlying procedures. This included a review of the governance processes and approach to external manager onboarding and ongoing monitoring. The audit found that controls were generally appropriate, working effectively to manage risks and provide reasonable assurance that objectives should be met. Some enhancements to the existing control framework were identified in particular the acquisition of an ESG data analysis tool (see Section 2.1.4 above) and improvements to flow of management information to key governance committees. Resource constraints in the responsible investment team were also noted. We are working through the audit actions and the appointment of one additional member of the RI&E Team has already been achieved.

### TECHNOLOGY AND DISRUPTIVE INDUSTRIES RISK - REPLACED BY HUMAN RIGHTS

The current technology theme is a sector-specific theme that covers several risks factors. LGPSC’s engagements have primarily focused on human rights risks for tech sector companies, including social media content control. These areas have come under increased scrutiny from regulators and stakeholders more broadly including companies that advertise on social media platforms. We envisage continuing engagement with tech sector companies (Alphabet,



# 03 Investment approach

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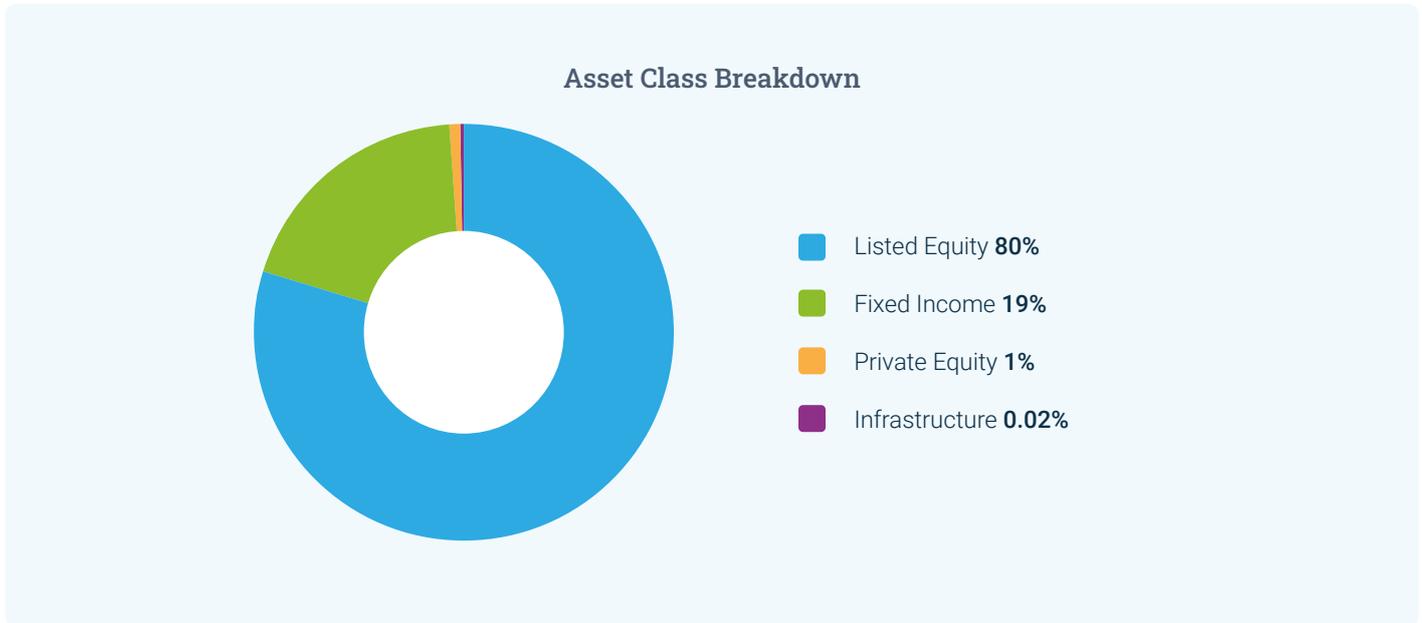


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### 3.1 Client communication on activities and outcomes of stewardship efforts

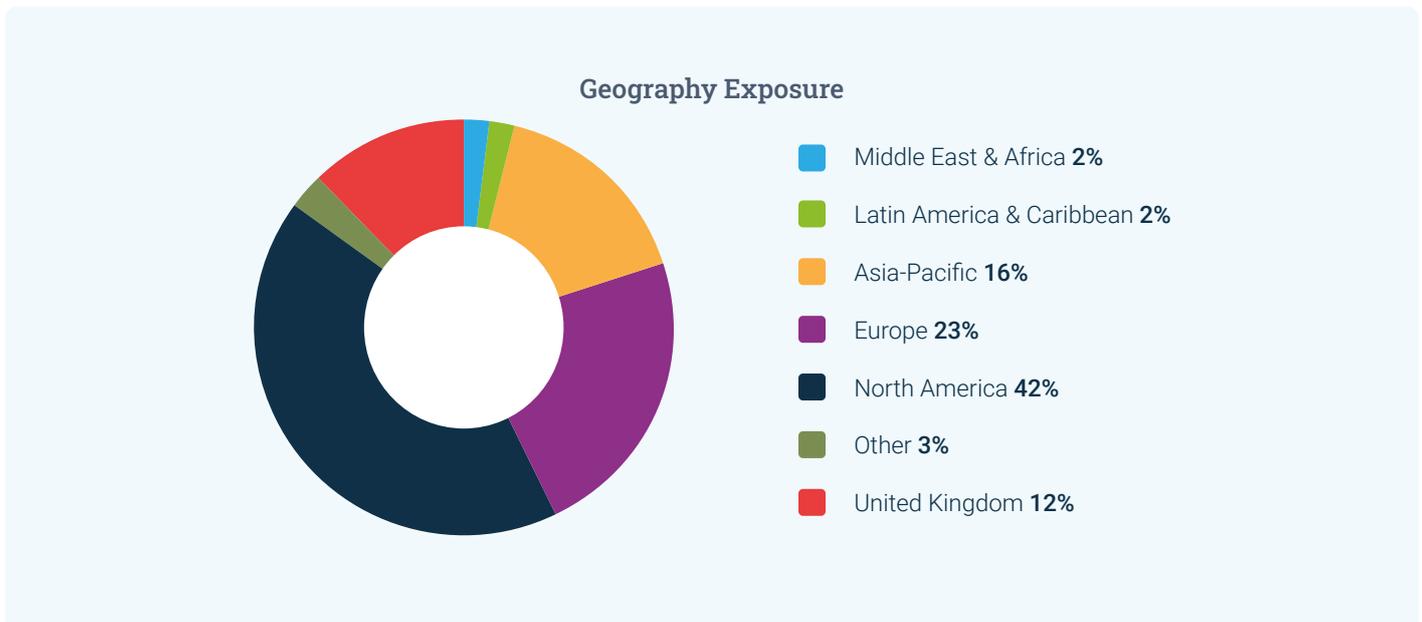
Figure 3.1.1: Breakdown of LGPSC Assets under Management as at 31 December 2021



\* Infrastructure is 0.02% of AUM

Figure 3.1.1 shows a breakdown of LGPSC ACS Fund which have been set up to meet Partner Fund investment needs. LGPSC is in continuous dialogue with its Partner Funds on both the development of new investment funds and reviewing existing funds to ensure that RI is clearly visible both at inception and throughout the life of the fund offerings. The primary tool to ensure this, is LGPSC’s RI Integrated Status approach (see Section 3.2 below).

Figure 3.1.2: Breakdown of exposure by geography<sup>3</sup>



<sup>3</sup> Includes listed equities, fixed income, private equity and infrastructure. Data for the listed equities and fixed income as at 31st December 2021 and private equity and infrastructure as at 31st September 2021. Total AUM represented is £16.3bn.

## Development of new funds

As investors increasingly take account of climate considerations, index providers continue to launch indexes that help investors align their funds with net zero and the transition to a low carbon economy. Initially, climate index products had a simple focus on reducing carbon emissions and fossil fuel reserves. These considerations were implemented successfully in the design of the **LGPSC AW Equity Climate Multi Factor Fund** launched in October 2019 and have helped considerably reduce the level of reserves and emissions compared to the traditional market cap index. However, more recent index launches make use of forward-looking data to reflect the commitments that companies are taking to become aligned to the Paris Climate Agreement.

There are two main types of benchmarks, Climate Transition Benchmarks (CTB) and Paris Aligned Benchmarks (PAB). The benchmarks are both designed to achieve net zero by 2050 and operate in line with the regulations and minimum standards laid out for EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks. The aim of these benchmarks is to achieve an immediate and an annual reduction in emissions, achieving net zero by 2050.

The Team at LGPSC are currently consulting with index providers and examining these index products to review and compare the offerings. The aim is to find a solution that would be attractive to our Partner Funds, be consistent with net zero commitments and allow us to develop a benchmark suitable for a future fund launch.

LGPSC's Active Equities Team continued to develop a **Global Sustainable Equity Investment solution** comprising three funds throughout the course of 2021. The funds are now expected to launch in Q2 2022. The Team has investigated different tools which could be used for measuring impact of the funds and looked at several different secondary benchmarks which could be used for internal measurement purposes. See further detail on the tendering process in Section 3.2 below.

## Ongoing dialogue with Partner Funds on application of the RI&E Framework

- LGPSC seeks Partner Fund views when identifying and revising Stewardship Themes
- Quarterly RI Working Group (RIWG) meetings allow for knowledge sharing and scrutiny
- Annual RI Days have been held over the last three years to allow a deeper debate on key topics (divest/engage; climate change; net zero alignment)
- Increasing attention to RI at the AGM and at Client Joint Committee Meetings with all Partner Funds
- PAF meetings: RI included as a standing item at the start of 2021, in response to increased interest in this area from Partner Fund Pension Committee members and the broader stakeholder group

## Ongoing Stewardship reporting

- [Regular Stewardship Updates](#) including engagement and voting examples (progress, outcomes)
- [Vote by vote disclosure on LGPSC website](#)
- Quarterly Performance Reporting including RI narrative
- Quarterly Media Roundup which gives highlights of RI-related news and developments
- Measures of Success against the Annual Stewardship Plan are presented to Partner Funds at RIWG meetings
- PRI report
- [Annual Stewardship Report](#)

## Bespoke assistance to Partner Funds

The bulk of the time for the LGPSC RI&E Team is intended for Mandate services which benefit all Partner Funds and ensures that existing LGPSC Funds are managed according to the Fund's RI Integrated Status. We also provide Call-off Services in the form of:

- Communications (ad-hoc ethical queries, Freedom of Information requests)
- Training
- Policy development
- Presentations
- Climate Risk Monitoring Service (see Section 2.4.2 above)
- Compliance with the UK Stewardship Code 2020

PRINCIPLE

## 7 3.2 Integration of material ESG issues including climate change

### 3.2.1 ESG Integration during Manager Selection

An assessment of RI&E is a core part of LGPSC’s manager selection process. Typically, manager selection processes are done in three broad stages: standard questionnaire, request for proposal, and manager meetings, of which RI&E assessments feature in all three. In stages one and two, the RI&E Team draft questions for insertion and then score the managers based on their responses. In both stages, a 10-15% weighting is attached to the RI&E questions to reflect the importance that LGPSC places on full ESG integration. A representative from the RI&E Team then attends all the manager meetings. A key objective in the assessment of a manager is whether the ultimate decision maker is engaged in the integration of ESG factors into his or her decision-making process. Managers will not be appointed unless they can demonstrate sufficient awareness of and ability to manage the risks posed by ESG factors.

CASE STUDY

#### Tendering for Global Sustainable Equities Mandates

In close dialogue with our Partner Funds, we decided that the tendering for Global Sustainable Equities Mandates would take the form of a three-sleeve approach encompassing Broad, Thematic and Targeted offerings. LGPSC’s Active Investment Team conducted a three-stage selection process, having advertised for potential managers in June 2021. The first stage, The Selection Questionnaire, attracted 77 applications across the three sleeves. Applications were all read and marked by members of the Team in a fair, transparent and consistent manner with support from the RI&E Director and the Investment Risk Manager. 22 applications were selected to progress to the next stage, The Request for Proposal. Submissions were read and marked by the Team in the same manner. Nine applications, comprising three for each sleeve, were taken through to the final Due Diligence Stage. This took place in September 2021 and consisted of 3-hour meetings for each manager. Due to Covid-19 restrictions, this took place online. Meetings included a 1.5-2-hour presentation followed by breakout sessions in separate virtual meeting rooms which provided the Team with further insight on focused areas such as RI&E and Risk. The presentations and interviews were scored by the Team and resulted in three managers being selected, one for each sleeve. Following the selection of the successful managers, the Team has received expressions of interest totalling around £1bn from Partner Funds. The funds are now expected to launch in Q2 2022. The Team has investigated different tools which could be used for measuring impact of the funds and also looked at a number of different secondary benchmarks which could be used for internal measurement purposes.

### 3.2.2 LGPSC’s RI Integrated Status for all ACS Funds

Since April 2018, LGPSC has been integrating RI&E into all (relevant) asset classes<sup>4</sup>. We have established an overarching KPI that 100% of product launches must receive our RI Integrated Status (RIIS). The RIIS is accorded to a product if a document explaining how RI will be integrated into the day-to-day management of the product has been approved by the Investment Committee. The process is designed to give internal and external stakeholders full assurance that RI is being integrated with the breadth and quality they desire. The proposal for RIIS within particular investment products is communicated via an RIIS Document, which is co-sponsored by the Director of RI&E and the relevant Investment Director for the product(s). By requiring co-sponsoring of the RIIS documents, we ensure that RI&E is an integrated process, not a siloed affair. The RIIS proposal will be approved by the Investment Committee if they are satisfied that the combination of processes, techniques,

activities and reporting achieve, in a manner suitable to the asset class, product, or mandate in question, the Company’s agreed RI aims: (1) primarily, to support investment objectives; (2) secondarily, to be an exemplar for RI within the financial services industry, promote collaboration and raise standards across the marketplace. RIIS is given to a fund once the Investment Committee approve the following criteria:

- Our RI beliefs relevant to that asset class are being followed
- Relevant RI related documentation support the decision to invest e.g., policies and procedures at external managers or co-investment companies
- Fund managers factor RI into their selection of portfolio assets
- RI reviews are carried out by the fund managers frequently and at appropriate levels

<sup>4</sup> Relevance is judged case by case but only in exceptional circumstances would it be deemed not relevant to integrate RI. In one case, UK Gilts, have we deemed RI and ESG integration as irrelevant.

