Surrey Pension Fund Committee

SURREY
COUNTY COUNCIL

Date & time	Place	Contact	Chief Executive
Friday, 11 December 2020 at 10.00 am	REMOTE	Angela Guest Tel 020 8541 9075 angela.guest@surreycc.gov.uk	Joanna Killian We're on Twitter: @SCCdemocracy

Please note that due to the COVID-19 situation this meeting will take place remotely.

Please be aware that this meeting will be webcast and can be accessed through the webcast portal on the Surrey County Council website. This page can be accessed by following the link below:
https://surreycc.public-i.tv/core/portal/webcasts

If you have any queries relating to accessing this agenda please email angela.guest@surreycc.gov.uk

Elected Members
Ms Charlotte Morley, Mr Tim Evans (Chairman), Mr Ben Carasco (Vice-Chairman), Mr John Beckett (Ewell), Mr David Mansfield and Mrs Hazel Watson

Co-opted Members:
Kelvin Menon, Borough Councillor Ruth Mitchell (Hersham), District Councillor Tony Elias (Bletchingley and Nutfield) and Philip Walker (Employees)

Mission statement
"The Surrey Pension Fund will deliver a first-class service through strong partnerships with scheme members, employers, the Border to Coast Pool and the wider LGPS community. Environmental, Social and Governance factors are fundamental to our approach which is underpinned by risk management, informed decision making, the use of technology and the highest standards of corporate governance."

PART 1
IN PUBLIC

1 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

2 MINUTES OF THE PREVIOUS MEETING [11 SEPTEMBER 2020] (Pages 1 - 16)

To agree the minutes as a true record of the meeting.

3 DECLARATIONS OF INTEREST

All Members present are required to declare, at this point in the meeting or as soon as possible thereafter

(i) Any disclosable pecuniary interests and / or

(ii) Other interests arising under the Code of Conduct in respect of any item(s) of business being considered at this meeting

NOTES:

- Members are reminded that they must not participate in any item where they have a disclosable pecuniary interest
- As well as an interest of the Member, this includes any interest, of which the Member is aware, that relates to the Member's spouse or civil partner (or any person with whom the Member is living as a spouse or civil partner)
- Members with a significant personal interest may participate in the discussion and vote on that matter unless that interest could be reasonably regarded as prejudicial.

4 QUESTIONS AND PETITIONS

To receive any questions or petitions.

Notes:

1. The deadline for Member's questions is 12.00pm four working days before the meeting (*7/12/2020)*.
2. The deadline for public questions is seven days before the meeting (*4/12/2020)*.
3. The deadline for petitions was 14 days before the meeting, and no petitions have been received.

5 LOCAL PENSION BOARD (Pages 17 - 22)

In accordance with Fund's governance objectives in the 2020/21 Business Plan.

6 CASHFLOW ANALYSIS (Pages 23 - 26)

In accordance with Fund's funding objectives in the 2020/21 Business Plan.

7	**EXIT CAP DECISIONS** This report provides the Pension Fund Committee with details of urgent decisions made regarding the processing of exit payments for eligible local government employees.	(Pages 27 - 34)
8	**MINISTRY OF HOUSING COMMUNITIES AND LOCAL GOVERNMENT - CONSULTATION ON THE REFORM OF LOCAL GOVERNMENT EXIT PAYMENTS** To provide details of the Ministry of Housing Communities and Local Government's (MHCLG) consultation on the reform of exit payments in local government and the response from Surrey.	(Pages 35 - 46)
9	**MINISTRY OF HOUSING COMMUNITIES AND LOCAL GOVERNMENT - CONSULTATION ON AMENDMENTS TO THE LOCAL GOVERNMENT PENSION SCHEME STATUTORY UNDERPIN** To provide details of the Ministry of Housing Communities and Local Government's (MHCLG) consultation on amendments to the Local Government Pension Scheme (LGPS) statutory underpin and the response from Surrey.	(Pages 47 - 60)
10	**NATIONAL KNOWLEDGE ASSESSMENT (NKA) RESULTS AND TRAINING PLAN** The report sets out the results of the National Knowledge Assessment (NKA) conducted by Hymans Robertson.	(Pages 61 - 84)
11	**DEPARTMENT FOR WORK AND PENSIONS - CONSULTATION ON TAKING ACTION ON CLIMATE RISK: IMPROVING GOVERNANCE AND REPORTING BY OCCUPATIONAL PENSION SCHEMES** This report provides details of the Department for Work and Pension's (DWP) consultation on Taking Action on Climate Risk: Improving Governance and Reporting by Occupational Pension Schemes and the response from Surrey.	(Pages 85 - 92)
12	**INVESTMENT CORE BELIEFS AND THE UNITED NATION'S SUSTAINABLE DEVELOPMENT GOALS** Surrey Pension Fund is reviewing its investment strategy with a view to ensuring that it is in line with its Mission Statement and the emphasis on environmental, social and governance (ESG) considerations, in the wider context of the United Nation's Sustainable Development Goals (SDGs).	(Pages 93 - 134)
13	**COMPANY ENGAGEMENT & VOTING** This report is a summary of various Environmental Social & Governance (ESG) issues that the Surrey Pension Fund, Local Authority Pension Fund Forum (LAPFF), Robeco, and Border to Coast Pensions Partnership (BCPP) have been involved in, for the attention of the Pension Fund Committee. Two annexes were originally published with the agenda that should not have been. These were working documents and information contained therein had not been verified.	(Pages 135 - 140)

14 **RESPONSIBLE INVESTMENT POLICY REVIEW** (Pages 141 - 170)

The Border to Coast Pension Partnership (BCPP) is now an established fully regulated asset management company when the authorised contractual scheme (ACS) went “live” on 26 July 2018. As part of this, BCPP now reviews is Responsible Investment (RI) and Corporate Governance and Voting Policy annually in advance of the proxy voting season.

15 **EXCLUSION OF THE PUBLIC**

Recommendation: That under Section 100(A) of the Local Government Act 1972, the public be excluded from the meeting for the following items of business on the grounds that they involve the likely disclosure of exempt information under the relevant paragraphs of Part 1 of Schedule 12A of the Act.

16 **INVESTMENT MANAGER ISSUES AND PERFORMANCE AND ASSET/LIABILITIES UPDATE** (Pages 171 - 190)

This report is a summary of all manager issues that need to be brought to the attention of the Pension Fund Committee, as well as an update on investment performance and the values of assets and liabilities.

Confidential: Not for publication under Paragraph 3
Information relating to the financial or business affairs of any particular person (including the authority holding that information)

17 **PRIVATE MARKET REVIEW** (Pages 191 - 204)

As part of good governance, the Committee reviews the performance of the Fund’s Private Market investments annually. This report is a review of the investment performance of the Private Market portfolio.

Confidential: Not for publication under Paragraph 3
Information relating to the financial or business affairs of any particular person (including the authority holding that information)

18 **PROVISION OF INVESTMENT ADVICE AND CONSULTATION SERVICES** (Pages 205 - 208)

This Part 2 report is consistent with the Fund’s investment objectives.

Confidential: Not for publication under Paragraph 3
Information relating to the financial or business affairs of any particular person (including the authority holding that information)

19 **BORDER TO COAST UPDATE** (Pages 209 - 228)

The Pension Fund Committee is asked to note the Part 2 report.

Confidential: Not for publication under Paragraph 3
Information relating to the financial or business affairs of any particular person (including the authority holding that information)

20 **PUBLICITY OF PART 2 ITEMS**

To consider whether the item considered under Part 2 of the agenda should be made available to the Press and public.

21 DATE OF NEXT MEETING

The next meeting of the Surrey Pension Fund Committee will be on 12 March 2021.

Joanna Killian
Chief Executive
Published: Wednesday, 2 November 2020

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MINUTES of the meeting of the **SURREY PENSION FUND COMMITTEE** held at 10.00 am on 11 September 2020 at REMOTE - https://www.surreycc.gov.uk/council-and-democracy/councillors-and-committees/webcasts.

These minutes are subject to confirmation by the Committee at its next meeting.

Elected Members:

- * Ms Charlotte Morley
- * Mr Tim Evans (Chairman)
- * Mr Ben Carasco (Vice-Chairman)
- Mr John Beckett
- * Mr David Mansfield
- * Mrs Hazel Watson

Co-opted Members:

- * Kelvin Menon
- * Borough Councillor Ruth Mitchell, Hersham
- * District Councillor Tony Elias, Bletchingley and Nutfield
- * Philip Walker, Employees

41/20 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS [Item 1]

An apology was received from Mr John Beckett.

42/20 MINUTES OF THE PREVIOUS MEETING [12 JUNE 2020] [Item 2]

The Minutes were approved as an accurate record of the previous meeting.

43/20 DECLARATIONS OF INTEREST [Item 3]

There were none.

44/20 QUESTIONS AND PETITIONS [Item 4]

There were five questions from members of the public. These and the responses are attached as an annex to the minutes.

Supplementary questions:-

Jennifer condit did not accept the reply to her question which she reiterated and asked if the Committee did not see that as owner of Exon that it was complicit in the crimes against humanity and the planet. The Chairman responded that her question had been answered.

Janice Baker asked if the Committee were going to push investments in renewables so that it was a more significant part of its interests? The Chairman responded that investment in renewables was considered as and when they became available.

Chris Neill, on behalf of Ian Chappell, stated that losses in fossil fuels was predicted and Surrey did nothing about this. He asked if each individual

Member would buy those shares today if they didn't own them already? The Chairman explained that Members were aware that investments could go up and down and that Investment Managers manage those and the Committee reviewed them regularly.

Simon Hallett stated that it was easy to provide an approximation of losses and asked the Committee if they disputed the value loss of fossil fuels was at least £50m and did it consider this loss irrelevant? The Chairman reiterated the response he gave to a previous question in that Investment Managers make the decisions within the remit given to them and the Committee reviewed regularly.

45/20 FORWARD PLAN [Item 5]

Resolved:

The Committee noted the Forward Plan.

46/20 CASH FLOW ANALYSIS [Item 6]

Declarations of interest:
None

Speakers:
Ayaz Malik Pensions Finance Specialist

Key points raised during the discussion:

1. The Chairman introduced the report for which there were no further questions or comments from Members.

Actions/ further information to be provided:
None.

Resolved:

1. The cash-flow position for quarters four and one were noted.

2. That no change was required to the investment or funding strategy as result of the current cash-flow position.

Reason for decision:
Cash-flow movements in the Fund influences both the investment and funding strategy. The Pension Fund Committee monitors cash-flow consistent with the Fund's strategic funding objectives.

47/20 LOCAL PENSION BOARD REPORT [Item 7]

Declarations of interest:
None

Speakers:
Nick Harrison, Chairman, Local Pension Board
Anna D'Alessandro, Director for Corporate Finance
Ayaz Malik - Pensions Finance Specialist

Key points raised during the discussion:

1. The Chairman of the Local Pension Board introduced the report to the Committee.
2. The Director for Corporate Finance explained that there were issues for the service and the report focussed on what was being done to ameliorate those issues. She also reported that a Programme Manager, Sonia Sharma, had been recruited in June and that there had been many changes made since then, mostly around governance arrangements and setting up projects to get the service into a better position.
3. A Member asked about the knowledge assessment and training policy and how the committee performed according to the assessment. The Chairman of the Board responded that the Committee were one of the higher performers and were still awaiting comments from some members of the board and committee.
4. The Pension Finance Specialist reported that all comments had since been received and a that a report would be drafted and reported to the December meeting of the Committee. He also reported that work would be undertaken with Hymans to produce a draft training plan which would also be presented to the December Committee meeting.

Actions/ further information to be provided:

1. Democratic Services to invite Sonia Sharma to the next meeting of the Board.
2. That the National Knowledge Assessment and Training Plan report be added to the forward plan for December 2020.

Resolved:

1. The minutes of the informal Local Pension Board meeting of 31 July 2020 were noted.

2. The following changes to the risk register were approved:
    - Risk A8 (conflicting priorities [Orbis v the Surrey Pension Fund]) on the Administration Register should be raised to amber;
    - Risk A5 (poor reconciliation process) to be should be raised to amber.

Reason for decision:

The Public Sector Pensions Act 2013, requires Local Pension Boards to assist the Scheme Manager in securing compliance with the LGPS Regulations and requirements imposed by the Pensions Regulator. This report provides the Pension Fund Committee with insight in to the activities of the Local Board and furthers the successful collaboration of the Committee and Board in managing risk and compliance and promoting effective governance.

This meets the Fund’s strategic governance and delivery objectives.

48/20 2019 VALUATION UPDATE [Item 8]

Declarations of interest:
None

Speakers:
Ayaz Malik - Pensions Finance Specialist
Gemma Sefton – Fund Actuary, Hymans
Neil Mason - Strategic Finance Manager (Pensions)

Key points raised during the discussion:
1. The Pension Finance Specialist introduced the report and set out the work undertaken so far on multiple employer strategies and that the paper provided by Hymans would be used for a training session.
2. The Chairman highlight paragraph five of the report which summarises the materiality of what was happening.
3. The Fund Actuary explained that strategies were used to assist employers meet their funding objectives.
4. A Member asked about the reaction of employers on the proposals. The Strategic Finance Manager responded that the Pension Finance Specialist had met with the cohort of effected employers and had constructive conversations. It was highlighted that it was prudent for employers to reduce their liability risk as they went through their exit strategies. Only one employer had requested to remain on the core strategy.
5. A Member asked if the fund was ring fenced for the strategies or can they call on the rest of the fund if their strategy is not as successful. The Fund Actuary explained that it was notional and reallocation could take place.

Actions/ further information to be provided:
None.

Resolved:
The progress on the implementation of multiple strategies for employers was noted.

Reason for decision:
To allow the fund to meet its strategic funding objectives as set out in 2019 Valuation.

Phil Walker joined the meeting at 11am.

49/20 INVESTMENT CORE BELIEFS AND THE UNITED NATION'S SUSTAINABLE DEVELOPMENT GOALS [Item 9]

Declarations of interest:
None

Speakers:
Mamon Zaman, Senior Pensions Finance Specialist
Niall O’Shea
David Crum, Sarah Wilson and Niall O’Shea - Minerva

Key points raised during the discussion:
1. The Senior Pensions Finance Specialist introduced the report and highlighted the strong Environmental, Social and Governance (ESG) credentials of the Fund and that work commissioned on mapping showed 70% coverage against the United Nations Sustainable Development Goals (UN SDGs) benchmark, the World Benchmarking Alliance Sustainable Development Goals 2000 Index (WBA SDG) .

2. David Crum, Minerva, explained that they had worked with Surrey officers, reaching out to external fund managers and highlighted their initial findings as contained within the report. He went on to explain that the (WBA SDG is a list of 2000 companies identified as most likely to be able to advance the delivery of the SDG's. A report would be provided to the Fund and will make suggestions for further actions from the Fund. A workshop would also be set up to look in details at where the Fund is and where it would like to go from there.
3. Members were happy with the work undertaken and looked forward to the workshop.
4. A Member asked David Crum if, in Minerva's opinion, there were any changes suggested to the Fund's roadmap following the work undertaken so far. David Crum explained that this was the first LGPS Fund to look at doing this and did not feel any changes to the roadmap were needed at this point.

Actions/ further information to be provided:
None.

Resolved:

1. The initial findings from the Fund's SDG Mapping provider were noted.

2. The follow up actions leading into December Committee were approved.

Reason for decision:
To keep the Pension Fund Committee apprised of the progress made in reviewing the Fund's investment strategy with a view to ensuring that it is in line with its Mission Statement and the emphasis on environmental, social and governance (ESG) considerations.

50/20 INVESTMENT MANAGER ISSUES AND PERFORMANCE AND ASSET/LIABILITIES UPDATE [Item 10]

Declarations of interest:
None

Speakers:
Mamon Zaman, Senior Pensions Finance Specialist

Key points raised during the discussion:
The Committee considered a report that summarised all manager issues that needed to be brought to the attention of the Pension Fund Committee, as well as an update on investment performance and the values of assets and liabilities.

Actions/ further information to be provided:
None.

Resolved:
The main findings of the report were noted; The Fund's 3 year annualised performance return for the period ending 31 March 2020 was 2.63% against its target return of 3.76%. The funding level as at 30 June 2020 was 97.7%.

2

Reason for decision:
In order to judge the performance of the Fund's investment managers against the Fund's target returns, and whether it is meeting its Strategic Investment objective in line with its Business Plan.

51/20 DRAFT ANNUAL REPORT & STATEMENT OF ACCOUNTS [Item 11]

Declarations of interest:
None

Speakers:
Mamon Zaman, Senior Pensions Finance Specialist

Key points raised during the discussion:
The Committee considered a report that provided the annual report which contains the unaudited statement of accounts together with other information about the Fund's performance during 2019/20.

Actions/ further information to be provided:
None.

Resolved:
The Draft Annual Report with the Audited Pension Fund Accounts for publication subject to audit approval were noted and approved.

Reason for decision:
Under the Local Government Pension Scheme (Administration) Regulations 2008, administering authorities of LGPS funds are required to prepare a pension fund annual report. This therefore meets the requirements of the Regulations, the Local Government Scheme Advisory Board (SAB) as well as wider stakeholders who have an interest in the Fund. The Pension Fund Committee must approve all financial statements produced for the Pension Fund.

52/20 COMPANY ENGAGEMENT AND VOTING REPORT [Item 12]

Declarations of interest:
None

Speakers:
Mamon Zaman, Senior Pensions Finance Specialist
David Crum – Minerva
Sarah Wilson - Minerva

Key points raised during the discussion:

1. The Senior Pensions Finance Specialist introduced a report explaining that a co-signed letter had been written to the Brazilian embassy in relation to deforestation in Brazil, attached as annex 1 the report. Also, Minerva had provided a report on issues experienced last quarter around voting. The Investor groups had since met with Brazilian authorities to discuss further outcomes. A positive short-term outcome was that Brazil banned forest fires for the four months of dry season and set up military operations due to this investor pressure. Due to the success of this investor dialogue, a working group had been set up to continue this work

going forward, of which the Fund has chosen to participate in going forward.

2. David Crum updated the Committee that Minerva has still been unable to go back to the office to check through the paperwork but they intended to do. Some analysis had been done on meetings missed:
    - There had been 45 companies meetings where Surrey votes were not cast. Of those meetings there were:
    - 782 individual resolutions that Surrey could have voted on
    - 702 of those Surrey would have voted in favour
    - 56 Surrey would have voted against
    - There would have been very few abstentions
    - There were no instances where Surrey's vote, if given, would have swayed the outcome on those resolutions one way or another.
3. Sarah Wilson spoke to Members about the issue that had arisen over securities lending as outlined in annex 2 to the submitted report. Further procedures had been put in place in terms of mandate changes to ensure that there are more eyes to do the sign off on any mandate changes. New elements had also been introduced to the stock lending support service so they could identify contentious upcoming meetings which may have an impact on stock lending so that clients could exercise their right to vote to retain the revenue of stock lending or to maintain the balance. Apologies were given but lessons had been learned and things were back on track.
4. A Member asked if it was only Surrey affected by the voting issue and why are stocks borrowed. Sarah Wilson responded that Surrey was the only one affected. David Crum explained stock lending in terms of assuring liquidity and would impact on the price and from Surrey's perspective, stock lending was good. However, short selling had received some bad press. Sarah Wilson reported that a good practice guidance around stock lending had recently been published.
5. A Member spoke of caution needed as stock lending may affect contentious voting.

Actions/ further information to be provided:
None.

Resolved:

1. That ESG Factors were fundamental to the Fund's approach, consistent with the Mission Statement through was affirmed;
    - Continuing to enhance its own Responsible Investment Approach, its Company Engagement policy, and SDG alignment with its external provider Minerva Analytics.
    - Commending the outcomes achieved for quarter ending 30 June 2020 by Robeco in their Active Ownership approach and the LAPFF in its Engagement with multinational companies as at 30 June 2020.
2. That Minerva's Voting Services Issue Update report in Annexe 2, was noted.

Reason for decision:
In accordance with The Fund's Mission Statement, as well as its Investment Strategic Objectives, the Fund is required to fulfil its fiduciary duty to protect the value of the Pension Fund, to meet its pension obligations. Part of this

involves consideration of its wider responsibilities in Responsible Investment as well as how it exercises its influence through engaging as active shareholders.

53/20 TASKFORCE FOR CLIMATE RELATED FINANCIAL DISCLOSURE REPORT 2019-20 (TCFD) [Item 13]

Declarations of interest:
None

Speakers:
Mamon

Key points raised during the discussion:
The Committee considered a report that summarised the Fund's first report complying with the Taskforce for Climate Related Financial Disclosures. The report supported the Fund's Strategic Investment Objectives, with particular focus on how it fulfilled its role as a Responsible Investor.

Actions/ further information to be provided:
None.

Resolved:

1. The 2019-20 Taskforce for Climate Related Financial Disclosure report was noted.
2. That the Committee continue to enhance its approach to Climate Risk in the context of its SDG Mapping work was agreed.

Reason for decision:
In accordance with The Fund's Mission Statement, as well as its Investment Strategic Objectives, the Fund is required to fulfil its fiduciary duty to protect the value of the Pension Fund, to meet its pension obligations. The role of the Fund as an investor includes being aware of its wider responsibilities in Responsible Investment, as well as how it exercises its influence through engaging as active shareholders.

Part of this consideration of Environmental, Social and Governance factors, is the systemic risk that Climate Change poses to economies as well as to the Fund's investments.

54/20 EXCLUSION OF THE PUBLIC [Item 14]

Resolved: That under Section 100(A) of the Local Government Act 1972, the public be excluded from the meeting for the following items of business on the grounds that they involve the likely disclosure of exempt information under the relevant paragraphs of Part 1 of Schedule 12A of the Act.

11.49 The Committee adjourned for seven minutes for a comfort break

Cllr Tony Elias left the meeting.

PART TWO – IN PRIVATE

55/20 BORDER TO COAST UPDATE [Item 15]

Declarations of interest:
None

Speakers:
Neil Mason - Strategic Finance Manager (Pensions)
Steve Turner,
Mamon Zaman, Senior Pensions Finance Specialist

Key points raised during the discussion:

1. Members were reminded of activities and the annual conference on 2 October 9.30am-3pm.
2. The Committee in June 2019 approved the delegation of authority to the Director of Corporate Finance, in consultation with the Chairman of the Pension Fund Committee, to transition the Multi-Asset Credit portion of the Surrey Pension Fund portfolio to the BCPP national pool.
3. It was reported that PIMCO had been selected as the Core MAC manager to be complemented with smaller (specialist) satellite managers.
4. The Chairman noted that the report was not about agreeing the strategic asset allocation as that had already been agreed but set out how the Fund would do it in practice.
5. Steve Turner highlighted that the timings when the Fund chooses to invest must be considered when setting return targets so that they are not easily outperformed as there must be a balance between the full market cycle and the prevailing market conditions.
6. A Member noted the substantial 1% saving for the new portfolio and asked if the Committee would get an update to those savings achieved over time. In response, the Senior Pensions Finance Specialist explained that there was a working group with the BCPP on establishing standardised methods across all partner funds concerning projected savings and identifying realised savings going forward.

Actions/ further information to be provided:
The Strategic Finance Manager would share the extensive set of Q&As from the property meeting held in September, to Members.

Resolved:

1. Notes recent updates in BCPP activity, including details of the BCCP joint committee meeting of 16 June 2020.

2. Notes the update on the Multi-asset credit (MAC) fund, including the appointment of the satellite managers to complement PIMCO as the core MAC manager.

3. Approves the delegation of authority to the Director of Corporate Finance, in consultation with the Chairman of the Pension Fund Committee, to transition the property portion of the Surrey Pension Fund portfolio to the UK and Global property sub-funds of the Border to Coast Pensions Partnership (BCPP) national pool when its design has been established to the satisfaction of officers and Fund advisors and assuming that the "necessary conditions" of governance have been satisfied.

Reason for decision:
To keep the Pension Fund Committee apprised of the progress made by the Officer Operations Group (OOG), Joint Committee and BCPP Shareholder Board in the drive to maintain a fully functioning asset pool, which will manage the significant majority of the Surrey fund assets. This is consistent with the Fund's strategic investment and governance objectives.

56/20 LOCAL PENSION BOARD REPORT [Item 16]

Declarations of interest:
None

Speakers:
Neil Mason - Strategic Finance Manager (Pensions)

Key points raised during the discussion:
1. The Strategic Finance Manager highlighted the Pensions Administration Turnaround (PAT) programme objectives and the PAT programme structure with the Director of Corporate Finance as the Senior Responsible Owner, the External Commercial Advisor as the Programme Manager and the Strategic Finance Manager – Pensions as the Pensions Lead. Quarterly reports would be presented to the Local Pension Board and the Committee and monthly updates given to the Chairmen of the Committee and the Local Pension Board.
2. The Chairman noted that the dissolution of the Orbis Pension Partnership, along with reversion to sovereign authorities and London Borough fund relationships were complex operations and noted the robust approach.

Actions/ further information to be provided:
None.

Resolved:
The Part 2 Annex to the main report at item 7 was noted.

57/20 INVESTMENT MANAGER ISSUES AND PERFORMANCE AND ASSET/LIABILITIES UPDATE [Item 17]

Declarations of interest:
None

Speakers:
None.

Key points raised during the discussion:
Members considered this Part 2 annex to Item 10 on the agenda.

Resolved:
The Part 2 Annex to the main report at Item 10 was noted.

58/20 DRAFT ANNUAL REPORT & STATEMENT OF ACCOUNTS [Item 18]

Declarations of interest:
None

Speakers:
None.

Key points raised during the discussion:
Members considered this Part 2 annex to Item 11 on the agenda.

Resolved:
The Part 2 Annex to the main report at Item 11 was noted.

59/20 INVESTMENT STRATEGY REVIEW [Item 19]

Declarations of interest:
None

Speakers:
Neil Mason - Strategic Finance Manager (Pensions)
Steve Turner and Ross Palmer, Mercer

Key points raised during the discussion:

1. Members considered this Part 2 report that reviewed the Fund's current Investment Strategy, in line with current progress made within BCPP's asset offerings, as well as taking account of its current Fund Managers' performance returns, since inception. This report developed the approvals of the Pension Fund Committee at its meetings of 12 September 2019 and 12 June 2020.
2. The recommendations were discussed in detail and agreed.
3. With regards to Annex 1, Mercer noted the long term strategy for property and was not envisaging any new changes in the next 12-18 months due to the structural difficulties as a result of Covid-19 with the UK market reliant on the affected high street, retail, leisure, hotels and office sectors; an increase in the property allocation to global markets to 50% of the property portfolio would address that as the US/EU markets were exposed to residential areas – less affected by the pandemic.
4. It was noted that at the last year's strategy review the Committee agreed to material changes. Mercer explained that those assets would be sourced from the Fund's listed equity and Diversified Growth Fund (DGF) and would take 3-5 years to be drawn down; therefore the Investment Consultant sets out proposals for exploring liquid alternative asset classes in the interim as 'warehousing' investments. The Investment Consultant suggested the use of listed private equity and listed infrastructure, for example companies listed on stock exchanges/passive vehicle by Legal and General (LGIM); as well as global loans, for example funds that invest in bank loans to corporations looking to expand businesses within secondary markets. As passive vehicles do not exist for loans an active manager search would be needed, linking in with BCPP. To do this successfully the routes must be consistent with pooling.
5. The Committee discussed in detail the information provided on gilts in Annex 4 to the report.
6. It was reported that the view from the property session, held with Paul Campbell, was the need for flexibility in the future particularly concerning property in respect of the new real asset class and long lease property was to be explored as likely to be delivered outside of the BCPP property portfolio.

2

7. The Strategic Finance Manager reported that it was likely the Committee would receive a report on the recommended direction of travel at the next Committee meeting in December.

Resolved:

1. That the increase in property allocation to global property assets to 50% of the property portfolio was approved.
2. That officers be authorised to work with the independent advisor, investment consultant and Border to Coast to explore a solution incorporating liquid alternatives as a proxy for the allocation to private market assets, while the transition to private market assets is incomplete.
3. That officers be authorised to work with the independent advisor, investment consultant and Border to Coast to explore a solution as a proxy for the target equity portfolio, while the transition to this target asset allocation is in build with Border to Coast.
4. That officers be authorised to work with the independent advisor, investment consultant and Border to Coast to explore alternatives to the gilts segment of the portfolio.

Reason for decision:
As part of the Fund's 2019 Investment Strategy Review, the Pension Fund Committee had agreed changes to the asset allocation (detail below) at its meetings on 12 September 2019 and 12 June 2020. As this was partly dependent on product offerings being available by Border to Coast Pensions Partnership (BCPP), the Fund will now explore options to move into its newly agreed asset allocation in the interim, while those products are being developed. The Purpose of this is to minimise risk and maximise returns through its asset allocation.

60/20 PUBLICITY OF PART 2 ITEMS [Item 20]

The Committee agreed that no confidential information within items considered under Part 2 of the agenda should be made available to the Press and public.

61/20 DATE OF NEXT MEETING [Item 21]

It was agreed that the next meeting of the Surrey Pension Fund Committee would take place on 11 December 2020.

Meeting ended at: 12.30 pm

Chairman

SURREY PENSION FUND COMMITTEE – 11 SEPTEMBER 2020

PROCEDURAL MATTERS – QUESTIONS AND RESPONSES

1. **Question Submitted by Jenifer Condit**

The Norwegian asset manager Storebrand has recently announced that they are divesting from Exxon Mobil and Chevron as part of a new climate policy targeting companies that use their political clout to block green policies. So the policy focuses on withdrawing support from those specific companies which have used their financial and political clout to distract, deny and delay action against climate change which threatens life on Earth. Will you consider adopting such a policy? I ask this in light of your investment in Exxon Mobil.

Response:

We share your concerns regarding those companies who lobby directly against environmental policies. The case for divestment from these companies requires a high bar to avoid the risk of a prescribed need to divest from all sectors that lobby their own interests to the detriment of others. Surrey makes investment decisions when there is compelling evidence that a company's practices are value-destructive to the point that they jeopardise any investment case.

2. Question Submitted by Janice Baker

Bloomberg NEF and UNEP [Trends in Renewable Energy by Investment 6/20] note the resilience, and falling price, of clean energy while the fossil fuel sector slumped due to Covid-19. They advise putting renewables at the heart of Covid-19 economic recovery instead of subsidizing the recovery of fossil-fuel industries. We consider this to be an essential element of a comprehensive strategy to protect funds from climate change risks, as well as ensuring a healthy natural world – the best insurance policy against global pandemics. Will the fund commit to increasing its share of low-carbon and renewable investments as a priority?

Response:

The Fund had made renewable energy investments in the past and will continue to seek these, although, the reality is that the market is still growing with most investment opportunities existing in private markets.

The Fund commissioned an independent provider in March 2020 to establish the Fund's starting position against the United Nations' 17 Sustainable Development Goals (UN SDGs). One of the elements we have asked our provider to undertake on our behalf is to assess how sophisticated our different asset managers are on the climate risk framework spearheaded by Mark Carney, the TCFD and even more importantly, how well the companies in those portfolios score for their own TCFD disclosures. This, along with an assessment of holdings potentially able to make large contributions towards the Sustainable Development Goals (which has climate at the heart of it). Phase 2 of this project will involve engaging with the Fund's Committee and Officers on exploring their investment beliefs and how this will integrate into the Fund's investment strategy. This will also mean the Fund will align itself against specific SDGs which is relevant to the Fund as an investor and represents its Investment Core Beliefs.

