Non-Executive Report of the: **Pensions Committee** 22 September 2020	TOWER HAMLETS
Report of Neville Murton, Corporate Director, Resources	**Classification:** Unrestricted
Responsible Investment and RI Accreditations	

Originating Officer(s)	Miriam Adams, Pensions & Investments Manager
Wards affected	All wards

SUMMARY

At the meeting of the Scheme Advisory Board (SAB) on the 6th November, approval was given for the first part of guidance on responsible investment to be published for consultation until the 11th January 2020 (Appendix A).

The aim of this first part of Responsible Investment (RI) guidance is to assist and help investment decision makers to identify the parameters of operation within scheme regulations, statutory guidance, fiduciary duty and the general public law and the scope for integrating ESG policies as part of investment strategy statements.

The SAB was clear that the extent to which ESG policies must be adopted by a scheme clearly remain a matter for local consideration and agreement in accordance with MHCLG's statutory guidance.

This paper considers the Responsible Investment Accreditations available to the Fund as part of its role as a Responsible Investor.

RECOMMENDATIONS

The Pensions Committee is recommended to:

1. Note the contents of this report;
2. Note the Scheme Advisory Board Guidance (Appendix A);
3. Consider the accreditation options presented in this paper;
4. Agree that officers investigate further the UNPRI and TCFD accreditations;
5. Note resource requirement for processing accreditation applications; and
6. Note the Responsible Investment course run by the UNPRI

1. REASONS FOR THE DECISION

1.1 This report considers the recommendations of the Local government Scheme Advisory Board (SAB) in England and Wales to assist administering authorities and those individuals delegated to make investment decision on behalf of the authority.

1.2 Responsible investment (RI) established by United Nations in 2006, is an approach to investing that aims to incorporate environmental, social and governance (ESG) factors into investment decisions to better manage risk and generate sustainable long-term returns.

1.3 The report also considers various Responsible Investment Accreditations. Involvement of the Fund with the initiatives should bring reputational benefits if communicated properly. However as with most initiatives, the level of benefits will depend on how much direct involvement with the initiatives the Fund has and their alignment with the Fund's own objectives. It should be noted that the drawbacks are costs as applicable as well as additional governance and officers time.

2. DETAILS OF REPORT

2.1 At the meeting of the Scheme Advisory Board on the 6th November, approval was given for the first part of guidance on responsible investment to be published for consultation until the 11th January 2020 (Appendix A). The aim of this first part of RI guidance is to assist and help investment decision makers to identify the parameters of operation within scheme regulations, statutory guidance, fiduciary duty and the general public law and the scope for integrating ESG policies as part of investment strategy statements. The Board was clear that the extent to which ESG policies must be adopted by a scheme clearly remain a matter for local consideration and agreement in accordance with MHCLG's statutory guidance.

2.2 Following its consultation for part 2 of the guidance, some respondents raised concerns around the issue of fiduciary duty in the context of the LGPS role and responsibilities of elected members responsible for making investment decisions. More so in relation to the recent case in the Supreme Court involving the Palestine Solidarity Campaign and MHCLG that could shed some light on how the fiduciary duty test applies to investment decision makers in the LGPS.

2.3 More recently, the government has introduced amendments to the Pension Schemes Bill which potentially could have a significant impact on the way in which investment strategy statements are prepared on issues like ESG and climate change.

For these reasons, the SAB has taken a view not to offer any definitive advice or guidance on how the fiduciary duty test applies to investment decision makers in the LGPS. The Board has therefore decided to take stock until it has had the opportunity to evaluate the judgement handed down by the Supreme Court and when more is known about the government's position on the proposed climate change provisions in the Pension Schemes Bill.

2.4 Notwithstanding this decision, the Board is mindful that there are matters outside of fiduciary duty where advice and information would continue to be helpful. The Board has therefore decided to restructure the proposed guidance to explain and clarify the terminology associated with responsible investment and provide investment decision makers with a range of information, case studies and tools to help them meet the challenges associated with responsible investment. The revised document will be circulated to the Committee once received.

2.5 In recent years, Regulatory and industry initiatives have been improving market mechanism in ESG. Initiatives are generally categorised as regulatory or industry related. Examples of Regulatory initiatives in the LGPS are LGPS Regulations 2016 and UK Stewardship Code. While industry initiatives either fall under international organisations (like UNPRI, UN Sustainable Development Goals and Green Bond Principles). While corporate disclosure standards include Task force for Climate related Financial Disclosures (TCFD), Carbon Disclosure Project and Sustainability Accounting Standards Board.

3. United Nations Principle for Responsible Investment (UN PRI)

3.1 This is a network of investors working together to understand the investment implications of ESG factors and to support each other to incorporate ESG into investment and ownership decisions.

3.2 The PRI defines responsible investment as a strategy and practice to incorporate environmental, social and governance (ESG) factors in investment decisions and active ownership.