- Our delegated stewardship responsibilities are carried out thoroughly e.g., engaging with companies, shareholder voting, manager monitoring, industry participation
- Fund managers are transparent in their reporting to clients and the wider public

We provide some examples below of how the RIIS differs for different funds and asset classes in question.

#### ACTIVE EQUITIES

LGPS has several investment beliefs specific to active equities which guide our integration of ESG within this asset class. These beliefs include, amongst others, that ESG risk is not always effectively priced (both in developed and emerging markets), the extent to which ESG factors apply to a particular stock or sector varies, and that engagement with companies is an active part of portfolio management. We place a lot of value on the manager selection process to ensure that these beliefs are being followed by the manager. Post-investment, monitoring in active equities is primarily achieved by analysing the portfolios in Bloomberg, inspecting managers' responses to quarterly data requests, and questioning managers during quarterly calls. We expect managers to be able to justify any new positions with a detailed analysis of the ESG risks and opportunities facing that company.

#### PASSIVE EQUITIES

For passive and factor-based equity funds we place a greater emphasis on stewardship and voting as our main tool for ESG integration. This reflects our belief that while index tracking funds can diversify away idiosyncratic ESG risk, long-term systemic ESG risk cannot be diversified. As a result, long-term investors should utilise thematic stewardship to mitigate long-term market risks and positively influence corporate practices. Reflecting this, LGPS Central focuses its engagement and voting activity on four Stewardship Themes which are agreed with our Partner Funds (See section 4.1.1 below).

#### FIXED INCOME

We believe that the extent to which, and the way, ESG is integrated into fixed income investing varies significantly by the type of issuer (corporate, sovereign, supranational, municipal, etc) and a one-size fits all approach is unlikely to be optimal. We reflect this belief in our selection process for Fixed Income mandates. During the selection of LGPSC's Multi Asset Credit Fund (launched in April 2021), we asked managers to provide three examples each pertaining to a different type of issuer to ensure that RI was being fully incorporated into all aspects of the portfolio.

#### PRIVATE EQUITY

Within Private Markets, RI is integrated into due diligence on a five-pillar scoring framework that covers: policy, people, process, performance, and transparency & disclosure. If a fund is considered high risk, either due to its sector or geographical location, a more rigorous due diligence assessment is conducted. The findings of the due diligence report are considered as part of the Private Markets Investment Committee approval process. Following appointment, we request that the manager report on material ESG incidents. For co-investments an RI risks report which is bespoke to the investment in question is issued.

### 3.2.3 LGPSC's monitoring of managers' ESG integration and engagement (ESG questionnaires etc.)

#### Active Equities and Fixed Income

Once appointed, we require external Public Market fund managers to complete a quarterly ESG questionnaire. Some disclosure items are "by exception" (for example alerting us to changes in ESG process or personnel) and others are mandatory. LGPSC receives quarterly data from external fund managers on the number of engagements undertaken and the weight in portfolio. We set expectations regarding the volume and quality of engagement, and we assess climate risk including portfolio carbon footprint, and exposure to oil, gas and coal producers. To send a unique voting signal to investee companies LGPSC votes its shares - whether externally or internally managed - according to one set of Voting Principles. While the ultimate voting decision rests with LGPSC, we have a procedure through which we capture intelligence and recommendations from external fund managers (See section 5.2 below).

The RI&E Team attend quarterly monitoring meetings with external managers. The purposes of RI&E monitoring are to analyse the level of ESG risk and climate risk in the portfolio, determine whether the manager is successfully applying the ESG process that was pitched, and assess whether that ESG process is proving successful. Monitoring is achieved through a combination of our own internal portfolio analysis, inspection of the manager's responses to quarterly data requests, and via dialogue at the quarterly meetings.

LGPSC has developed a Red, Amber, Yellow, Green (RAYG) rating for manager monitoring, of which RI&E is a core component. These ratings get updated each quarter based on the discussion at the manager meetings. The RAYG rating is split into four possible ratings: red (manager fails to convince, warrants formal review with potential manager exit), amber (manager warrants closer scrutiny with potential for going on "watch"), yellow (manager is fulfilling role but with minor areas of concern) and green (manager shows clear strengths tailored to requirement). We score managers on four components of their RI&E approach:

1. philosophy, people and process
2. evidence of integration
3. engagement with portfolio companies
4. climate risk management.

Reflecting its importance, the RI&E component carries 13% of the weight in the overall score.

#### Private Equity

For our primary private equity funds, LGPSC conducts a review, every 2 to 3 years, of each fund's RI&E processes. We utilise the same five-pillar scoring framework (policy, people, process, performance, and transparency & collaboration) that we assess during the original due diligence. The review is based on literature provided by the fund and on responses to specific RI&E questions put to the manager. Following this, we rescore the manager on each pillar and assess whether they have improved since the initial due diligence. In 2021 LGPSC completed RI&E reviews for all the Funds within our 2018 Fund Vintage.

For our private equity co-investments, the RI&E Team worked closely with the Private Equity Team in 2021 to implement a KPI ESG programme. As part of this process, we established a set of RI&E KPIs, covering both generic metrics to be collected from all co-investments irrespective of sector, as well as metrics specific to the co-investment in question. On the latter, it was important to us that the KPIs were bespoke and covered the material ESG risks specific to the business model of the company in question. It is our intention to receive annual disclosures against the KPIs from each of our co-investments, allowing us to track their ESG performance on a regular basis. Examples of generic KPI metrics that are being collected on an annual basis include Scope 1 and 2 GHG emissions, staff turnover rate and lost-time incident rate. This will provide confidence that the companies we invest in are managing their ESG-related risks effectively.





### 3.2.4 Cross-team interaction in development of new LGPSC funds

Proposals for product development are discussed and challenged at the Investment Committee (IC) and the Private Markets Investment Committee (PMIC), which derives its authority from the IC and the Board. The Director of RI&E is a voting member of IC and PMIC. These committees scrutinise investment proposals at a preliminary stage and authorise appropriate expenditure in connection with full due diligence and negotiation of investments. The RI and Stewardship implications are first discussed and scrutinised during this initial preliminary review. A due diligence report, including due diligence by the RI&E Team, is presented to the IC or PMIC for scrutiny and final approval.

#### CASE STUDY

##### Launch of Infrastructure Fund

A recent example of cross-team interaction is provided by the Q1 2021 launch of the LGPSC Infrastructure Fund which invests in a variety of renewable energy solutions. The RI&E Team had full access to all the deal documentation and met with the ESG teams of the shortlisted managers. Due diligence showed that overall ESG integration and stewardship were strong at both managers, however areas for improvement were identified around supply chain management and one of the company's human rights' policies. We will re-assess and discuss the situation related to human rights risk oversight and management at the first review in 2022.

#### CASE STUDY

##### Due diligence for Targeted Return funds

LGPSC are looking at targeted return funds, i.e., funds that aim to achieve a positive total return in all market conditions over a specific timeframe. The intention is to create a pooled investment fund for targeted return to be launched in H2 of 2022. These fund types present challenges from an ESG integration perspective as they cover a range of strategies (to obtain a return across both falling and rising markets), and contain an asset mix that includes hedging strategies, bank loans and other securities for which ESG integration methodologies are still nascent. The RI&E Team conducted initial due diligence on the responses submitted by the asset managers, leveraging knowledge around leading practice when assessing various strategies used. For instance, looking at incorporation of specific ESG signals and data analytics into managers' quant models and investment analysis as well as other approaches such as using ESG Futures, where the weightings within the index are based on ESG scores. Further diligence was done via meetings with the senior representatives of the respective managers, where the LGPSC RI&E Team were able to clarify any points around their integration, monitoring and stewardship. Special regard was given to intent and forward-looking plans to build out their current KPIs and metrics across all the ESG pillars. It was interesting to note that the managers were using an ESG overlay not just to mitigate risk but also in many instances as a value creation lever for generating better returns.

PRINCIPLE

8

## 3.3 Signatories monitor and hold to account managers and/or service providers

### 3.3.1 Monitoring of external managers

#### Active Equities

External fund managers are monitored in order to ensure the ongoing application and efficacy of their approaches to RI and stewardship. Managers report on a regular basis to LGPSC in respect of how engagement activities have been discharged during the period in review.

In 2021, LGPSC’s external managers conducted 203 direct engagements with companies held in the Global Equity Active Multi-Manager Fund and Emerging Market Equity Active Multi-Manager Fund. We provide below some case studies of engagements undertaken by our managers.

#### Deere & Co, Union, LGPSC Global Equity Active Multi-Manager Fund

**OBJECTIVE:**

Disclosure improvements and implementation of a climate policy

**SECTOR:**

Industrials

**ESG TOPICS ADDRESSED:**

Transparency & Disclosure; Management Remuneration

**ISSUE/ REASON FOR ENGAGEMENT:**

The company was a middling ESG candidate, lacking a net-zero policy and general transparency on a number of ESG measures.

**SCOPE AND PROCESS / ACTION TAKEN:**

Union conducted repeated engagements with the company since Biden’s election (which served as an impetus to develop their sustainability competencies before regulation forced them to do so).

**OUTCOMES AND NEXT STEPS:**

While the company does not use ESG KPIs as a criterion for manager remuneration, engagement efforts on this topic have been successful, and the company has committed to introducing these by 2023. Additionally, they are drafting a net-zero policy and have shown openness to integrating the UN SDGs into their practices. Union sees these actions as promising ‘first steps’ and hope to continue acting in an advisory role to help encourage Deere’s continued ESG growth.

#### China Mengniu Dairy Company, UBS, LGPSC Emerging Market Equity Active Multi Manager Fund

**OBJECTIVE:**

Disclosure improvements

**SECTOR:**

Consumer Staples

**ESG TOPICS ADDRESSED:**

Strategy and Business Model; Transparency & Disclosure; Nutrition

**ISSUE/ REASON FOR ENGAGEMENT:**

China Mengniu scored poorly on the Access to Nutrition Index. This appeared to be due to the sole use of publicly disclosed information. In the past, other companies have had the opportunity to engage with the Access to Nutrition Foundation to share additional information and work towards enhanced practices and disclosures.

**SCOPE AND PROCESS / ACTION TAKEN:**

UBS co-led a collaborative engagement as part of their membership of the Access to Nutrition Network. There were a total of 30 investors supporting the engagement and 10 participating in the engagement meeting itself.

**OUTCOMES AND NEXT STEPS:**

The company has proved to be very receptive to the engagement and has requested a follow-up meeting with UBS and the Access to Nutrition Foundation to better understand best practices as well as the methodology of the Index. They have committed to enhance disclosure on existing practices and to enhance practices.

Engagement undertaken by LGPSC’s external managers in 2021 has been comprehensive and robust. These managers are all long-term investors with sizeable positions in their highest conviction portfolio holdings, giving them excellent access to company management which they used effectively to drive company change. There were a few occasions where the level of engagement disclosure was unsatisfactory, or where the link between an engagement and subsequent investment decision-making was not clear. In these instances,

fund managers were marked down during our RAYG rating (red – amber – yellow – green) review and LGPSC discussed its concerns in the quarterly meetings.

An example of LGPSC changing the RAYG rating occurred in Q3 2021. Going into 2021, one of our managers achieved only a 'yellow' status due to concerns around the level of engagement being conducted. Compared to other managers, the number of engagements appeared low, and the accompanying description was poor. LGPSC initiated a dialogue with the manager around this issue and reiterated our expectations for managers' stewardship activities. Following this, the level of disclosure greatly improved. The manager now provides a full summary of their interactions with investee companies, and we are able to gain greater confidence that the manager is using their ownership position to maximum effect. We subsequently upgraded the managers engagement rating from a 'yellow' to a 'green'.

evidence of robust issuer engagement and any manager unable to provide this is marked down. Once appointed, LGPSC monitors engagements undertaken by fixed income managers during quarterly meetings. We seek to determine whether the manager is fulfilling the level of engagement that was pitched, and challenge accordingly if the response is unsatisfactory. These discussions subsequently feed into LGPSC's manager scoring system.

We consider our fixed income managers to have conducted meaningful and effective engagement in 2021. Throughout the year, LGPSC's external managers conducted 349 direct engagements with companies held in the Global Active Investment Grade Corporate Bond Multi Manager Fund, Global Active Emerging Market Bond Multi Manager Fund and Multi Asset Credit Fund. We provide below two case studies of engagements our managers have undertaken on our behalf.

### Fixed Income

LGPSC views engagement with fixed income issuers as essential and value accretive, both via information gains and via the potential to influence company management. LGPSC observes this belief when selecting and onboarding managers. We look for

#### HDFC Bank, M&G, LGPSC Emerging Market Debt Fund

**OBJECTIVE:**

To encourage better clarity on HDFC's policy on coal

**SECTOR:**

Financials

**ESG TOPICS ADDRESSED:**

Coal lending

**ISSUE/ REASON FOR ENGAGEMENT:**

To gain a better insight into the group's coal exposure and look for clearer disclosure on its policies around lending to coal companies.

**SCOPE AND PROCESS / ACTION TAKEN:**

M&G met with the company twice to discuss this issue.

**OUTCOMES AND NEXT STEPS:**

Following M&G's meeting, HDFC Bank committed to becoming carbon neutral by 2031/2032. As part of this initiative, the Bank is looking at reducing its emissions, energy and water consumption. While this is a step in the right direction, M&G still believe there is little visibility on whether the bank will be more direct in its communications around lending to the coal sector. M&G intend to monitor the situation for further progress.