2

3. **Question Submitted by Helena Ritter**

How much autonomy do you have to divest your fossil fuel holdings? Please describe the process you would need to follow if you choose to eliminate an investment (of any kind) which you own by each of these three routes:

- directly via Newton or Majedie
- As part of an investment consortium in the case of Border to Coast
- As part of an investment fund, in the cases of Legal & General.

Response:

Surrey has ultimate authority to act independently, but, within the framework of MHCLG Guidance and LGPS Regulations. This means that the terms of engagement with its Fund Managers are detailed in its relevant Investment Management Agreement (IMA), which are agreed and signed prior to the assets being managed. It's then the Fund Manager's responsibility to pick investment holdings in accordance with that IMA with Surrey Pension Fund, having the freedom to terminate an agreement should it feel that the manager has not met the requirements of the IMA.

The Fund's passive holdings are overseen by Legal and General, and as such, are not actively managed. With our investments held with Border to Coast we act in partnership with other partner funds when determining investment decisions. All partner funds review and approve BCPP's Responsible Investment Policy, which is then integrated into Fund Manager Selection, internal investment decisions as well as its policies on Corporate Governance and Voting.

4. **Question Submitted by Ian Chappell**

Since your last meeting, fossil fuel companies have slashed tens of billions off their balance sheets in recognition of their permanent reduction in value. They've also cut dividends, recognising their substantial reduction in cash generating capability. And now Exxon has been kicked out of the Dow Jones average, reflecting the diminishing importance of fossil fuels in the new economy. Every day brings new signals that fossil fuels are in rapid decline

These stocks can and almost certainly will go lower. Indeed they have fallen further in price since your last meeting. Can I ask whether you continue to hold fossil fuels in the hope that there will be price recovery affording you the chance to sell at higher prices, or whether you hold fossil fuels as part of your long term investment outlook?

Response:

In reaching our investment strategy decisions we consult with investment professionals and BCPP and we appoint and scrutinise fund managers/BCPP in the delivery of our investment strategy. Our investment strategy, which includes our responsible investment policy, does anticipate all future developments.

5. **Question Submitted by Simon Hallett**

From data you provided in response to other questions (including an FOI request from J Condit), the value of fossil fuel shares in your fund declined from £151.4m at end May 2019 to £77.1m at end May 2020, a reduction in value of £74.3m. Since over this period the global energy sector index fell by 28% and BP alone by 43% I am inferring that most of this decline represents an investment loss to the portfolio.

During the same period the FTSE World Index rose 8.5% - from 1434.79 on May 31st 2019 to 1556.74 on May 31st 2020. Had you divested your fossil fuel shares on May 31, 2019 and reinvested in a broad market index this portion of your portfolio could have grown to £164.3m 12 months later. This means the opportunity cost could have been up to £164-77m, or £87m.

Although the information disclosed in your recent FOI reply (to J Condit) is of some help, it remains impossible to fully understand how much of the decline in your fossil fuel exposure results from any action on your part, and how much is simply the result of market movements. **Could you now quantify how much of this reduction is due to the collapse in oil share prices and how much is due to changes in the holdings of fossil fuel companies in your portfolio?**

In consideration of the fact that the collapse of oil share prices was <u>both predictable and predicted</u>, and the fact that numerous members of the Surrey Pension Fund and taxpayers have been imploring you to sell these share since before May 31, 2019, **how do you explain your losses in this sector to your stakeholders?**

Response:

To quantify and distinguish the exact difference in the Fund's actual fossil fuel exposure between the reductions in fossil fuel companies in our portfolio compared to the collapse in oil share prices, is not something the Fund views as a relevant area of work to commission internally or externally.

Our governance process entails regular review and scrutiny of our investment strategy and performance. This is communicated to our stakeholders through the documents shared in public meetings and is summarised in our annual report (add link). We allow ample opportunity for stakeholders to seek further information; including questions to this Committee.

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **11 DECEMBER 2020**

LEAD OFFICER: **ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**

SUBJECT: **LOCAL BOARD REPORT**

SUMMARY OF ISSUE:

Strategic objectives	
Governance	Delivery

This report provides a summary of administration and governance issues reviewed, or approved, by the Local Pension Board at its meeting that require noting or action by the Pension Fund Committee.

RECOMMENDATIONS:

It is recommended that the Committee:

1. Notes the minutes of the Local Pension Board meeting of 12 November 2020 (included as Annexe 1).
2. Approves the following minor changes to the risk register: risks A21 the McCloud judgement, A22 migrating from County Hall, and A23 management of the backlog in the Administration Risk Register have all been updated.
3. Note the Local Board's concern at the position that the Fund has been placed in due to conflicts between the Restriction of Public Sector Exit Payments Regulations 2020 and the Local Government Pension Scheme Regulations 2013.

REASONS FOR RECOMMENDATIONS:

The Public Sector Pensions Act 2013 requires Local Pension Boards to assist the Scheme Manager in securing compliance with the LGPS Regulations and requirements imposed by the Pensions Regulator. This report provides the Pension Fund Committee with insight into the activities of the Local Board and furthers the successful collaboration of the Committee and Board in managing risk and compliance and promoting effective governance.

This meets the Fund's strategic governance and delivery objectives.

DETAILS:

Turnaround Update Report

1. As a result of a review of the Orbis partnership, management of pension administration is to revert to the sovereign control of East Sussex (ESCC) and Surrey County Councils (SCC) respectively.

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2. A Pension Administration Turnaround (PAT) Board has been established to oversee the dissolution of the Orbis pension partnership, along with reversion to sovereign authorities and updating the relationships with the London Borough funds.

3. The PAT comprises six projects:
    - Dissolution of the Orbis pension administration
    - SCC sovereign return
    - ESCC sovereign return
    - Systems procurement
    - On-going relationships with existing Orbis partners
    - On-going relationship with Surrey Fire and Rescue service (SFRS)

4. The Chairman of the Pension Fund Committee and Local Pensions Board are apprised on a monthly basis on the progress of the PAT. The PAT programme currently has a green risk rating.

Administration Update

5. While Internal Audit did acknowledge the significant improvement work that was being undertaken at programme level, they have as yet been unable to provide the assurance that progress has been made against the agreed audit action plan. As a consequence, a position statement, as opposed to a full audit, was produced in 2019/20.

6. Internal Audit will carry out interim testing on data cleansing, Pension Payroll and procedure notes with a view to conducting a full audit in quarter four of 2020/21.

7. Only 46 of 33,293 active annual benefit statements missed the 31 August 2020 deadline, and 4 of these were due to the failure of scheme employers to provide annual data returns. The remaining 42 statements were based on last year's (2018/19) pay because the scheme employer did not provide this year's pay figure.

8. All the deferred member annual benefit statements were issued by the end of September. Unfortunately, 4,589 missed the deadline including 4,143 due to incorrect addresses ("gone away"), which will be remedied by the imminent address tracing exercise. A further 257 were delayed by error messages on Altair that have been investigated and corrected.

9. A software procurement exercise has been undertaken using the Norfolk Framework and there was one response from, the incumbent Heywood Aquilla.

10. After carrying out due diligence Surrey County Council has awarded the contract to Heywoods, although discussions to finalise the contract are continuing.

11. I-Connect is a software system that allows data and payroll input from employers to be interfaced with the pension administration system Altair. Implementation is progressing although there were some expected data compatibility issues that need to be investigated prior to the "go live" date.

12. There has been a focus on housekeeping with duplicate records and completed records that had not been closed being "cleansed."

13. The death process has been completely re-engineered to simplify processes and to utilise improved software modules. 5

14. The key performance indicator matrix in the Administration Performance Report records the average number of days taken to complete a case. The Board requested that an additional column be added to annexe 3 of Administration Update Report to identify the oldest outstanding cases to provide focus on any long outstanding cases.

Administration Performance Report

15. 3,246 cases were completed, which is a slight improvement on last quarter. The current staff utilisation rate is being investigated and the Board will be updated when this analysis of efficiency is complete.

16. There were 1,537 new starters reported this quarter, which compares with 811 in the same quarter last year and the administration Team is investigating why there has been a spike in cases during a lockdown.

17. Deaths have been identified as a key priority and 108 (63%) of initial death notifications were processed within SLA this quarter.

18. There is an imbalance in the distribution of cases and the Administration Team is investigating why there are so few transfers-in of all types in comparison to the number of new starters.

19. Members emphasised the importance of data quality and asked officers to review how data was extracted and presented. Members would like to have a better understanding of the resources required to do the work required.

20. A Board member asked why the number of pension recharge invoices raised in the key performance indicators did not agree with the number paid in the quarter - and yet performance was shown as being 100% within SLA. An officer explained that most invoices relate to pension strain costs which employers can pay over one, two or three years and, therefore, invoices that are not settled in the quarter are not necessarily overdue. Officers agreed to refine the statistics to capture the process more effectively.

Exit Cap Emergency Decision

21. The Restriction of Public Sector Exit Payments Regulations 2020 conflicts with the Local Government Pension Scheme Regulations 2013 forcing the Fund to make decisions that contradict the regulations.

22. In cases where the member is over 55 and the exit package exceeds £95,000, the Fund has decided to pay an actuarially reduced pension or a deferred benefit, instead of the unreduced pension required by regulation 30(7).

23. This is a pragmatic decision flowing from legal advice obtained by the Scheme Advisory Board and allows any balance of pension benefits to be paid later if required once the conflict of laws is resolved.

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Risk Register

24. The Board noted that risks A21 the McCloud judgement, A22 migrating from County Hall, and A23 management of the backlog in the Administration Risk Register (annex 2) have all been updated in the light of developments.

Pension Fund Committee Update

25. The Board asked for the next Committee report to include table showing the transfers and allocations of assets into Border to Coast, with a forecast of anticipated transfers to come as Border to Coast launches new funds.

Action Tracker

26. The Board requested environmental, social and governance (ESG) training for the next meeting.

Forward Plan

27. The Board requested that a turnaround report be added as a standing item for each meeting.

Communications Update

28. Examples of recent members' and employers' newsletters were presented to the Board for review and the Chairman asked the Administration Team to provide a copy of its communications schedule for 2020/21.

CONSULTATION:

29. The Chairmen of the Pension Fund Committee and the Local Pension Board have been consulted on this report.

RISK MANAGEMENT AND IMPLICATIONS:

30. Risk related issues have been discussed and are contained within the report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

31. The performance of the Pensions Administration function does present potential financial and value for money implications to the Pension Fund. The monitoring of these implications is discussed within the report.

DIRECTOR OF CORPORATE FINANCE COMMENTARY

32. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

33. A Local Pension Board is a requirement under the Public Service Pensions Act 2013. There are no legal implications or legislative requirements. 5

EQUALITIES AND DIVERSITY

34. The approval of the various options will not require an equality analysis, as there is no major policy, project or function being created or changed.

OTHER IMPLICATIONS

35. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

36. The following next steps are planned:

- Monitor the progress of the pension administration turnaround board (PAT).
- Receive further reports and continue collaboration between the Pension Fund Committee and Local Pension Board.

Report contact: John Smith, Pension Governance and Employer Manager

Contact details: T: 020 8213 2700 E-mail: john.smith@surreycc.gov.uk

Annexes:

1. Minutes of the Local Pension Board meeting 12 November 2020 (when available)

Sources/background papers:

1. The Pension Fund risk register (Administration)

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

Surrey Pension Fund

DATE:	**11 DECEMBER 2020**
LEAD OFFICER:	**ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**
SUBJECT:	**CASHFLOW ANALYSIS**

SUMMARY OF ISSUE:

Strategic objectives	
Investment	Funding

Cash-flow analysis allows the Fund to ascertain a projection as to when benefit payments may exceed income. This information can influence both the investment and funding strategy.

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1. Notes the cash-flow position for quarters one and two.
2. Determines that no change is required to the investment or funding strategy as result of the current cash-flow position.

REASON FOR RECOMMENDATIONS:

Cash-flow movements in the Fund influences both the investment and funding strategy. The Pension Fund Committee monitors cash-flow consistent with the Fund's strategic funding objectives.

DETAILS:

Cash-flows for quarters One - Two (1 July 2020 – 30 September 2020)

1. Pensions Funds have a positive cash-flow when their contribution inflows exceed pension benefits paid.
2. Contributions are derived from employers and employees. Pension benefits are derived from pensions and lump sum benefits paid to retired members and benefits paid to employees on leaving the Fund.
3. Any positive cash-flow is invested in accordance with the Fund's cash management plan.
4. The half-yearly (quarters one-two) cash-flow for the Surrey Pension Fund shows positive cash flow of £26,189,515 as follows:

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Quarter	Total contributions received	Total pension benefits paid	Net cash-flow
One (1 Apr 2020 – 30 Jun 2020)	£57,236,797	£36,151,423	£21,085,373
Two (1 Jul 2020 – 30 Sep 2020)	£43,058,556	£37,954,415	£5,104,141

5. The cash flow was significantly higher in Q1 due to number of the employers paying their deficit contribution in advance following the implementation of new contribution rates.

6. An indication of the current membership trends is shown by movements in membership over quarters one-two, compared to the position at the 2019 valuation (as taken from statistics provided by the pension administration team):

Period	Active members	Deferred members	Pension members	Total members
2019 valuation (31 Mar 2019)	36,469	31,993	26,015	94,477
Quarter One 2020/21 (1 Apr 2020 – 30 Jun 2020)	36,834	39,291	27,460	103,585
Quarter Two 2020/21 (1 Jul 2020 – 30 Sept 2020)	37,510	40,598	27,802	105,910

CONSULTATION:

7. The Chairman of the Pension Fund has been consulted and offered full support for the proposals.

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RISK MANAGEMENT AND IMPLICATIONS:

8. The Fund will keep the cash-flow position under review and ensure the investment strategy remains consistent and appropriate.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

9. There are no financial and value for money implications.

DIRECTOR OF CORPORATE FINANCE COMMENTARY

10. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered.

LEGAL IMPLICATIONS – MONITORING OFFICER

11. There are no legal implications or legislative requirements

EQUALITIES AND DIVERSITY

12. Cash-flow analysis does not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

13. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

14. The following next steps are planned:

A cash-flow analysis update to be provided to the Committee at least quarterly. The next report will be produced for the 12 March 2021 meeting.

Contact Officer:
Ayaz Malik, Pensions Finance Specialist

Consulted:
Pension Fund Committee Chairman.

Annexes:
None

Sources/background papers:
Administration performance monitoring progress log

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **11 DECEMBER 2020**

LEAD OFFICER: **ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**

SUBJECT: **EXIT CAP DECISIONS**

SUMMARY OF ISSUE:

Strategic objectives	
Governance	Delivery

This report provides the Pension Fund Committee with details of urgent decisions made regarding the processing of exit payments for eligible local government employees, including that which required an officer delegated decision from the Executive Director of Resources (Section 151 officer) and Director of Law and Governance (Monitoring Officer) in consultation with the Chairman of the Pension Fund Committee.

RECOMMENDATIONS:

That the Pension Fund Committee:

1. Notes the details of this report.

2. Note the Local Board's concern at the position that the Fund has been placed in due to conflicts between the Restriction of Public Sector Exit Payments Regulations 2020 and the Local Government Pension Scheme Regulations 2013.

REASONS FOR RECOMMENDATIONS:

To provide the Pension Fund Committee with full transparency over the Surrey Pension Fund's compliance with the Restriction of Public Sector Exit Payments Regulations 2020 and the Local Government Regulations.

This meets the Fund's strategic governance and delivery objectives.

BACKGROUND:

1. On 4th November 2020, the government activated the legislation to introduce an exit cap for public sector termination payments. This has been enacted before the supporting legislation is in place and the Local Government Pension Scheme (LGPS) regulations have been amended.

2. Although the exit cap is in force, the other provisions are still being consulted on and are unlikely to be implemented until the new year. This has the effect of existing scheme regulations conflicting with the exit cap in key areas.

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3. The main area of conflict concerns members who are aged 55 and over and this obliges the fund to find pragmatic solutions until the situation is resolved.

4. This only applies to terminations where the effective date is after 3rd November 2020 and the employer is subject of the exit cap.

5. These conflicts require the Administering Authority to balance the different requirements of competing legislation and the proposed policy and, where relevant, have been approved by the Executive Director of Resources and Director of Law and Governance, in consultation with the Chairman of the Pension Fund Committee.

6. In reaching these decisions regard has been taken of the legal advice obtained by the Scheme Advisory Board (SAB. Regard is also taken of the letter from MHCLG to LGPS administering authorities dated 28 October 2020.

7. The Administering Authority decisions follow the principle of a prudent approach on the basis of potentially paying an additional balance rather than seeking to recover an overpayment.

8. Regulation 30(7) of the LGPS regulations requires the fund to pay unreduced pensions to members aged 55 and over who leave on the grounds of redundancy, business efficiency or mutual consent on grounds of business efficiency (compromise agreements). The immediate payment of pensions generates strain costs that can be considerable and may exceed the £95,000 cap. This creates a dilemma because the Fund is forced to navigate a pragmatic course between two conflicting pieces of legislation.

DETAILS:

Decision 1: Legislation in force should be observed and the following decisions only affect terminations that breach the £95,000 cap.

9. It should be noted that pending legislation includes provisions that may affect members whose packages are lower than the £95,000 cap and they may be introduced retrospectively.

Decision 2: Recommend for employers in the Fund to NOT pay discretionary compensation if they have a liability to a strain cost.

10. There may be situations where the employer cannot pay a strain cost if they pay discretionary compensation (they are required to pay a redundancy payment under ERA 1996) without breaching of the cap. The fund recommends to employers that they follow the SAB suggestion of refraining from paying discretionary compensation in these circumstances.

Decision 3: To use the generic public sector (GAD) factors as they address equality issues and any marginal shortfalls in funding can be made good at the triennial valuations.

11. If an employer releases an employee under regulation 30(7) it is required to make a payment to the pension fund to compensate it for paying the pension earlier and for longer. This is known as a strain cost. A decision is required on how this is calculated:
    - Using our existing factors which are fund and gender specific;

- Adopt the draft unisex generic (GAD) public sector factors.

12. The draft public sector Government Actuarial Department (GAD) factors will provide consistent results and there will be no differences in notional costs between men and women and different employers within the public sector. The generic factors will lead to lower headline strain costs for a variety of reasons and, therefore they will be less likely to breach the cap; however, they will be unlikely to cover the true costs of early within local government.

Decision 4: To offer a deferred benefit or a reduced the pension under 30(5) as it can be re-calculated retrospectively. 7

13. There will be occasions where the strain costs alone will exceed the exit cap and the Fund is forced to choose between breaching the scheme regulations by offering a deferred pension under 6(1), paying a reduced pension under 30(5) or paying an unreduced pension. If it opts the latter, it may not be able to recover the whole strain cost at exit and the employer may resist making good the shortfall at the triennial valuation by arguing that the additional payments would exceed the exit cap.

14. It should be noted that the member could appeal this decision on the grounds that it is technically ultra vires as it conflicts with the scheme regulations. It is understood that the Pensions Ombudsman is willing to fast track exit cap cases and we can review our recommendations in the light of the case law.

Decision 5: To apply the LGPS specific actuarial reductions.

15. If actuarial reductions are applied to members leaving under regulation 30(7) there is a decision to be made regarding whether to apply the standard scheme reductions or an alternative.

16. This is in keeping with a prudent approach, as they are likely to be higher than any generic public sector reductions that the government actuary may produce.

CONSULTATION:

17. The Chairmen of the Pension Fund Committee has been consulted on this report.

RISK MANAGEMENT AND IMPLICATIONS:

18. Risk related issues have been discussed and are contained within the report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

19. The performance of the Pensions Administration function does present potential financial and value for money implications to the Pension Fund. The monitoring of these implications is discussed within the report.

DIRECTOR OF CORPORATE FINANCE COMMENTARY

20. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

21. The Director of Law and Governance is satisfied that all legal issues have been considered and addressed.

EQUALITIES AND DIVERSITY

22. The approval of the various options will not require an equality analysis, as there is no major policy, project or function being created or changed.

7

OTHER IMPLICATIONS

23. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

24. Process will be implemented in accordance with the decisions as shown.

Contact Officer:
Neil Mason, Strategic Finance Manager

Annexes:

1. Delegated Officer Decision

Sources/background papers:

1. The Restriction of Public Sector Exit Payments Regulations 2020
https://www.legislation.gov.uk/uksi/2020/1122/contents/made

2. Exit cap information for LGPS administering authorities (LGA)
http://lgpslibrary.org/assets/gas/ew/Exit%20Cap%20AA%20v1.0.pdf

3. Letter from MHCLG to LGPS administering authorities
https://www.lgpsboard.org/images/PDF/letters/MHCLGtoLAs.pdf

Record of decision taken under delegated powers by a council officer

SURREY COUNTY COUNCIL

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Title:	**Local Government Exit Cap**
Divisions Affected:	Surrey Pension Fund
Key Decision:	Yes
Reason Key:	Conflict in legislation
Decision taken under delegation by virtue of:	Scheme of Delegation Part 3 – Specific Delegation to Officers FIN 16

Summary

On 4th November 2020, the government activated the legislation to introduce an exit cap for public sector termination payments. This has been enacted before the supporting legislation is in place and the Local Government Pension Scheme (LGPS) regulations have been amended.

Although the exit cap is in force, the other provisions are still being consulted on and are unlikely to be implemented until the new year. This has the effect of existing scheme regulations conflicting with the exit cap in key areas.

The main area of conflict concerns members who are aged 55 and over and this obliges the fund to find pragmatic solutions until the situation is resolved.
This guidance only applies to terminations where the effective date is after 3rd November 2020 and the employer is subject of the exit cap.

These conflicts require the Administering Authority to balance the different requirements of competing legislation.

Decision made

<u>Decision made:</u>

It was AGREED that:

1. The Surrey Pension Fund provide the option of either a deferred pension under regulation 6(1) or an immediate reduced pension under regulation 30(5) in line with the Government's recommendations.

<u>Reasons for Decision:</u>

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The decision follows the principle of a prudent approach, on the basis of potentially paying an additional balance rather than seeking to recover an overpayment. Regulation 30(7) of the LGPS requires the pension fund to pay unreduced pensions to members aged 55 and over who leave on the grounds of redundancy, business efficiency or mutual consent on grounds of business efficiency (compromise agreements). The immediate payment of pensions generates strain costs that can be considerable and may exceed the £95K cap. This creates a dilemma because the pension fund is forced to navigate a pragmatic course between two conflicting pieces of legislation. If the alternative option, to pay an unreduced pension, in line with regulation 30(7)is decided upon, there is a risk that: i) the pension fund could end up in the position of having to try and recover monies from the employer and/or the member; ii) the pension fund will not be able to obtain the whole strain cost from the employer; iii) the employer will be restricted to a maximum of £95k for all exit payments In reaching this decision regard has been taken of the legal advice obtained by the Scheme Advisory Board (SAB). Regard is also taken of the letter from MHCLG to LGPS administering authorities dated 28 October 2020.

Decision taken by:	Leigh Whitehouse (Executive Director of Resources) Paul Evans (Director of Law and Governance)
Decision taken on:	9 November 2020
To be implemented on:	16 November 2020

Alternative options considered

1. Pay an unreduced pension in line with regulation 30(7)

Summary of any financial implications

Offering a deferred or reduced pension risks challenge from the member seeking to enforce their rights under regulation 30(7). Regardless of the outcome of any challenge, this approach should result in the member receiving additional monies as:

i) an unreduced pension, or
ii) a cash alternative payment to the member, or

iii) a cash alternative paid to you to provide additional pension under regulation 31 or waive reductions under regulation 30(8).

Declarations of conflicts of interest

None

Consultation/Process Followed

Officer decision made after consultation with Councillor Tim Evans, Chairman of the Pension Fund Committee.

Background Documents	Exempt:
Local Government Association Exit cap information for LGPS administering authorities http://lgpslibrary.org/assets/gas/ew/Exit%20Cap%20AA%20v1.0.pdf	

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **11 DECEMBER 2020**

LEAD OFFICER: **ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**

SUBJECT: **MINISTRY OF HOUSING COMMUNITIES AND LOCAL GOVERNMENT – CONSULTATION ON THE REFORM OF LOCAL GOVERNMENT EXIT PAYMENTS**

Strategic objectives
Governance

SUMMARY OF ISSUE:

To provide details of the Ministry of Housing Communities and Local Government's (MHCLG) consultation on the reform of exit payments in local government and the response from Surrey.

RECOMMENDATIONS:

To note the report and annexe.

REASON FOR RECOMMENDATIONS:

The Pension Fund Committee will be made aware of all national initiatives with a consultation process with a response sent within stated deadlines, in accordance with the Fund's strategic governance objectives.

BACKGROUND:

1. The government announced in the Spending Review and Autumn Statement 2015 that it will continue to modernise the terms and conditions of public sector workers, by taking forward targeted reforms in areas where the public sector has more generous rights than most of the private sector. As part of this, the government committed to consulting on further cross public sector action on exit payment terms, to reduce the costs to the taxpayer of redundancy payments and ensure greater consistency between workforces.

2. In September 2020 the MHCLG issued a consultation on the government's proposals for reforming local government exit payment, as part of a wider programme of cross-public sector action on exit payment terms.

DETAILS:

3. The consultation outlines proposals to reform redundancy payments in local government are as follows:

- A maximum tariff for calculating exit payments of three weeks' pay per year of service. Employers could apply tariff rates below these limits;
- A ceiling of 15 months (66 weeks) on the maximum number of months' or weeks salary that can be paid as a redundancy compensation payment. Employers will have discretion to apply lower limits, as they do at present under 2006 Regulations;
- A maximum salary of £80,000 on which a redundancy compensation payment can be based, to be reviewed on an annual basis using an appropriate mechanism, for example: CPI (Consumer Prices Index).

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4. MHCLG also states a wish to introduce an element of choice into the current arrangements. To meet this objective, it proposes that for members of the LGPS who are at least 55 years old when made redundant, the benefits and the associated strain cost due from the employer should be limited as follows:
    - The strain cost cannot exceed the overall cap contained in the Exit Payment Regulations (£95k);
    - Strain cost will be further reduced by the value of any Statutory Redundancy Payment required to be paid (which the employee will still receive as a cash payment);
    - A further reduction would be made to reflect any voluntary payments made to cover grant of additional pension under regulation 31 of the LGPS Regulations 2013;
    - Any reduction in the strain cost due to the above limitations may be made up by the worker from his own resources;
    - The member will receive an actuarially adjusted pension benefit in line with the revised strain cost under these provisions.

Surrey's response

5. Surrey's response to the consultation (shown as Annexe 1) expresses concerns about the latest proposals and considers the proposals to be more problematic than the ones that were consulted on twice before in relation to exit payments.

6. Surrey considers the proposals depart significantly from the ones considered in previous consultations. They are much harsher than a simple £95,000 payment cap and moves from restricting the packages of high earners to a general reduction in the potential compensation package available for redundancy and early retirement, regardless of the member's earnings.

7. Surrey also opines that the proposals could reduce the options for employers to take measures designed to ensure that work forces are restructured efficiently, which could result in an ageing workforce and increased costs.

CONSULTATION:

8. The Chairman of the Pension Fund Committee has been consulted on this report

RISK MANAGEMENT AND IMPLICATIONS:

9. Risk related issues have been discussed and are contained within the report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

10. Financial and value for money implications are discussed within the report.

DIRECTOR OF CORPORATE FINANCE COMMENTARY

11. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

8

12. There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

13. This does not require an equality analysis, as there is no major policy, project or function being created or changed.

OTHER IMPLICATIONS

14. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

15. The following next steps are planned:

- Provide the Pension Fund Committee with details of the results of the consultation.

Contact Officer: Neil Mason, Strategic Finance Manager (Pensions)

Consulted:
Pension Fund Committee Chairman

Sources/background papers:

1. The MHCLG consultation on the reform of exit payments in local government
http://lgpslibrary.org/assets/cons/lgpsew/20200907_CD.pdf

Annexes:

1. Surrey County Council response to the MHCLG consultation on the reform of exit payments in local government

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E-Mail: neil.mason@surreycc.gov.uk

Our Ref: LGPS Reforming Local Government Exit Pay Consultation

Your Ref:

8

Local Government Finance Stewardship
Ministry of Housing, Communities and Local Government
2nd Floor, Fry Building
2 Marsham Street
London
SW1P 4DF

LGPensions@communities.gov.uk

By email

9th November 2020

Dear Sir or Madam,

Local Government Pension Scheme: Reforming Local Government Exit Pay

Surrey County Council (Surrey) welcomes the opportunity to respond to the consultation on proposed amendments to the statutory underpin.

Surrey is the Administering Authority for the Surrey Pension Fund (the Fund) as part of the Local Government Pension Scheme (LGPS). The Fund has assets of over £4billion and includes nearly 300 employers.

Surrey has concerns about the latest proposals and it has articulated them in its response the questions posited in the consultation below:

The Fund considers these proposals to be more problematic than the ones that were consulted on twice, which many practitioners criticised as being impractical, and it is surprised that the Ministry of Housing Communities & Local Government (MHCLG) *"is not seeking views or representations on the government's position regarding exit pay reform"*.

Question 1: Are there any groups of local government employees that would be more adversely affected than others by our proposed action on employer funded early access to pension?

8

Members who leave employment aged 55 and over are more affected than other groups - particularly if they would otherwise have had an immediate entitlement to unreduced pension benefits.

These proposals are more regressive than previous iterations as they oblige members who are made redundant to defer or draw a reduced pension, unless their lump sum compensation exceeds their strain cost. The focus on the £95,000 cap is misleading; it would be more accurate to describe these proposals as eviscerating compensation payments with additional penalties for packages exceeding £95,000.

For example, a member with relatively low pay, with 30 years' service, a £15,000 statutory redundancy payment and a £20,000 strain cost would be forced to take the £15,000 redundancy payment and pay a £5,000 partial strain cost to lower the reductions to their pension. Conversely, a higher earner with 15 years' service, a £30,000 redundancy payment and a £20,000 strain cost could draw an unreduced pension **and** receive a £10,000 compensation payment. The reason for this stark anomaly is that the redundancy payment must be offset against the strain cost, unless it exceeds the strain cost when the excess can be paid.

The Fund considers that offsetting statutory redundancy payments (which must be paid) against strain costs will have a disproportionate impact on the low paid.

Question 2: What is the most appropriate mechanism or index when considering how the maximum salary might be reviewed on an annual basis?

The Fund considers Average Earnings to be the most appropriate index for reviewing the earnings cap. It reflects average earnings and the real economy.

Question 3: Are there any groups of local government employees that would be more adversely affected than others by our proposed ceiling of 15 months or 66 weeks as the maximum number of months or week's salary that can be paid as a redundancy payment?

Very few leavers receive any compensation in excess of a statutory redundancy payment unless they are under 55 and leave without an immediate entitlement to unreduced pension benefits. Employers tend to use multiples of the redundancy ready reckoner to calculate discretionary compensation and it is highly unusual for employers to award more than 66 weeks.

Question 4: Are there any groups of local government employees that would be more adversely affected than others by our proposal to put in place a maximum salary of £80,000 on which an exit payment can be based?