Approaches are typically a combination of two overarching areas:

a.) Considering ESG issues when building a portfolio (ESG incorporation) using approaches like integration, screening and thematic

b.) Improving investees performance (active ownership or stewardship) by encouraging companies Trustees invest in to develop more sustainable business practices through engagement and proxy voting.

3.3 There are 6 principles investors should sign up to. These are voluntary and act as a guide or menu for possible actions for incorporating ESG issues into investment practice.

- Principle 1: We will incorporate ESG issues into investment analysis and decision-making processes.
- Principle 2: be active owners and incorporate ESG issues into their ownership policies and practices.
- Principle 3: We will seek appropriate disclosure on ESG issues by the entities in which we invest.
- Principle 4: We will promote acceptance and implementation of the principles within the investment industry
- Principle5: We will work together to enhance our effectiveness in implementing the Principles.
- Principle 6: We will each report on our activities and progress towards implementing the Principles.

3.4 Membership entails annual membership fee and annual public reporting through the Reporting Framework. There are three requirements for prospective signatories to comply with before registration:

- Investment policy that covers the Fund's responsible investment approach, covering greater than 50%
- Internal/external staff responsible for implementing RI policy
- Senior level/Trustee commitment and accountability mechanisms for RI implementation.

Signatories that do not meet the criteria will be informed privately and delisting will only be a last resort following unsuccessful engagement over the two-year period.

3.5 Responsible Investment certification for Trustees. This course outlines why responsible investment is important for Trustee and board members. It covers areas like setting out a process for establishing organisational purpose and values, investment beliefs and how to get the best out of your investment consultants and managers to support the Fund's approach to RI. There is no exam at the end of the course.

4. UK Stewardship Code 2020

4.1 This broadly covers ESG via governance. In November the Committee considered the UK Code. This is mandatory for the Fund to comply with. It takes a broader, more comprehensive approach than previous iterations, which largely focused on voting and engagement activity with respect to equity assets.

4.2 The latest code defines stewardship as "the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society." Further, the new code requires investors to explain how they are exercising their stewardship duties across asset classes.

4.3 It is free to join and annual reporting requirements with a focus on outcomes.

4.4 The Investment Strategy Statement Guidance notes that LGPS Funds are expected to be signatories to the UK Stewardship Code already.

5. CLIMATE ACTION 100 +

5.1 Climate Action 100+ is an investor engagement focused initiative launched in 2017 to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change. It is free to support however participation in engagements with company executives and board members is expected while engagements are taken by a lead investor working in a group of collaborating investors. Within the LGPS this role is widely undertaken by the LAPFF.

6. TASK FORCE ON CLIMATE – RELATED FINANCIAL DISCLOSURE FRAMEWORK (TCFD)

6.1 This is generally Climate specific with its main aim to create consistent climate-related financial risks disclosures for use by companies and asset owners. Through their asset owner specific recommendation, the TCFD offers a framework from governance to risk management for asset owners to think about how climate crisis will impact their investments and how those effects can be managed. Recommendations will consider the physical, liability and transition risks associated with climate change and what constitutes effective financial disclosures across.

6.2 it is free to support, while recommendations lay out annual disclosures which are fully voluntary and in line with the framework which are centred around four pillars namely governance, strategy, risk management, metrics and target as well as scenario analysis.

6.3 The general conception is that TCFD is likely to become mandatory as the UK Green Finance Strategy specifically mentions the intention of this task force to become mandatory for large Asset Owners by 2022. In addition, the Fund's investment adviser Mercer are a supporter of their views.

7. COMMENTS OF THE CHIEF FINANCE OFFICER

7.1 Although most accreditations are free to join, there are indirect financial costs associated to resourcing and officers time required to maintain the memberships and annual reporting.

8. LEGAL COMMENTS

8.1 One of the functions of the Pensions Committee is to meet the Council's duties in respect of responsible investment matters. It is appropriate having regard to these matters, for the Committee to receive information about new guidance to ensure the Fund is being managed in accordance with the Council's statutory obligations. There are no immediate legal implications arising from the report.

9. ONE TOWER HAMLETS CONSIDERATIONS

9.1 The employer's contribution is a significant element of the Council's budget and consequently any improvement in investment performance will reduce the contribution and increase the funds available for other corporate priorities.

10. BEST VALUE (BV) IMPLICATIONS

10.1 The Pension Fund accounts demonstrate the financial stewardship of the scheme members and employers' assets.

11. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

11.1 Being a Responsible Investor has direct Sustainable Action for a Greener Environment.

12. RISK MANAGEMENT IMPLICATIONS

12.1 Any form of investment inevitably involves a degree of risk. The rigorous robust management of LBTH Pension Fund results in better performance ad reduction in the contribution required from the Council towards the Fund.

12.2 To minimise risk, the Pensions Committee attempts to achieve a diversified portfolio.

13. CRIME AND DISORDER REDUCTION IMPLICATIONS

13.1 There are no crime and disorder reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report

- None

Appendices

Appendix 1 - Scheme Advisory Board Guidance – Responsible Investment in the Local Government Pension Scheme A Guide to the duties of Investment Decision Makers in LGPS Administering authorities

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report

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