#### National Grid, Neuberger Berman, LGPSC Global Active Investment Grade Corporate Bond Multi Manager Fund

**OBJECTIVE:**

- (1) To gain a greater understanding of how the company is managing the physical climate risk facing parts of its asset base and;
- (2) to encourage a repositioning towards electrical infrastructure assets and away from gas assets.

**SECTOR:**

Utilities

**ESG TOPICS ADDRESSED:**

Energy transition

**ISSUE/ REASON FOR ENGAGEMENT:**

Neuberger Berman have concerns over the long-term stranded asset risk and limited growth potential exhibited in the firm's gas transportation assets.

**SCOPE AND PROCESS / ACTION TAKEN:**

Neuberger Berman have been conducting engagement with the National Grid over several years, a programme which has included regular discussions with the issuer's management team, investor relations team, segmental managers, industry competitors, and regulators.

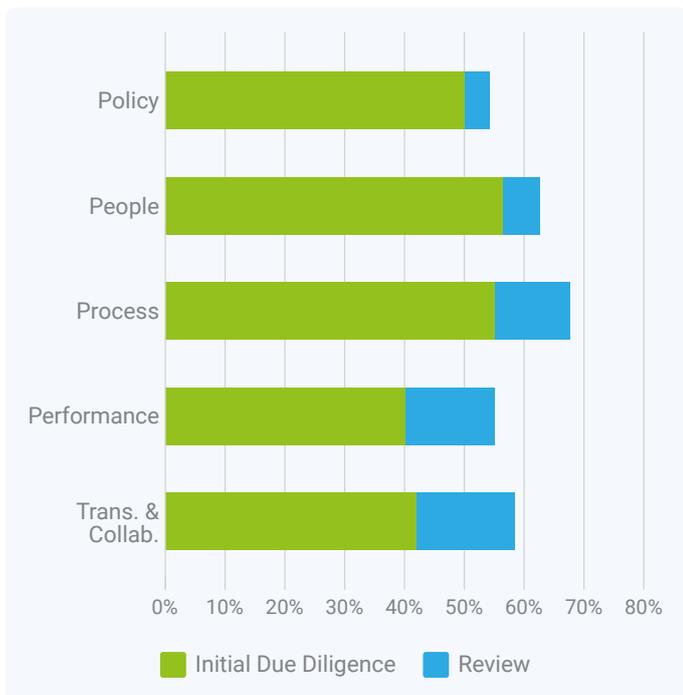
**OUTCOMES AND NEXT STEPS:**

As a result of the engagement, National Grid have agreed to an asset swap which significantly increases their exposure to fast growing infrastructure assets. The deal strengthens the company's role in building and operating the infrastructure required to meet the rising demand and changing energy mix that accompanies the low carbon transition. Neuberger Berman are encouraged by the capital allocation shift.

**Private Markets**

Private equity fund managers are monitored through regular RI&E reviews every 2-3 years. In 2021, all of our private equity funds took steps to improve their RI&E processes, reflected in improved ratings against our five-pillar scoring framework. Figure 3.3.1.1 provides a summary of the areas where our private equity managers made improvements in 2021.

**Figure 3.3.1.1 RI&E improvements between the initial due diligence and review**



At a high level, we observed the following trends within our 2021 Private Equity RI&E Reviews. GPs are rapidly expanding their RI&E resource. A number of our managers are hiring dedicated ESG professionals, initiating ESG working groups and utilising external advisors to provide RI training for all staff members. In turn, we've seen an increase in the number of GPs collecting ESG data from their portfolio companies. Transparency has also improved, with more GPs offering annual ESG reports and material incident reporting to LPs. While these trends are positive, we are conscious that private markets continue to lag public markets in several aspects, so we will continue to engage with our private equity managers on these areas. A particular focus point for LGPSC in 2022 includes pushing for even greater transparency as we would like to see greater standardisation in the metrics reported across different PE funds.

As part of our KPI monitoring programme we reached out to 80% of our co-investment GPs in 2021. During meetings with the GPs, we noted that collecting comparable and standardised data on our co-investments would prove challenging due to the different RI&E programmes and approaches that each GP employs. To overcome

this challenge, we worked closely with each GP to identify areas where we can currently collect data, and areas which would require further work and engagement with the co-investment firm to bring relevant information to light. In addition, we will challenge the GP if we believe they are not engaging enough with the co-investment firm on issues we deem material. Currently we are satisfied with the GP's monitoring efforts but will continue to work with them on any areas we believe require enhancements in the future. We provide our Partner Funds detailed reporting on each co-investment's RI&E KPIs.

In Q1 2021 we reached out to one of our GPs to establish RI&E KPIs for a co-investment firm. The GP provided an overview of its current monitoring efforts, which included an ESG dashboard and impact KPIs. LGPSC found the monitoring and KPI programme to be highly comprehensive and detailed, exceeding our expectations. Through its due diligence and KPI monitoring, the GP identified several areas that the co-investment could improve. As a result, the GP engaged with the firm to create an action plan, which included a 5-year ESG journey strategy and an environmental impact assessment. The GP was very transparent, sharing metrics and underlying data and welcomed LGPSC's input on KPI development. Moving forward, LGPSC will receive updated disclosure against the dashboard and KPIs on an annual basis, allowing us to track the progress of the Firm. In addition, we will continue to meet with the GP on an annual basis to discuss any areas we believe require enhancements in the future.

**Future developments to the manager monitoring**

We plan to undertake a three-yearly review in 2022 of our Active Equity and Fixed Income managers. While we attend regular monitoring meetings, these reviews will include a deep dive of the managers RI processes so LGPSC can ensure their ESG integration remains best practice.

In the private markets space, we intend to continue our private equity RI&E reviews. We also envisage that this practice will be rolled out to our private debt, infrastructure and property investments once these are finalised. In the co-investments space, we intend to work with our GPs to improve the quality of data being disclosed. As part of this, LGPSC has recently become a supporter of the ESG Data Convergence Project, an initiative which aims to standardise ESG data across the private equity industry, and eventually private debt industry, by providing one set of metrics for companies to report against. We contacted all of our GPs to identify whether they have joined or intend to join this project and will work with our GPs over the next year to encourage participation.

This structure is further evidence of LCPSC's commitment to integrating RI across Investment Teams and our belief that RI is not just a prerogative of the RI&E Team, it is something that all colleagues need to embrace if we are to realise the benefits in full.

### 3.3.2 Review of EOS' services

LGPSC holds, at minimum, one client service review meeting per year with EOS to discuss our overall satisfaction with their services, any issues over the last period; alongside engagement and voting trends and voting policy reviews. However, we meet more frequently during the year to discuss specific votes and engagements and we find this ongoing dialogue to be extremely helpful particularly during proxy voting season. The EOS Team also attend our quarterly PAF RI WG meetings, which gives our Partner Funds the opportunity to ask specific questions about engagements and prioritisation. Further to this, there are multiple touchpoints for clients to review EOS' activities, by way of regular reporting (client portal, quarterly and annual reporting) and opportunities to provide feedback, for instance through EOS' semi-annual client conference which hosts client-only discussion forum.

The RI&E Team undertakes an annual review of EOS' services to provide assurance to the Investment Committee that the Stewardship Provider, EOS at Federated Hermes, is delivering sufficiently against the terms of the contract. This document is issued to and approved by the Investment Committee on an annual basis. See below an extract from the 2021 review, which highlights Q3 engagement and voting data as full-year data at this point was not yet available.

**Summary for 2021 review:**

- Provider has given generally strong and value-adding services to LGPSC, including close dialogue during voting season related to LGPSC's Voting Watch List
- Provider has given direct support to Partner Funds through participation at virtual RI Day in October 2021 and at all PAF RI Working Group meetings during the year.

KPI AREA	KPI REVIEW
<b>Global engagement</b>	Engaged 212 companies, with a regional and thematic breakdown shown in Appendix 1.
<b>Engagement quality</b>	At least one milestone was moved forward for 39% of current engagement objectives (year to end Q3 2021).
<b>Voting coverage</b>	Made voting recommendations at 332 meetings, with a regional breakdown shown in Appendix 3.
<b>Client service</b>	Majority of queries to EOS were dealt with in less than 24 hours, but with some timeliness issues during the last months of 2021 (see immediately below).
<b>Complaint handling</b>	Head of Stewardship has had dialogue with EOS' Director of Business and Client Development following a change of client relationship manager in October 2021, to discuss concerns around timeliness in responses to LGSPC queries. EOS has come up with a solution whereby any email to EOS will go to both our client relationship manager and to an email account set up specifically for LGPSC, to avoid any requests not being picked up.
<b>Client service meeting</b>	Several meetings held pre, during and post voting season 2021 relating to planning of voting season, overall feedback on EOS' services, hand-over meeting between previous and new client relationship manager, and a separate meeting with Head of EOS' Client Relations.
<b>Reporting punctuality</b>	Reporting on schedule for Q1, Q2 and Q3 2021. Data for the Global Multifactor Fund was initially missing for Q1, but there was quick turnaround on EOS' side when the missing data was discovered so no impact on our delivery to PFs.
<b>Reporting quality</b>	Overall good quality.
<b>Team stability</b>	Staff turnover during 2021 was just below 32%. This is a much higher number than previous years (10% for 2020 and 19% for 2019). EOS says this increase in turnover is due to unprecedented demand and competition for ESG/stewardship experience and talent in the market, particularly in the UK. They remain confident of their ability to attract the best engagers, currently EOS' employs 40 engagers, and that the situation will normalise going forward.

# 04 Engagement



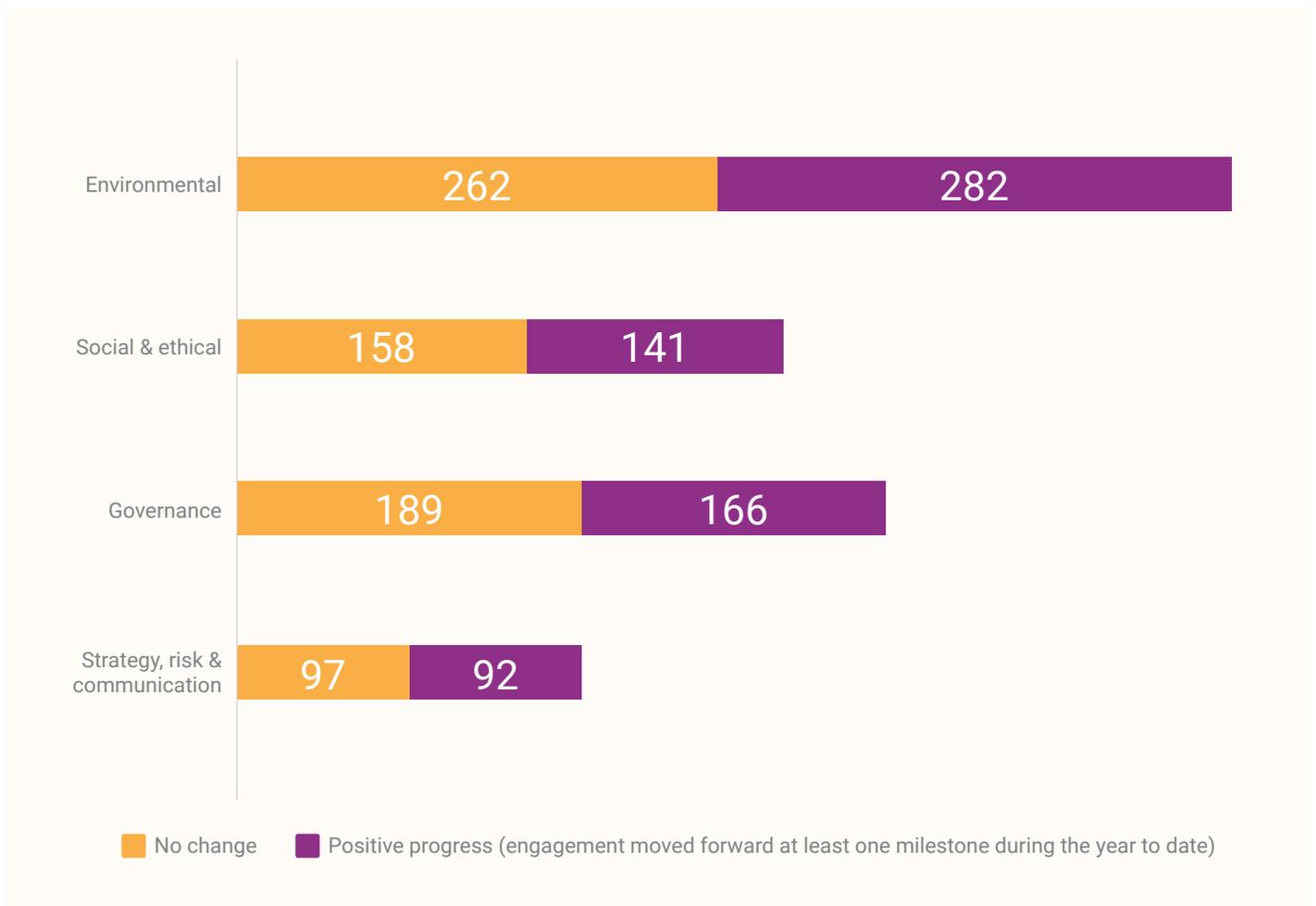
**PRINCIPLE 9** 4.1 Engagement with issuers

Alongside our own direct engagements, we have partners that engage companies on our behalf: EOS at Federated Hermes (Stewardship provider to LGPSC) and the Local Authority Pension Fund Forum (LAPFF). Through these partnerships, LGPSC was able to engage more than 1000 companies on material ESG related issues in the course of 2021. Below we give further detail to a selection of engagements, how they are progressing and what outcomes have been achieved during the reporting period.