Employees who earn more than £80,000 per annum are adversely affected. However, if the 66 weeks / 15 months limits engage that threshold drops below £80,000 as, otherwise, the £95,000 limit would be breached. If the 66 weeks or 15 months limits apply the pay figure is effectively restricted, which means that employees earning more than £74,848 are potentially adversely affected by the new proposals. 8

The Government's has imposed an £80,000 limit on pay for calculating exit payments in local government; however, the Local Government Association has pointed out that it has allowed the civil service to retain its £149,500 limit, which seems to cut across its stated policy aim of "fairness and consistency". Although the Government is intent on imposing an earnings limit, it seems to be conflicted about where that threshold should be set.

If so please provide data/evidence to back up your view?

Please see previous answer.

Question 5: Do you agree with these proposals? If not, how else can the Government's policy objectives on exit pay be delivered for local government workers?

It is not clear to the Fund what the underlying policy intention is. It was originally trailed as means of curtailing payments to high earners; however, respondents to the previous consultations pointed out that the (then) arrangements could adversely affect members earning as little as £23,500 per annum. In response to these observations in previous consultation the Government has instead introduced proposals that will potentially hit anyone who is made redundant, no matter how little they earn.

The proposals have changed dramatically and the Fund notes that the latest iteration is titled "Reforming Local Government Exit Pay". As the title implies, this proposal focuses on reducing exit payments across the board and probably ought to have been the subject a separate consultation.

The proposals concerning relaxing the cap are complicated and unwieldy. In particular, the proposal to refer a case approved by the full council to not only the Secretary of State for Housing Communities and Local Government but also, possibly, a Treasury minister.
The requirement to offset compensation payments against the strain cost unless they exceed the strain cost, when the excess compensation can be paid, means that most members who are made redundant will be forced to draw a reduced pension or defer their pension benefits. This is because the redundancy payment, which must

be paid, is offset against the strain cost even if the whole package is within the £95,000 cap. This provision is regressive, and it will have a disproportionate impact on low paid workers, many whom are women who work part-time.

One of the principle justifications offered for these proposals is that when someone is made redundant aged 55 or over *"… it sends the signal that their working life is over. In the modern world of work people have good reasons for wanting to work longer and someone made redundant in their late 50s may still look forward to a satisfying career for many years to come".* This is a very positive take on discouraging members aged 55 and over from drawing their pensions; however, it is predicated on the availability of employment opportunities for this cohort of workers.

8 **Question 6: Do you agree that the further option identified at paragraph 4.8 should be offered?**

The proposal to offer members aged 55 and over the option to defer their pension benefits and draw a redundancy / compensation payment instead of an unreduced pension appears to be a natural concomitant to the change in policy. The proposals appear to be designed to encourage members to take lump sum compensation. It should be noted that lump sum compensation can have potential tax implications, as compensation payments above £30,000 attract Income Tax. A lower rate taxpayer leaving mid-way through the year could find themselves paying upper rate tax on part of their package. Employees receiving anything approaching a £95,000 compensation payment would be looking at a substantial upper rate tax charge.

Question 7: Are there any groups of local government employees that would be more adversely affected than others by our proposals?

There are groups of employers such as universities, sixth form colleges and certain admitted bodies who are not covered by these proposals. The employees of local government employers who are covered by these proposals are adversely affected in comparison to the ones who are not.

All members who are affected by these proposals will lose out in comparison to the existing provisions. However, the impact of the loss will vary depending on whether it is weighed in absolute or relative terms, with. high earners tending to lose the most in absolute terms. However, the relative losers are likely to be low earners who will see their termination packages significantly eroded by these proposals.

As respondents to earlier consultations pointed out, these measures are unlikely to affect very high earners because they are likely to have input into; their remuneration package, their reason for and timing of leaving, the prospect of an Employment Tribunal, the possibility of a waiver. It is unfortunate that a measure originally promoted as being targeted at high earners is now likely to have a big impact on median and (particularly) low earners.

Although it is the only progressive measure put forward, the proposal to allow members whose compensation payments exceed their strain cost to benefit from the difference is potentially indirectly age discriminatory because it favours older members within the over 55 demographic. This is because (1) older members tend to have more service and bigger redundancy payments and (2) actuarial reductions fall away as they approach retirement and the strain costs diminish.

This policy started out as a £95,000 cap on high earners' exit payments in 2015 and has subsequently morphed into something much harsher as the £95,000 cap, has not been index linked and the policy intention appears to have moved from a cap on high earners to a general levelling down of exit payments. Again, as noted in responses to previous consultations, these proposals reduce the options for employers to take measures designed to ensure that work forces are restructured efficiently, which could result in an ageing workforce and increased costs.

The net effect is that members appear to be being incentivised, and in some cases forced, to draw lump sum compensation with an actuarially reduced/deferred pension instead of an unreduced pension. 8

How would you mitigate the impact on these employees?

The Government could mitigate the impact by incorporating feedback from previous consultations in its revised proposals.

Question 8: From a local government perspective, are there any impacts not covered at Section 5 (impact analysis) which you would highlight in relation to the proposals and /or process above?

These proposals seem to be predicated on the notion that early retirements/redundancies are just additional costs. In normal circumstances potential early retirements are supported by a comprehensive business case that shows the potential net savings to the organisation.

The direct and indirect costs in paragraph 5.6 focus on savings and the perceived benefits to local government without pausing to consider the arguments of previous consultation responses. It is more efficient and effective to restructure work forces consensually and these proposals could hamper employer flexibility in this area.

The Fund is of a view that the policy is poorly conceived. Early retirement costs are counter intuitive because the percentage reductions to annual pensions shrink as life expectancy increases; this is because early retirement is treated as a fixed overpayment and it can be recovered if life expectancy increases. As life expectancy is lower in local government than the public sector as-a-whole the early retirement costs would increase if local government specific factors were used. The imposition of generic factors by the Treasury serves to reduce the costs artificially, thereby delivering precisely the outcome that the Government sought to avoid and leaving pension funds in deficit.

The Treasury appears to view early retirement costs as standalone additional expenditure as opposed to one element of a costed business case. So far from saving money, this policy is likely to lose money and make it much harder to restructure workforces.

These proposals could make it more challenging to manage workforces if it results in a higher likelihood of employees resisting redundancy/early retirement. It is important to note that members who retire with unreduced pensions aged 55 and over will have a significantly smaller incomes in retirement than they would have enjoyed had they worked to normal retirement age.

These measures could encourage an ageing, highly paid work force that presents a challenge for succession planning.

The proposals mean that employees could be more likely to resist redundancy/early
retirement, and this could generate additional costs for smaller employers who may
not have the internal human resources / legal services capacity of larger
8 organisations. Even for larger organisations this could lead to unwelcome additional
costs.

The efficacy of these proposals needs to be judged in the round, not solely on the headline costs. The perceived saving for each early retirement needs to be weighed against increased numbers of appeals (IDRP), Employment Tribunals (ET) and, occasionally, Employment Appeals Tribunals (EAT) and - most importantly - the lost efficiency savings.

It appears that the Government has identified potential savings that practitioners think are unlikely to be realised in practice. Moreover, the long-term costs of having an increasingly aged and inflexible workforce are likely to be considerable.

Question 9: Are these transparency arrangements suitably robust? If not, how could the current arrangements be improved?

The Fund understands the Government's concern about the immediate re-employment of high earners, but, contends that this has largely been reduced due to the advent of flexible retirement. Flexible retirement facilitates the retention of key skills and less experienced officers being mentored into key positions. Any IR35 employees are usually recruited from agencies in order to acquire specialist skills that are not available within the organisation.

The Fund no longer uses the discretion to abate re-employed pensioners because it is not cost effective. The Fund understands that the funds who persevere with abatement have found that the cost of administering the scheme outweighs the overpayments recovered, without considering the costs of internal disputes from members. The Fund is aware that the biennial National Insurance data matching exercise run by Internal Audit uncovered significant overpayments when it was first introduced but the matches have dwindled in both number and the size of the overpayments over time. Although big overpayments were discovered in the first two or three exercises the latest ones mainly flag-up existing cases and false matches that take a lot of time to investigate. The few cases that are uncovered tend to be small overpayments as they should not be more than two years old.

Although this is not the intended locus of this question, it is important to note that these proposals depart significantly from the ones considered in previous

consultations and the Fund is surprised that the government *"is not seeking views or representations on the government's position regarding exit pay reform"*.
The Fund believes that the Government should consult on the new package because, amongst other things, it has a much bigger impact on low earners than the original proposals.

Question 10: Would any transitional arrangements be useful in helping to smooth the introduction of these arrangements.

A transitional period would be helpful because it would enable employers to carry out carefully considered strategic restructures that realise genuine savings.

Question 11: Is there any other information specific to the proposals set in this consultation which may be relevant to the reforms. 8

These proposals go further than previous iterations and they have moved from restricting the packages of high earners to a general reduction in the potential compensation package available for redundancy and early retirement, regardless of the member's earnings. This is a major shift in both content and underlying philosophy and, in the Fund's opinion, merits a separate consultation.

The rationale behind the proposals appears to be to save money and yet the way the way it has been structured has the (unintentional) consequence of frustrating considered early retirements that would deliver measurable savings.

Question 12: Would you recommend anything else to be addressed as part of this consultation?

The Fund believes that the proposals have changed significantly from previous iterations and that the new elements should be consulted upon properly.

The Fund is disappointed that each subsequent iteration of this proposal does not appear to have incorporated sensible observations contained in the responses to previous consultations and instead progressively moved away from the original policy intention, which was to curtail the exit payments of high earners.

On the 4th November, in the middle of a consultation, the £95,000 exit cap was enacted without any of the supporting or amending legislation required. This has forced practitioners to try to navigate a course between two competing tranches of legislation.

Yours sincerely

Anna D'Alessandro

Director of Corporate Finance
Surrey County Council

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **11 DECEMBER 2020**

LEAD OFFICER: **ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**

SUBJECT: **MINISTRY OF HOUSING COMMUNITIES AND LOCAL GOVERNMENT – CONSULTATION ON AMENDMENTS TO THE LOCAL GOVERNMENT PENSION SCHEME STATUTORY UNDERPIN**

Strategic objectives
Governance

9

SUMMARY OF ISSUE:

To provide details of the Ministry of Housing Communities and Local Government's (MHCLG) consultation on amendments to the Local Government Pension Scheme (LGPS) statutory underpin and the response from Surrey.

RECOMMENDATIONS:

To note the report and annexe.

REASON FOR RECOMMENDATIONS:

The Pension Fund Committee will be made aware of all national initiatives with a consultation process with a response sent within stated deadlines, in accordance with the Fund's strategic governance objectives.

BACKGROUND:

1. In July 2020 the MHCLG issued a consultation on amendments to the LGPS statutory underpin, which provided transitional protection to older workers when they moved from the 2008 scheme into the 2014 Scheme.

2. The consultation outlines proposed changes to the LGPS statutory underpin protection to remove unlawful discrimination following a successful legal challenge to transitional protection arrangements in the firefighters' and judicial pension schemes (the McCloud and Sergeant cases).

3. Specifically, it proposes to remove the condition that required a member to have been within ten years of their normal pension age on 1st April 2012 to be eligible for underpin protection. In removing the discrimination, it proposes a number of supplementary changes to ensure the revised underpin works effectively and consistently for all members.

DETAILS:

4. MHCLG propose to remove the age requirements from the underpin qualification criteria. Furthermore, they are also proposing additional changes to ensure that the underpin works effectively and consistently for all qualifying members following the extension of the underpin to younger members.

5. From April 2022, it is proposed that the period of underpin protection will cease and all active LGPS members will accrue benefits in the career average scheme, without a continuing final salary underpin.

Surrey's response

6. Surrey's response to the consultation (shown as Annexe 1) is supportive of
9 most of the proposals although it thinks that adjustments are needed in order to eliminate age discrimination.

7. Surrey posits that the replacement for the original (flawed) underpin should have been designed from scratch, as, by recycling elements of the original mechanism MHCLG appears to have inadvertently introduced direct age discrimination that curtails the final salary membership of older members who could, otherwise, have remained in the 2007 scheme until 31st March 2022.

8. Surrey recommends making the provisional underpin the earlier of 31st March 2022 and the date of leaving active membership and that serious consideration is given to extending the underpin to all members who were active on 31st March 2014.

CONSULTATION:

9. The Chairman of the Pension Fund Committee has been consulted on this report

RISK MANAGEMENT AND IMPLICATIONS:

10. Risk related issues have been discussed and are contained within the report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

11. Financial and value for money implications are discussed within the report.

DIRECTOR OF CORPORATE FINANCE COMMENTARY

12. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

13. There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

14. This does not require an equality analysis, as there is no major policy, project or function being created or changed.

OTHER IMPLICATIONS

15. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

16. The following next steps are planned:

    - Provide the Pension Fund Committee with details of the results of the consultation.

9

Contact Officer: Neil Mason, Strategic Finance Manager (Pensions)

Consulted:
Pension Fund Committee Chairman

Sources/background papers:

1. The MHCLG consultation on amendments to the LGPS statutory underpin
   http://lgpslibrary.org/assets/cons/lgpsew/20200716_CD.pdf

Annexes:

1. Surrey County Council response to the MHCLG consultation on amendments to the LGPS statutory underpin

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Surrey Pension Fund

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Our Ref: LGPS Underpin Consultation
Your Ref:

Local Government Finance Stewardship
Ministry of Housing, Communities and Local Government 9
2nd Floor, Fry Building
2 Marsham Street
London
SW1P 4DF

By email LGPensions@communities.gov.uk

5th October 2020

Dear Sir or Madam,

Local Government Pension Scheme: Amendments to the statutory underpin

Surrey County Council (Surrey) welcomes the opportunity to respond to the consultation on proposed amendments to the statutory underpin.

Surrey is the Administering Authority for the Surrey Pension Fund (the Fund) as part of the Local Government Pension Scheme (LGPS). The Fund has assets of over £4billion and includes nearly 300 employers.

Surrey is supportive of most of the proposals although it thinks that adjustments are needed in order to completely eliminate age discrimination. We set our response the questions posited in the consultation below:

Question 1 – Do you agree with our proposal to remove the discrimination found in the McCloud and Sargeant case by extending the underpin to younger scheme members?

Surrey County Council (the Fund) agrees that the underlying discrimination should be addressed but it believes that the suggested remedy is flawed.

Question 2 - Do you agree that the proposed underpin should end in March 2022?

The original underpin was due to end on 31st March 2022 and the Fund agrees that it is a natural watershed and it cannot see any logical reason for extending it.

Question 3 – Do you agree that the revised regulations should apply retrospectively to 1st April 2014?

The regulations that introduced the discrimination came into force on 1st April 2014 and, therefore, it is logical that the remedy should also take effect from that date.

Question 4 - Do the regulations implement the revised underpin which we describe in this paper?

The draft regulations appear to implement the proposed remedy effectively; however, the Fund believes that the remedy is flawed and may itself be age discriminatory.

9 **Question 5 - Do the draft regulations provide a framework of protection which would work effectively for members, employers and administrators?**

There will be challenges in collating data, identifying resources and communicating with members and employers. Employers are only required to retain payroll data for six years, records are already degrading and there needs to be clear guidance on how to handle cases where the records are incomplete. It is the Fund's view that the remedy does not cover all members equitably and would benefit from considered amendments.

Question 6 – Do you have comments on technical matters related to the draft regulations?

The consultation appears to postulate that, for an active member, the provisional underpin date and underpin crystallisation date will always be the date of death. However, this will not be the case if the member is aged 65 or over at the date of death and this is one of several reasons why the Fund thinks that the provisional underpin date should be the earlier of the date of leaving active membership and 31st March 2022.

The Fund accepts that a few ill-health retirements may benefit from an underpin, particularly if they left before state pensionable started to rise; however, this is becoming less likely (longer enhancements in the current scheme). Moreover, the members who are likely to benefit from the 2007 scheme ill-health enhancements are either close to retirement or part-timers who previously worked full-time - and the former group are protected by regulation 12 of the Transitional Regulations if they were aged 45 or over before 1st April 2008 in any case. For these reasons it would be much simpler to exclude ill-health retirements from the underpin arrangements although the Fund accepts that it is a sensitive topic as the most likely losers are part-timers, the majority of whom are women.

Question 7 – Do you agree that members should not need to have an immediate entitlement to pension at the date they leave the scheme for an underpin protection to apply?

If the intention is to remove the link to retirement and to introduce a general protection to the 31st March 2022 or the date of leaving active membership, if earlier, then it makes sense to remove the requirement to have an immediate entitlement to retirement benefits.

The old underpin created a dichotomy even within the protected group as those who left with preserved benefits were not covered and the extension of the new underpin to (almost) all age groups risks exacerbating that problem. Offering the underpin to members who leave with preserved benefits addresses the problem, given that younger members are more likely to leave with an entitlement to preserved benefits, but it creates administrative issues. It will be much harder to collate, retrieve or reconstruct data for members who left some time ago.

In the Fund’s opinion the remedy is reminiscent of the flaws in the 85-year rule transitional protection. MHCLG focused its attention on the members who narrowly missed out on protection (group B members) in that exercise but, in doing so, it put some of them in a better position than the originally protected group (group A members). This was because members who reached 60 shortly after 2016 suffered miniscule actuarial reductions but their pension was protected until 2020 instead of 2016. It appears that the suggested underpin remedy also has the potential to put younger members in a better position than the original group but, fortunately, this could be addressed with minor changes.

Question 8 – Are there any other comments regarding the proposed underpin qualifying criteria you would like to make?

9

The proposed remedy seems to extend the underpin to 31st March 2022 for all members, except those who reach age 65. This limit was a feature of the old underpin set aside by the Court of Appeal and it seems incongruous to include it in the proposed remedy as there was no mandatory scheme retirement age in the 2007 scheme. If a member continued working beyond age 65 they would simply have continued to accrue 60ths and it seems counterintuitive to insert an arbitrary deadline that appears to discriminate against older members.

Persevering with the age 65 deadline will affect some members whose SPA is 66 or later and it seems to complicate matters unnecessarily. The Fund believes it would be both logical and simple to make the test for the provisional underpin the earlier of the date of leaving active membership and 31st March 2022.

Conversely, there is an argument that says it is unfair to restrict the extension of 2007 scheme to members who were active on both 31st March 2012 and 31st March 2014. It would be certainly be simpler to offer the underpin to all members who were active on 31st March 2014 and it would make it much easier to determine eligibility. The two dates requirement is an unnecessary vestige of the defunct underpin but, given that it applies to all members equally and without exception, it does not appear to be inherently age discriminatory.

Question 9 – Do you agree that members should meet the underpin qualifying criteria in a single scheme membership for underpin protection to apply?

This addresses an anomaly in the existing underpin provisions and it is both logical and consistent with the intention that the underpin should relate to a single employment. Nonetheless, and notwithstanding reopening the aggregation window, there will be potential losers and a thorough impact assessment should be undertaken and digested before the final regulations are drafted

Question 10 Do you agree with our proposal that certain active and deferred members should have an additional 12 month period to decide to aggregate previous LGPS as a consequence of the proposed changes?

Re-opening the aggregation window is necessary if the underpin is to be restricted to a single employment and this resource has been used in similar circumstances before, most recently in

2011. However, unlike previous exercises, the proposed option is not a general reopening of the aggregation window but, rather, a targeted one focused members who might lose out if they can no longer rely on an underpin straddling two employments. This will be very difficult to administer not least because many of the members who might qualify for an underpin in relation to two separate employments may not be aware that they are entitled to one. How will the limited option to aggregate work in practice; will it be restricted to members who potentially benefit from an underpin, regardless of whether they actually qualify or not, or simply to the ones who are already entitled to an underpin – even though many of them may not even know that they are eligible? It is evident that potential cases can only be identified by administrators and software providers and doing this, and presenting the options to eligible members, will require considerable resource.

If a member has a pre-2014 preserved benefit and a post-2014 benefit without a disqualifying break it is also necessary to reopen the election window under regulation 5(5) of the Transitional Regulations 2014, or deem them to have made an election, in order for them to benefit from a final salary underpin.

9 It should be noted that reopening the aggregation window is not a complete solution for the loss of an underpin straddling two separate employments. This is because members would only be able to retain an existing guarantee by making a committal decision (to aggregate), which may not necessarily be to their advantage. Although the proposed remedy will mitigate the potential detriment, unfortunately, it will not remove it entirely.

It makes sense, although it is unusual, to extend the option to aggregate to deferred beneficiaries although it is not clear how it would work in practice and the same policy concerns that affect active aggregations also apply here. Moreover, how would you treat a member who had suffered a big pay drop and elected to keep their pension benefits separate only to become a deferred beneficiary in the second employment within two years; although they were eligible for an underpin in the original employment they would cease to qualify unless they elected to aggregate? Happily, aggregating would work well for this member because they can elect to have their pension benefits calculated under regulation 8 of 2007 benefit regulations (best of the last three years). However, this provision has the potential to be unfair to employers because members can transfer substantial pension benefits – as long as it is to their advantage - thereby disturbing long-standing funding positions. This is most likely to happen when members opt for preserved benefits following a big pay drop - only for their career to take off again and their final pay to increase significantly allowing for inflation, although this is unlikely to be common in practice.

The option to aggregate benefits is not open to members who opted out after 11th April 2015, which means that some members who may be adversely affected may not have a remedy to hand. It may be worth considering relaxing this restriction for a year for underpin cases in the interests of consistency – although there are contrary arguments.

Turning to members who suffer a major pay cut in a single employment, should we simply alert them to the options of aggregating or keeping their pension benefits separate or should we draw their attention to the possibility of doing nothing and invoking regulation 10 (a three year pay average in the last ten years) which would protect their higher pay - and their underpin – for ten years. This may not seem attractive to members who are more than ten years from retirement which, in turn, begs the question of whether it is ethical to mention that they can invoke regulation 10 and subsequently elect to opt-out up to ten years after the material reduction, thereby cementing their higher final pay/underpin - albeit that this approach is not without risk.

The policy intention appears to be to leave pensions that are already in payment with underpins alone and this is sensible as to reduce them would not only be unfair but technically challenging.

Question 11 – Do you consider that the proposal in paragraphs 50 to 52 would have "significant adverse effects" in relation to the pension payable to or in respect of affected members, as described in section 23 of the Public Service Pensions Act 2013?

Members who chose to keep their pension benefits separate following a substantial reduction in pay and who currently benefit from an underpin, would lose it unless they aggregate their pension benefits under the current proposals. It would seem rational - depending on circumstances - to keep the benefits separate unless the new underpin would produce a better outcome, which may not be clear until the provisional underpin date or, possibly, the underpin crystallisation date. The Public Sector Pensions Act 2013 requires the responsible body proposing the changes to first obtain the consent of the members who are significantly adversely affected - or their representatives - in order to make retrospective changes. Although relatively few members are likely to be significantly adversely affected it is not immediately clear how the responsible authority would obtain their consent without offering concessions and it may be necessary to submit a report and seek affirmation from both Houses of Parliament.

9

The replacement for the original (flawed) underpin should have been designed from scratch. Unfortunately, in recycling elements of the original mechanism MHCLG appears to have inadvertently introduced direct age discrimination that curtails the final salary membership of older members who could, otherwise, have remained in the 2007 scheme until 31st March 2022. As the original underpin is considered unlawful and the proposed underpin effectively extends the old scheme to 31st March 2022, it is arguable that MHCLG is obliged to obtain older member's consent for this potential diminution of their pension benefits.

Question 12 – do you have any comments on the proposed amendments described in paragraphs 56 to 59?

The proposals are generally progressive, reasonable and consistent with the policy intentions. Although the element of retrospection is logical it will present challenges in collecting/recovering data that may have been eroded or destroyed. It would be helpful if SAB could produce clear and pragmatic guidance on how to address these issues.

Question 13 – Do you agree with the two stage underpin process?

It is a pragmatic solution to have a provisional underpin date and an underpin crystallisation date. The provisional calculations can be performed when the member leaves employment, and accurate records are available, and the final adjustments can be made at the date they eventually crystallise their pension benefits, which may be many years later.

The two-stage process has the potential to create annual allowance complications which are considered in question 18 below.

Question 14 – Do you have any comments regarding the proposed approaches outlined above?

If a member aged 65 or over without a five-year gap re-joins the LGPS before 31st March 2022 they would not benefit from an underpin and this appears to be overtly age discriminatory. It is a discordant feature of the new underpin that it extends the best of both schemes' protection for all members until 31st March 2022, unless they happen to be older ones.

The fund would like to see more detail about the proposals covering club transfers and how the mechanism would work in practice. It does not object to members being asked to make a committal decision in principle as this was a feature of previous iterations of the club memorandum, which allowed members to elect for a non-club transfer if that would give a better outcome (usually if they had taken a large reduction in pay or they were aged 63 or over).

Question 15 – Do you consider there to be any notable omissions in our proposals on the changes to the underpin?

There is one commission that the Fund believes needs to be addressed; the age 65 limit should be removed because it is directly age discriminatory.

Question 16 – do you agree that annual benefit statements should include information about a qualifying member's underpin protection?

The Fund believes that annual benefit statements are already too complicated for a lot of
members to understand and adding more information simply exacerbates the problem. As the
underpin is a guarantee it might be better to omit it from ABS at least until the run up to
9 retirement, if not retirement.

Underpins are likely to be few and (usually) low in value to start with - but they will become increasingly common and grow in value over time. As a rule, the further a member is from retirement on 31st March 2022 the larger any eventual underpin is likely to be and, therefore, it might be better to omit them from standard ABS.

Question 17 –Do you have any comments regarding how the underpin should be presented on annual benefit statements.

If it is a policy decision to include underpin information in ABS a lot will depend upon what the software providers can deliver. It would seem logical that the notional ABS underpin for active members should be based on the assumption that they left active membership on 31st March each year, excluding regulation 8 and regulation 10 protections which are time limited, and deferred member's provisional underpins could be updated each year automatically.

Question 18 - Do you have any comments on the potential issue identified in paragraph 110?

On balance SCC believes that the underpin should be tested against the annual allowance / lifetime allowance at the underpin crystallisation date. It expects underpins to be modest in the short to medium term and unlikely to generate tax charges unless the member is a high earner or has enhanced their pension benefits significantly. Moreover, there is a possibility that, otherwise, a few members may incur an annual allowance tax charge but not qualify for an underpin when they eventually leave active membership.

Ideally the Fund would prefer a fluid approach with an eye to moving to an annual assessment in the medium to long-term if – as seems likely – the median underpin grows in value over time. This way, the increase would be staggered and be less likely to generate an annual allowance tax charge than assessing it in one fell swoop at the underpin crystallisation date; however, the fund accepts that the Treasury is unlikely to be sympathetic to this idea.

Although the Fund advocates a utilitarian approach, it accepts that it is finely judged decision and there will be winners and losers whichever approach is adopted.

Question19 – Do the proposals contained in this consultation adequately address the discrimination found in the “McCloud” and “Sargeant” cases?

The remedy addresses the discrimination identified in the above cases but the Fund thinks that it inadvertently introduces direct age discrimination.

The original underpin was a time-limited protection for older members and it was reasonable to cap it at “normal” retirement age even though there was no formal retirement age in the 2007 scheme and members could continue to accrue 60ths until the day before their 75th birthday.

The old underpin has been swept away and replaced by a guarantee that offers the better of the old and the new scheme for all active members until 31st March 2022 - unless they happen to be older members.

Another way of looking at it is that members who could otherwise have remained in the 2007 scheme until age 75 are being expelled from the best of both schemes lifeboat at age 65 by a measure intended to address age discrimination. The proposed remedy arbitrarily restricts the protection to age 65, regardless of whether the member has reached state pensionable age (pensionable age in the current scheme) or not. 9

What would or should have been a general guarantee to 31st March 2022 has been undermined by a, perhaps understandable, desire to recycle elements of the existing underpin. The new underpin is an entirely new and separate entity that must be judged on its merits and there does not appear to be any objective justification for imposing an arbitrary age limit on what is, otherwise, a universal protection. This appears to be direct age discrimination and the judgement in Walker v Innospec suggests that its proponents cannot take any comfort from the pension regulations exemptions in the Equality Act 2010.

Question 20 - Do you agree with our equalities impact assessment?

The Fund has concerns about the equality impact.

The proposed underpin is predicated on ensuring that members are no worse off than they would have been had they remained in the 2007 scheme until 31st March 2022 and yet it excludes older members who could otherwise have continued in the old scheme until 2022. The remedy removes one form of age discrimination, namely the requirement to be within ten years of retirement, and introduces another because the underpin is extended to 2022 for everyone, except those who reach age 65 in the meantime. The impact of this anomaly is illustrated by a member with a SPA of 66 who reaches age 65 on 31st March 2021, is awarded a provisional underpin but cannot draw their pension benefits without reductions until 31st March 2022.

The underpin is no longer an age-related protection and it is, or should be, a general guarantee. It would be both simple and logical to extend the provisional underpin to the earlier of 31st March 2022 and the date the member left active service. It would be both easier to administer and cost very little as few members benefit from significant pay rises close to retirement and fewer still work beyond age 65.

Few of the original cohort benefited from an underpin but younger members are likely to benefit considerably from the extension of the underpin when they eventually retire. That is happy development for the younger members but the (very) few older members who might benefit from the removal of the arbitrary age 65 limit should not be treated unfairly.

The Fund is aware that some commentators have advanced a counterintuitive argument that the age 65 restriction is intended to favour younger members who have lost access to a final salary pension scheme. In fact, the government has imposed a general deadline on 31st March 2022, it does not favour younger members and neither do they benefit from older members being treated less favourably. The Fund believes that the age 65 limit merely introduces direct age discrimination against older members.

Question 21 – Are you aware of additional data sets that would help assess the potential impacts of the proposed changes on the LGPS membership, in particular for the protected characteristics not covered by the GAD analysis (age and sex)?

No.

Question 22 – Are there any other comments or observations on equalities impacts you would wish to make?

The Fund's views are set out in questions 9, 19 and 20.

9 **Question 23 – What principles should be adopted to help members and employers understand the implications of the proposals outlined in this paper?**

The key to engaging with members and employers is a carefully considered programme of communications and the fund touches on this below.

Question 24 – Do you have any comments to make on the administrative impacts of the proposals outlined in this paper?

All qualifying leavers must be identified and have their pension benefits reviewed as soon as possible in order to determine whether the revised underpin will apply. The scheme employers will have to be contacted promptly in order to optimise the data available and to give them the best chance of recovering / reconstructing incomplete records.

Data collection / cleansing will consume significant additional resources in both employing and administering authorities. It is critical to engage with actuaries and software providers as soon as possible and, although some of the work can be performed electronically, it will require substantial manual intervention and this demands resources.

A structured communication plan is vital and generic material produced by SAB/LGA should be used as much as possible. Targeted messages should be delivered using websites, regular newsletters, brief messages on payslips and annual benefit statements augmented by sending more detailed general letters to members and specific ones to members who have suffered tax charges or are leaving with provisional underpins. In all cases the content should be carefully calibrated for the intended audience (e.g. members, dependants and employers).

Question 25 – What principles should be adopted in determining how to prioritise cases?

Members who were active on 31st March 2012, accrued benefits after 1st April 2014 and who have died, retired, transferred out or left must be prioritised. This is because the payroll and the membership records required to calculate final salary benefits are gradually degrading and the six-year requirement to maintain payroll records has already expired for some members. Moreover, some employers will have changed payroll providers, lost experienced payroll managers and suffered other misfortunes that can slowly erode data quality.

This is a real challenge as details of final pay, part-time hours, changes of hours, aggregated concurrent employments etcetera may not have been maintained properly since 2014.

Question 26 – Are there material ways in which the principles could be simplified to ease the impacts on employers, software systems and scheme administrators?