Most of these engagements were conducted by EOS who engaged with 888 companies on 3,375 environmental, social, governance, strategy, risk and communication issues and objectives<sup>5</sup>. EOS

takes a holistic approach to engagement and typically engage with companies on more than one topic simultaneously. Near 40% of engagements centred around governance issues, and close to 30% involved discussions on environmental issues. 1,951 of the issues and objectives engaged in 2021 were linked to one or more of the UN Sustainable Development Goals (see Figure 4.1.2 below). **At least one milestone<sup>6</sup> was moved forward for about 49% of EOS’ engagement objectives during the year.** Figure 4.1.1 below describes how much progress has been made in achieving the milestones set for each engagement.

Figure 4.1.1 Progress against engagement objectives in 2021

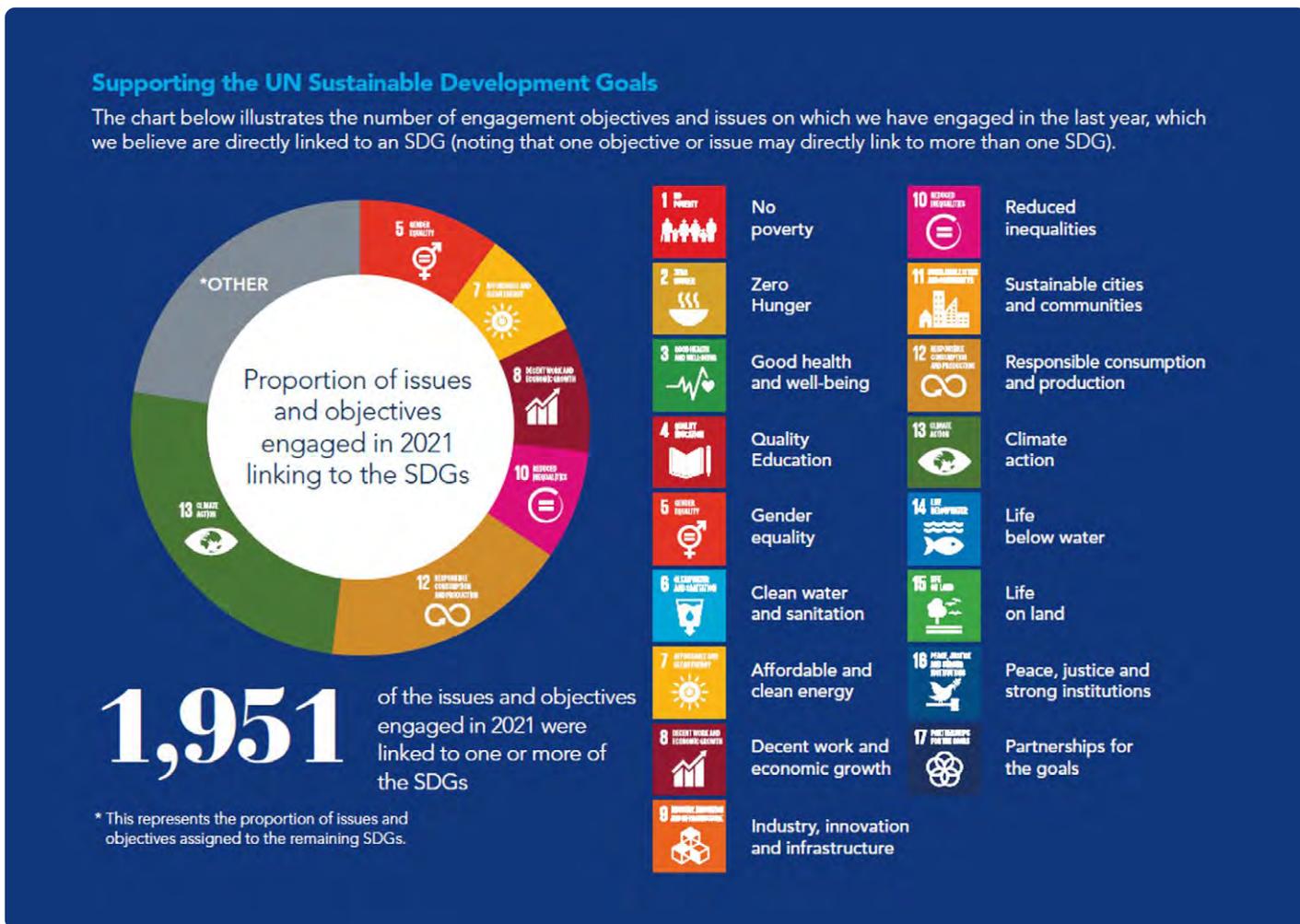


<sup>5</sup> Our Stewardship provider EOS distinguishes between engagement issue and engagement objective. Specific engagement objectives will be set at the beginning of company dialogue and progress is measured on these through a proprietary milestone system. An issue is a topic EOS has raised with a company in engagement, for instance around the time of an AGM, but where a precisely defined outcome for the engagement has not been set in advance. This can be more appropriate if the issue is of lower materiality and EOS would not anticipate engaging with the frequency required to pursue an engagement objective.

<sup>6</sup> EOS’ proprietary milestone system allows tracking of engagement progress relative to the objectives set at the beginning of interactions with companies. The specific milestones used to measure progress in an engagement vary depending on each concern and its related objective. They can broadly be defined as follows:

- **Milestone 1** Concern raised with the company at the appropriate level
- **Milestone 2** The company acknowledges the issue as a serious investor concern
- **Milestone 3** Development of a credible strategy/Stretching targets set to address the concern
- **Milestone 4** Implementation of a strategy or measures to address the concern

Figure 4.1.2 Engagement supporting the UN Sustainable Development Goals



LGPS and all our Partner Funds are members of the Local Authority Pension Fund Forum (LAPFF). LAPFF conducts engagements with companies on behalf of local authority pension funds. In 2021, LAPFF engaged 165 companies through more than 97 meetings across a spectrum of 299 material ESG issues. In these engagements, LAPFF saw 123 instances of improvements or change in progress.

During 2021, LGPS’s external managers conducted 203 direct engagements with companies held in active equity funds, and 349 engagements with companies held in fixed income funds on our behalf. Overall, we view these engagements as comprehensive and robust. Our external managers are all long-term investors with sizeable positions in their highest conviction portfolio holdings, and we expect them to use this lever to effectively drive company change on a material ESG issues. Topics covered during 2021 include, amongst others, environmental management and climate change, energy transition, greater focus and disclosure of health and safety within ESG priorities, data protection and information security risk, and forced labour issues in supply chains. See further detail and examples under Section 3.3 above, and Section 4.3 below.

### 4.1.1 Stewardship Themes

It is not feasible to engage all companies we hold through ACS portfolios (currently c2,900 companies held across equity portfolios), even with the assistance of a high-calibre external stewardship specialist. Identifying core themes that are material to our investment objectives and time horizon, and that are perceived to be of relevance to stakeholders, helps prioritise and direct engagement.

In collaboration with our Partner Funds, we have continued engagement on four themes that are in scope for engagement over rolling three-year periods, subject to annual review. For the reporting period 2021 these were:

- Climate Change,
- Plastics,
- Fair and Transparent Tax Behaviour, and
- Technology and Disruptive Industries Risks.

## 4.1.2 Stewardship Theme engagements - progress and outcomes

### 4.1.2.a Climate Change



#### STEWARDSHIP STRATEGY:

Engagement is done through key collaborative initiatives including CA100+, Institutional Investor Group on Climate Change (IIGCC) and the Transition Pathway Initiative (TPI).

#### MEASURES OF SUCCESS:

We assess progress against the underlying objectives of the CA100+ engagement project, and against improvements on TPI score for management quality and carbon performance. Our aims are:

- To lead or be in the focus group of at least five CA100+ company engagements over the next year, prioritising engagements that overlap with companies that are identified as high risk within Partner Fund Climate Risk Reports
- To see progress in the CA100+ Benchmark Framework (launched March 2021)
- To see improvements on TPI score for management quality in key engagements
- To see improvements on TPI score for carbon performance in key engagements

#### ENGAGEMENT HIGHLIGHTS DURING 2021:

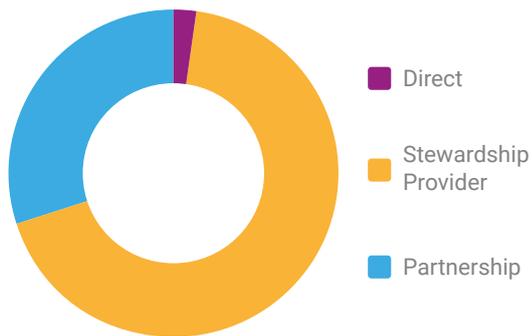
- 627 companies engaged on 978 climate-related issues and objectives with progress on 426 specific objectives out of 741 total objectives set.
- Ongoing engagement with 68 banks on Paris-alignment and protection of biodiversity. 50 banks have responded and 19 confirmed they will publish new climate targets in connection with COP26, the end of the year, and/or their 2022 AGM. This includes **BBVA, BNP Paribas, Citigroup, and Standard Chartered**. See more detail in Section 4.3 below.
- Investor expectations on **Paris-aligned accounting** were

communicated to 36 European energy, material and transportation companies in 2020, and again reiterated in letters to 29 of the same companies in November 2021 as we have not seen sufficient progress. See more detail in Section 4.2 below.

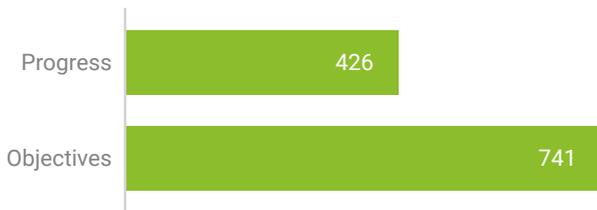
- **Progress on TPI score:** EOS on our behalf engaged over 250 companies that fall short on TPI score (against an expectation that European companies, coal mining and oil & gas companies need to be at level 4 in climate management quality), with a high level of response. During 2021 we opposed the election of the responsible director for climate change (usually the Chair) at over 100 companies, including **Canadian Natural Resources** and **China Resources Cement Holdings**.
- **Progress against CA100+ benchmark:** Data as of March 2021 from CA100+ shows that 52% of the world's largest emitters have net-zero goals, but only 20% have short and medium-term emissions reduction targets, and only 7% have targets aligned with the Paris Agreement. Gaps also remain in aligning capital expenditure plans with net-zero ambitions and in linking delivery of climate targets with remuneration. Climate policy lobbying also remains an area of concern, where most companies need to improve processes and transparency around how they ensure alignment with their own climate positions and the advocacy done on their behalf through industry associations.
- In 2021, we voted against directors at companies that were failing to address deforestation risks, including at **Yakult Honsha, Li Ning Company, and WH Group**. Going into 2022, we will specifically include biodiversity in our engagement efforts related to climate change. We will amongst others initiate engagements to fulfil a commitment to tackle agricultural commodity-driven deforestation and help drive the shift towards sustainable production and nature-based climate solutions (see further detail in Section 4.2 below).



**ENGAGEMENT VOLUME BY TYPE:**



**ENGAGEMENT VOLUME BY OUTCOME:**



**CLIMATE ENGAGEMENT CASE:**

In the role of co-lead for CA100+ engagement with **Centrica**, we have been in frequent and constructive dialogue with the company to discuss their climate strategy and to provide views on its climate transition plan.

**We were pleased to see the company set a clear net-zero by 2045 commitment accompanied by short- and medium-term targets in the transition plan.** We also welcome the company’s clear ambition to help customers decarbonise by 2050, e.g., through decarbonisation of heat. We explained our expectations relating to the indicators of the CA100+ benchmark and pointed to areas where the company would need to make further commitments to align with the benchmark. This includes short-term target setting (up to 2025) that substantiates a clear Net-Zero pathway this decade. Investors would also like to see a commitment from the company to decarbonise its electric utility power generation by 2035.

The company is enhancing transparency on climate policy lobbying in the climate transition plan, which we welcome. We encourage further transparency around policy barriers so that investors can support specific policy action that will help achieve net-zero for the company and its sector.

## 4.1.2.b Plastic pollution



### STEWARDSHIP STRATEGY:

We will leverage investor collaboration opportunities for instance through the PRI Plastics Working Group and Investor Forum's Marine Plastic Pollution project. Voting will be engagement led, and we will consider co-filing or supporting shareholder resolutions that relate to better risk management (reduce plastic use, reduce plastic waste, increase recycling, invest in relevant R&D).

### MEASURES OF SUCCESS:

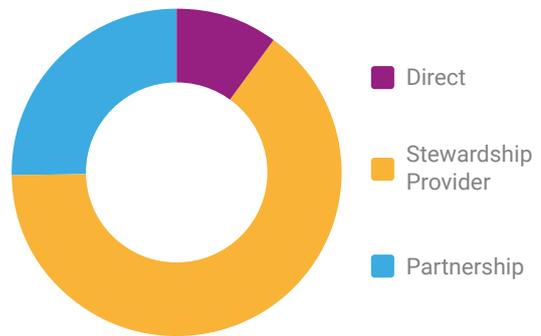
- We aim for positive interactions at senior levels of target companies and acknowledgement of plastic as a business risk, along with commitments to strategies or targets to manage those risks
- We aim to lead or be part of at least five plastics-related company engagements over the next financial year
- We aim to support investor expectations – e.g., as expressed by the PRI Working Group – in dialogue with companies

### ENGAGEMENT HIGHLIGHTS DURING 2021:

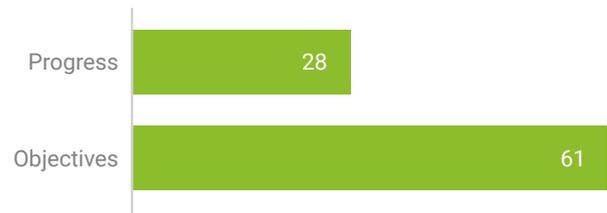
- 57 companies engaged on 71 plastics and circular economy related issues and objectives, with progress on 28 specific objectives out of 61 total objectives set
- LGPSC member of collaborative engagement led by Dutch investor Achmea Investment Management with seven **packaging companies**, to reduce, re-use and replace fossil-fuel based plastics
- 2-3 meetings have been held with each of the packaging companies in 2020-2021 asking for more transparency on materials used, (more ambitious) targets for the use of more sustainable and circular materials, and ESG performance indicators in executive remuneration. **Companies respond positively to our asks e.g., by introducing SASB reporting standards providing more insight into materials used.** Most companies focus on increasing the use of recycled plastics, although pace and ambitions vary. **We see progress with companies on adding ESG related KPIs in remuneration**
- Collaborative engagement led by First Sentier Investors engaging 13 companies to help **combat microplastics pollution** to the environment (see case study below)
- Launch of first **industry specification to prevent plastic pellet pollution** co-sponsored by LGPSC alongside nine other institutional investors through an Investor Forum led multi-stakeholder project
- Businesses and investors, including LGPSC, have called for **UN treaty on plastic pollution** ([plasticpollutiontreaty.org](https://plasticpollutiontreaty.org) – agreement has since been found to negotiate a treaty (See further detail below in Section 4.2)).