The Fund believes that the provisional underpin date should be simplified to the earlier of the date the member leaves active employment and 31st March 2022. This makes it simpler for everyone as it avoids the differential actuarial reductions of members who are capped at 31st March 2022 but are not eligible to retire until age 66 or older. It is also a simpler message to convey to members, employers and administrators and no additional work for software providers as they would have to write new calculation routines anyway.

Question 27 – What issues should be covered in administrative guidance issued by the Scheme Advisory Board, in particular regarding the potential additional data requirements that would apply to employers?

It would be very helpful if SAB could publish a generic guidance on collating/recovering data where records are incomplete. It is important to have carefully considered pragmatic solutions that would help to ensure consistency across the LGPS.

9

Question 28 – On what matters should there be a consistent approach to implementation of the changes proposed?

The Fund believes that the underpin should be treated as a general guarantee for all eligible members – without exception - until the earlier of 31st March 2022 or the date of leaving active membership.

Question 29 – Do you have any comments regarding the potential costs of McCloud remedy, and steps that should be taken to prevent increased costs being passed to local taxpayers?

Our actuaries built a generous contingency into the funding model and we expect the proposed remedy to fall within the anticipated cost envelope. They also expect pay increases in the LGPS to fall well below the generic assumptions the Government used for the whole of the public sector because pay increases in local government are expected to be lower. However, the good news is tempered by the costs of identifying cases and implementing the remedy, which are likely to be considerable, and that is why the Fund advocates keeping the remedy as simple as possible. For this reason, we recommend making the provisional underpin the earlier of 31st March 2022 and the date of leaving active membership and that serious consideration is given to extending the underpin to all members who were active on 31st March 2014.

Yours faithfully,

Anna D'Alessandro
Director of Corporate Finance

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **11 DECEMBER 2020**

LEAD OFFICER: **ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**

SUBJECT: **NATIONAL KNOWLEDGE ASSESSMENT (NKA) RESULTS AND TRAINING PLAN**

SUMMARY OF ISSUE:

Strategic objectives	
Investment	Funding

The report sets out the results of the National Knowledge Assessment (NKA) conducted by Hymans Robertson. The aim of NKA was to identify where there are gaps in knowledge in Pension Fund committee members, and assist in devising an appropriate training plan.

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RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1. Note the NKA report (Annexe 1).
2. Note the results including the overall ranking of the Pension Fund Committee against other participating funds.
3. Note and approve the suggested training plan.

REASON FOR RECOMMENDATIONS:

Members of the Committee play a vital role in the scheme, and to exercise their roles effectively must be able to address all relevant topics including governance, administration, investment and actuarial methods.

DETAILS:

Background Information

1. In recent years there has been an increase in the scrutiny of public service pension schemes including the LGPS. The Chartered Institute of Public Finance and Accountancy (CIPFA) 2013 Code of Practice on Public Sector Pensions Finance Knowledge and Skills applies to all individuals that take on a decision-making, scrutiny or oversight role with respect to LGPS schemes, which includes the pension fund committee.

2. The Scheme Advisory Board Good Governance report Phase II also highlighted the need for LGPS scheme to maintain skills and knowledge were

assessed and maintained, to ensure that decision making and scrutiny bodies had the appropriate skills and knowledge to perform their roles.

3. Furthermore, the introduction of Markets in Financial Instruments Directive II (MIFID II) in January 2018 REQUIRED Committee members to evidence their knowledge in order to be treated as professional investors.

4. While fund officers may deal with the day-to-day running of the funds, pension fund committee members play an important role in the scheme, and to exercise their role effectively must to be able to address all relevant topics including governance, administration, investment and actuarial methods.

5. National Knowledge Assessment (NKA)

6. In order to assess the skills and knowledge of the Pension Fund Committee members, they were requested to participate in the LGPS NKA, conducted by Hymans Robertson based on the CIPFA Skills and Knowledge Framework for pensions. The assessment aimed to evaluate the current knowledge level of Pensions Committee members at a collective as well as individual level.

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7. Members were asked set of 47 questions on the 8 areas below:

    i. Committee Role and Pensions Legislation
    ii. Pensions Governance
    iii. Pensions Administrations
    iv. Pensions Accounting and Audit Standards
    v. Procurement and Relationship Management
    vi. Investment Performance and Risk Management
    vii. Financial markets and product knowledge
    viii. Actuarial methods, standard and practices

8. Overall Results

9. Annexe 1, summarises the results of the assessment. Surrey Pension Fund ranked 3rd out of 18 funds, with Pension Fund Committee ranking 6th out of 18 from the national average of all LGPS committee members who took part in the assessment.

10. The Committee scored highest on financial markets and product knowledge and there was a good spread of knowledge across other areas.

11. The assessment identified particular areas in which the members did not perform as well, namely, Actuarial methods, standards and practices which need to be the focus of more training.

12. Training Plan 2021/22

13. The following training plan is proposed by Hymans for the Committee as a result of the exercise:

Period	Key areas for development	Potential Attendees
Q1	• Actuarial Methods • Pensions administration and SAB Good Governance	All
Q2	• The role of the Committee and pensions legislation	All
Q3	• Pensions governance	All
Q4	• Valuation training for 2022 Actuarial Valuations.	All

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14. The training programme can be revised based on member feedback and any additional training requirements.

CONSULTATION:

15. The Chairman of the Pension Fund has been consulted and offered full support for the proposals.

RISK MANAGEMENT AND IMPLICATIONS:

16. Effective training and development will help Members to gain sufficient knowledge and skills necessary to make appropriate decisions in minimising risk associated with their roles and responsibilities.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

17. The cost of the National Knowledge Assessment (NKA) was £6,000 + VAT.

DIRECTOR OF CORPORATE FINANCE COMMENTARY

18. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered.

LEGAL IMPLICATIONS – MONITORING OFFICER

19. There are no legal implications or legislative requirements

EQUALITIES AND DIVERSITY

20. The approval of Training plan does not require an equality analysis, as the initiative is not a major policy, project or function.

OTHER IMPLICATIONS

21. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

22. The following next steps are planned:

- Officers will forward relevant training invites to members of the Pension Fund Committee.

Contact Officer:
Ayaz Malik, Pensions Finance Specialist

Consulted:
Pension Fund Committee Chairman.

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Annexes:
Annexe 1: National Knowledge Assessment Results

Sources/background papers:
None

LGPS

HYMANS ROBERTSON

National Knowledge Assessment

Surrey Pension Fund

June 2020

National Knowledge Assessment

Overview

Following the success of the 2018 LGPS National Confidence Assessment, Hymans Robertson continued the journey to understand and develop knowledge levels in the LGPS with the 2020 LGPS National Knowledge Assessment (NKA). The NKA's key goal is to provide LGPS funds with an insight into the pensions specific knowledge and understanding of the people who hold decision making and oversight responsibility within their organisations.

18 LGPS funds and over 200 members have participated in this first ever National Knowledge Assessment of Pension Committee ('Committee') and Pension Board ('Board') members. The findings from this assessment will provide LGPS Funds with a quantitative report of the current knowledge levels of the individuals responsible for running their fund, aiding the development of more appropriately targeted and tailored training plans for both groups. This report is also a key document in evidencing your fund's commitment to training.

Background

The Surrey Pension Fund ("the Fund") agreed to participate in the NKA using our online assessment. This report provides the participants' results broken down into 8 key areas. The online assessment opened in mid-March and closed at the end of May, and there were weekly progress updates provided to the Fund confirming participation levels. Each participant received their individual results report following completion of the assessment.

Challenging test

This was a challenging multiple-choice assessment of participants knowledge and understanding of relevant subject areas. There was no expectation that participants would score 100% on each subject area tested. Rather the goal was to gain a true insight into members' knowledge in the areas covered by the CIPFA Knowledge and Skills Framework and the Pensions Regulator's (TPR) Code of Practice 14.

Why does this matter?

In recent years there has been a marked increase in the scrutiny of public service pension schemes, including the 100 regional funds that make up the LGPS across the UK. The Public Service Pensions Act 2013 introduced new governance legislation, including the requirement for Local Pension Boards to be set up and extended the remit of the Pensions Regulator to public service schemes as set out in its Code of Practice 14[1]. Additionally, the Ministry of Housing, Communities and Local Government ("MHCLG") in England & Wales and Scottish Ministers in Scotland, and their respective Scheme Advisory Boards have emphasised the need for the highest standards of governance in the LGPS. This includes ensuring that all involved in the governance of public sector funds can evidence they have the knowledge, skills and commitment to carry out their role effectively.

While fund officers may deal with the day-to-day running of the funds, members of the Committee play a vital role in the scheme, and to exercise their roles effectively must be able to address all relevant topics including investment matters, issues concerning funding, pension administration and governance.

[1] Governance and administration of public service pension schemes – issued April 2015

Recent events

The introduction of Markets In Financial Instruments Directive II (MIFID II) in January 2018 required Committee members to evidence their knowledge in order to be treated as professional investors. Also, in late 2019 the Scheme Advisory Board for England and Wales began a review of governance arrangements for LGPS funds. This project – termed 'Good Governance' – addressed stakeholder knowledge and skills. A clear recommendation of the Good Governance project is that the knowledge levels already statutorily required of Board members should also be required of Committee members. These recent events have reaffirmed that LGPS funds should evidence the training provided and current knowledge and understanding levels retained within their Committee and Board.

We would encourage the use of these results to better understand the areas where Committee and Board members feel comfortably informed, but crucially where further training may be of benefit.

In keeping with the theme of increased external scrutiny, it is important not only that the Committee and Board have confidence in their roles, but also that the Fund can demonstrate the steps taken to facilitate this. We would suggest you keep a record of the process used to assist the Committee and Board with training and development. This report should form part of the overall training records for both groups.

Approach

The members of the Surrey Pension Fund Committee and Board were invited to complete an online knowledge assessment. In total there were 9 respondents from the Committee and there were 6 respondents from the Board. Each respondent was given the same set of 47 questions on the 8 areas below:

1	Committee Role and Pensions Legislation	**5**	Procurement and Relationship Management
2	Pensions Governance	**6**	Investment Performance and Risk Management
3	Pensions Administration	**7**	Financial Markets and Product Knowledge
4	Pensions Accounting and Audit Standards	**8**	Actuarial Methods, Standards and Practices

Under each subject heading, there were at least 5 multiple choice questions to answer. Each question had 4 possible answers, of which one answer was correct. This allows us to build a picture of the knowledge levels of each individual member in each of the topics, but crucially to help inform you of the overall levels of knowledge in each area.

Results

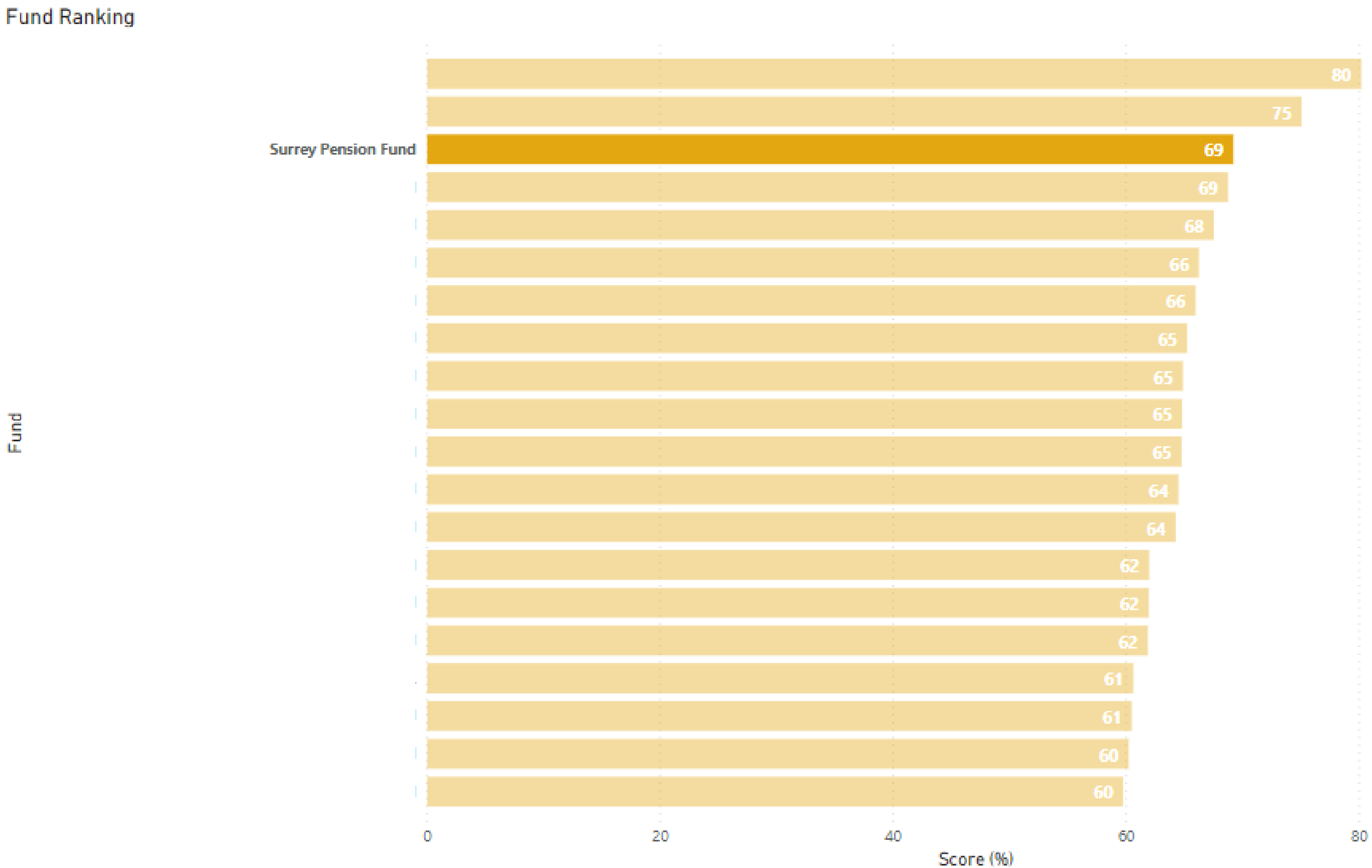
The responses for all members who participated have been collated and analysed. For each section we have shown:

- The Fund's overall ranking against other participating LGPS funds
- The average score for each of the 8 subject areas, for both the Committee and Board.
- Each average score benchmarked for both groups against the other NKA participant funds' Committee and Board for each of the 8 subject areas
- Engagement levels for both the Committee and Board and how these levels rank against other LGPS funds

Based on the results and the responses received from participants we have also completed a proposed training plan for the Fund over the next 18 months, as well as some other "next steps" to consider.

Overall Results

The table below shows how the overall average score for your Fund compares with that of all other funds who took part in the Assessment. The "score" shown below is the average score of all participating Committee and Board members from each Fund. The Surrey Fund is 3rd out of 18 Funds.



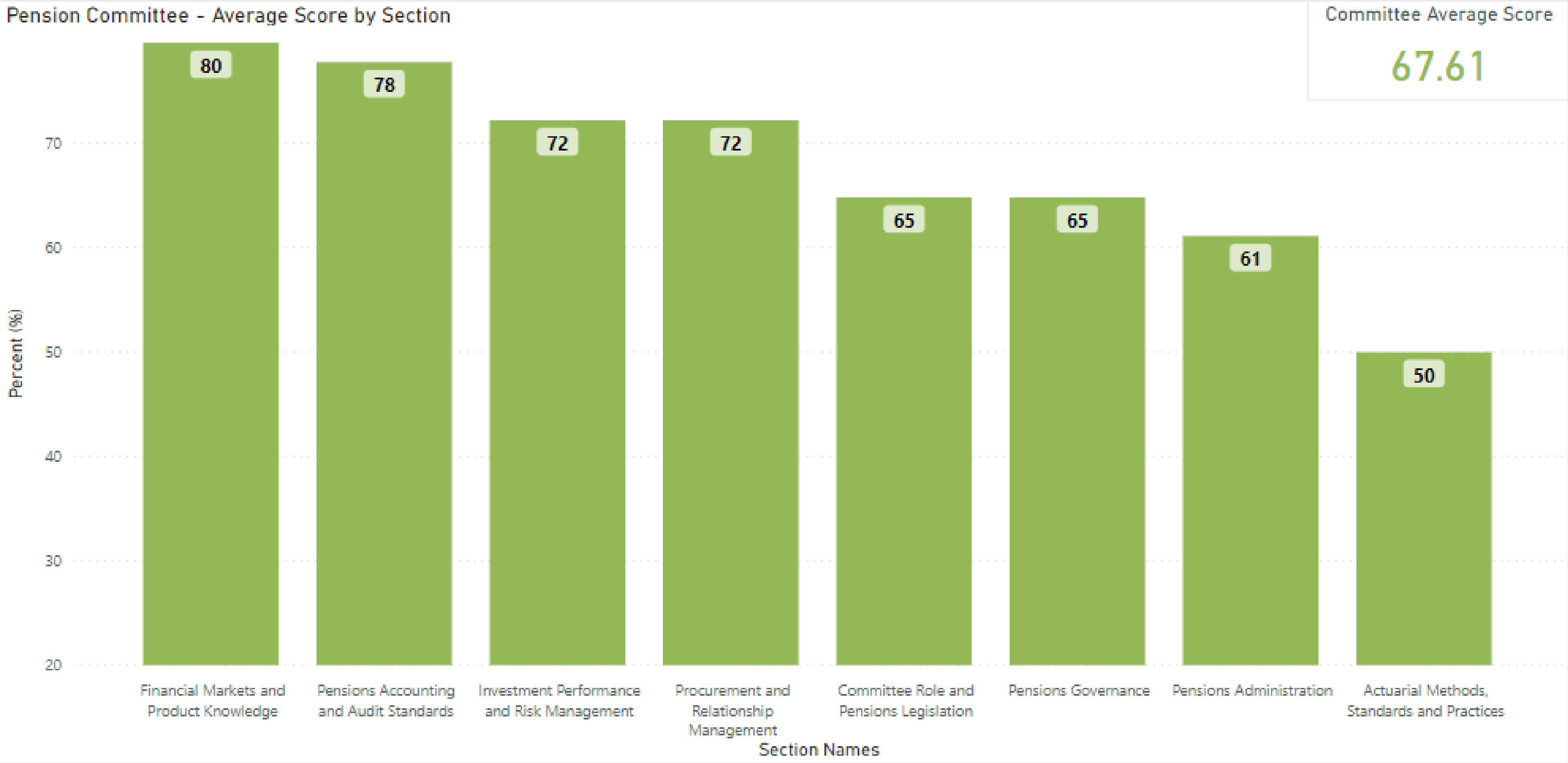
For each of the assessment's 8 areas we have shown the results of both the Committee and Board. These have been shown in the order in which the sections appeared in the survey. There is also a summary showing the average scores across all sections for the Committee and Board.

The results show that the Board participants scored stronger on almost all areas apart from pensions accounting and investment performance in comparison to their Committee counterparts. This is perhaps due to a historical preference shown by many LGPS Committees where they concentrated most of their time on areas like this and Investments.

Performance in each area

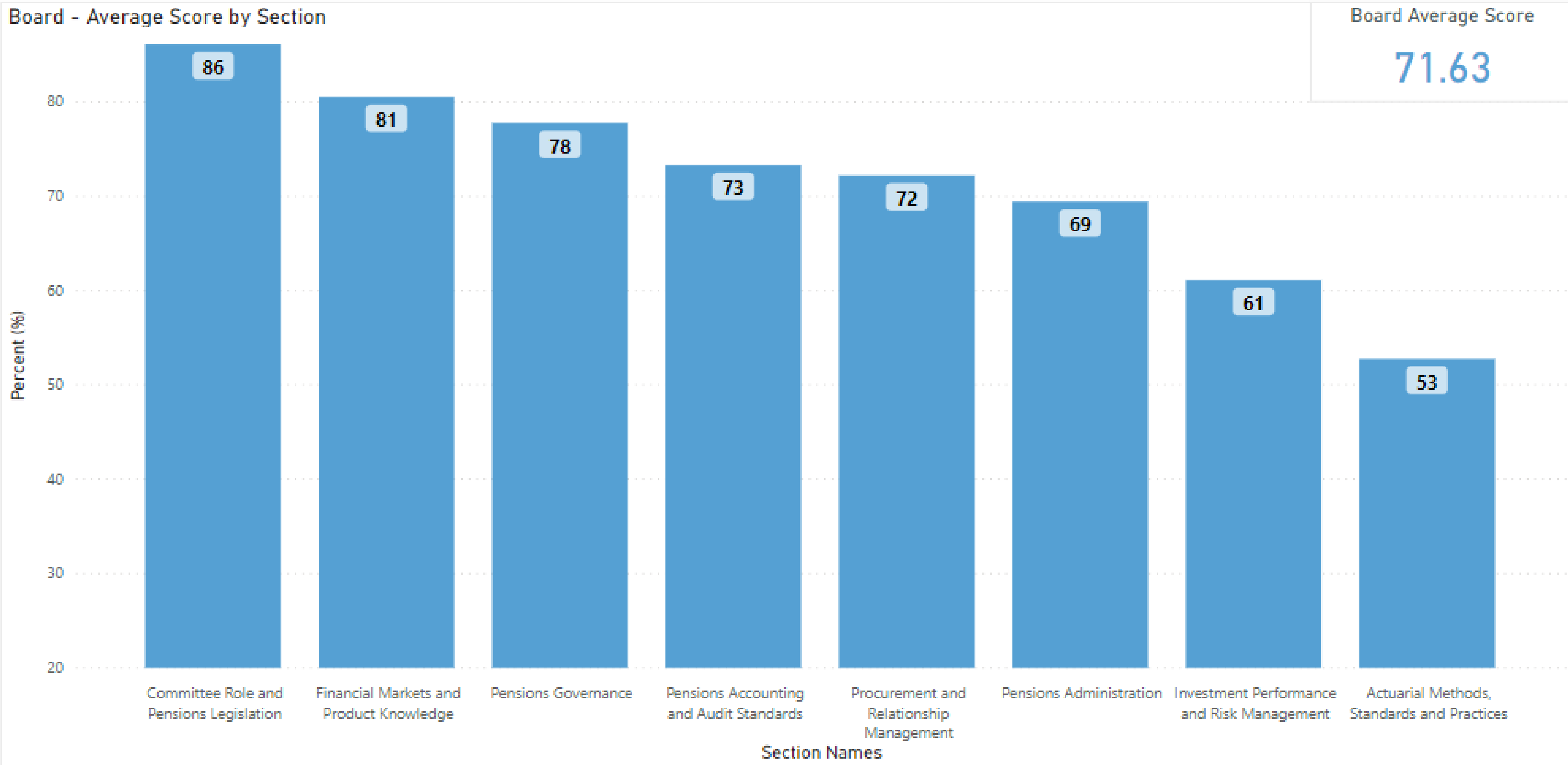
The results can be ranked for each section from the highest score (greatest knowledge) to lowest score (least knowledge). This is shown separately for both the Committee and the Board. The intention is that training plans and/or timetables can be tailored to focus on the areas of least knowledge, whilst ensuring the Committee and Board maintain the high level of knowledge in the stronger areas.

Pension Committee



The results show the scores for Financial markets and product knowledge as well as pensions accounting were significantly higher than other areas. There was a good spread of knowledge across other areas too. Actuarial methods, standards and practices was the area with weakest scores – significantly lower than all other areas.

Pension Board



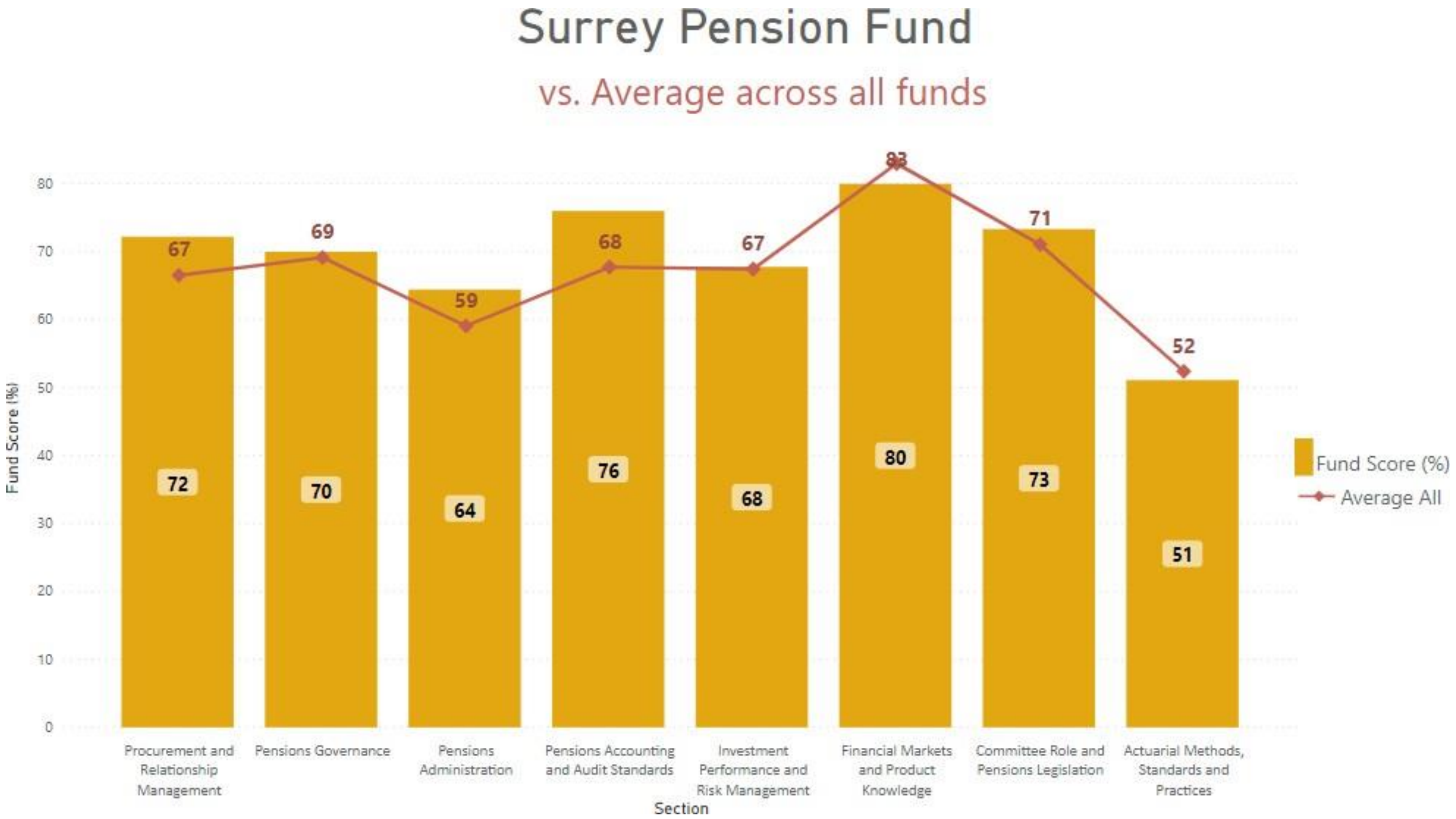
The Committee's role and pensions legislation was the highest scoring area for the Board. Financial markets and product knowledge was also answered strongly.

It does appear that the Board's knowledge in the other areas is generally good. Actuarial methods, pension administration and investment performance would be the key areas to focus on. This is highlighted further in the following section which compares the Surrey results, with all participating funds' results.

Benchmarking

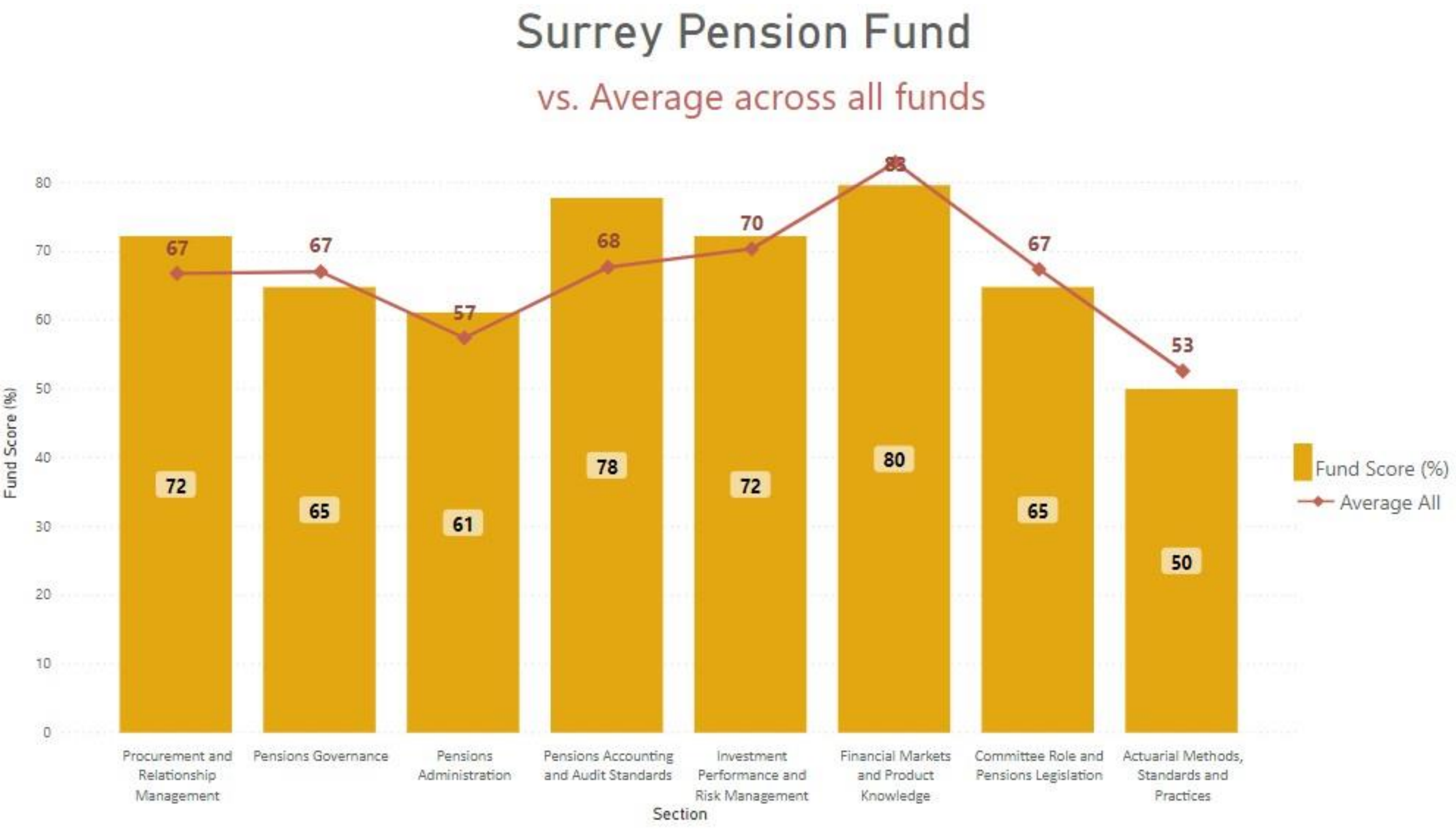
As this assessment is being conducted at national level across a number of LGPS funds we are able to provide details of how your Fund's results compare to those across the average of all funds who have taken part to date. We have provided a comparison of the results for both your Fund's Committee and Board, versus the average scores nationally for each group. This gives an idea of the knowledge levels across these groups, relative to the national average.

Committee and Board combined



Pension Committee

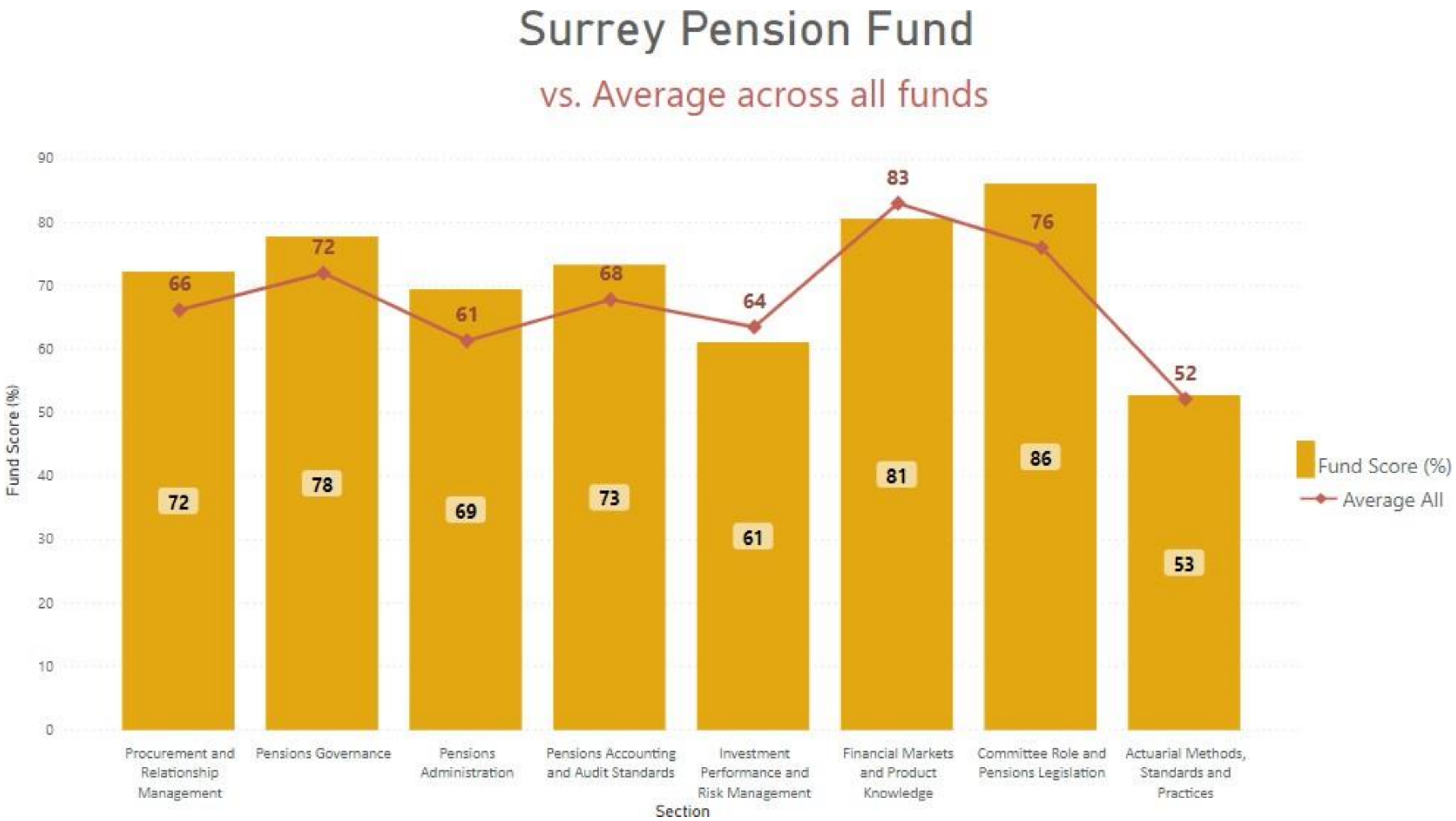
The following chart shows how your Fund's Committee scored in each section, versus the national average of all Committee members who took part.



The Committee ranked 6 out of 20 Funds' Committee results

Pension Board

The chart below shows how your Fund's Board scored in each section, versus the national average of all Board members who took part.



The Board ranked 4 out of 20 Funds' Board results.

Commentary

It is very encouraging that 15 participants from your Fund took part in the assessment. Overall the results were positive and it is clear that there are areas of greater knowledge and there are those that should be developed over time. We would fully expect there to be gaps in the knowledge of all members, no matter their role on the Committee/Board, their tenure or indeed their background in terms of pensions experience. The most important thing to emphasise is that not everybody needs to be an expert in all areas, rather there should be a spread of knowledge across your Committee and Board which is supported by advice from officers and professional advisors.

Just as important as gaining the relevant knowledge and understanding expected of a Pension Committee or Board is the application of that knowledge and understanding, including the utilisation of an individual's own background and perspective. To supplement a Fund's training plan, we recommend that case study analysis is also included as part of both the Committee and Board training plans, allowing time for reflection on how both groups react and act on issues.

Committee

The results show that Financial markets and product knowledge has the highest levels of knowledge, but that the areas to focus any specific training on might be actuarial methods, governance, as well as pensions administration.

Local Pension Board

The results show that the highest levels of knowledge relate to financial markets and the role of the Committee, with Governance also scoring well. The areas to focus any specific training on might be actuarial methods and investment performance for the Board.

The next step would be to try an develop the knowledge about the lower scoring areas. You might already have a training plan in place, in which case you could use these results to tailor the specific training and with the knowledge of these results, ensure it aligns with your priorities.

Engagement

One of the key areas that we recommend funds focus on is Committee and Board engagement. With the ever-increasing pace of change in the pensions and investments world, member engagement is critical to maintaining strong collective knowledge. There is an expectation that they need to be not only willing, but keen to develop their knowledge and understanding across the raft of topics upon which they will need to make, or ratify, decisions.

Overall engagement

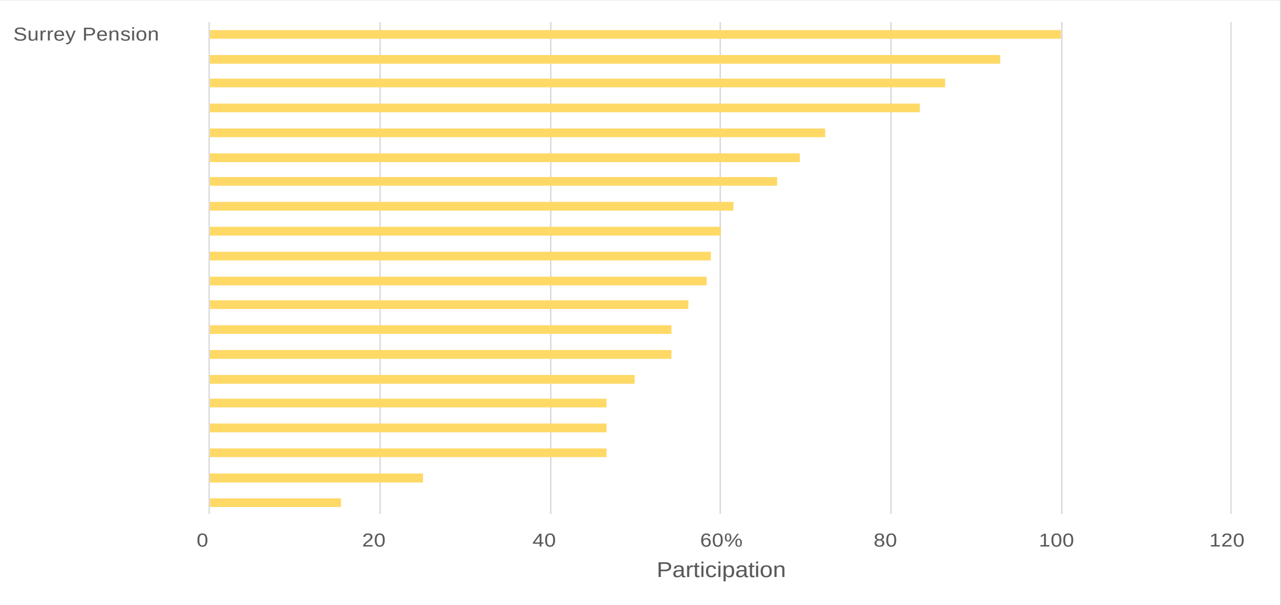
One measure of the engagement of members is their willingness to participate in training. As such, we have used the participation level of this survey to measure the engagement of your Committee and Board members. The table below shows the breakdown of the total number of participants from the Surrey Fund, as a proportion of those who could have responded.

	Participants	Total Number	Participation rate
Committee	9	9	100%
Board	6	6	100%
Total	**15**	**15**	**100%**

We understand that different Committees function in different ways and have different numbers of members. We therefore draw no conclusions or make any inferences from these results. The information is simply being provided to the Fund officers, as they will be best placed to draw any conclusions.

Engagement benchmarking

The chart below shows how your Fund's participation level compares with that of all other funds who took part.



Commentary on engagement

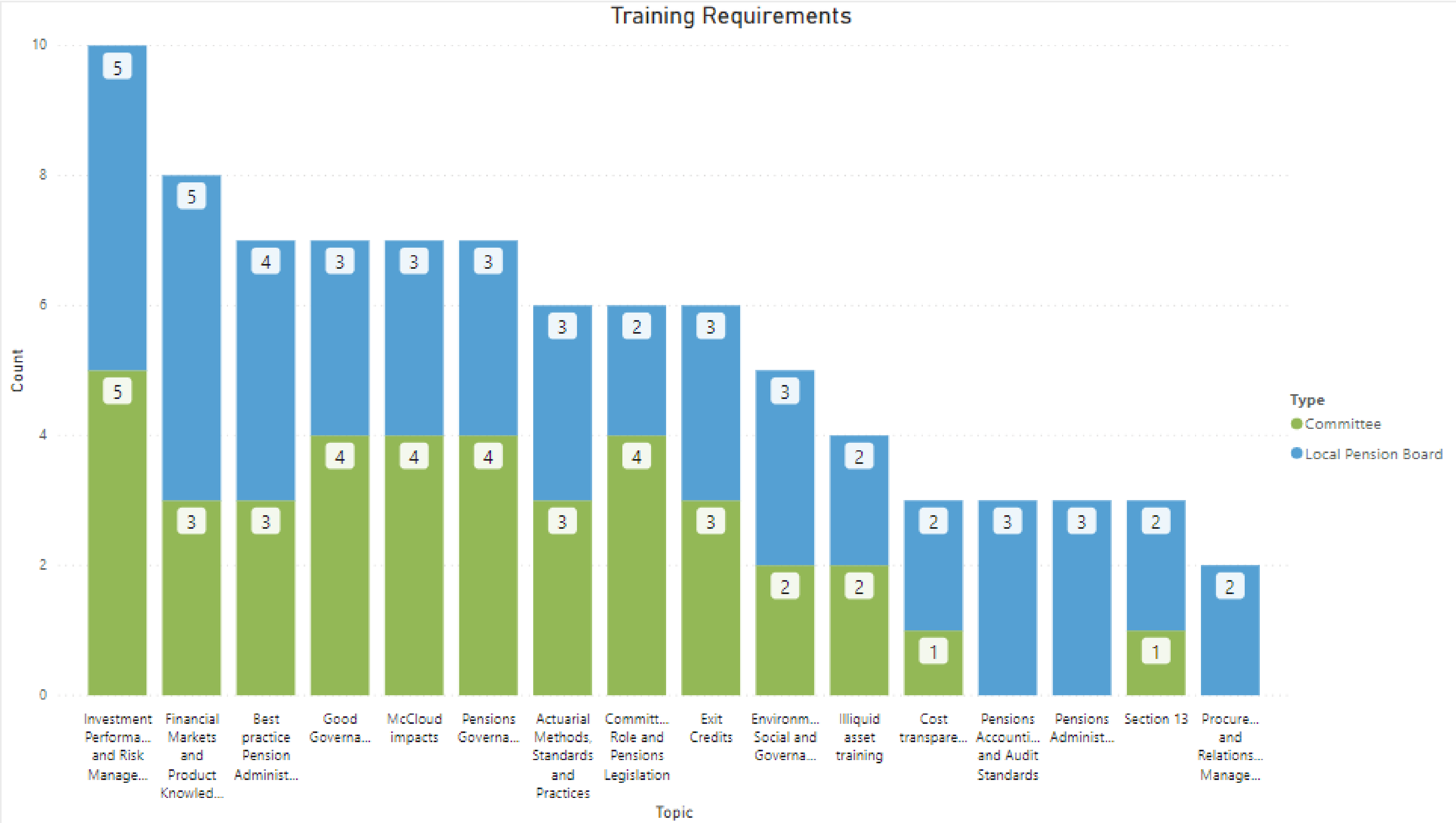
That all15 participants from your Fund took part in the assessment is extremely encouraging. With the number of changes to the LGPS in recent years, it is vital that Committee and Board members remain abreast of the latest developments and feel confident that they have the knowledge required to make the decisions required of them. Their level of engagement is a key driver of this.

Engagement is at a high level and the focus should now be on maintaining this, particularly in the current climate where face-to-face meetings and therefore delivery of training sessions might be difficult for some time to come.

Training feedback from participants.

One of the final sections of the survey asked participants to indicate which topics they would like to receive training on. There was a list of options available, covering a broad spectrum of the topics we believe are most relevant to allowing Committee and Board members to effectively perform their roles. Members were also given the option to indicate any other areas in which they would benefit from further training.

The table below summarises the areas in which members indicated training would be beneficial.



In the addition to the pre-defined list of training, we also asked participants for comment and areas in which they feel further training would be beneficial. We have provided a selection of these comments below:

"Risk Management in practice"

"I would benefit from training in all relevant areas"

Suggested Training Plan

We have put together a summarised training plan below, picking out the key areas for development based on participant assessment results and the training requests. This might be identical for the Committee and Board, to ensure consistency. Alternatively, you may in the short term, wish to implement different training plans, to assist in the areas of development highlighted in this report.

2021/22 – Q1	• Investment performance and risk management – this was the most requested training topic, and one for which knowledge levels were around average level of NKA participant scores. • Impact of McCloud (Administration, Governance and Funding) • Actuarial Methods
2021/22 – Q2	• Pensions administration (ever increasing complexity) and SAB Good Governance
2021/22 – Q3	• For the Committee – the role of the Committee and pensions legislation • For the Board – Procurement and relationship management
2021/22 – Q4	• For the Committee - Pensions governance • For the Board - Accounting and audit standards for the Board
2022/23 – Q1	• Valuation training sessions – purpose, role, outcomes etc. This has been timed to coincide with the 2022 Actuarial Valuations.

Training support

Tools such as this online assessment offer different ways for members to take part in training. There might be more options for online training sessions which you could take advantage of. We have noted some training materials and websites below which might help you deliver focussed sessions to your Committee and Board and keep them informed on the most pertinent pension areas.

- CIPFA Knowledge and Skills Framework
- TPR Public Service Toolkit
- LGA fundamental training – currently a ‘physical’ attendance course
- LGA monthly bulletins
- Hymans Robertson Training videos for Committee and Board members (details noted below)

Next Steps

Based on the results we would suggest that there should be consideration to the following next steps:

- This report should be **reviewed** by the funds officers and results shared with the Committee and Board
- Set up a **structured training plan** for the next 18 months covering the main areas highlighted in this report
- Plan for the **delivery** of training over a 6-month period while meeting restrictions might continue to be in place
- Consider the most **pressing** training requirements in the coming months, to ensure members have the required knowledge such as the effect of COVID-19 on assets and liabilities and how this might develop over time
- **Assess** the tools available to the Fund to assist with training.
- Consider ways of **maintaining** and **increasing** the engagement of both the Board and Committee. This could include providing them with more information, training materials, briefing notes etc.
- Ensure that the Fund's training strategy is up to date and **appropriate** for purpose
- Look to conduct a **case study workshop** with your Committee and Board. This will gain officers a further insight into the **practical application** of both groups knowledge and understanding. This could be presenting various scenarios e.g. how the administration teams will deal with the McCloud judgement and allowing group discussion on how the Committee and Board would deal with selected case studies in their role as decision makers and oversight bodies. Hymans Robertson can facilitate a case study workshop for your Committee and Pension Board, as well as preparing an observation report for the Fund.

Hymans Support

We are happy to run training sessions, and/or provide training materials covering any of the topics covered in this report. The value of a face-to-face session for this type of training lies in members being able to ask relevant questions and interrogate the trainer on the specific areas they want to develop knowledge in. We understand that at present this will exclude physical attendance, but we are happy to set up video conference calls to assist with the ongoing training of both groups now. We will very soon be releasing our Hymans LGPS online training support that will give a comprehensive but bitesize training course.

We will be producing an NKA report discussing and analysing the results at the national level. A copy of this will be made available to the Fund when that report is complete.

If you wish to discuss the contents of this report further, please get in touch with either myself, Alan or Gemma.

Prepared by Hymans Robertson LLP.

Andrew McKerns

LGPS Governance, Administration and Projects (GAP) Consultant

Alan Johnson

LGPS Governance, Administration and Projects (GAP) Consultant

Reliances and Limitations

This report has been prepared for the Surrey Pension Fund.

This report must not be released or otherwise disclosed to any third party except with our prior written consent, in which case it should be released in its entirety.

Hymans Robertson LLP do not accept any liability to any party unless we have expressly accepted such liability in writing.

This report has been prepared by Hymans Robertson LLP, based upon its understanding of legislation and events as at September 2020.

SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **11 DECEMBER 2020**

LEAD OFFICER: **ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**

SUBJECT: **DEPARTMENT FOR WORK AND PENSIONS – CONSULTATION ON TAKING ACTION ON CLIMATE RISK: IMPROVING GOVERNANCE AND REPORTING BY OCCUPATIONAL PENSION SCHEMES**

Strategic objectives
Governance

SUMMARY OF ISSUE:

To provide details of the Department for Work and Pension's (DWP) consultation on Taking Action on Climate Risk: Improving Governance and Reporting by Occupational Pension Schemes and the response from Surrey.

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RECOMMENDATIONS:

To note the report and annexe.

REASON FOR RECOMMENDATIONS:

The Pension Fund Committee will be made aware of all national initiatives with a consultation process with a response sent within stated deadlines, in accordance with the Fund's strategic governance objectives.

BACKGROUND:

1. In August 2020, the DWP consultation sought views on policy proposals to require trustees of larger occupational pension scheme, authorised master trusts and authorised schemes providing collective money purchase benefits to have effective governance, strategy, risk management and accompanying metrics and targets for the assessment and management of climate risks and opportunities. It also invited responses on proposals to disclose these in line with the recommendations of the international industry-led Task Force on Climate-related Financial Disclosures (TCFD).

2. It is proposed that among the activities required would be calculating the 'carbon footprint' of pension schemes and assessing how the value of the schemes' assets or liabilities would be affected by different temperature rise scenarios, including the ambitions on limiting the global average temperature rise set out in the Paris Agreement. The disclosures would be required to be made publicly available, referenced from the schemes' Annual reports and

Accounts, and pension savers informed of the availability of the information via their annual benefit statement.

DETAILS:

3. The consultation outlines proposals to require trustees to meet climate governance requirements which underpin the 11 recommendations of the TCFD, and to report on how they have done so.

4. It is proposed to set out statutory guidance, which trustees must have regard to, which will set out steps to meet and report to TCFD requirements.

5. DWP further proposes that schemes be required to publish their TCFD report on their own website, or the website of the scheme's sponsor. As a key financial disclosure - TCFD reporting is referenced from the Annual Report.

6. It is proposed that members will be told via the annual benefit statement that the information has been published and where they can locate it.

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7. DWP also proposes to require that trustees provide the Pensions Regulator (TPR) with the web address of where they have published their TCFD report via the annual scheme return form. We also propose to require that trustees provide a link to their SIP and (where applicable) implementation statement and published excerpts of the chair's statement in the annual scheme return form.

8. DWP further proposes that a mandatory penalty is appropriate for complete failure to publish any TCFD report.

Surrey's response

9. Surrey response (shown as Annexe 1) supports the stated purpose of the consultation to measure the carbon footprint of portfolios as well as potential risks with different temperature levels. It also welcomes the decision to keep members informed through their Annual Benefit Statements.

10. Surrey believes that trustees should be urged to take the lead in integrating Climate Risk into their portfolio, as opposed to waiting on policy changes. Surrey also supports this view. A Pension Fund Trustee's fiduciary duty requires them to take into account any significant factors, which can impact future financial returns. The consultation does well in highlighting that this goes beyond 'traditional' factors such as interest rate, exchange rate and inflation.

11. Although the decision to make TCFD mandatory amongst larger pension schemes is welcomed, the Government should actively encourage smaller schemes to also start making voluntary TCFD disclosures, for the benefit of their members, Trustees and wider public.

12. Surrey appreciates that providing TCFD disclosures should not in any way lead to increased pressure to divest, and this decision still lies ultimately with Pension Fund Trustees.

13. Surrey is also supportive of the methodology of portfolio warming as a means to measure likely temperature rise levels based on a scheme's current portfolio along with other methods to assess physical and transition risk. This would therefore allow Trustees to view how at risk their portfolios are in relation to carbon policy changes, at a sector and potentially geographic level.

CONSULTATION:

14. The Chairman of the Pension Fund Committee has been consulted on this report

RISK MANAGEMENT AND IMPLICATIONS:

15. Risk related issues have been discussed and are contained within the report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

16. Financial and value for money implications are discussed within the report.

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DIRECTOR OF CORPORATE FINANCE COMMENTARY

17. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

18. There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

19. This does not require an equality analysis, as there is no major policy, project or function being created or changed.

OTHER IMPLICATIONS

20. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

21. The following next steps are planned:

    - Provide the Pension Fund Committee with details of the results of the consultation.

Contact Officer: Mamon Zaman, Senior Pensions Finance Specialist

Consulted:
Pension Fund Committee Chairman

Annexes:

1. Surrey County Council response to the DWP consultation on Taking Action on Climate Risk: Improving Governance and Reporting by Occupational Pension Schemes

Sources/background papers:

1. The DWP consultation on Taking Action on Climate Risk: Improving Governance and Reporting by Occupational Pension Schemes https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/911894/tcfd-taking-action-on-climate-risk.pdf

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Tel: 020 8213 2739

E-Mail: neil.mason@surreycc.gov.uk

Our Ref: Taking Action against Climate Risk
Your Ref:

Climate Governance and ESG team

By email to pensions.governance@dwp.gov.uk

1 October 2020

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Dear Climate Governance and ESG team,

RE: Taking Action on Climate Risk in the Local Government Pension Scheme

Surrey County Council (Surrey) welcomes the opportunity to respond to the draft guidance on taking action on Climate Risk issued by the Minister for Pensions and Financial Inclusion.

Surrey is the Administering Authority for the Surrey Pension Fund (the Fund) as part of the Local Government Pension Scheme (LGPS). The Fund has assets of over £4.3billion and includes nearly 300 employers.

We are supportive of much of the guidance and appreciate the desire to lead the way for a financial services sector to address Climate Risk.

Introduction

Surrey supports the stated purpose of the Consultation to measure the carbon footprint of portfolios as well as potential risks with different temperature levels. It also welcomes the decision to keep members informed through their Annual Benefit Statements.

Chapter 1: Trustees' duties to consider climate change

5. The Fund agrees that current pricing methods for stocks focus more on extrapolation of shorter term cash-flows, so doesn't take into consideration the longer term risk of Climate Change. A sudden shift in investor expectations can have a dramatic impact on market prices,

bearing similarities to the market fluctuations as a result of the COVID-19 Pandemic, although the impact could potentially be longer lasting or even permanent.

11. Trustees are urged to take the lead in integrating Climate Risk into their portfolio, as opposed to waiting on policy changes. Surrey also supports this view. A Pension Fund Trustee's fiduciary duty requires them to take into account any significant factors, which can impact future financial returns. The consultation does well in highlighting that this goes beyond 'traditional' factors such as interest rate, exchange rate and inflation.

35. Although the decision to make TCFD mandatory amongst larger pension schemes is welcomed, the Government should actively encourage smaller schemes to also start making voluntary TCFD disclosures, for the benefit of their members, Trustees and wider public.

67. The Fund appreciates that providing TCFD disclosures should not in any way lead to increased pressure to divest, and this decision still lies ultimately with Pension Fund Trustees.

72. The Surrey Fund supports the methodology of portfolio warming as a means to measure likely temperature rise levels based on a scheme's current portfolio along with other methods to assess physical and transition risk. This would therefore allow Trustees to view how at risk their portfolios are in relation to carbon policy changes, at a sector and potentially geographic level.

Chapter 2: Scope & Timing

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5. The Surrey Fund, recognises that although the implied cost of £15k per year would not be seen to be material in comparison to the actual costs of investment, carrying out these analyses yearly may be excessive and may not add value from year to year. Biennial and triennial reporting may be more appropriate.

29. The Surrey Fund supports the size of funds in scope for TCFD reporting (first and second wave) as well as the timing of the end of 2022, and 2023 respectively.

46. The Fund also welcomes the extended deadline for schemes with assets ranging from £1bn to £5bn. This will prevent the reporting being a tick-box exercise and will allow funds the time to provide meaningful disclosures.

59. The Fund agrees with the approach to keep TCFD reporting consistent from year to year for those schemes which may fall in and out of the threshold for the benefit of consistent reporting for their stakeholders.

75. The proposal to review effectiveness of TCFD reporting in 2024 and how it impacts Trustee decision making is welcomed to ensure there are positive outcomes being achieved from this.

Chapter 3: Climate Governance and TCFD

26. The proposal to carry out a scenario analysis along with choosing of metrics and targets to be completed at least annually is something that Surrey Pension Fund does not agree with and seems excessive. The reason being most investment strategies along with fund manager selection would not vary considerably from year to year. A more pragmatic approach would be to carry out this analysis at least every two years or triennially so there can be overlaps and integration during investment strategy reviews.

27. The Fund does not see quarterly emissions reporting as being feasible nor would this be readily available. Although this may enhance fund manager selection, the Fund does not see this frequency of reporting being possible.

47. The requirement to demonstrate and report on the various climate related risks and opportunities at a portfolio level and how this is factored into a scheme's investment strategy or funding strategy is welcomed.

58. The Fund commends the proposal to carry our scenario analysis on 2 Degrees or lower, but there should include an option of 3 degrees, seeing as this is the current projection of global temperature rise based on carbon emissions. This is for information purposes only, as opposed to target setting.

Chapter 4: Disclosing TCFD

9. The Fund also agrees that making TCFD reporting publicly available by default would enhance the quality of reporting. We also agree that a summarised version would be useful in the Annual Report but the full TCFD report should be published separately.

31. The Fund supports the view to require trustees to post links to TCFD in the annual benefit statement.

Chapter 5: Penalties and Impacts

13. The Fund is happy with the minimum mandatory penalty of £2,500 for non-compliance, with 11
the option to review penalties once TCFD reporting becomes more common.

Yours sincerely

Anna D'Alessandro
Director of Corporate Finance

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **11 DECEMBER 2020**

LEAD OFFICER: **ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**

SUBJECT: **INVESTMENT CORE BELIEFS AND THE UNITED NATION'S SUSTAINABLE DEVELOPMENT GOALS**

SUMMARY OF ISSUE:

Strategic objectives	
Investment	Governance

Surrey Pension Fund is reviewing its investment strategy with a view to ensuring that it is in line with its Mission Statement and the emphasis on environmental, social and governance (ESG) considerations, in the wider context of the United Nation's Sustainable Development Goals (SDGs).

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1. Having considered all aspects of incorporating ESG considerations in to the investment approach, and in acknowledgement that there is no universally agreed approach in this area, agrees that the use of UN SDGs provides a forward thinking and comprehensive approach in referencing the transition to sustainability within the Fund's investment strategy

2. Agrees that the Minerva Report provides sufficient assurance to enable a decision to move to the next stage of more detailed preparation and implementation.

3. Requests further action from officers and, where appropriate, advisors, to cover the following areas:

- Draft relevant changes to the Investment strategy
- Develop SDG in to an engagement framework for companies as well as Investment Manager activity
- Work to incorporate SDG metrics in selecting, monitoring and evaluating investment managers
- Work with Border to Coast on developing SDG approach to Pooled assets

4. Agrees that officers provide the following updates for the next meeting:

- Presentation of an implementation plan
- Propose the method by which progress on implementation is incorporated as part of all future investment strategy reviews

- Propose the timeline for the assessment and ongoing viability and effectiveness of this approach

REASON FOR RECOMMENDATIONS:

To keep the Pension Fund Committee apprised of the progress made in reviewing the Fund's investment strategy with a view to ensuring that it is in line with its Mission Statement and the emphasis on environmental, social and governance (ESG) considerations.

DETAILS:

Background

1. At its meeting of 7 June 2019, the Pension Fund Committee approved the following mission statement:

   ''The Surrey Pension Fund will deliver a first-class service through strong partnerships with scheme members, employers, the Border to Coast Pool and the wider LGPS community. Environmental, Social and Governance factors are fundamental to our approach which is underpinned by risk management, informed decision making, the use of technology and the highest standards of corporate governance''.

2. Further to this, at its meeting of 20 December 2019, the Pension Fund Committee approved for a Committee sub-group to be convened to develop the Fund's RI Approach. To include, but not limited to:

   - The Fund's positioning of Responsible Investment in its Core Investment Beliefs;
   - The Fund's relationship with BCPP, more specifically BCPP's RI approach to the Fund's pooled assets;
   - The Fund's RI approach to existing legacy portfolios yet to be transitioned to BCPP;
   - The Fund's RI approach to its Indexed Funds currently held with Legal & General Investment Management (LGIM);
   - Reaching a recommendation on the position of The Fund on the Spectrum of Capital;
   - Exploring the analysis of scenario mapping The Fund's portfolio in line with the United Nations' (UN) Sustainable Development Goals (SDGs) (Paragraph 17), carried out by an independent provider.

3. The Fund had chosen to use the United Nations Sustainable Development Goals as a reference for Responsible Investment, as it represents a framework of universally agreed goals in which all countries within the United Nations should aim to achieve by 2030. Logically these goals can also become a target for the financial services industry, specifically Pension Funds who can provide the necessary capital to accelerate these goals.

4. On 24 January 2020, officers issued an invitation to tender for the following scope of work:

   To examine the existing Investment Portfolio holdings of Surrey Pension Fund and their relationship (positive/ negative) to the United Nations Sustainable Development Goals, and identify the risks and opportunities associated with the analysis.

   In particular to comment on:

   - The Core Investment Beliefs of the Committee; informing and assisting the Fund in identifying its Core Investment Beliefs against specific SDGs and how it fits into its Investment Strategy;
   - The starting position of the Fund against the UN's SDGs;
   - How the Fund can continue further as Impact Investors and integrate the SDGs into its Investment Strategy;
   - Where there is an Investment risk/ opportunity to the Fund, within its assets, in relation to the transition to sustainability and a low carbon economy;
   - The methods used to map sustainability to investment strategy and how robust they are;
   - The Fund's own Responsible Investment Approach and in the context of Border to Coast Pensions Partnership.

5. After a competitive tender process, with a selection panel of the Vice Chairman of the Committee, the Independent Advisor and officers, Minerva were appointed to support the Fund in this work.