ENGAGEMENT VOLUME BY TYPE:



ENGAGEMENT VOLUME BY OUTCOME:



CASE STUDY:

Through a **micro-plastics engagement project** led by First Sentier Investors, we seek to encourage domestic and commercial washing machine manufacturers to add filter technology as standard to all new washing machines produced by the end of 2023. This is to help combat microplastics pollution to the environment, a problem caused in large proportion by synthetic textiles which release microfibres (a type of microplastic) when washed. A first round of engagements with 13 target companies<sup>7</sup> have been concluded by the investor group this year.

At the AGM of **Sainsbury's** and through subsequent dialogue with the investor group, **the company is taking positive steps to engage its washing machine manufacturers and aims to introduce products with microplastic filters within the next 18 months.** We also welcome recommendations from the "All Party Parliamentary Group on Microplastics" issued in 2021, which could be influential in determining the direction of government policy in this area. The key recommendation in relation to microfiber filtration is to: *"Introduce legislation and standards which require microfibre filters to be fitted into all new domestic and commercial washing machines from 2025."*

<sup>7</sup> Arcelic, Dixons Carphone, Electrolux, Haier Group, Hitachi, Koc Holdings, LG Electronics, Midea, Panasonic, Sainsbury's, Samsung, Sharp and Whirlpool

### 4.1.2.c Responsible Tax Behaviour



#### STEWARDSHIP STRATEGY:

We will leverage investor collaboration opportunities for instance through PRI Tax Investor Working Group and a Tax Roundtable (led by NBIM (Norway) and APG (Netherlands)). Voting will be engagement led, and we will e.g., consider co-filing or supporting shareholder resolutions that relate to better risk management (through tax policy, board oversight, country-by-country reporting).

#### MEASURES OF SUCCESS:

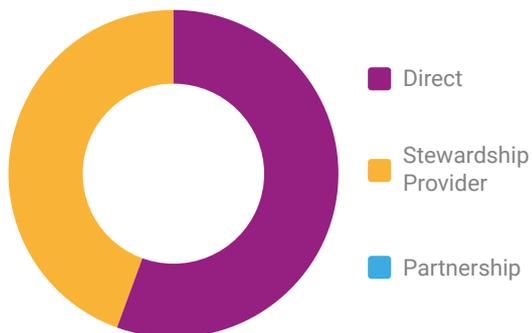
- We aim for positive interactions at senior levels of target companies and acknowledgement of lack of tax transparency as a business risk, along with commitments to strategies or targets to manage those risks
- We aim to lead or be part of at least five tax-related company engagements over the next financial year
- We aim to support investor expectations – e.g., as expressed by the GRI tax standard and the UK Fair Tax Mark – in dialogue with companies

#### ENGAGEMENT HIGHLIGHTS DURING 2021:

- 14 companies engaged on 16 tax related issues and objectives, with progress on four specific objectives out of 12 total objectives set
- LGPSC has continued collaboration with four other, European investors which is a sub-group to a broader Tax Roundtable led by Norges Bank Investment Management and APG
- Group has sought **engagement with six companies across technology, telecommunications, finance and mining sectors where a low effective tax rate was an initial concern with several of these**
- Key asks: Board oversight of tax policy and risk assessment; disclosure of tax strategy and policy; robust management of tax related risks, including preferably a country-by-country tax disclosure; link between company's purpose, sustainability goals and tax strategy; engagement with tax policy makers and other stakeholders
- **Two out of the six companies have during this engagement signalled an intention to publish a stand-alone tax report which will provide country-by-country tax-relevant information**, and thus increase transparency in line with our expectations
- Co-signed a letter to the European Parliament supporting a draft directive on **public country-by-country reporting (CBCR)** in the EU.



**ENGAGEMENT VOLUME BY TYPE:**



**ENGAGEMENT VOLUME BY OUTCOME:**



**CASE STUDY:**

Together with three fellow European institutional investors we have had constructive engagement with a **global business services company** to discuss tax transparency and responsible tax behaviour. A core expectation from investors is that the company share tax-relevant Country-by-Country Reporting (CBCR) with shareholders so that we can make a meaningful assessment of their tax behaviour. We were pleased to hear that **the company is considering publishing a stand-alone tax report that would enhance the disclosure of the company's approach to tax and its tax policies and may also give greater granularity on where tax is paid.** In addition to its corporation tax contributions, the company makes significant tax contributions via its employee taxes (reflecting the company's highly skilled employee base). The company is considering ways of enhancing transparency for instance by providing information on where employees are based alongside where taxes are paid. We also encourage the company to explain its use of low-tax jurisdictions and to provide assurance that this correlates well to the company's business and strategy. The company explained that the Board takes a keen interest and receives regular reports on long term strategic tax issues.

It seems clear that the company wishes to understand best practice for tax transparency and is embarking on a benchmarking exercise for that purpose. The investor group welcome these developments, alongside the company's ongoing revision of its Tax Policy. We will continue dialogue with the company to understand how its tax transparency work is progressing and to what degree industry standards like the Global Reporting Initiative tax standard<sup>8</sup> can be used in this regard.

<sup>8</sup> The Global Reporting Initiative (GRI) Tax Standard is the first global standard for comprehensive tax disclosure at the country-by-country level. It supports public reporting of a company's business activities and payments within tax jurisdictions, as well as their approach to tax strategy and governance.

### 4.1.2.d Technology and disruptive industries risk



#### STEWARDSHIP STRATEGY:

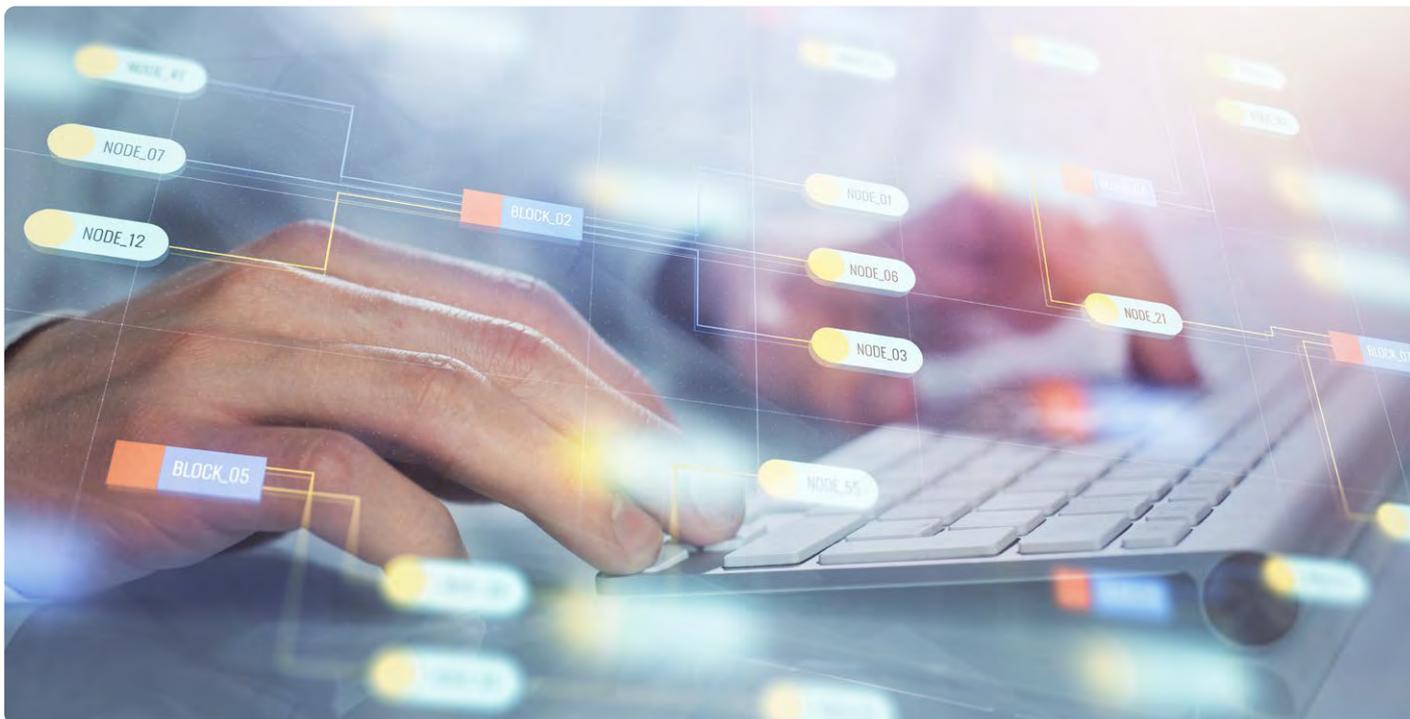
We will leverage investor collaboration opportunities for instance the New Zealand Crown-owned investors’ coalition aimed at eliminating terrorist and violent extremist content online. Voting will be engagement led, and we will e.g., consider co-filing or supporting shareholder resolutions that relate to better risk management on social media content control and human rights risks.

#### MEASURES OF SUCCESS:

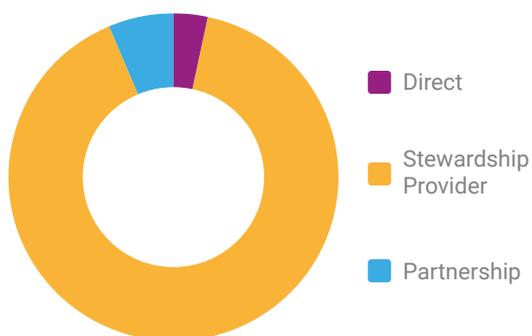
- We aim for positive interactions at senior levels of target companies and acknowledgement of the above-mentioned risks faced by many tech companies.
- We aim to lead or be part of at least five engagements with tech companies over the next financial year.
- We aim to support benchmarks such as Ranking Digital Rights, the Workforce Disclosure Initiative and SASB’s Content Moderation taxonomy.

#### ENGAGEMENT HIGHLIGHTS DURING 2021:

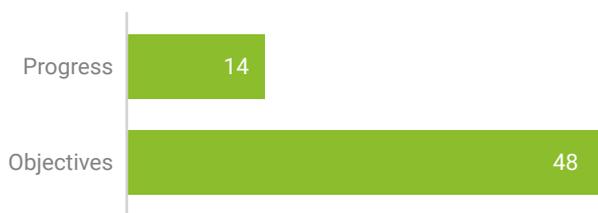
- 37 technology companies engaged on a range of 79 ESG risks including governance, cyber security, supply chain risks, social media content control and broader human rights risks. Progress was seen in 14 cases against a total of 48 specific objectives
- **LGPS has been part of two collaborative initiatives: one focusing on social media content control, and one addressing human rights more broadly**
- In the face of COVID19 and a highly polarised US presidential election November 2020, the social media content control engagements garnered momentum through pressure from advertisers and other stakeholders (including World Federation of Advertisers) on harmful content including hate speech and aggression
- While initially hard to engage, the three companies in scope of social media content control engagement (**Facebook**, **Twitter** and **Alphabet**) have taken steps during 2020 – 2021 to strengthen controls and to prevent the live streaming and distribution of objectionable content
- Human rights risks engagement initiative has built momentum after Investor Expectations were published, including engagement with **Facebook** on their newly launched Human Rights Policy, and **Amazon** on their recent Human Rights Impact assessment



**ENGAGEMENT VOLUME BY TYPE:**



**ENGAGEMENT VOLUME BY OUTCOME:**



**CASE STUDY:**

We have over the last two and a half years engaged the world's three largest social media companies, **Facebook, Twitter** and **Alphabet**, specifically on the issue of social media content moderation. This engagement has been led by the Guardians of New Zealand Superannuation (Guardians) alongside the New Zealand government-owned investors and supported by more than 100 investors globally. This project, which as of H2 2021 is drawn to a close having seen some significant progress, adds to growing investor scrutiny on the critically important role of social and traditional media in our societies. **The platforms have all moved to strengthen controls to prevent the live streaming and distribution of objectional content.** However, it is a difficult job for investors to assess if these changes are appropriate for the scale of the problem and a continued focus on the evolution of preventative safeguards will be needed.

The issue of content moderation is becoming one of the defining legal and socio-political issues of our time. It deserves its own body of specialist expertise stretching across a range of academia, law and policy. Our expectation is that these companies carry out their duty of care with absolute resolve, and while we've seen some good progress throughout our engagement – the goal posts keep moving and the companies need to remain focused on managing this. **The engagement project received Stewardship Initiative of the Year award at the UN PRI 2021 Awards for its success in engaging these multinational giants.** Key elements of its success lie in building a large investor coalition, escalating the engagement, and discussing specific steps companies can take to tighten controls as well encouraging more transparency about their ongoing work and interaction with various stakeholders.

### 4.1.3 Engagement on themes and issues outside of Stewardship Themes



#### Engagement case: Diversity

Japanese boards have one of the lowest proportions of female representation in developed markets and as a member of the 30% Investor Club we very much welcome recent developments with the 30% Investor Club opening a 30% Investor Club Chapter in Japan in May 2019. Over the last 18 months, we have together with fellow 30% Investor Club members, and led by Royal London Asset Management, engaged a **Japanese bank** to encourage better diversity and to seek more disclosure on diversity-related policies. A general hurdle to achieving greater diversity at board level in the Japanese market is the fact that historically, Japanese women in their 40's and 50's gave up their careers to raise families. **It is therefore particularly welcome that the company recently appointed a woman to the Board** who had been on the management team since 2019, and with the company since 1987. This brings female representation at the Board to 13%. This move does not seem to have entailed broader changes to the Board's nomination policies and the low number of female executives remains an obstacle to greater diversity. An objective for this engagement was to encourage the company to join the 30% Club, and we were pleased to see the company take this step during H1 of 2021. While we would like the company to set more ambitious targets for diversity at all levels of the organisation, we note that the company aims to achieve increase in diversity by looking at recruitment and supporting women in career positions from early on. This engagement will continue alongside new engagements with a selection of other Japanese companies based on our exposure and/or their less than 10% gender diversity at board level in 2020, to be commenced in Q2 2022.



#### Combatting modern slavery

Over the last two years, LGPSC has been a member of a collaborative investor-initiative convened by Rathbones Group Plc (Rathbones) that has successfully encouraged laggard **FTSE 350 companies** to meet the reporting requirements of Section 54 of the Modern Slavery Act 2015. According to the Act, companies with a turnover of more than £36 million per year must publish a modern slavery statement and ensure that the statement is approved by the board; signed by a director; and reviewed annually and published on the company's UK website. During 2021, we engaged 61 FTSE350 companies asking for Modern Slavery Act compliance. **As per end 2021, all companies have responded and are now compliant.** Initial positive responses have given an opening for meetings to discuss companies' approaches to modern slavery. This is an important step beyond the initial ask of compliance with the Modern Slavery Act, to focus on the content of the statement and to enable investors an understanding of the key risks facing individual companies.

In June 2021, we joined Rathbones in engagement with a **UK retailer** who has chosen to broaden its net zero climate strategy to include social risks, aiming to capture the interlinkages that exist between environmental and social factors. Human rights as a theme gets specific attention through a working group with a direct line to the company Board. In 2017, **the company established a Modern Slavery Risk tool which has since been extended to include all human rights risks.** The tool is both product and region specific and it is possible to select specific risks (for instance gender, forced labour, child labour) but also assess the broader risk picture. The company strives to continue embedding the tool further in its business functions. Areas of increasing concern in relation to modern slavery are transport and haulage, as well as sea freight. **We commended the company for its detailed modern slavery statement and for the high level of transparency around high-risk areas.**

## PRINCIPLE 10 4.2 Participation in collaborative engagement to influence issuers

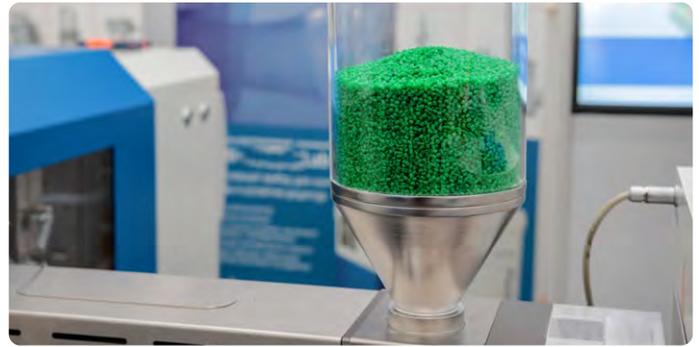
LGPSC has continued active involvement in several strong investor collaborations that pursue better corporate standards across ESG issues, including for several Stewardship Themes<sup>9</sup>, during 2021. The pool has also supported theme-relevant industry standards and benchmarks, which clarify investor expectations of companies and provide a mechanism for measurement of progress. For a list of initiatives that LGPSC actively supports and engages with, we refer to Section 2.4 above.

Examples of collaborative initiatives of particular importance to LGPSC's stewardship effort in 2021:



### Accounting and Audit of climate risk

LGPSC has over the last two years been a member of an investor coalition, led by Sarasin and Partners LLP, engaging both auditors and companies asking for the provision of Paris-aligned accounting. **Investors expect that directors of companies that face material climate risk consider these risks in their financial statements and make disclosures accordingly.** If climate risk is not considered, the longevity and value of assets held by the company may be over-estimated, which could lead to capital being misdirected. The IIGCC Investor expectations for Paris-aligned Accounts that were communicated to 36 European energy, material and transportation companies in November 2020, were again reiterated in **letters to 17 of the same companies in late 2021/early 2022 as we have not seen sufficient progress.** An increasing number of investors are setting a net-zero by 2050 ambition at portfolio level, including LGPSC. It is critical that we have the component building blocks including full clarity on climate risk held at individual company level, how this risk is being managed and companies' transition trajectories. Companies themselves are also setting net-zero by 2050 targets and we expect them to make net zero accounting adjustments in line with such an ambition. Should a company not use a 2050 net-zero pathway as their base case for their financial statements – for instance, because they do not believe this is the most likely outcome – we are still asking them to disclose how the entity's financial position would likely be impacted by such a pathway in the notes to the accounts. Our strategy is to maximise engagement leverage with investee companies to ensure a transition that can achieve net-zero. In the letters sent out most recently, companies are made aware that **an increasing number of investors may be voting against Audit Committee directors' reappointment, the financial statements or the company auditor, where high-risk companies fail to meet the expectations for Paris-aligned accounting.**



### Plastic pellet industry standard and UN treaty on plastic pollution

Billions of plastic pellets or "nurdles" make their way into the natural environment each year, which poses a serious threat to the ecosystem and potentially also a health threat to people. LGPSC has collaborated with the Investor Forum, peer investors and other stakeholders including Marine Scotland, the British Plastics Federation and the British Standards Institute to sponsor and create the first **industry specification to prevent plastic pellet pollution.** The new specification, a so-called Publicly Available Specification (PAS), was formally launched in July 2021 after nine months of preparation by an expert group. We consider the publication of this standard as positive progress which will start to direct corporate behaviour. We intend to use the plastic pellet PAS as a direct reference in engagement with relevant industries, for example in ongoing engagements with packaging companies and plastics manufacturers. Another interesting industry development is businesses and investors, including LGPSC, calling for **UN treaty on plastic pollution** ([plasticpollutiontreaty.org](http://plasticpollutiontreaty.org) – agreement has since been found to negotiate a treaty<sup>10</sup>). The aim of a treaty would be to establish a coordinated international response that aligns businesses and governments behind a shared understanding of the causes of plastic pollution, and a clear approach to addressing them.

<sup>9</sup> Confer with response to Section 4.1.2 above for further detail on LGPS Central Stewardship Themes

<sup>10</sup> On 2 March 2022, Heads of State, Ministers of environment and other representatives from 175 nations endorsed a historic resolution at the UN Environment Assembly (UNEA-5) today in Nairobi to End Plastic Pollution and forge an international legally binding agreement by 2024. The resolution addresses the full lifecycle of plastic, including its production, design and disposal.



### Tax transparency

We have co-signed a letter to the European Parliament supporting **public country-by-country reporting (CBCR)** in the EU coordinated by the PRI<sup>11</sup>. We view it as vital that multinational companies provide disaggregated information on taxes paid in all countries and across operations. **The EU legislation was adopted in November 2021** and will require public reporting of certain information such as revenues, number of employees, profit or loss before tax, tax accrued and paid, accumulated earnings, stated capital and tangible assets. Many multinationals already report revenue, profit and tax paid by territory to tax authorities as part of a requirement under the OECD Base Erosion and Profit Shifting guidelines. These large multinationals therefore already collect CBCR data and could readily report it to stakeholders more broadly. CBCR is crystallising as best practice in tax transparency. The most widely used sustainability reporting framework, the Global Reporting Initiative, has launched a Tax Standard which includes CBCR. This provides companies with a ready-made and consistent format. While only a minority of multinationals currently provide shareholders and other stakeholders with CBCR, those that do view it as an opportunity to “demystify” tax and have expressed to us that it has largely been well received by stakeholders.

### Deforestation given heightened attention during COP26

During COP26 negotiations in Glasgow in November last year, LGPSC alongside 30 financial institutions, made a commitment to tackle agricultural commodity-driven deforestation and help drive the shift towards sustainable production and nature-based climate solutions. **This commitment encourages a focus on active ownership and ongoing stewardship as the principle means to work towards portfolios that are free from forest-risk agricultural commodity-driven deforestation activities**, as part of a global transition towards sustainable production, supply chains and associated investment and financing opportunities. The aim is to achieve “real world” impact in halting some of the most common causes of deforestation and, and will focus on high-risk sectors beef, soy, palm oil, pulp and paper. We are cognisant that the timeframe is tight and will require joint effort among investors to strive for elimination of deforestation caused by sourcing for those agricultural commodities from investment and lending portfolios by 2025. **We continue our policy engagement with the Brazilian government**, and along with lead engagers of the Investor Policy Dialogue on Deforestation (IPDD), have met with federal representatives, state representatives, congress members, and civil society in Brazil. IPDD has also held educational and knowledge sharing sessions, both in and outside of Brazil, and conducted outreach with investor coalitions, foreign representatives, and other relevant stakeholders.

<sup>11</sup> 35 investors representing US\$5.6trn in AUM signed the PRI letter on public CBPCR in the EU



**PRINCIPLE 11** 4.3 Escalation of stewardship activities to influence issuers

The stewardship themes that we have identified as priority areas for engagement are all long-term and systemic in nature. Against that backdrop, we will often use escalation tactics to enhance the chances of achieving long-term engagement outcomes. However, a decision to escalate, and the form or sequence of subsequent escalation will be particular to the engagement in question.

Examples of how we might escalate include, but are not limited to:

- Additional meetings with the management or the directors of an investee company
- Escalating the dialogue from the executive to the board of directors or from one board member to the Chair and/or a more amenable board member
- Collaboration with fellow investors and/or with partnership organisations
- Public statement
- Voting against management, e.g., against the annual report, the appointment of directors or the auditors
- Co-filing shareholder resolutions
- Attendance and raising questions at the company AGM

Through our involvement in collaborative engagement projects, like Climate Action 100+ (CA100+), we are continuously assessing the need for escalation depending on individual companies’ response to expectations from investors. Due to the nature and complexity of the transition challenge, there is also an element of “moving target” which means that both investors and companies need to be ready to step up ambition. Going into 2021, CA100+ had established a Benchmark Framework which allows evaluation of company progress against Paris alignment on key parameters (short/medium/long-term targets, decarbonisation strategy, capex plans, remuneration, disclosures).

**Through our role of co-lead in CA100+ engagement with Glencore,** we have held constructive discussions ahead of their 2021 AGM and encouraged the company to put forward a Climate Transition Plan to shareholders for an advisory vote. While the company still has some gaps relative to the CA100+ Benchmark Framework, we consider that they have taken strong steps toward

Paris alignment. This includes setting absolute GHG emissions reduction targets across all scopes against a net-zero by 2050 ambition, including a medium-term target of 50% reduction by 2035 and a 15% reduction target by 2026, which will largely come from decline in coal exposure. **LGPS would like Glencore to set more ambitious short-term targets, including a specific 2030 target, that marries up with the long-term ambition and ensures a steady decline in emissions in line with Paris over this next, critical decade.** Furthermore, we will continue to push the company to proactively and transparently lobby for Paris-aligned climate policies in key markets, including Australia, both directly and through industry associations they are a member of. Positive advocacy is a material action that Glencore can take in support of its own decarbonisation commitments and to drive demand in minerals segments, such as copper, cobalt, nickel, zinc, silver and vanadium which they want to grow.

**Engagement with banks**

Together with more than 100 investors and coordinated by ShareAction, LGPSC co-signed letters to **68 banks** setting out expectations for Paris-alignment and protection and restoration of biodiversity. **Banks play a critical role in provision of finance to support transition to a low-carbon economy.** While we have previously asked banks to set targets in line with Paris, this letter specifically addresses biodiversity, alongside climate, as an area that banks are expected to assess in their risk management and in their dialogue with clients. We consider that asking banks to include biodiversity in their broader climate mitigation effort, is in and of itself a form of escalation. **Encouragingly, 45 banks have responded to the letter and dialogue is ongoing with a selection of these banks.** Our first ask is for banks to publish climate targets covering all relevant financial services that are aligned with global efforts to hold temperature rise below 1.5 degrees Celsius. **19 confirmed they will publish new climate targets ahead of COP26, the end of the year, and/or their 2022 AGM.** This includes BBVA, BNP Paribas, Citigroup, and Standard Chartered. A critical next step for the investor group is to assess whether these targets put banks on a clear path to net zero.

## Escalation of engagement with Motorola

We expect businesses that operate in areas of war and conflict to take particular care to respect human rights. The Israeli-Palestinian conflict poses clear human rights risks for companies, but the sensitive political situation makes engagement challenging. During 2020 we initiated engagement with Motorola Solutions Inc. on human rights risks in operations through the wholly owned subsidiary Motorola Solutions Israel Ltd. We sought this engagement to bolster ongoing engagement that the Local Authority Pension Fund Forum (LAPFF) is undertaking with a selection of companies on human rights risks that stem from operating in Occupied Palestinian Territories (OPT). In our initial letter, **we asked that the company carry out human rights impact assessments in line with the UN Guiding Principles on Business and Human Rights.** We also stated that we would take the company's response into account as we formulate voting decisions at the next AGM. The initial response from Motorola did not provide us with enough detail to understand how the company

manages and mitigates human rights risks that are specific to operations in the OPT. Hence, we voted against the Chair at the 2021 AGM to send a clear message that the initial response had been unsatisfactory. We also followed up with further letters, the latest signed by our CIO, to explain why this remains a concern and emphasising our willingness to engage. We were pleased when the company agreed to meet and discuss these issues, **a meeting that took place in January 2022, and we will continue this engagement with the company.**

## Expectations on external managers to escalate on our behalf

We expect managers to be ready to escalate any engagement where there is lack of progress relative to engagement objectives, on any material ESG topic. During 2021, we have asked managers to give particular attention to companies' climate transition, or lack thereof, in line with the Paris Accord. This is part of a broader discussion with external managers around the implementation of our net zero targets.