Initial Findings on External Manager approach to ESG

6. Some of the initial findings on the Fund's external managers have been summarised below;

   - They have varying levels of internal ESG and sustainability personnel, which are not necessarily linked to the size of the firm;
   - Most are developing, or have developed, some kind of an approach towards the SDGs; and
   - Most are signatories to the Taskforce for Climate-Related Financial Disclosures (TCFD) and the Transition Pathway Initiative (TPI)

Initial Findings on Benchmarking against World Benchmarking Alliance's SDG 2000 Index

7. Initial findings from the Fund's mapping against the WBA SDG 2000 have been summarised below;

   - Approximately 70% of the Fund's equity and corporate bond portfolio holdings are also in the WBA SDG 2000 Index
   - The overlap against the WBA SDG 2000 is purely coincidental, but does present an opportunity to focus on these holdings, and how these

companies are managed. Improving the management of these companies can allow them to make progress in aligning against the SDGs.

8. The Fund's mapping provider had opted to use the World Benchmarking Alliance as the most robust approach in understanding how best to target systematic change with the world's most influential companies. The companies targeted within the SDG 2000 have the most potential to deliver these goals and become leaders in their sector for others to follow as an example. The Committee is satisfied that this methodology is vigorous and that portfolio analysis can continue using this basis

Engagement Workshop

9. The Fund held a workshop along with Minerva, Members of the Pension Fund Committee as well as its Independent Adviser. A summary of the workshop has been provided below;

- The findings from the mapping exercise was discussed along with the more extensive analysis on Fund Manager policies on ESG as well as the SDGs
- There was also discussion as to how the findings can be integrated within the Fund's Investment Strategy Statement and also how this can be integrated with its Index Fund provider Legal and General
- There was an acknowledgement that the concept of aligning investments against the SDGs are still in its infancy

CONSULTATION:

10. The Chairman of the Pension Fund Committee has been consulted on this report.

RISK MANAGEMENT AND IMPLICATIONS:

11. The consideration of risk related issues, including investment, governance and reputational risk, are an integral part of this project and will be considered as part of the project development.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

12. There are no financial and value for money implications contained in this report.

DIRECTOR OF CORPORATE FINANCE COMMENTARY

13. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

14. There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

15. There are no equality or diversity issues.

OTHER IMPLICATIONS

16. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

17. The following next steps are planned:

- Officers to work with Minerva and Adviser on implementation of recommendations.

Contact Officer:
Neil Mason, Strategic Finance Manager (Pensions),
Mamon Zaman, Senior Pensions Finance Specialist

Consulted:
Pension Fund Committee Chairman

Annexes:

1. Findings Report from Minerva

Sources/background papers:

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MINERVA ANALYTICS

DISCERN sustainability

Surrey Pension Fund

SDG Mapping Project Report

18 November 2020

About Minerva Analytics & Discern Sustainability

Minerva Analytics helps investors and other stakeholders to overcome data disclosure complexity with robust, objective research and voting policy tools. Users can quickly and easily identify departures from good practice based on their own individual preferences, local market requirements or apply a universal good practice standard across all markets.

Discern Sustainability helps financial institutions excel in sustainable, responsible investment and ESG across three areas:

- Bespoke research and strategic advisory;
- Financial product design & integration; and
- Thought leadership.

For more information please email hello@minerva.info or call + 44 (0)1376 503500

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Minerva Analytics Ltd
2020

Contents

1 Introduction

In April 2020, Surrey County Council, as the administering authority of the Surrey Pension Fund ('the Fund'), appointed Minerva Analytics to carry out a United Nations Sustainable Development Goals ('SDGs') mapping project for the Fund. The impetus behind this project was that Surrey recognised that there is currently no universally agreed approach in the investment industry towards incorporating ESG considerations into the investment process. Having considered all aspects of this question, the Fund decided to explore whether the use of the SDGs might provide a robust, comprehensive and practical method of ESG factor implementation.

The objectives of the exercise were specified as follows:

The Fund wishes to examine its existing investment arrangements in the wider context of the SDGs, to identify risks and opportunities.

Specifically, the outcomes from the exercise are to focus on:

- *Informing & assisting the Fund in identifying its Core Investment Beliefs against specific SDGs and how they fit into its Investment Strategy;*
- *The starting position of the Fund against the SDGs;*
- *How the Fund can continue further as Impact Investors and integrate the SDGs into its Investment Strategy;*
- *Where there is an investment risk/opportunity to the Fund, within its assets, in relation to the transition to sustainability and a low carbon economy;*
- *The methods used to map sustainability to investment strategy and how robust they are; and*
- *The Fund's own Responsible Investment approach and in the context of Border to Coast Pensions Partnership.*

Since our appointment in April, the delivery team of Minerva Analytics and Discern Sustainability ("the Minerva team") have followed the exercise delivery approach proposed in our formal project brief submission, to meet the Fund's exercise requirements:

Goal	Task	Status
Examine	Look at your current position, reviewing relevant documentation and Pension Committee minutes;	✓
Benchmark	Examine Fund's equity and bond holdings data across 9 managers for bench-marking;	✓
Inform	Hold a workshop where our initial findings are delivered, and engage with Members and Officers on investment beliefs; and	✓
Deliver	Take on board feedback, refine reporting and any proposals, and return to deliver final report at formal Pensions Committee meeting.	December

In this SDG mapping project report, we begin with an Executive Summary before describing the approach taken to map the Fund's investments to the SDGs, as represented by the World Benchmarking Alliance's SDG 2000 benchmark. We elaborate further on the mapping method taken and cover its strengths and weaknesses, before presenting the findings of our analysis of the Fund's investments. We conclude the report by summarising the 'Inform' activity that took place in the online Workshop that we held with Officers and Elected Members in October, setting out the high-level outcomes, before ending with a Summary of the exercise.

Minerva Analytics & Discern Sustainability

18th November 2020

2 Executive Summary

Having examined the Fund's investment arrangements, focussing on the Fund's prioritised outcomes, we can report the following high-level summary:

Table 1: Key Facts

Key Facts	Outcome
Investment Managers analysed	Nine
Manager mandates covering ESG, SDG or Climate Change	One
WBA SDG2000 Overlap by Count of Companies / % of Assets Analysed	870 / 43%
WBA SDG2000 Overlap by Value of Companies / % of Assets Analysed	£1.86bn /63.2%
Portfolio companies analysed referencing Taskforce for Climate-Related Financial Disclosures (TCFD) / % of Assets Analysed	38% by number or 53.2% in £ invested (£1.56bn)
Surrey's initial greatest exposures to the SDGs *(as defined by the SDG2000 benchmark):* SDG8 – Decent Work & Economic Growth SDG13 – Climate Action SDG12 – Responsible Consumption & Production	 £2.16 billion £1.99 billion £1.82 billion
Surrey's initial smallest exposures to the SDGs by Sector: *(as defined by the SDG2000 benchmark):* SDG4 – Quality Education SDG15 – Life on Land SDG14 – Life Below Water	 £0.39 billion £0.42 billion £0.42 billion

2.1 Key Facts – Further Details

- Nine of the Fund's current investment managers, covering all of its equity and corporate bond investments, provided qualitative and quantitative information that was analysed in this exercise.
- None of the existing investment managers' investment management agreements (other than the LGIM Low Carbon portfolio) has any specific references to incorporating ESG, climate change, or SDG-alignment factors into their specific mandates besides proxy voting matters.
- The qualitative analysis of managers' policies and sophistication of ESG strategies identified practices that can be described as either Developing or Good.
- Using the SDG2000 benchmark to measure the Fund's current starting position with respect to the SDGs, we found that:
  - → At the end of December 2019, the Fund's investment managers collectively held **870 (43.5%) of the 2,000 companies in the SDG2000** that are deemed most likely by the WBA to help deliver the SDGs by 2030;
  - → The Fund had a total of **£1.86bn invested** in these 870 companies' equities and corporate bonds, **representing 63.2% of the total value of the in-scope assets** as at end December 2019. Note: Despite the high overlap, **<u>this is not by design</u>**. None of the managers surveyed is employing an SDG selection strategy, either generally, or specifically for the portfolio(s) they manage for the Fund.
  - → The starting Fund's in-scope holdings and value of economic exposure **to each of the 17 SDGs have been calculated,** with the top three greatest and least exposures summarised in the following table:

Table 2: Headline SDG Exposures

Greatest Exposures		Least Exposures	
SDG	£ Invested / Individual Holdings	SDG	£ Invested / Individual Holdings
8 DECENT WORK AND ECONOMIC GROWTH	£2.16 billion	4 QUALITY EDUCATION	£0.39 billion
	2,596		388
13 CLIMATE ACTION	£1.99 billion	15 LIFE ON LAND	£0.42 billion
	2,624		549
12 RESPONSIBLE CONSUMPTION AND PRODUCTION	£1.82 billion	14 LIFE BELOW WATER	£0.42 billion
	2,419		556

- Using Minerva's Sustainability Governance Rating to measure company standards in relation to governance and sustainability, including climate change, most of the Fund's underlying investee companies can be classified as being, on average, either 'Good' or 'Developing' in their approach;
  - → At the end of December 2019, **approximately 38% of the Fund's listed equities covered by Minerva's analysis had made some material reference to TCFD** in their latest public disclosures in their Annual Reports and Accounts. By material reference, we mean an investee company's explicit or implicit alignment with the recommendations of the TCFD;
  - → This equated to **approximately 53% in £ invested (£1.56bn) in investee company securities that made reference to TCFD** in their public disclosures; and
  - → A **number of investment risks and opportunities to the Fund were identified** within its assets, in relation to the transition to sustainability and a low carbon economy.
- At the Workshop that took place with Elected Members, Officers and the Independent Advisor, we discussed the findings of the project, and suggested that there are at least three potential ways to use the results of this exercise to integrate the SDGs into the Fund's investment strategy:
  - → Close monitoring of and engagement with SDG2000 constituents;
  - → Making the case to Border to Coast for a formal approach towards SDG alignment; and
  - → Committing Fund capital to a specific SDG-focussed product(s).
- Having duly considered the findings of this SDG mapping exercise at the Workshop, the Pensions Committee decided that it should inform further actions in relation to the Fund's approach to the SDGs, investment strategy and investments, focussing on:

→ Developing a framework for selecting, monitoring and evaluating investment managers that includes SDG metrics;

→ Building a formal framework for engagement with, and divestment from, underlying investee companies; and

→ Integrating the SDGs into investment manager engagement activity, focusing on activity undertaken by BCPP and LGIM where possible.

3 Our Approach to the SDG Mapping

The United Nations' Sustainable Development Goals ("SDGs") are, at just five years old, very young in investment terms. Only very recently have asset managers begun creating products and approaches specifically aligned to the SDG. Surrey is– as far as we are aware – the first LGPS pension scheme (and quite possibly one of the first UK pension schemes) to actively seek to create a link between their investment approach and the SDGs.

At the heart of any client exercise, Minerva's approach is to use independent, robustly defensible, and academically evidenced good practice or regulatory standards. The SDGs are no different. Given that approaches to align investments with the SDGs continue to evolve, part of our own approach is to ensure that Surrey is not tied to a "one size fits all" vendor-specific solution. Instead, we are equipped with solutions that can flex and respond as attitudes and approaches towards the SDGs, including potential regulation, develop over time.

Minerva measured the Fund's current position in relation to SDG alignment using the World Benchmarking Alliance (WBA) SDG2000 list.[1.] The SDG2000 is an analytical framework that has been developed in conjunction with leading accounting and investment practitioners to identify robust ways of measuring progress against the SDGs. We chose the WBA because its approach to the SDGs is both distinctive and pragmatic. Rather than, as with most vended methodologies, merely focus on the companies with the most 'green revenues' (itself difficult to estimate) or least controversial activities (potentially highly subjective), the WBA looks at negative and positive impacts combined with 'clout', the size and footprint of a company, and asks the question: *"what if this company aligned with the SDGs?"* These 2,000 keystone companies are, therefore, the companies where a pivot to the SDGs would produce the greatest impact, regardless of where they currently are in their sustainability journey, and where investors, through engaged stewardship, can play a role in encouraging companies to realise their latent net impact.

Using the SDG2000 as the core project framework, we have produced research, data and insights which benchmark the Fund's existing investments against the WBA companies and have identified those investments most likely to 'move the needle' towards delivering the SDGs. We have also assessed the bench strength of the Fund's asset managers on ESG and any known plans to use the SDGs. Consequently, Surrey is now better placed to understand its current position, in terms of where there is the potential to closely align with the aims of the SDGs and where there it is not, from both fund manager and individual portfolio holding perspectives. The exercise is predicated on understanding potential within the portfolios and manager responsibilities on stewardship 'as they are'. This does not preclude options to develop bespoke SDG fund solutions, later.

3.1 Starting the SDG Mapping Exercise

As set out in the introduction to this report, we have taken a four-step approach to the delivery of the SDG mapping project objectives for the Fund. Set out on the next page is some additional information on how we have approached the first two steps in the project, 'Examine' and 'Benchmark':

[1] https://www.worldbenchmarkingalliance.org/research/sdg2000-methodology/

3.2 Examine

The purpose of the 'Examine' stage was to carry out a mostly ***qualitative assessment*** of where the Surrey Pension Fund and its external investment managers sit from a general sustainable investment perspective. It included giving consideration as to whether any specific commitments or policy alignments had already been made towards the delivery or promotion of the SDGs. The 'Inputs' for this first step in the project covered a range of written documents, including:

- Surrey Pension Fund investment and governance policies;
- Pensions Committee reports and minutes;
- Surrey's managers' investment mandates & specific asset manager agreements; and
- Routine and special reporting from the Fund's managers.

Working with Officers of the Fund, we agreed the range of managers 'in-scope' for the exercise, which included the specific parts of their existing mandates that covered equity and corporate bond investments. Since the Border to Coast Pensions Partnership is increasingly closely involved with the investment management of Surrey's assets, we also paid particularly close attention to their voting, governance and sustainability policies.

As part of the information collection aspect of the 'Examine' stage, we also sent each of the in-scope managers a questionnaire to complete. This questionnaire covered a wide range of active ownership topics, grouped under the following categories:

- Portfolio Description;
- Portfolio Environmental, Social and Governance ("ESG") Approach;
- Firm-wide ESG Practices;
- Voting & Stewardship.

Through the questionnaire, we sought to understand each manager's approach to:

- Sustainable investment; and
- ESG factors, including:
    - Climate change (via TCFD disclosures); and
    - the SDGs.

The questionnaires were augmented by stewardship information disclosed on each manager's website. We also carried out a review of each manager's latest UN-backed Principles for Responsible Investment Transparency Reporting[2]. We then reviewed all the information and created a 'Sustainability Profile' for each manager. Finally, overlaying our knowledge and expertise, we devised an easily-understandable visual 'dashboard' to summarise our analysis of the qualitative information (effectively turning them into additional quantitative data) to show how each of the Fund's managers were 'scored' by us.

[2] https://www.unpri.org/signatories

Table 3: Managers Reviewed

Asset Manager	Asset Class	Value @ 31/12/19	Comments
Aviva	Equities and Corporate Bonds	£131.0m	Approximately half of the value shown was invested in instruments other than equities and corporate bonds (e.g. derivatives), and so was excluded from the SDG mapping exercise.
Baillie Gifford	Equities and Corporate Bonds	£176.2m	Most of the value of the portfolio relates to investments in pooled funds, which were beyond the scope of the data gathering. This manager was therefore not qualitatively analysed.
Border to Coast	Equities	£1,111.7m	The majority of these investments were included in the exercise (e.g. cash was excluded).
Franklin Templeton	Corporate Bonds	£72.3m	The majority of these investments were included in the exercise.
Legal & General	Equities	£985.2m	The majority of these investments were included in the exercise.
Majedie	Equities	£262.1m	The majority of these investments were included in the exercise.
Newton	Equities	£379.6m	The majority of these investments were included in the exercise.
Ruffer	Equities and Corporate Bonds	£131.1m	Approximately half of the value shown was invested in instruments other than equities and corporate bonds, and so was excluded from the mapping exercise.
Western	Corporate Bonds	£456.4m	Approximately half of the value shown was invested in instruments other than corporate bonds, and so was excluded from the mapping exercise.
Total		**£3,705.6m**	All managers except Baillie Gifford had their ESG policies, processes and supplied evidence of implementation assessed.

3.3 Benchmark

The 'Benchmark' stage of the SDG mapping exercise was focussed more on carrying out the ***quantitative assessment*** of the Fund's investments, central to the delivery of the project, and specifically required to meet the key objective of establishing '*The starting position of the Fund against the UN SDGs*'.

At the same time as we contacted each of the in-scope managers for the qualitative information needed, we also asked them to provide quantitative information relating to the underlying portfolios that they managed for Surrey. Each manager was asked to provide portfolio data for a three-year period encompassing Q1 2017 to Q4 2019. For those managers whose mandates were not in place for that specific period, they were asked to provide as much information for that period as possible. We then ingested the portfolio holding data as provided into the Minerva database, to allow us to carry out a two-part quantitative analysis:

1. **For SDG Alignment:**
    a. using a 2019 year-end "snapshot basis", identify the number and value of holdings in the Fund that were constituents of the WBA SDG2000 benchmark.
2. **For SDG and Climate Stewardship Potential:**
    a. Where data was available, assess the Fund's holdings against the Minerva Sustainability Governance Rating for each portfolio;[3]
    b. Where data was available, determine an investee company's explicit or implicit alignment with the recommendations of the Financial Stability Board's Taskforce on Climate-related Financial Disclosure[4] ("TCFD"); and
    c. The extent and quality of each manager's policies in relation to climate change was also factored into its overall qualitative bench strength assessment.

Given the potentially wide scope of reporting possibilities, we have focussed on addressing the three specific areas we identified in the Project Plan. The option remains for us to provide additional analysis and reporting that may be required following any further discussion of this report with Officers, the Pensions Committee, and the Independent Advisor.

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[3] Minerva analyses >90% of the World's listed equity markets by value but does not necessarily cover every security in either the SDG2000, or Surrey's entire portfolio of investments – e.g. the Fund's property and private markets investments or SDG2000 companies which are themselves private companies.

[4] Source: https://www.fsb-tcfd.org/. Our analysis looks for both explicit references to the TCFD recommendations as well as practices that are aligned to TCFD but not necessarily labelled as such.

4 Mapping the SDGs – Which Framework?

Surrey's priority exercise outcome(s) addressed in this section of the report are:

	Informing & assisting the Fund in identifying its Core Investment Beliefs against specific SDGs and how they fit into its Investment Strategy;
✓	**The starting position of the Fund against the UN SDGs;**
	How the Fund can continue further as Impact Investors and integrate the SDGs into its Investment Strategy;
	Where there is an investment risk/opportunity to the Fund, within its assets, in relation to the transition to sustainability and a low carbon economy;
✓	**The methods used to map sustainability to investment strategy and how robust they are; and**
	The Fund's own Responsible Investment approach and in the context of Border to Coast Pensions Partnership.

To meet the stated objective of understanding the Fund's starting position in relation to the SDGs, our proposed solution was to take a two-pronged approach:

- Firstly, to compare the Fund's individual equity (and associated corporate bond holdings) to the World Benchmarking Alliance (WBA) SDG2000 benchmark, looking for the overlap in companies held between the two data sources.

- Secondly, the Fund's portfolios and the SDGs were mapped against the widely-used Industry Classification Benchmark ("ICB").[5] This enables us to identify important industry and sector-specific ESG targets and goals which will either contribute or detract from SDG performance.

It is useful to spend a moment talking about the SDG2000, to note why we think it represents the best map to use when considering the alignment between the Fund's investments and the SDGs.

The WBA is an independent organisation, with funding coming from a number of partners, including the Ministry of Foreign Affairs of Denmark, the German Federal Ministry of Economic Cooperation and Development, the Netherlands' Ministry of Foreign Affairs, and UK Aid, which is itself funded by the UK Government's Foreign, Commonwealth & Development Office.

The WBA seeks to generate movement around increasing the private sector's impact towards a sustainable future for all, and is working to incentivise and accelerate companies' efforts towards achieving the SDGs. The WBA believes that the private sector has a crucial role to play in advancing the SDGs, but to boost companies' motivation, there needs to be real change in the way that their impact is measured. That is why the WBA have developed – and continue to develop - transformative benchmarks that compare companies' performance on the SDGs. The benchmarks are the result of extensive, systems-based academic research on the connectivity of economic activities and social and environmental effects. They also leverage existing international norms and standards. The WBA benchmarks aim to empower all stakeholders, from consumers and investors to employees and business leaders, with key data and insights to encourage sustainable business practices across all sectors. The benchmarks' methodologies are also open access and are continually improved through an ongoing and open multi-stakeholder dialogue.

[5] https://www.ftserussell.com/data/industry-classification-benchmark-icb

4.1 WBA SDG2000

As the private sector will be critical in helping achieve the UN's Sustainable Development Goals by 2030, the WBA SDG2000 benchmark list identifies the 2,000 most influential companies, from Algeria to Vietnam, that are going to shape our future. The WBA's hope is that, in using the SDG2000, investors such as Surrey can promote a 'race to the top' in which company leaders are motivated to do more and company laggards are held to account.

The WBA SDG2000 framework is fully integrated with Minerva's sustainability governance frameworks, enabling Minerva to produced independent and objective insights and data against the public rankings of the world's companies with the greatest potential to transform systems and influence outcomes on the SDGs. From this, Surrey is now able to better understand its current position, where there is close alignment with the aims of the SDGs and where there is not.

The presence of SDG2000 companies within the Fund's portfolios, at whatever level, at this stage, represents unrealised potential positive impact rather than actual positive impact. Many of the companies in the SDG2000 currently perform poorly on conventional ESG and corporate governance metrics. It is the companies' industry sectors, geographical footprint, size and other structural factors that mean they have outsized impact potential. Understanding this means that Surrey can more effectively hold their investee companies individually accountable for their role in advancing the SDGs.

In Section 6 of this report, we set out what we have found when analysing the Fund's investments against the SDG2000. Before that, however, we summarise our findings from the analysis of the qualitative information collected from the Fund and the Fund's external asset managers, with a focus on the SDGs and as seen from a general sustainability perspective.

5 Initial Findings – Qualitative Perspective

Surrey's priority exercise outcome(s) addressed in this section of the report are:

	Informing & assisting the Fund in identifying its Core Investment Beliefs against specific SDGs and how they fit into its Investment Strategy;
✓	**The starting position of the Fund against the UN SDGs;**
	How the Fund can continue further as Impact Investors and integrate the SDGs into its Investment Strategy;
✓	**Where there is an investment risk/opportunity to the Fund, within its assets, in relation to the transition to sustainability and a low carbon economy;**
	The methods used to map sustainability to investment strategy and how robust they are; and
✓	**The Fund's own Responsible Investment approach and in the context of Border to Coast Pensions Partnership.**

The '**Examine**' step of our approach to the SDG mapping exercise resulted in Discern Sustainability reviewing all of the policies and documentation we collected as part of our initial data gathering that relate to Surrey, its external asset managers in general, and Border to Coast specifically.

In this report, we have prioritised the findings in relation to the Fund itself and Border to Coast, given the latter organisation's significant current and future involvement in the management of the Fund's investments. The scores for the qualitative assessment for each manager (including Border to Coast) have been created and integrated with the other SDG2000, Minerva Sustainability Governance Rating and TCFD data. We can say that the qualitative analysis of managers' policies and sophistication of ESG strategies identified practices can be described as either 'Developing' or 'Good'.

5.1 The Fund's Formal Approach to Responsible Investment

Surrey's current 'Responsible Investment' ("RI") position is to align with the LGPS Regulations, and:

- Surrey currently follows Border to Coast's RI, voting and engagement policies[6], even for assets managed outside of the pool;
- Surrey has made its own statement of compliance with the UK Stewardship Code 2012[7], even though as an asset owner, rather than an asset manager, it is not required to;
- Surrey has prepared TCFD-aligned fund reporting on the Fund's activities, and a report outlining this was considered by the Pensions Committee at its September 2020 meeting; and
- Surrey has moved into low-carbon investing through the fund managed by LGIM - but otherwise has not allocated dedicated funds with other hardwired sustainability objectives, nor required managers to meet an explicit standard.

In terms of our understanding of how Surrey interprets 'ESG', the three most important sentences we identified from the various policy documents that set the tenor of the discussion are, in our view:

1. **Long-term approach:** "*Well governed companies that manage their business in a responsible manner will likely produce higher returns over the long term*" and that "*the Committee wishes to*

[6] https://www.bordertocoast.org.uk/app/uploads/2020/08/Border-to-Coast-RI-Policy-2020-pdf.pdf

[7] https://www.frc.org.uk/investors/uk-stewardship-code/2020-uk-stewardship-code-(1)

have an active influence on issues of environmental, social or governance (ESG) concern with companies in which the Fund is a shareholder."

2. **Risk measurement and management:** "*The Committee requires the Fund Managers to take into account the implications of substantial "extra-financial" considerations, e.g., ESG or reputational issues that could bring a particular investment decision into the public arena.*"
3. **ESG policy:** *"The Fund has no specific policy on investing or divesting investments wholly with regard to ESG issues."* However, the Border to Coast RI Policy is more emphatic: *"Border to Coast will not divest from companies principally on social, ethical or environmental reasons"*. The policies emphasise engagement, instead.

We found these statements to be revealing, in that they show that the primary motivations expressed are:

a. **Reducing unnecessary ESG risk in investments,** as much from a reputational point of view (i.e. unintended negative consequences for Surrey);

b. **A negative stance on divestment.** We wondered if discussions between all the partners within Border to Coast on divestment may have yielded little in the way of agreement, and that the most conservative position possible was the only one that would pass: 'we do not divest'. Surrey's words stating 'no specific policy' could be read as studied agnosticism. While it is conceivable that the case was successfully made that no mandate exists for sector-level exclusions on 'ethical' grounds, it is apparently not considered here or in the Border to Coast material that, at times, divestment might be the financially prudent thing to do because ESG risks are material enough. Such an approach is consistent with generally accepted definitions of fiduciary duty, and so Surrey and the wider Border to Coast Pool membership may wish to consider this possible action, in the future.

5.2 Surrey's approach to ESG & Asset Managers

We were pleased to note that Surrey had already requested details from their external investment managers, including Border to Coast, on how they conduct ESG integration and stewardship, as a matter of good practice. Our aim in this report, therefore, is to provide a more detailed stock-take that will put Surrey in a stronger position from both internal and third-party perspectives.

The ESG and asset manager appointments and regular reporting materials we have received are of variable quality. This will partly reflect manager idiosyncrasies, but we also suspect is a product of history and a lack of consistency or more than a tick-box approach to ESG when it came to historic manager selection, e.g. the manager must be a UK Stewardship Code or PRI signatory.

Key Finding: There were no specific ESG references in any of the asset management agreements that we looked at, except for perfunctory voting matters. We have assumed no side letters exist on specific ESG requirements.

The disclosures in the 2018-19 Surrey Annual Report and Accounts ("ARA") meet the reporting minima set out by the LGPS Regulations, however there are significant opportunities for improvement to bring the Fund up to wider pension scheme investment practice. We know Surrey has already recognized this fact and we recommend that Surrey goes beyond the narrow scope of its existing reporting obligations. Surrey could take the opportunity to extend its disclosures in the ARA, including how it might interact more fully with members. The formal introduction of 'Implementations Statements' for private sector DB and DC pension schemes may yet come to apply to LGPS Funds and Surrey could get ahead of this development.

5.3 Divestment

We wonder if Surrey and the other Border to Coast founding members may have come to an impasse when it came to the topic of divestment. While divestment is not our main concern in this project, it is difficult to ignore, particularly in light of the recent Supreme Court ruling on the LGPS and ethical investments.[8] It may be the case that individual Pool members have to severally build up a *fait accompli* of core aligned policies (e.g. on coal), such that an overarching Border to Coast Pool policy then becomes within grasp, since it would then be easier for recusant member Funds to fall in with the majority.

We are mindful that the direction of travel with pooling means that Surrey may eventually have most of its assets invested with Border to Coast. Obviously, this eventuality makes a considered, comprehensive, and robust Border to Coast ESG approach & policy crucial.

[8] Government loses Supreme Court ruling on LGPS ethical investments 29 April 2020 [Online: LGC Plus]

5.4 Border to Coast's Approach to Stewardship

Considering how 'young' the Pool is, we classed Border to Coast approach in the 'Good' category in relation to Stewardship and ESG as demonstrated by their RI Policy, detailed Voting Policy and TCFD statement. The fact that they are looking at climate scenario analysis is an encouraging sign of a willingness to take a leadership approach and engage with emerging best practice.

Nevertheless, their approach relies heavily on the outsourcing of voting and stewardship activities, including collective engagement, to Robeco. We believe that this approach has been taken as a functional efficiency, and in our view Robeco is a credible partner with a platinum heritage in RI and ESG. As an overlay provider, Robeco's reporting is of high quality and Robeco's external auditor audits active ownership controls on an annual basis, as this audit is part of their annual International Standard for Assurance Engagements control (AAF 01/06).[9] It should be noted that AAF01/06 is an audit of the procedures and controls associated with the implementation of stated policies, not a review of the quality or relevance of their engagement on specific stewardship or ESG issues.

On climate change in particular, Border to Coast has set out its position well in terms of how climate could affect its investments and also acknowledging its limitations, for example, in the discussion of carbon footprinting in its TCFD report, of which it is (justifiably) critical.

One area where we believe needs more work is demonstrating the 'how' and the outputs of ESG integration for the assets that it manages in-house. In the Border to Coast Annual Responsible Investment & Stewardship Report 2019/20,[10] Daniel Booth, CIO, says:

"For our internal portfolios, in addition to conducting quarterly screening and benchmarking, we also incorporate ESG risk consideration at the individual stock level. Portfolio managers complete detailed investment analysis, including in depth review of ESG factors for portfolio investments, with the support of our Research and RI team. We also include an ESG questionnaire as part of our request for proposal process for selecting external fund managers and private market funds, and on an annual basis after appointment, which are assessed by our portfolio managers and RI team." [page 5]

Border to Coast's identified priorities for 2022 are sound, in our view:

a. Well-embedded ESG tools and analysis across asset classes for both internally and externally managed sub-funds;

b. A holistic engagement framework in place, tracking milestones across portfolios and asset classes;

c. A well-researched approach to requiring disclosures to support our investment process; and

d. The PRI Principles embedded throughout [their] procurement process and contract monitoring.

There is some mention of the Sustainable Development Goals in the context of Robeco's engagements and how these could be more SDG-focused. This is something that could be explored further, given the potential overlap between the SDGs and an engagement-led approach.

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[9] AAF 01/06 Assurance Reports On Internal Controls Of Service Organisations Made Available To Third Parties [Online: ICAEW]

[10] Border To Coast Responsible Investment And Stewardship Report 2019/20 [Online: Border to Coast Website]

5.5 Qualitative Assessment Summary

Overall, we are broadly satisfied with the RI/ESG/Sustainability information provided on Border to Coast and its RI agents. Going forward, the Fund may well wish to discuss with Border to Coast its current managers' approaches on RI, ESG, sustainability and SDG-alignment. Certainly, more could, and should, be demanded of the poorer performing managers to close the gap. Minerva can make recommendation on this, if desired.

We recommend that the Fund looks deeper into Border to Coast's internal approach to ESG integration, as well as seeking to understand the role of ESG in the external asset manager selection and monitoring process. This latter point is of particular importance, given that Border to Coast's present and future influence in this area is so highly consequential for Surrey, overall.

6 Initial Findings – Quantitative Perspective

Surrey's priority exercise outcome(s) addressed in this section of the report are:

	Informing & assisting the Fund in identifying its Core Investment Beliefs against specific SDGs and how they fit into its Investment Strategy;
✓	**The starting position of the Fund against the UN SDGs;**
	How the Fund can continue further as Impact Investors and integrate the SDGs into its Investment Strategy;
✓	**Where there is an investment risk/opportunity to the Fund, within its assets, in relation to the transition to sustainability and a low carbon economy;**
✓	**The methods used to map sustainability to investment strategy and how robust they are**; and
	The Fund's own Responsible Investment approach and in the context of Border to Coast Pensions Partnership.

The '**Benchmark**' step of our approach to the SDG mapping exercise saw us take the Fund's existing investments – at the individual portfolio holding level as provided by the in-scope managers – and ingest this information into the Minerva database. There were three main reasons for doing this:

1. **To analyse** the existing investments to establish the Fund's starting position against the SDGs (as represented by the SDG2000);

2. **To identify** material leaders or, more importantly, laggards which would likely increase the risk of undershooting achievement of the SDG goals, we needed to assess the quality of the sustainability governance of the investee companies using Minerva's Sustainable Governance Rating framework; and

3. **To help inform discussions** with the Fund related to investment risks & opportunities in relation to the transition to sustainability and a low carbon economy, we needed to identify which of the Fund's existing investee companies were or were not making emissions disclosures in line with TCFD reporting standards.

6.1 Fund Starting Position vs the SDGs

Fund Exposure by Individual SDG2000 Company

Having ingested the individual equity and corporate bond holdings from the Fund's asset managers, we aggregated them together to effectively create a single line entry listing the Fund's economic exposure to each single company.

Comparing the Fund against the SDG2000 we found **an overlap of 43.5%**.

This means that, as at the end of 2019, of the 2,000 companies deemed by the WBA as having the greatest potential to help deliver the SDGs by 2030, **the Surrey Pension Fund had economic exposure to 870 of them** across all of its managers.

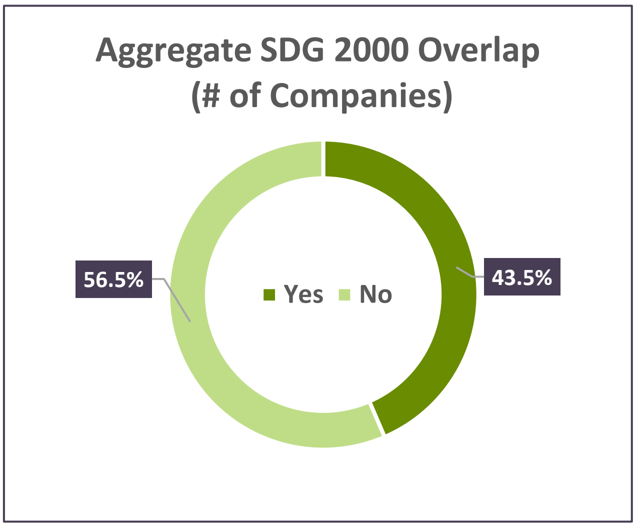


Figure 1: SDG Overlap by # of Companies Overall

It is important to note that this **this overlap is purely accidental**; neither the Fund nor its external asset managers have in place any specific instructions that would have resulted in a conscious alignment with either the SDGs or the SDG2000 (which itself only came into being at the end of 2019).

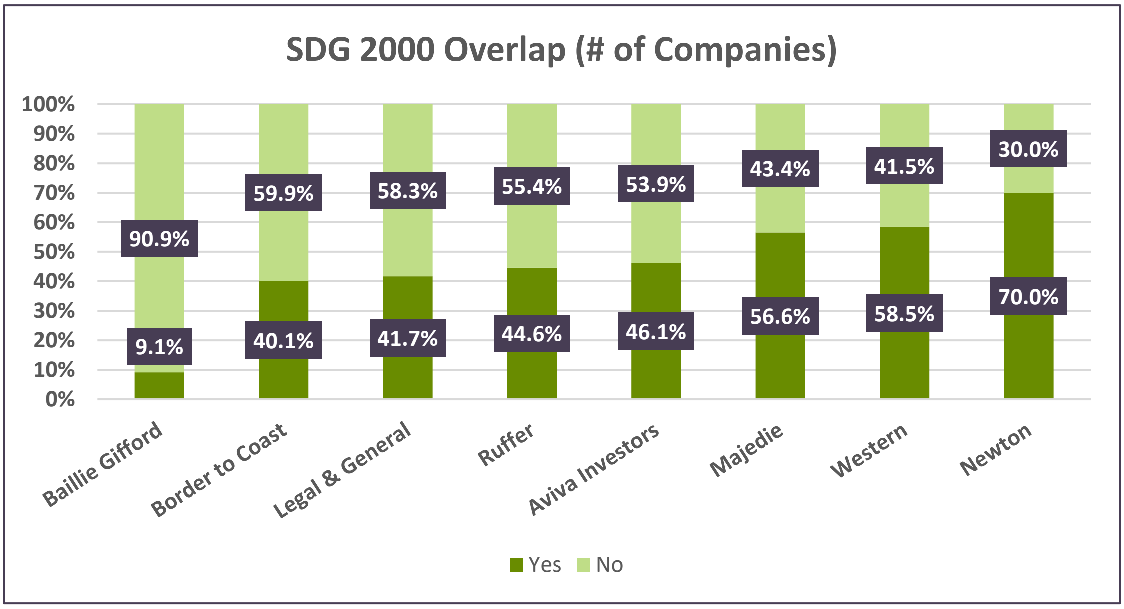


Figure 2: SDG Overlap by Manager

The next piece of analysis undertaken was to show the distribution of this overall exposure to the SDG2000 across the in-scope managers. The chart above shows the overlap between the holdings in each of the managers' portfolios and the SDG2000 companies, again as at 31-Dec-19. Whilst there is a slight anomaly in terms of the Baillie Gifford portfolio (as most of the investments in the DGF are in pooled funds), the percentages shown for the other managers are an accurate reflection of their portfolios' exposure to the companies in the SDG2000.

Newton had the greatest exposure to companies in the SDG2000. This is again an accidental occurrence, and a by-product of their managing a large cap US equity mandate, since some of the largest US companies are prominent members of the SDG2000. We note that Newton is the one manager with a stated intention to bring an SDG product or approach to market, though it is almost certainly coincidental to the WBA overlap, being explained by the US large cap bias. Border to Coast had the lowest exposure to the SDG2000 companies, with only just over 40% holdings overlap.

Fund Exposure by £ Invested in SDG2000 Companies

Whilst the overlap of the number of companies between those held in the Fund and those in the SDG2000 is of interest, the Fund's true economic exposure to the SDG2000 companies makes for more interesting reading.

Having analysed the Fund portfolio holding valuation data for 31/12/19, we saw that of the £2.94bn ingested from in-scope managers and assets, **£1.86bn – or 63.2% -** of the total 'in-scope' value **was invested in SDG2000 holdings**. This presents a much more meaningful picture in terms of the Fund's economic exposure to the companies most likely to deliver the SDGs, should they be governed and managed on a sustainable basis (see below for further discussion).

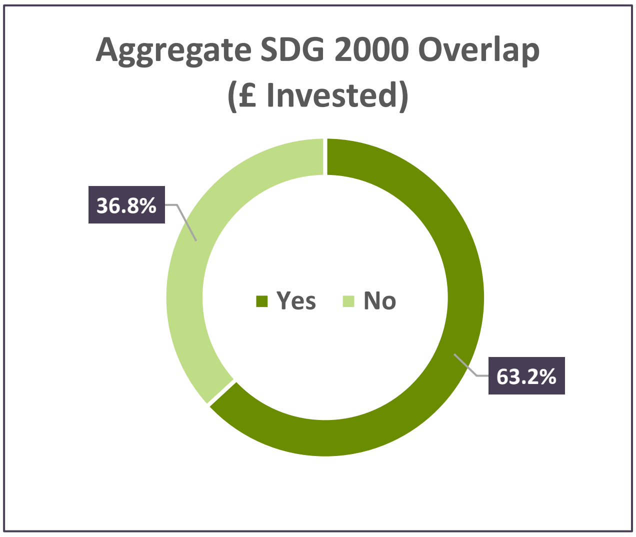


Figure 3: SDG Overlap by £ Invested Overall

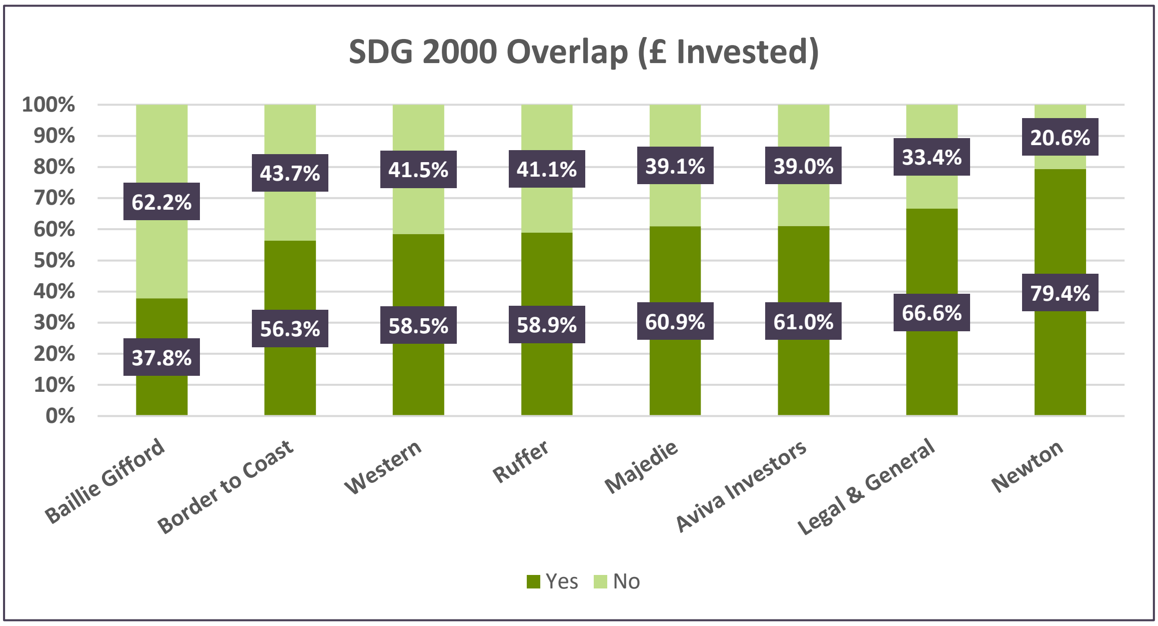


Figure 4: SDG Overlap £ Invested by Manager

The associated piece of analysis shows the value invested in SDG2000 companies for each of the in-scope managers. The previous chart again shows the overlap between the holdings in each of the managers' portfolios and the companies listed in the SDG2000 as at end December 2019, but this time from a £ invested perspective. Again, setting aside the Baillie Gifford portfolio due to its predominantly pooled fund structure, the percentages shown for the other managers are an accurate reflection of their £ invested in the companies in the SDG2000.

Newton again had the greatest economic exposure to companies in the SDG2000, and Border to Coast had the lowest exposure to the SDG2000 constituents, with only just over 56% of their portfolios being in the index – however, this still represent a total of £0.59bn of the Fund's total value.

Fund Geographical Exposure by Individual SDG2000 Company

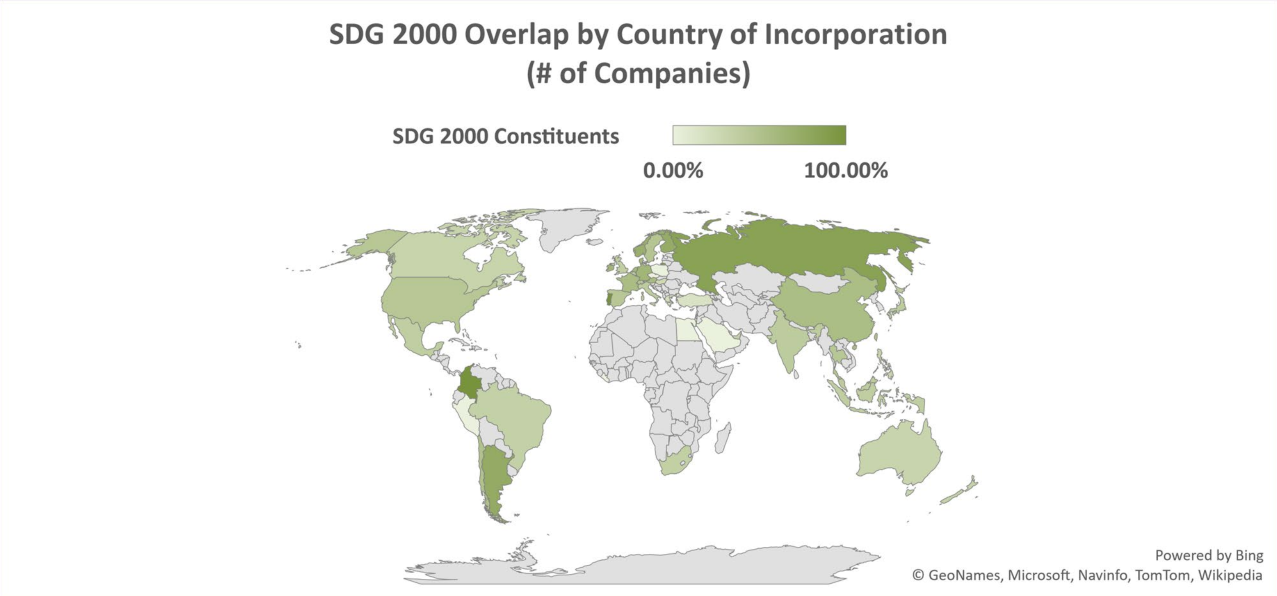


Figure 5: SDG2000 Overlap by Country (# of companies)

When looking at the geographical distribution of Fund's companies in the latest portfolio valuation data provided against the SDG2000; the data shows that the **US market** concentrates the biggest number of companies, followed by the **UK market,** with a proportion of **33% and 11.3% respectively**, of the companies contained within the fund. Looking at the proportion of SDG2000 constituents in the forementioned countries, **44.9% of the companies in the US market** are listed in the SDG200, whereas **36.4% of the companies in the UK market** are in this list, as at 31 Dec 2019.

Fund Geographical Exposure by £ Invested in SDG2000 Companies

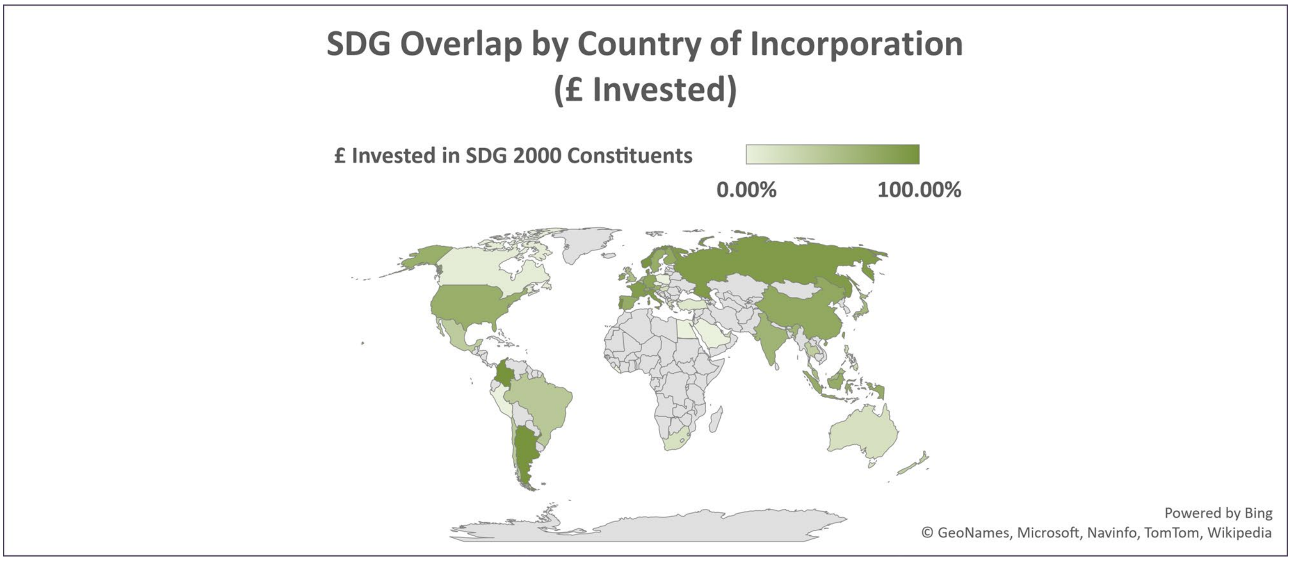


Figure 6: SDG2000 Overlap by Country (£ of investment)

Interestingly, when conducting an analysis of the geographical distribution of the value invested in SDG2000 companies, the **UK market is ahead, with 32.4% of the total value invested,** followed by the **US market, with 30.8%**. Therefore, these two markets concentrate 63.2% of the value invested. However, while **70.7% of the value invested in US is in SDG 2000 constituents, for the UK market,** this percentage only represents **53.8%** of the value invested.

6.2 Minerva's Sustainability Governance Ratings

In order to determine the stewardship and engagement momentum needed to drive the SDG potential in each company, the second part of the '**Examine**' step in our review was for Minerva to analyse the Fund and individual portfolios from a 'governance of sustainability' perspective.

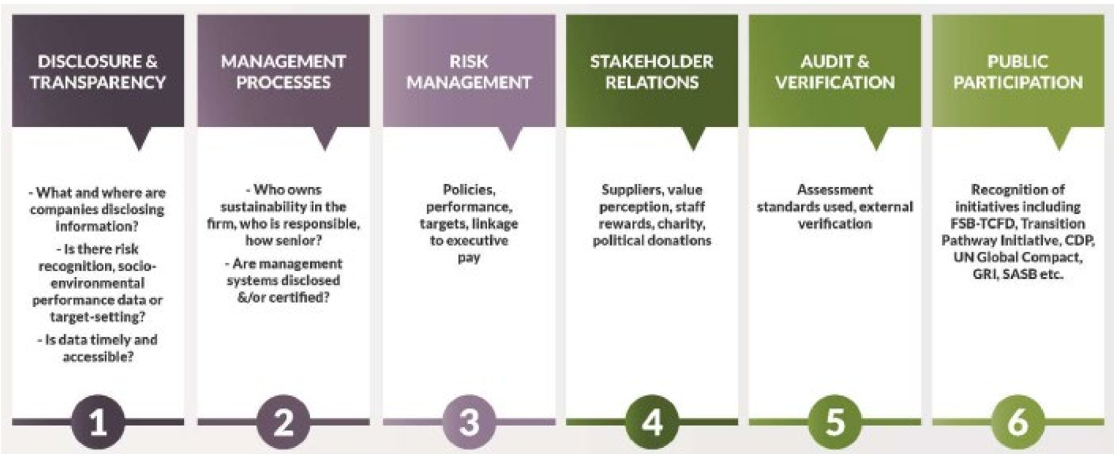
In almost every global market, securities regulators and industry codes of best practice identify ESG and stewardship as a fiduciary responsibility. Key regulatory initiatives are driving stewardship responsibilities, requiring more transparency and public reporting. Understanding how a fund is impacted by these developments is an important first step to meeting fiduciary objectives.

Minerva's Sustainability Governance Rating ("SGR") measures the alignment of the Fund against global corporate governance and sustainability good practices. The rating works not only at portfolio level, but also cascades down to individual holdings (equities and fixed income).

Minerva's philosophy is to understand the governance of sustainability by issuers, with emphasis on their disclosure of sustainability risks, management, and accountability. The SGR therefore assesses a company across seven pillars of good practice which are fully-aligned with TCFD, Transition Pathway Initiative, UN Global Compact, OECD and ICGN governance principles. In this way the score offers a consistent measure of a company's governance and sustainability maturity rather than performance in respect of specific ESG topics.

Each portfolio constituent is attributed an overall score ranging from A to F (where A stands for best-in-class) representing its cumulative assessment of the governance standards. These scores are then aggregated to provide a single letter score perspective of the Sustainability Governance for the portfolio as a whole.

Figure 7: Minerva Sustainability Governance Pillars



Minerva Sustainable Governance Rating

Using the Fund's external asset managers' portfolio information as at 31-Dec-19, we analysed the holdings to create a Sustainable Governance Rating for each portfolio:

Table 4: Portfolio Sustainable Governance Rating

Manager/Fund	Pillar 1	Pillar 2	Pillar 3	Pillar 4	Pillar 5	Pillar 6	Pillar 7	Rating
	Board and Committees	Financial Reporting	Capital Stewardship	Audit and Reporting	Remuneration	Shareholder Support	Sustainability Governance	Overall
Portfolio 1	51%	100%	65%	69%	35%	94%	52%	Developing
Portfolio 2	60%	100%	64%	57%	49%	100%	33%	Basic
Portfolio 3	54%	100%	67%	74%	38%	96%	54%	Developing
Portfolio 4	59%	100%	67%	81%	65%	99%	43%	Good
Portfolio 5	54%	100%	66%	71%	40%	95%	51%	Developing
Portfolio 6	54%	100%	66%	73%	38%	94%	50%	Developing
Portfolio 7	43%	100%	64%	47%	38%	98%	43%	Basic
Portfolio 8	55%	100%	64%	76%	41%	92%	61%	Good
Portfolio 9	60%	100%	62%	80%	64%	93%	64%	Good
Portfolio 10	55%	100%	73%	75%	34%	98%	63%	Good
Portfolio 11	54%	100%	60%	68%	42%	93%	54%	Developing
Portfolio 12	52%	100%	59%	73%	34%	91%	51%	Basic

Key Takeaway: Achieving a high degree of symmetry between stock selection and ongoing stewardship is essential to help the Fund to achieve its objectives. From this analysis we can see **significant degrees of variance** across a number of dimensions of good governance practice – **notably in respect of sustainability governance factors which are aligned with the TCFD and TPI**. However, the summarised SGR results offer an insight which will help frame future discussions relating to setting and/or assessing external investment managers' approaches to stewardship and sustainability issues which can be addressed in the immediate near term.

6.3 TCFD Alignment of Underlying Fund Investments

TCFD Alignment by Individual Fund Equity Holding

The third, and final, part of the '**Benchmark**' step in our SDG mapping exercise project approach relates to the TCFD disclosures made by the Fund's underlying investee companies for which Minerva provides research coverage, across all of the Fund's external investment managers.

TCFD has become the de facto standard for disclosing climate related risks and opportunities. As part of our sustainability governance research process, we look not only for instances where companies have made generalised references to the TCFD but - to protect against box-ticking or 'green-washing' – but our analysts also review the detail of corporate disclosures looking for alignment with the TCFD's four core elements: Governance; Strategy, Risk Management and Metrics/Targets.

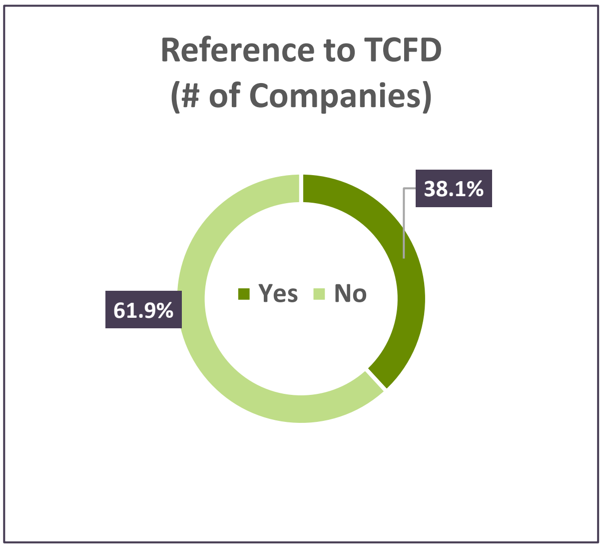


Figure 8: TCFD References by Companies

Minerva's analysts examined the Fund's holdings as provided by the Fund's managers – not just the SDG2000 constituents - and found that **just over 38.1% of the Fund's listed in-scope equities under coverage have had made some material reference to TCFD** in their latest Annual Report and Accounts.

TCFD Alignment by £ Invested in Individual Fund Equity Holding

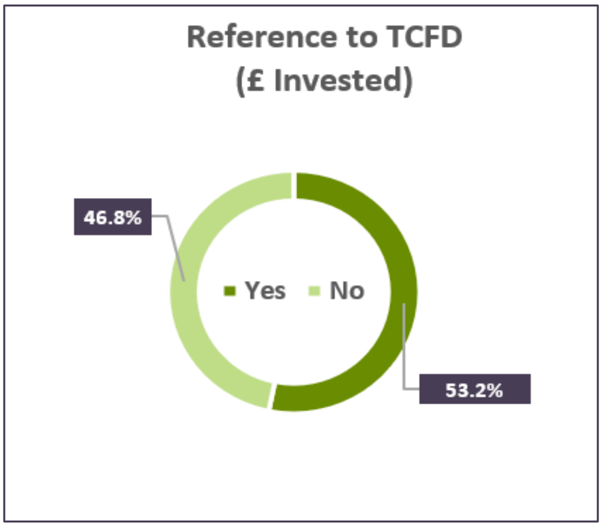


Figure 9: TCFD Reference by £ Invested

Whilst the number of companies held by the Fund making TCFD disclosures is of course of interest, again the Fund's economic exposure to such companies is likely to be more telling, given that it actually represents the money effectively at risk in terms of climate-related risks, and how underlying investee companies treat these risks.

The analysis showed that of the c£3bn analysed from in-scope managers and assets, **£1.56bn – or 53.2% - of the total in-scope value was invested in companies we cover that make meaningful reference to TCFD**.

Again, this presents a more helpful picture in terms of the Fund's economic exposure to the companies that do – and do not – seem to have identified climate change as a specific risk to their business model, and have begun making disclosure that are helpful to institutional investors, in terms of starting to assess which companies are taking the risk of climate change seriously. As TFCD has been around for the same time as the SDGs, having 53% of the Fund's investee companies by economic value use it as the charting process for climate strategy already is a promising result.

6.4 Quantitative Assessment Summary

Surrey's priority exercise outcome(s) addressed in this section of the report are:

	Informing & assisting the Fund in identifying its Core Investment Beliefs against specific SDGs and how they fit into its Investment Strategy;
	The starting position of the Fund against the UN SDGs;
	How the Fund can continue further as Impact Investors and integrate the SDGs into its Investment Strategy;
✔	**Where there is an investment risk/opportunity to the Fund, within its assets, in relation to the transition to sustainability and a low carbon economy;**
	The methods used to map sustainability to investment strategy and how robust they are; and
	The Fund's own Responsible Investment approach and in the context of Border to Coast Pensions Partnership

The quantitative assessment process of the Fund's underlying investments has produced the following high-level results, which address the key question posed by the Fund relating to its current position with regards the SDGs. As at the end of December 2019:

	43.5% of the Fund's listed equity holdings (including their associated corporate bonds) – or 870 companies in actual terms - were members of the SDG2000;
	However, a more meaningful measure of £1.86bn overlapped with the SDG2000 companies, representing **63.2% of the total in-scope value**;
	Almost all the Fund's external managers had a meaningful £ exposure to the SDG2000 companies;
	Minerva's Sustainability Governance Ratings for the UK and Global Equity portfolios totalling £1.04bn managed by Border to Coast were broadly positive; and
	53% of the in-scope assets by value, totalling £1.56bn, have made some reference to TCFD in their public disclosures, compared with only 38% of the Fund's investee companies by number.

The analysis undertaken and the results generated will help

Inform	Future discussions associated with the Fund's potential for SDG-aligned investment approaches;
Supplement	Qualitative analysis of the policies and implementation of incumbent and future asset managers, in giving a more complete picture, being independently assessed. The benefit of this is chiefly in making the relationship between owner and manager more symmetrical and so enable higher standards and better accountability; and
Contribute	Future deeper dives into investment risks and opportunities in the Fund's assets, in the context of the transition to sustainability and a low carbon economy.

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7 Investment Risks & Opportunities

When thinking about the Fund's investments in the context of sustainability and the low carbon economy, there are three levels where these issues can be addressed:

Fund level	**Policy**: setting an overarching policy, generated from Core Investment Beliefs, that shapes the direction of travel;
Manager level	**Expectations**: setting explicit expectations at the investment manager mandate level; and
Investment level	**Integration**: understanding how an investment manager incorporates these twin issues into their everyday individual investment selection, monitoring and engagement processes.

7.1 Investment Risks & Opportunities

The Fund's SDG mapping exercise undertaken by Minerva and Discern has revealed a number of investment risk and opportunity issues, on which Officers and Elected Members may wish to reflect.

It is perhaps not accidental in the key project objectives that Surrey wanted to know whether there was an "..*investment risk/opportunity to the Fund, within its assets*……" using a joined risk/opportunity phrase, since – from an investment perspective - one tends to be closely associated with the other.

Therefore in Table 5 on the following page we have summarised several key issues emerging from our analysis, together with what we believe to be their associated investment risks and opportunities in relation to the transition to sustainability and a low carbon economy.

Table 5: Investment Risks & Opportunities

Issue	Source	Why Investment Risk?	Why Investment Opportunity?
Absence of explicit ESG, climate change or SDG references in any of the Fund's external asset manager investment management agreements	Qual. Analysis	By not explicitly raising these issues, they could be unintentionally left out of the investment process	Adding the consideration of these topics to investment management agreements may help asset managers focus on, and then better understand, these issues
Insufficient detail/rigour in the Selection, Appointment and Monitoring process on RI/ESG by the Fund and by Border to Coast (though latter is recognised as an area for development)	Qual Analysis	The market is rife with greenwash and grade inflation, while there is still a large spread in the quality and sincerity of approaches by asset managers. Failure to uphold a high standard could indulge lacklustre approaches by managers and expose the Fund to the investment and reputational risk of being 'absentee'	Having a well-considered process for assessing asset managers' approaches to sustainability has the potential to result in more risk aware managers being appointed, investing in better run companies who should deliver better long-term investment returns
Voice versus Exit. Omission of the option of divestment from an existing investment on ESG grounds.	Qual Analysis	Not having the option of divesting from companies that are unwilling or unable to mitigate highly material ESG risks or who are unwilling to address similar governance failings reduces the Fund's choices	Having the option to divest provides the opportunity to reallocate capital to other, more sustainably-managed – and therefore more risk-aware – investment opportunities
Analysis has identified the current overlap between the Fund's existing investments and the SDG2000 companies	Quant Analysis	Analysis has identified the lowest sustainability-rated holdings of the Fund's SDG2000 holdings, which represent a potential investment risk if company management are not identifying and addressing all known risks and issues	Taking a proactive identification and engagement approach with the lowest sustainability rated of the Fund's SDG2000 holdings, the Fund has the potential of improving these investee companies' governance of sustainability issues, to potentially improve long term returns
Analysis has identified the current overlap between the Fund's existing investments and companies that publicly state some appreciation of TCFD reporting requirements	Quant Analysis	A significant proportion of the Fund's existing investee companies have made no disclosures relating to TCFD, and so they may not be taking full account of the risks posed by climate change	By seeking out companies that make TCFD-related disclosures, the potential exists that such better-run companies – in terms of being more climate risk aware – have the potential to deliver better returns over the longer term
Historic drivers of equity performance, at the asset class level, may no longer be relevant	Known External Issue	Any investment strategy modelling based on historic performance drivers is, by construction, unlikely to address recently emerging risks such as climate change	By incorporating sustainability and climate change factors into the investment strategy modelling process, the potential outcomes are more likely to reflect more closely the actual reality
Opportunity to implement new benchmarks aligned to SDGs	New Issue	Limited experience with SDG investing due to relative youth of concept	Incorporating SDGs into investment strategy can help to overcome "ethical subjectivity" often associated with ESG investing; new investment opportunities becoming available with pivot towards SDGs/Low Carbon transition

8 Integrating the SDGs

Surrey's priority exercise outcome(s) addressed in this section of the report are:

	Informing & assisting the Fund in identifying its Core Investment Beliefs against specific SDGs and how they fit into its Investment Strategy;
	The starting position of the Fund against the UN SDGs;
✔	**How the Fund can continue further as Impact Investors and integrate the SDGs into its Investment Strategy;**
	Where there is an investment risk/opportunity to the Fund, within its assets, in relation to the transition to sustainability and a low carbon economy;
	The methods used to map sustainability to investment strategy and how robust they are; and
	The Fund's own Responsible Investment approach and in the context of Border to Coast Pensions Partnership.