### US utility company, Schroders, LGPSC Global Equity Active Multi Manager Fund

**OBJECTIVE:**

For company to set a clear decarbonisation strategy

**ESG TOPICS ADDRESSED:**

Climate change

**ISSUE/ REASON FOR ENGAGEMENT:**

The company does not have an overarching net zero commitment or quantitative targets to reduce emissions.

**SCOPE AND PROCESS/ ACTION TAKEN:**

Schroders engaged with the company in September 2021, with an expectations letter to the company's chair requesting a commitment to achieve net zero emissions by 2050 or sooner, alongside short-, medium-, and long-term targets aligned to a 1.5°C scenario.

**ESCALATION:**

Following the initial letter, Schroders sent a tailored letter to the CEO of the utility and followed this up with a one-to-one call with Investor Relations.

**OUTCOMES AND NEXT STEPS:**

The company has been receptive to Schroder's requests, making valid points about the importance of having shorter term targets that the current management team can be held to, rather than long-term targets which have to be achieved by future teams. Schroders agree with this, but don't believe this prevents the company having a long-term target. In 2022 if the company fails to announce 2030 and/or 2050 targets, Schroders will re-engage.

### European Bank, Fidelity, LGPSC Global Active Investment Grade Corporate Bond Multi Manager Fund

**OBJECTIVE:**

Improved financial product safety

**SECTOR:**

Financials

**ESG TOPICS ADDRESSED:**

Strategy

**ISSUE/ REASON FOR ENGAGEMENT:**

Fidelity's ESG rating for the bank highlighted the bank's weak financial product safety efforts which can be a financially material issue for banks.

**SCOPE AND PROCESS/ ACTION TAKEN:**

Fidelity's ESG analyst initially raised this issue with the bank in an engagement meeting.

**ESCALATION:**

Fidelity had a second specific meeting on this topic in which their analyst was joined by a portfolio manager alongside the Bank's Head of Compliance and Group AMLO and Head of Advisory and Solutions. Fidelity highlighted that the bank's reporting could be improved.

**OUTCOMES AND NEXT STEPS:**

After the meeting, Fidelity received more information and became more comfortable with this risk.

# 05 Exercise of rights and responsibilities

PRINCIPLE  
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It remains critical to LGPSC that we utilise all levers to influence corporate behaviour across our equity and fixed income investments. Voting is a core part of our overall Stewardship effort as a shareholder (see sections 5.1 – 5.3 below). Equally, exercising rights and responsibilities as bond holders is of key importance (see section 5.4 below). During 2021, we have increased our exposure to private markets. We have worked with private market partners to identify key performance indicators that are relevant for the underlying asset, and which we would request reporting against (see section 5.5 below).

## 5.1 Voting approach and objectives

### High-level objectives:

LGPSC views voting as a core component of our Stewardship efforts. In a long-term perspective, all voting activities we undertake aim to:

- 1) support the long-term economic interests of our stakeholders
- 2) ensure boards of directors are accountable to shareholders
- 3) encourage sustainable market behaviour across companies and sectors

### Principles-based approach:

We take a principles-based approach to voting and are guided by LGPSC's established Voting Principles.

At high level, we expect companies to:

- Adhere to essential standards of good governance for board composition and oversight
- Be transparent in their communication with shareholders
- Remunerate executives fairly
- Protect shareholder rights and align interests with shareholders
- Promote sustainable business practices and consider the interests of other stakeholders

In situations where companies are faced with a market-wide crisis that cause unprecedented disruption, uncertainty and challenges to their business models, operations, workforce and finances – such as the Coronavirus pandemic – we will consider applying a more flexible voting approach. We would in these situations explain to our Partner Funds and other stakeholders, including external managers, how we may deviate from our Voting Principles, on what issues and relative to which sectors (if different sectors are affected differently).

### Scope of voting:

To send a unique voting signal to investee companies LGPSC votes all its shares - whether externally or internally managed - according to one set of Voting Principles. While the ultimate voting decision rests with LGPSC, we have a procedure through which we capture intelligence and recommendations from external fund managers.

### Stock-lending:

LGPSC has an active securities lending programme. During 2021, we considered options for restriction on securities lending to bolster our overall stewardship and voting impact. The securities

lending policy that has been in place since inception of LGPSC ensures that we hold some securities back, a portion not on loan, to ensure that we can vote at all AGMs of investee companies. We also have the option of recalling securities out on loan e.g., in the case of filing a shareholder proposal. Based on dialogue with our Partner Funds, alongside discussions in-house at Investment Committee and Operations, Risk, Compliance and Administration, **we have now revised the securities lending policy with effect from 2022.** The revision means that we fully restrict certain securities from lending at the start of voting season. This is to ensure that we maximise our voting impact, e.g., in relation to critical, ongoing engagements that we expect to escalate through shareholder resolutions or other forms of voting (e.g., votes against Board members). Among critical engagements are companies identified as high risk relative to climate change through Partner Fund Climate Risk Reports and that sit within the scope of Climate Action 100+. We considered the cost implications of excluding all companies in our Voting Watch List from lending and concluded that a more targeted approach would be the most proportionate and efficient response. **This targeted approach entails a restriction of lending on a sub-set of companies that we view as critical engagements ahead of each voting season.** Ahead of voting season 2022, 12 companies on our Voting Watch List (of 50 companies) are restricted from lending. The restriction will be lifted once relevant AGMs are held. This change guarantees that we are able to vote all the shares we hold for certain companies in the portfolio.

### Voting reinforcing engagement:

As far as possible, we aim to use voting to reinforce and promote ongoing engagements, whether carried out directly through LGPSC, through collaborative initiatives or through our external stewardship provider EOS at Federated Hermes. This means that we regularly raise issues concerning environmental sustainability, including climate change, and broader social issue like human rights risk oversight and management through our voting. Many votes against management concern good governance (board composition, board oversight and skill sets, remuneration etc.) – these votes are often an expression of underlying concerns with lack of expertise and or/oversight at board level on issues like climate change or human rights. We also know that strong governance increases the likelihood of companies dealing well with environmental and social risks. During April – June 2021

(high voting season) many ESG-related shareholder proposals got very strong or even majority support.

### Transparency:

LGPSC's disclosure of its Voting Principles, and its voting outcomes, supports the Company's ambition of full transparency. With regards to voting outcomes, disclosures are made in three formats. Firstly, a report summarising our voting activities is

provided in [Stewardship Updates](#) three times a year (covering the first three quarters of the calendar year). Secondly, we provide an annual summary of our voting activities, as part of the Annual Stewardship Report, and thirdly, we disclose our voting decision for every resolution at every eligible company meeting via an [online portal](#). Each of these disclosures is available to the public.

## 5.2 Voting strategy

### Ensuring that Voting Principles are applied:

We have set up a structure whereby EOS at Federated Hermes provides us with voting recommendations based on our Voting Principles which are input on the ISS voting platform prior to the vote deadline. The voting recommendations are then cast as voting instructions if there is no further intervention, except in the case of share-blocking votes. We currently hold approximately 2,900 companies through our ACS equities funds. With this voting structure, we have confidence that votes are cast according to LGPSC Voting Principles across a voting universe that under no circumstance could be checked manually at each individual company level. In minority cases where a company we are engaging and/or that the Local Authority Pension Fund Forum has issued a voting alert for falls outside EOS' main engagement, we often consult ISS research directly.

### Voting Watch List:

It is not feasible to do in-depth research into all proxies that will be voted at each of the companies we hold through our ACS equity funds. To prioritise, we establish a "Voting Watch List" annually that consists of approximately 50 companies which cover larger holdings and/or core engagements in and outside of Stewardship Themes. Votes at these companies will be given particular scrutiny ahead of the AGM. While it is not feasible to attend all these companies' AGMs, we would aim to attend AGMs virtually (if permissible) for core Climate Action 100+ engagements and for any company with which we have filed a shareholder resolution. Watch List companies are a combination of larger holdings across our equity universe and/or core engagement companies and/or ongoing controversies. The Voting Watch List serves a further purpose, in allowing us to test whether our votes are generally cast in alignment with our Voting Principles.

### Interaction with EOS at Federated Hermes:

Ahead of each voting season, we share our Voting Watch List with EOS to ensure that we receive a more detailed analysis to substantiate their voting recommendations for companies on this list ahead of relevant AGMs. We will seek ad-hoc interactions/meetings with EOS regarding core engagements, where either they or we would like further input from the other ahead of a vote.

As an example, we had in-depth discussions with EOS ahead of the vote at **Barclays AGM 2021** on a climate-related shareholder proposal. The resolution requested the company to set short-, medium and long-term emissions reduction targets and to phase out the provision of financial services to fossil fuel projects and companies, in timeframes consistent with the Paris Agreement. LGPSC has engaged Barclays actively through a ShareAction-led collaboration during 2020 centred around the asks in a shareholder proposal which we co-filed in January 2020. The January 2020 shareholder proposal makes explicit reference to phasing out of finance to *non-Paris aligned* energy and utility companies. Dialogue has been constructive, and the company seems receptive to and appreciative of investor input and dialogue.

The bank has made progress in developing its climate strategy, putting forward a new methodology for determining alignment with the goals of the Paris Agreement for the energy and power sectors, including relevant 2025 targets. It has also accepted the principle of the need to withdraw finance from misaligned activities over time (for example in its current coal policy).

While we fully support the underlying sentiment of the 2021 shareholder proposal in terms of Paris alignment, we asked ourselves what would at this point be more conducive to engagement and to further progress? After careful consideration we found that the 2021 resolution was premature in light of very recent progress made by the company and the prospect of ongoing engagement. We were also concerned about the wording of the resolution which could be interpreted to mean that certain projects and companies from the outset are not considered to be in line with Paris. As such, it appeared to be missing nuance around the potential and ability for transition also within the fossil fuel sector, which is both complex and dynamic.

Looking to the 2022 AGM, we will carefully consider Barclays' climate transition plan, in particular their coal policy and commitments to phase out from thermal coal mining and whether these support a 1.5C trajectory in line with Paris.



### Interaction with external managers:

It is our intention to capture intelligence and recommendations from active equity fund managers relative to key holdings and/or contentious voting issues, as well as influence managers' wider voting on key issues like climate risk management:

- LGPSC meets with each external manager annually ahead of the voting season for a dedicated voting-related discussion.
- External Managers will be kept up to date on any changes to LGPSC Voting Principles, and vice-versa.
- We will share with each external manager our Voting Watch List with an explicit incentive to communicate their views on companies on this list that are held in their portfolio.
- The RI&E Team may reach out on an ad-hoc basis in cases where we would like to elicit views on contentious issues in core holdings or key engagements that can supplement views from EOS.

As an example, we had detailed discussions with one of our external managers ahead of the vote at **Berkshire Hathaway** on a **shareholder proposal requesting that the company report on its management of physical and transitional climate-related risks and opportunities**. We consider that reporting on climate related risks and opportunities is a critical first step for the company to manage these risks and allowing shareholders the ability to assess whether it does so effectively. **60% voted in favour of the proposal, adjusted for non-insiders**. Berkshire Hathaway is the second largest power company in the US without a net-zero goal and we note that the company achieves the lowest score on TPI's climate risk management ladder. We considered arguments made by our external manager to vote against the resolution, although ultimately the decision rests with us. These included the fact that Berkshire's autonomous subsidiaries already report on operational risk, including climate risk, which makes a centralised report less appropriate. Furthermore, that the reporting from subsidiaries make it possible to assess climate risk exposure for Berkshire Hathaway.

In our view, the current reporting at subsidiary level is not decision useful nor sufficiently complete for investors to fully appraise material climate-related risks. It is concerning that the company's board believe such disclosure to be unnecessary for investor interest. Shareholder interest lies with the parent company, not individual subsidiaries. **We think it appropriate to ask this of a holding company like Berkshire Hathaway, which is a situation akin to asset owners and asset managers reporting on climate risks throughout their portfolios**. While in this case, we did not see eye-to-eye with the manager in question, we will continue dialogue on amongst others climate-related votes which are only increasing in importance against LGPSC's newly announced net-zero ambition.

## 5.3 Voting highlights and outcomes 2021

### Proportion of shares voted during 2021

Based on our voting set-up with EOS at Federated Hermes – whereby EOS’ voting recommendations (aligned with LGPSC Voting Principles) are cast as voting instructions for all shares – we can ensure that all shares are indeed voted. There are occasions where a vote is not cast due to for instance share blocking or a non-standard voting procedure. However, these are very limited instances. Based on checks done by EOS on unvoted ballots due to an error (e.g., a missed deadline in an instance of share blocking) during voting seasons 2013 – 2021, the % of errors lie between 0.591% and 0.04% of votes not being cast. We consider this an acceptable level of error, and we also note the downward trend in terms of errors.

### 5.3.1 Voting highlights

While the health pandemic understandably took centre stage in 2020 and to a degree overshadowed the climate crisis, the latter clearly came to the fore in 2021. The 2021 voting season saw a new development in climate transparency and dialogue with shareholders through 18 votes on climate transition across oil and gas, construction, aviation and consumer goods. All of these passed with support ranging from 88% to 99%. Some plans met notable opposition, including Shell and BHP, and we expect investors to scrutinise these plans at a more detailed level against evolving climate risk management standards such as the Climate Action 100+ Benchmark assessment over the next years.

#### 2021 Voting Statistics

- Voted at 3,344 meetings
- 40,288 resolutions
- Attended virtual AGM of Glencore
- EOS attended 66 AGMs on our behalf, including Deutsche Bank, BP, Google owner Alphabet, Novartis, Amazon and Facebook
- Voted against management for one or more resolutions at 58.6% of meetings

### Tippling point for investor engagement and voting on climate change

- 18 votes on climate transition across oil and gas, construction, aviation and consumer goods – all passed with support ranging from 88% to 99%.
- Shell’s transition plan was opposed by a notable number of shareholders (ca. 12%), including LGPSC, while a shareholder proposal asking the company to set and publish targets for GHG emissions reduction in line with Paris received a healthy 30% support.
- We supported a shareholder resolution at Chevron requiring

Scope 3 targets which gained 61% support.

- LGPSC supported minority shareholders in proxy battle at Exxon resulting in three climate-savvy directors appointed to Exxon’s board against management advice.
- We supported a shareholder proposal at Berkshire Hathaway on management of physical and transitional climate-related risks and opportunities. Company is the largest power company without a net-zero goal. 60% voted in favour of the proposal (adjusted for non-insiders).

### Diversity and inclusion higher up the agenda

- We opposed FTSE 100 chairs in the UK at five meetings for failing to meet minimum expectations for racial diversity on boards.
- We opposed the directors responsible (typically the board chair) at companies that fell below our expectation on UK FTSE 100 companies to have at least one woman on the executive committee. Examples include Ocado, Imperial Brands and Glencore.
- In the US, we opposed 39% of nominating committee chairs, including at Kinder Morgan, Thermo Fisher Scientific and Discovery against an expectation that women and ethnic minorities make up at least 40% of the board at large companies.
- Lack of progress on gender diversity in China, Hong Kong and Taiwan.
- Japanese companies express support for the concept of board gender diversity, but this has not translated to more women on boards.

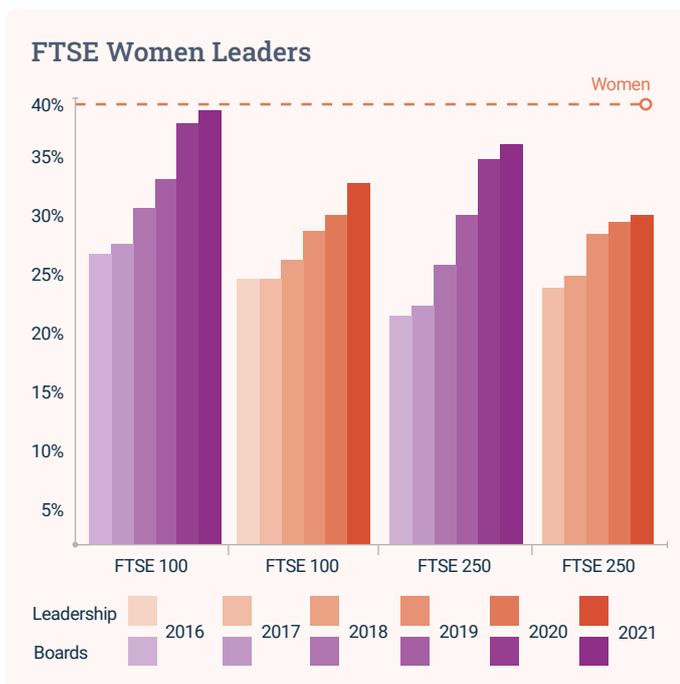
### Remuneration during the pandemic

- Executive pay should be justified in the context of the experience of other stakeholders, particularly companies that had made redundancies, benefited from government support, or otherwise in distress.
- Some good practices among UK companies repaying money received from the government to furlough employees and/or business rates relief. Generally accepted that companies not able to do so would not pay bonuses to executives.
- At publisher Informa, we opposed the rem report (alongside 62% of investors), considering pay-outs to executives from a long-term incentive scheme that would have lapsed, in the face of significant negative impact from Covid-19.
- We opposed 80% of “say-on-pay” proposals in the US. Our concerns were exacerbated by decisions to insulate executives from the impacts of Covid-19, relative to other stakeholders.
- Rio Tinto suffered 60% opposition to the rem report due to heavy focus on shareholder returns, with limited consideration of other strategic stakeholders, and pay-outs to departing executives, which did not reflect Juukan Gorge failures.



### 5.3.2 Voting outcomes

In the UK, where the Hampton-Alexander Review established 2020 targets for 33% female representation on boards and in leadership roles, we have consistently opposed director proposals over concerns about insufficient diversity, including gender diversity, at board level and below. In 2021, we opposed 37 proposals due to lack of diversity, versus 35 and 45 proposals in 2020 and 2019, respectively. While the progress detailed in the latest FTSE Women Leaders Review released in February 2022 is encouraging, we agree with the report’s notion that more work still needs to be done to achieve gender balance in leadership teams. As such we will monitor companies with a view to opposing director proposals at offending companies.



Source: FTSE Women Leaders Review, February 2022 (FTSE Women Leaders - February 2022)

#### CASE STUDY

### AVEVA Group Plc

#### THEME:

Board gender diversity

#### OBJECTIVE:

We believe the most effective boards include a diversity of skills, experiences and perspectives. Through our voting decisions (and otherwise) we support the Davies Review, the Hampton-Alexander Review and the Parker Review.

#### PROCESS:

EOS at Federated Hermes, on our behalf informed the company of our intention to vote against the re-election of the chair of the board who is also the nominations committee chair due to insufficient gender diversity on the board. As per our voting principles, we expect FTSE 100 and 250 companies to have at least 33% women on their Boards and will consider voting against the Chair of companies with materially less female representation unless there are clear and justifiable reasons why 33% is not achievable in an interim period.

#### ESCALATION THROUGH VOTING:

During the 2021 annual general meeting, LGPSC voted against Chair Philip Aiken when the company failed to respond to our concerns.

#### OUTCOME:

The company has since appointed two female directors to its board in 2021. The two appointments lift the company above the gender diversity guideline threshold.



**CASE STUDY**

**TotalEnergies SE**

**THEME:**  
Climate change

**OBJECTIVE:**  
We expect companies to consider relevant, material social and environmental risk factors in their long-term strategic business planning. We will consider voting against the Chair, and other relevant directors or resolutions, at companies where we consider a company’s response to the risks and opportunities presented by climate change to be materially misaligned with the goals of the Paris Accord.

**PROCESS:**  
EOS at Federated Hermes, on our behalf, has co-led engagement efforts with TotalEnergies SE as part of the Climate Action 100+ initiative since 2017. Throughout its tenure as co-lead, EOS has corresponded with TotalEnergies on issues including investor expectations on scope 1, 2 and 3 greenhouse gas emissions reduction, Paris-aligned accounting, and TotalEnergies’s energy transition plan.

**ESCALATION THROUGH VOTING:**  
During the 2021 annual general meeting, LGPSC voted against TotalEnergies energy transition plan due to the lack of alignment with Paris Agreement goals, while being clear in a letter to the company that engagements should continue.

**OUTCOME:**  
In December 2021 TotalEnergies indicated that the company would enhance its disclosure in its next sustainability and climate report including publishing a short-term target for Scope 3 emissions which will entail a 10% reduction of the average carbon intensity of its energy products.

**NEXT STEPS:**  
Monitor implementation of energy transition plan and sustainability disclosures. Engage with company to get commitment on three-year say on climate votes.



**CASE STUDY**

**Amazon.com, Inc**

**THEME:**  
Executive remuneration

**OBJECTIVE:**  
To encourage company to align executive remuneration with long-term performance through the cycle. Incentive schemes should be transparent, understandable, long-term and appropriate to the circumstances and strategy of the company. In order to achieve alignment with shareholders, executives should make a material, long-term investment in company shares and these shares should be subject to a suitable holding period following an executive’s departure. Companies should disclose the time by which new executives should reach the target level share ownership.

**PROCESS:**  
In 2018, EOS, on our behalf, informed the company on its recommendation to vote against the say-on-pay proposal due to the lack of or poor disclosure of explicit share ownership requirements. In 2020, the company acknowledged that it should disclose policies on share ownership requirements.

**ESCALATION THROUGH VOTING:**  
During the 2021 annual general meeting, LGPSC voted against Amazon’s say-on-pay proposal due to the lack of pledging policy, clawback policy, and minimum share ownership requirement.

**OUTCOME:**  
The company has instituted a ban on executives being able to make hedging transactions against share-based-equity awards and implemented a clawback policy. We continue to monitor the company for updates relating to share ownership requirement.



**CASE STUDY**

**DuPont de Nemours, Inc. (DuPont)**

**THEME:**

Plastic

**OBJECTIVE:**

Plastics pollution is one of LGPSC’s Stewardship Themes and we leverage collaboration opportunities to deliver progress in the subject. Voting is engagement led, and we will consider co-filing or supporting shareholder resolutions that relate to better risk management (reduce plastic use, reduce plastic waste, increase recycling, invest in relevant R&D).

**PROCESS:**

EOS Hermes on our behalf engaged DuPont on sustainability issues including plastics. We thanked DuPont for producing a 10-year sustainability roadmap with scope 1 and 2 targets in 2020. We reiterated the need for transparency and alignment with Paris Accord. Prior to the 2021 annual general meeting, EOS communicated our intention to support a shareholder proposal asking the company to issue a report on plastic pollution. We believe the company is lagging its peers who have committed to disclosing this information and currently the company produces no metrics on plastic pellet spills and the report will improve disclosure on how the company is mitigating plastic pollution related risks.

**ESCALATION THROUGH VOTING:**

During the 2021 annual general meeting, LGPSC voted for the shareholder proposal requesting the company to publish an annual report on plastic pollution.

**OUTCOME:**

In September 2021, DuPont announced that it has become a member of Operation Clean Sweep® Blue, a campaign dedicated to helping every plastic resin handling operation achieve zero plastic resin loss. OCS blue enhances the commitment to management, measurement, and reporting of unrecovered plastic releases into the environment from resin handling facilities. The company reported that there have been no releases in the third quarter 2021.

**5.4 Fixed income – exercise of rights and responsibilities**

We expect all our Fixed Income managers to fully exercise their rights and responsibilities. We provide below an example of how our external managers approach this.

Neuberger Berman, a manager in our Corporate Bond Fund, engages with capital markets participants in respect to new issue documentation and pushes back on weaknesses identified in the documentation, when possible. Neuberger Berman believes engagement with management teams is also critical in identifying material ESG factors as credit documentation generally provides a range of flexibility to an issuer in respect to capital allocation and business strategy.

For example, Neuberger Berman recently identified an issuer in which credit documentation flexibility, coupled with governance concerns at the issuer’s parent, led to weakness in the issuer’s trading levels due to market concern the equity owners would extract value from the issuer. Based on Neuberger Berman’s ongoing engagement with the management team and the company’s commitment to conservative capital allocation policies and a strong ratings profile, they encouraged the issuer to proactively strengthen the credit documentation in its indentures to alleviate market concerns. The issuer ultimately enhanced structural bondholder protections and its governance framework, which was a positive development for the issuer’s credit profile.





## 5.5 Private markets

When one of our primary managers took a controlling stake in a **genealogy and gene testing business**, questions were raised in the media around **data protection and information security risk**. Questions around the evolution of the investee companies' business model and the potential monetisation of the company's DNA database were also raised. In recognition of the potential risks and sensitivities associated with the transaction, the RI&E Team at LGPSC worked with colleagues in the Private Equity Team to engage with the manager to raise these concerns. The manager recognised the significance of data privacy to the investee company and provided assurance around the capabilities of their own data team outlining the extensive involvement of the team in the deal from the outset. It was clear that due consideration was given to key regulations such as GDPR. Assurances were also given that the company's commitment to transparency and disclosure around data processing would remain post-acquisition and that policies and procedures would remain best in class. Through this engagement, LGPSC was able to establish that the specific risks raised were managed appropriately thus mitigating the risk of litigation and reputational damage.

An allegation was made by a US capital management company that the CEO of a **diversified environmental services company** (held by LGPSC through a co-investment vehicle) had **connections to organised crime**. This raised significant concerns around the leadership and governance of the company, particularly as the CEO was a founder of the company. The LGPSC Private Equity Team raised the issue with the primary manager who refuted the allegations robustly pointing to the extensive due diligence undertaken by themselves and other investors during the deal process. A number of other sources of information were also referenced including broker research. Credible question marks were also raised around the motivation of the capital manager who raised the allegations.

Through this interaction with our co-investment manager, LGPSC was able to get comfort that these allegations posed no risk to the value of our investment, nor did they raise concerns around culture and governance. We remain confident that the company is able to execute its strategy and continue to provide critical sustainable environmental solutions to its clients.

One of our primary managers notified us of an issue with a potential co-investment opportunity in a **medical supplies company**. The company had found **evidence of forced labour issues in the supply chain of one of their largest medical glove suppliers**. Issues that had come to the attention of US Border Protection authorities. We took comfort that the manager notified us of the issue. However, we still challenged them hard on their due diligence and their efforts to ensure that the company addressed the issue as a matter of urgency. We communicated to the manager that we have a zero-tolerance for forced labour issues regardless of the jurisdiction in which they arise.

We consider that supply chain disruption can be a material risk for corporations and can cause reputational damage that is hard to quantify and difficult to rectify. In this case regulatory censure was also a potential issue.

Therefore, by pursuing the matter to a satisfactory conclusion we were acting in the best financial interests of our beneficiaries as well as acting as a responsible steward on their behalf.

Following an article in the Financial Times, the Private Markets Team at LGPSC raised concerns about one of our Primary managers handling of an **alleged harassment case involving a leading media and technology company** which was a subsidiary of a conglomerate they held a significant stake in. While LGPSC is not a direct investor in the media and technology company, we were concerned about the implications of the case in terms of the Primary managers' handling of ESG issues more broadly. Following discussions with the manager we recognised their role on the supervisory board of the parent company afforded them limited involvement in the direct handling of the case beyond the appointment of an independent law firm to investigate.

We took comfort that once the true nature of events was understood, swift action was taken to remove the member of staff involved and to implement a programme of cultural change within the firm which included diversity training. We provided robust challenge but concluded that the manager acted appropriately in the circumstances and that they took the issue very seriously. Our understanding of the company's approach to ESG matters gleaned during the initial due diligence process was ultimately reinforced. We concluded that the rating applied to the manager during the initial due diligence process in terms of their ESG capabilities remained valid.

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All information is prepared as of **25 April 2022**.

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