Whilst neither Minerva nor Discern are in the position of giving regulated investment advice, we were – and are – of the view that, in carrying out the SDG mapping exercise, certain possible options would become apparent as to how the Fund could move forward with its desire to more closely align its investment approach with the SDGs, and to integrate them into its investment strategy.

Having carried out both the qualitative and quantitative analysis on the Fund's listed equity (and associated corporate bond) holdings against the SDG2000, we see three main possibilities when it comes to incorporating the SDGs more formally into the Fund's overall investment approach:

1. **Close monitoring of SDG2000 constituents**

The Fund could, with the help of managers and advisers, agree to closely monitor its exposure to any underlying investee company in any manager portfolio that is also in the SDG2000 index, and their respective performance on the metrics that best reflect a positive or negative contribution to the most relevant SDGs. Given the close working relationship with Border to Coast, the Fund could specify to Border to Coast that Surrey wishes for them to pay particular attention to any such company, and to create a monitoring and engagement policy for them that ensured SDG laggards were identified and contacted, and that SDG leaders were supported and encouraged to strive towards helping deliver the SDGs. There is also logic in asking for those companies who are strong performers on more conventional ESG measures to consider and act on the implications of the WBA analysis. The WBA approach, on its own terms, only has merit if all companies in a benchmark, regardless of their stage of evolution, take the necessary steps to close the 'SDG gap'.

Given that the Fund is in a state of transition as regards pooling, such an approach would have the benefit of not actually requiring any specific short-term changes to the Fund's managers, mandates or indeed overarching investment strategy. It would allow the Fund to act on the SDGs now, while keeping more root-and-branch options under review, as manager approaches develop. Its weakness is that, even assuming managers will be willing to advocate the Fund's position, a positive outcome for engagement can never be assured and is difficult to attribute. It may appear merely as relying on the fallback of more engagement, buying time for a position of 'no change'.

2. **Formal inclusion of an SDG alignment standard**

The Fund could instruct its managers that in considering investee companies for the Fund to own, they must also include an agreed definition or standard in relation to the SDGs as part of the investment screening process. This may or may not include a formal link to the SDG2000 - but may have associated consequences for asset managers, portfolio benchmarks and even potentially fund investment strategy modelling, since certain sectors with SDG laggards (e.g. oil & gas) might effectively be excluded from the Fund's investible universe. A counter-intuitive aspect of the WBA2000 is that it does contain sectors with high, negative impacts - but is more concerned by what **could** be achieved by these and other companies in transformative activities pivoting to the SDGs.

3. **Committing Fund capital to a specific SDG-focussed product**

In the same way that the Fund has invested in a Low Carbon product with Legal and General, the Fund could take the same approach and create a passive or active SDG fund, with the option of incorporating the SDG2000 or an alternative (many are being developed by index providers and asset managers) either as the portfolio's benchmark or as a reference point for any mandate. Although this would provide a clear line of sight to the Fund's commitment to the SDGs, it could also be viewed as not fully aligning with the to-be-defined Core Investment Beliefs. For example, if the Elected Members believe that ESG factors, including climate change and the SDGs, should be considered by all companies, then there would be no need for individual mandates specifically set up to address the SDG alignment issue, as all investments should aim to do that. From a practical perspective, the fewer managers that have to adopt aligned approaches to SDGs, the greater chance of agreement and ability to assess results.

9 Workshop Summary

Surrey's priority exercise outcome(s) addressed in this section of the report are:

✓	**Informing & assisting the Fund in identifying its Core Investment Beliefs against specific SDGs and how they fit into its Investment Strategy;**
✓	**The starting position of the Fund against the UN SDGs;**
✓	**How the Fund can continue further as Impact Investors and integrate the SDGs into its Investment Strategy;**
✓	**Where there is an investment risk/opportunity to the Fund, within its assets, in relation to the transition to sustainability and a low carbon economy;**
✓	**The methods used to map sustainability to investment strategy and how robust they are; and**
✓	**The Fund's own Responsible Investment approach and in the context of Border to Coast Pensions Partnership.**

Minerva provided an initial version of this report to Officers, Elected Members and the Independent Advisor at the end of September 2020, as background reading for the project Workshop. These two steps represented the 'Inform' part of the 4 step process we have followed for this mapping exercise. The Workshop gave us the opportunity to present the findings of our analysis to the Pensions Committee for discussion, and for the Committee to consider whether we had met the Fund's original objective in carrying out this exercise, and what the findings might represent in terms of potential changes to the Fund's overall investment approach. Due to COVID-19 restrictions, the Workshop was held virtually on Thursday 15th October 2020. Minerva divided the Workshop into the following sections, to facilitate discussions around the SDG mapping exercise findings:

- Recap of the Surrey SDGs Mapping Project
- Review the project findings
- Discuss the findings in the context of:
  - PRI's Responsible Investment (RI) Framework
  - "Spectrum of Capital"
  - Surrey's Investment Strategy Statement
  - Border to Coast Stewardship & Investment Policies
- Consider next steps in the context of:
  - The SDGs and the Fund's Investment Strategy Statement (ISS) & stewardship policy
  - Prioritising any specific SDGs that have most investment relevance for Surrey

9.1 Workshop Outcome

The collective view was expressed that the exercise objectives had been broadly met, whilst acknowledging that the concept of aligning investments with the SDGs is still in its infancy, and recognising that there is no universally agreed approach in the investment industry to incorporating ESG considerations.

The analysis undertaken was helpful in terms of knowing where the Fund was starting from, in terms of its current approach to ESG factors and the SDGs. Given the direction of travel for Border to Coast to take on more of the Fund's investments to manage, particular attention to the Surrey/BCPP relationship was deemed of importance – and as the Fund also has a significant exposure to Legal & General, that relationship was also highlighted as being important in terms of next steps. The Committee believed that the exercise report provides sufficient assurance to enable a decision to move to the next stage of more detailed preparation and implementation. Further consideration would be given as to whether the Committee wants to prioritise any specific SDGs over any others.

10 Next Steps

We have now arrived at the final step in the SDG mapping exercise:

Deliver	Take on board feedback, refine reporting and any proposals, and return to deliver final report at formal Pensions Committee meeting

We have taken on board Officers', Elected Members' and the Independent Advisor's feedback following the delivery of the initial report and the holding of the Workshop, to create this final version of the Project Report. Minerva will be present at the next Pensions Committee meeting to summarise the content of this report, and to answer any questions that arise in relation to it during the meeting.

There were three main outcomes from the Workshop, that the Committee indicated are the next steps in terms of the SDG alignment journey:

1) Developing a framework for selecting, monitoring and evaluating investment managers that includes SDG metrics

The exercise identified the relatively early stage that all of the Fund's investment managers are at in terms of developing their own approaches to the SDGs. The qualitative analysis shone a light on this area, and as a result the Committee believe that the Fund needs to update its process when it comes to the appointment and ongoing monitoring of external asset managers, to include reference to the SDGs. This means that the Fund would seek to work with Border to Coast Pensions Partnership to include some agreed SDG metrics in any future investment manager appointment process, whilst also looking to update existing investment manager reporting to capture SDG alignment information.

2) Create a formal framework for engagement /divestment with investee companies

In identifying potential SDG alignment with existing investee company holdings, this exercise has made clear that companies' approaches towards the SDGs, and 'sustainable stewardship' in general, remain variable across industries, sectors and countries. Having a coherent, considered approach towards engaging with its investee companies to help deliver the SDGs is a logical outcome for the Fund from this exercise – since it is through engagement that companies will be encouraged to operate responsibly. The Fund should also consider reserving the right to divest from any given company, should its engagement policy deliver no tangible improvement in company behaviour or conduct. Therefore, the Committee intend to review the Fund's approach towards company engagement, and there is scope for the Fund to explore a collaborative approach with Border to Coast and Robeco to look to incorporate a common set of SDGs metrics.

3) Integrate the SDGs into investment manager engagement activity

Given the importance it has placed on aligning the Fund's investment strategy with the SDGs, the Committee also intend to review how the Fund's external investment managers should best address the topic of the SDGs in their engagements with underlying investee companies. This extends to consideration of how Border to Coast appoint and monitor external investment managers, as much as any directly made and held investment manager appointments and investments.

Officers will now take forward these three main project outcomes, and will work with the Committee to ensure any actions associated with the project outcomes are incorporated into the Fund's Investment Strategy Statement at the appropriate time. Minerva and Discern Sustainability remain available to assist in any way that may be deemed appropriate.

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11 Conclusion

Whilst the formal SDG Mapping Exercise is now drawing to a close, we believe that the information provided in this report, and through our regular contact with representatives of the Fund, has met the project brief.

The Fund is now in a better position in terms of understanding where it currently stands from a 'sustainable stewardship' perspective:

- Nine of the Fund's current investment managers, covering all of its equity and corporate bond investments, were carefully assessed through a sustainable investing lens, focussing on the alignment of the underlying investments with the SDGs, best practice sustainability, and TCFD reporting;
- Using the SDG2000 benchmark to measure the Fund's current starting position with respect to the SDGs, we found that there was a high overlap in the Fund's existing investments with the SDGs, although this was not necessarily by design;
- The Fund's greatest SDG exposures were to SDG 8: Decent Work and Economic Growth, SDG 13: Climate Action and SDG 12: Responsible Consumption and Production;
- The Fund's smallest SDG exposures were to SDG 4: Quality Education, SDG 15: Life on Land and SDG 14: Life Below Water;
- Using Minerva's Sustainability Governance Rating to measure company standards in relation to governance and sustainability, including climate change, most of the Fund's underlying investee companies can be classified as being, on average, either 'Good' or 'Developing' in their overall approach to sustainability;
- At the end of December 2019, approximately 38% of the Fund's listed equities covered by Minerva's analysis had made some material reference to TCFD in their latest public disclosures in their Annual Reports and Accounts;
- A number of investment risks and opportunities to the Fund were identified within its assets, in relation to the transition to sustainability and a low carbon economy;
- At the Workshop that took place with Elected Members, having duly considered the findings of this SDG mapping exercise, the Pensions Committee decided that it should inform further actions in relation to the Fund's approach to the SDGs, investment strategy and investments, focussing on:

  → Developing a framework for selecting, monitoring and evaluating investment managers that includes SDG metrics;

  → Building a formal framework for engagement with, and divestment from, underlying investee companies; and

  → Integrating the SDGs into investment manager engagement activity, focusing on activity undertaken by BCPP and LGIM where possible.

We would like to thank Officers, Elected Members, the Fund's Independent Investment Advisor and the Fund's external investment managers for their assistance and active participation throughout this exercise, and look forward to discussing the findings of this report further at their convenience.

Minerva Analytics & Discern Sustainability

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **11 DECEMBER 2020**

LEAD OFFICER: **ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**

SUBJECT: **COMPANY ENGAGEMENT & VOTING**

SUMMARY OF ISSUE:

Strategic objectives
Investment

This report is a summary of various Environmental Social & Governance (ESG) issues that the Surrey Pension Fund, Local Authority Pension Fund Forum (LAPFF), Robeco, and Border to Coast Pensions Partnership (BCPP) have been involved in, for the attention of the Pension Fund Committee. The Fund is a member of LAPFF so enhances its own influence in company engagement by collaborating with other Pension Fund investors through the Forum. Robeco has been appointed to provide BCPP's voting and engagement services so acts in accordance with BCPP's Responsible Investment Policy, which is reviewed and approved every year by all 12 partner funds within the Pool.

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

Reaffirms that ESG Factors are fundamental to the Fund's approach, consistent with the Mission Statement through;

- Continuing to enhance its own Responsible Investment Approach, its Company Engagement policy, and SDG alignment, referenced in the Investment Core Beliefs & SDG Mapping report.

- Applauding the outcomes achieved for quarter ending 30 September 2020 by Robeco in their Active Ownership approach and the LAPFF in its Engagement with multinational companies as at 30 September 2020.

REASONS FOR RECOMMENDATIONS

In accordance with The Fund's Mission Statement, as well as its Investment Strategic Objectives, the Fund is required to fulfil its fiduciary duty to protect the value of the Pension Fund, to meet its pension obligations. Part of this involves consideration of its wider responsibilities in Responsible Investment as well as how it exercises its influence through engaging as active shareholders.

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DETAILS:

Background

1. LAPFF is a collaborative shareholder engagement group representing most of the Local Government Pension Scheme Funds and UK Pension Pools, including Border to Coast Pensions Partnership (BCPP). Its aim is to engage with companies to promote the highest standards of corporate governance and corporate responsibility amongst investee companies. By

2. Robeco is an international asset manager, also carrying out independent research on various ESG issues, which can contribute to a company's investment strategy. By providing regular sustainability reports, it reinforces the fact that good corporate governance and social responsibility can enhance the long-term risk-return profiles of our investment portfolios. Robeco has been appointed to provide voting and engagement services.

3. The informed use of shareholder votes, whilst not a legal duty, is a responsibility of shareholders and an implicit fiduciary duty of pension fund trustees and officers to whom they may delegate this function. Such a process is strengthened by the advice of a consultant skilled in this particular field.

4. The Surrey Pension Fund has been with Minerva Analytics (formerly Manifest) since 2013 to provide consultancy advice on share voting and the whole spectrum of company corporate governance. Minerva Analytics has assisted in ensuring that the Fund's stewardship policy reflects the most up-to-date standards and officers learn of the latest developments and can reflect these developments in the Investment Strategy Statement (ISS).

Outcomes Achieved through Company Engagement

LAPFF Engagement Outcomes

5. The LAPFF had engaged with 27 companies on issues such as Climate Change, Community Engagement and the Just Transition during the Quarter Ending 30 June 2020.

6. ArcelorMittal (Climate Action) – Met with company officials to establish 2030 carbon emission targets, including scope 3 targets

7. HSBC/ Allianz (Climate Change) – LAPFF engaged with both companies to ensure they gain awareness of the impact the insurance side of their businesses does - and can - have on climate change, in addition to the investment aspects.

8. Pharmaceutical Companies (COVID-19) – Joined a collaborative engagement and sent letters to 17 pharmaceutical companies, to seek assurances that there won't be unfair distribution and pricing practices in the context of the virus

9. Department of Business, Energy and Industrial Strategy (Policy Engagement) – Supported findings from the Kingman Review in replacing the Financial Reporting Council as well as the Competition and Markets Authority's Review on the audit market.

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Robeco Engagement Outcomes

10. Robeco had voted at 1299 shareholder meetings, voting against at least one agenda item in 52% of cases during the quarter ending 30 June 2020.

ESG Challenges in the Auto Industry

Reason for Engagement

11. With the shift towards zero-emissions mobility, the automotive industry can play a role in making a positive contribution towards the Sustainable Development Goals (SDGs), in particular to SDG 11: Sustainable cities and communities. Electric vehicles and sustainable transport systems can create environmental and social benefits that can contribute to the SDGs.

Engagement Outcomes

12. At the start of this engagement, the goal of achieving zero-emission transport was not taken seriously by any major car manufacturer. Three years later there is a broad acknowledgement of this ambition.

- All companies under engagement had set targets around emissions reductions or electrification of their fleets
- Two companies had set ambitious commitments; one of which was certified as being aligned with 1.5 degree scenario by the Science based Target Initiative (SBTi)
- Another company has also set a mid-term (2030) emissions reduction target that has been certified by SBTi, and was considering setting a long-term target by the end of the engagement.
- A fourth is in the process of merging with another car manufacturer in order to become better positioned to weather the industry's transition to automated, connected, electric mobility.

Food security and COVID-19

Reason for Engagement

13. According to a World Food Program (WFP) projection, the number of people facing acute food insecurity stands to double to 265 million in 2020 from 2019. This negative trend represents a remarkable setback to global efforts to reach Sustainable Development Goal (SDG) 2: Zero Hunger by 2030.

14. In these uncertain times, it remains important to keep markets well supplied with affordable and nutritious food, while allowing consumers to access and purchase food despite movement restrictions and income losses.

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Engagement Update

15. In Robeco's engagement over the past 6 months, they focused on companies across different stages of the supply chain; agrochemicals, food processing and commodities trading, agricultural mechanisation and irrigation.

- Agricultural machinery manufacturers experienced the largest drop in demand for their products in the first half of 2020.
- As the global economy headed into an economic downturn, farmers around the globe took a cautious approach to their short-term capital investments by postponing large investment decisions such as purchasing new machinery.
- One company has managed to shift its strategy from only servicing commercial farmers growing high-value crops in high-income countries, to also servicing smallholder farmers growing basic crops in middle and low-income countries.
- The key to success was to partner with local governments to roll out community-wide projects to reach the smallholder farmer consumer base and transition the business model to service this market. The company's drip irrigation technology helps farmers to double their yields with only half of the water.

Surrey Share Voting

16. The table below shows the total number of resolutions which Surrey was entitled to vote along with the number of contentious resolutions voted during the quarter. Surrey did not vote against management on any resolutions for the quarter ending 30 September 2020

17. Votes against Management by Resolution Category

Resolution Category	Total Resolutions	Voted Against Management	% votes Against Management	Average Shareholder Dissent %
Audit & Reporting	32	0	0.00	1.27%
Board	106	0	0.00	2.81%
Capital	46	0	0.00	1.96%
Corporate Actions	4	0	0.00	8.12%
Remuneration	31	0	0.00	4.23%
Shareholder Rights	17	0	0.00	3.62%
Sustainability	6	0	0.00	4.64%
Total	242	0	0.00	2.81%

Shareholder Proposed Resolutions/ Management Resolutions

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18. Shareholder proposals are resolutions put forward by shareholders who want the board of a company to implement certain measures, for example around corporate governance, social and environmental practices. Although they are generally not binding, they are a powerful way to advocate publicly for change on policies such as climate change and often attract relatively high levels of votes against management.

19. Surrey did not vote on any resolutions proposed by shareholders during the quarter ending 30 September 2020. In 2020 Q2 Surrey voted on 46 shareholder-proposed resolutions.

CONSULTATION:

20. The Chairman of the Pension Fund has been consulted and fully supports the conclusions of the report.

RISK MANAGEMENT AND IMPLICATIONS:

21. There are no risk related issues contained within the report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

22. There are no financial and value for money implications.

DIRECTOR OF CORPORATE FINANCE COMMENTARY

23. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

24. There are no legal implications or legislative requirements

EQUALITIES AND DIVERSITY

25. The Company Engagement Review does not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

26. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

27. The Pension Fund continue to monitor the progress of the voting and engagement work carried out by the LAPFF and Robeco over the medium and long term, and how this can impact investment decisions.

Contact Officer:

Mamon Zaman, Senior Pensions Finance Specialist

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Consulted:
Pension Fund Committee Chairman

Annexes:

Sources/background papers:

1. LAPFF Quarterly Engagement Report QE 30 September 2020 http://www.lapfforum.org/publications/qrtly-engagement-reports/
2. Robeco Active Ownership Report QE 30 September 2020 https://www.bordertocoast.org.uk/?dlm_download_category=engagement

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **11 DECEMBER 2020**

LEAD OFFICER: **ANNA D'ALESSANDRO, DIRECTOR OF CORPORATE FINANCE**

SUBJECT: **RESPONSIBLE INVESTMENT POLICY REVIEW**

SUMMARY OF ISSUE:

The Border to Coast Pension Partnership (BCPP) is now an established fully regulated asset management company when the authorised contractual scheme (ACS) went "live" on 26 July 2018. As part of this, BCPP now reviews is Responsible Investment (RI) and Corporate Governance and Voting Policy annually in advance of the proxy voting season.

In light of the continual transitioning of assets and voting responsibilities over to BCPP, the Surrey Fund is developing its own approach in the context of Responsible Investing.

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1. Approves the revised BCPP Responsible Investment (RI) Policy 2021 and Corporate Governance & Voting Guidelines 2021.
2. Approves continuing work to be carried out by officers in collaboration with BCPP and partner funds, with the principle of embedding a consistent approach to Responsible Investment approach between the Fund and BCPP.

REASON FOR RECOMMENDATIONS:

The Government required, as part of the initial pooling submission in July 2016, that each Pool has an approach to Responsible Investment (RI) with a commitment that a written RI policy would be in place at Pool level by 1st April 2018. The Responsible Investment Policy and Corporate Governance & Voting Guidelines were developed in 2017 in conjunction with the twelve Partner Funds and are reviewed annually and require approval from the Surrey Pension Fund Committee.

An investment objective of the Fund in the 2020/21 Business Plan is to review its Responsible Investment Policy.

DETAILS:

Responsible Investment Policy updates

1. Both Responsible Investment Policy and Corporate Governance & Voting Guidelines policies are due to be reviewed annually or whenever revisions

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are proposed; policies will then be updated as necessary through the appropriate governance channels. The process for review includes the participation of all the Partner Funds; this is to ensure that we have a strong, unified voice. The annual review and governance processes need to be completed, with policies approved and ready to be implemented ahead of the 2020 proxy voting season.

2. BCPP is a strong advocate of Responsible Investment. Its approach is to hold companies to account on environmental, social and governance (ESG) issues and practice active ownership through voting, monitoring companies, engagement and litigation. The RI policy sets out the approach to RI and stewardship, and the Corporate Governance & Voting Guidelines sets out the approach and principles to voting. The aim is to manage risk and generate sustainable, long-term returns which is a key part of improving outcomes for our Partner Funds and delivering their objectives.

3. The LGPS (Management and Investment of Funds) 2016 regulations state that the responsibility for stewardship, which includes shareholder voting, remains with the Partner Funds. The day-to-day administration and implementation however, will be done by BCPP with appropriate monitoring and challenge to ensure this continues to be in line with Partner Fund requirements

4. Both policies have been evaluated by Robeco using the International Corporate Governance Network Global Governance Principles, UK Stewardship Code and Principles for Responsible Investment as benchmarks.

5. After taking into account any comments from the OOG, the policies had gone to BCPP's Investment Committee, Board and finally to the Joint Committee in November for approval.

6. The main changes to the BCPP RI Policy is summarised in the below table while the full revised RI Policy can be viewed as Annex 1;

Section	**Page**	**Type of Change**	**Rationale**
1. Introduction	5	Clarification	Implementation of policy.
1.1 Policy framework	5/6	Addition	Policy framework context.
5. Integrating RI into investment decisions	7	Addition Addition	Biodiversity. Text explaining 'overarching principles' apply to all asset classes.
5.1 Listed equities – internally managed	8	Clarification	Extra text to clarify process.
5.2 Private markets	8	Addition	Monitoring ESG policies and encourage improvement.
5.4 External manager selection	9	Addition	Extra detail on expectations.

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	9	Addition	PRI Principle 4: We will promote acceptance and implementation of the Principles within the investment industry.
5.5 Climate change	10	Addition Addition Addition Addition	Reference to climate risk reporting via TCFD report. Use of Transition Pathway Initiative (TPI). Vote against Chair where rated zero or 1 by TPI. Private market investment themes.
6. Stewardship	10	Addition	Extra clarification text. Commitment to 2020 UK Stewardship Code.
6.1 Voting	11	Addition	Clarification on split voting circumstances - clear rationale from Partner Fund.
6.1.1 Use of proxy advisers	7	Clarification Clarification	Monitoring of Robeco. Updated text on share blocking.
6.2 Engagement	13	Addition Addition Addition	Input into Robeco process for new themes. Include OECD Guidelines breaches. Sharing engagement information.
9. Training and assistance	15	Addition	Training for Investment Team, Board and Joint Committee.

7. The main changes to the BCPP Corporate Governance and Voting Guidelines Policy is summarised in the below table

8. **Section**	**Page**	**Type of Change**	**Rationale**
Diversity	7	Addition / clarification	Rewording and increasing scope of approach.
Re-election	8	Addition / clarification	Board member election using majority voting standard.
Board evaluation	8	Addition	Assess skills.
Stakeholder engagement	8	Addition	Company response where significant votes against received.
Directors' remuneration	9	Clarification Addition	Rephrasing. Greater detail on ESG incorporation into exec pay.
Annual bonus	9/10	Addition	Deferral of portion of short-term bonus.
Political donations	12	Clarification	Oppose political donation proposals.
Dividends	12	Addition	No publicly disclosed capital allocation strategy.
Virtual shareholder General Meetings	13	Addition	Loosen current approach but need to safeguard shareholder participation.
Shareholder proposals	14	Addition	Expand text to include types of proposal we would usually support.
Climate change	14	Addition	Vote against Chair if high emitting company with TPI* score of zero or 1.

*The Transition Pathway Initiative ('TPI') is a global initiative led by asset owners and supported by asset managers. Aimed at investors, it is a free-to-use tool that assesses how prepared companies are for the low carbon transition. Companies are assessed to one of 5 levels based on their position in relation to the recognition and management of transition risks.

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CONSULTATION:

8. The Chairman of the Pension Fund Committee has been consulted and fully supports the conclusions of the report.

RISK MANAGEMENT AND IMPLICATIONS:

9. The consideration of risk related issues specific to Responsible Investment are an integral part of the Border to Coast project plan and a risk register is presented to every Project Team, Officer Group and Joint Committee meeting.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

10. There are no financial and value for money implications contained in this report.

DIRECTOR OF CORPORATE FINANCE COMMENTARY

11. The Director of Corporate Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

    The Director of Corporate Finance will continue to work closely with other officers and the other BCPP S151 officers to ensure effective governance and assurance of administering authority responsibilities under the new pooling arrangement.

LEGAL IMPLICATIONS – MONITORING OFFICER

12. There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

13. There are no equality or diversity issues.

OTHER IMPLICATIONS

14. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

15. The following next steps are planned:
    - Implementation of BCPP's revised RI Policy across Partner Fund pooled assets as well as inclusion in the Fund's Investment Strategy Statement

Contact Officer:
Mamon Zaman, Senior Pensions Finance Specialist

Consulted:
Pension Fund Committee Chairman

Annexes: 14

Annex 1 – BCPP Responsible Investment Policy 2021
Annex 2 – BCPP Corporate Governance & Voting Guidelines 2021

Sources/background papers:
Transition Pathway Initiative
https://www.transitionpathwayinitiative.org/

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Annex 1

Responsible Investment Policy

Border to Coast Pensions Partnership

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November 2020

Responsible Investment Policy

This Responsible Investment Policy details the approach that Border to Coast Pensions Partnership will follow in fulfilling its commitment to our Partner Funds in their delegation of the implementation of certain responsible investment (RI) and stewardship responsibilities.

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1. Introduction

Border to Coast Pensions Partnership Ltd is an FCA-authorised investment fund manager (AIFM). It operates investment funds for its eleven shareholders which are Local Government Pension Scheme funds (Partner Funds). The purpose is to make a difference to the investment outcomes for our Partner Funds through pooling to create a stronger voice; working in partnership to deliver cost effective, innovative, and responsible investment now and into the future; thereby enabling great, sustainable performance.

Border to Coast takes a long-term approach to investing and believes that businesses that are governed well and run in a sustainable way are more resilient, able to survive shocks and have the potential to provide better financial returns for investors. Environmental, social and governance (ESG) issues can have a material impact on the value of financial assets and on the long-term performance of investments, and therefore need to be considered across all asset classes in order to better manage risk and generate sustainable, long term returns. Well-managed companies with strong governance are more likely to be successful long-term investments.

Border to Coast is an active owner and steward of its investments, both internally and externally managed, across all asset classes. The commitment to responsible investment is communicated in the Border to Coast UK Stewardship Code compliance statement. As a long-term investor and representative of asset owners, we will hold companies and asset managers to account regarding environmental, societal and governance factors that have the potential to impact corporate value. We will incorporate such factors into our investment analysis and decision making, enabling long-term sustainable investment performance for our Partner Funds. As a shareowner, Border to Coast has a responsibility for effective stewardship of the companies it invests in, whether directly or indirectly through mandates with fund managers. It will practice active ownership through voting, monitoring companies, engagement and litigation.

1.1 Policy framework

The LGPS (Management and Investment of Funds) 2016 regulations state that the responsibility for stewardship, which includes shareholder voting, remains with the Partner Funds. Stewardship day-to-day administration and implementation have been delegated to Border to Coast by the Partner Funds, on assets managed by Border to Coast, with appropriate monitoring and challenge to ensure this continues to be in line with Partner Fund requirements. To leverage scale and for operational purposes, Border to Coast has, in conjunction with Partner Funds, developed this RI Policy and accompanying Corporate Governance & Voting Guidelines to ensure clarity of approach on behalf of Partner Funds. This collaborative approach results in an RI policy framework illustrated below with the colours demonstrating ownership of the various aspects of the framework:

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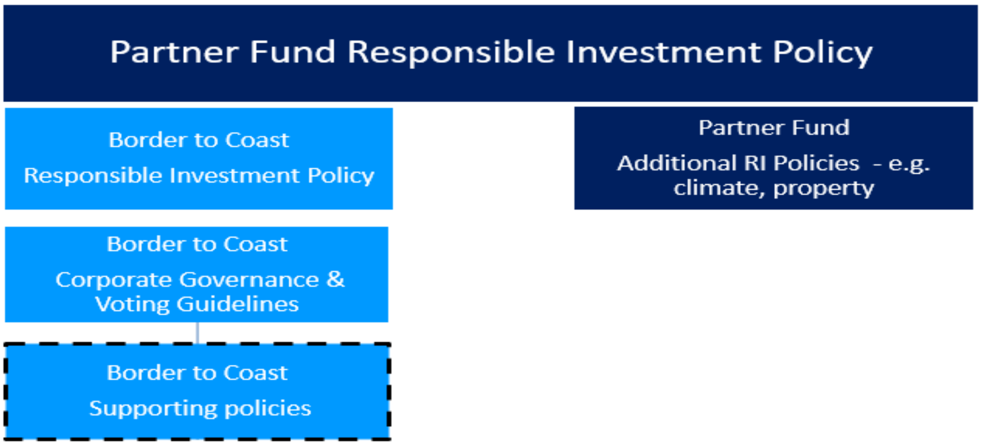
RI Policy Framework



2. What is responsible investment?

Responsible investment (RI) is the practice of incorporating ESG issues into the investment decision making process and practicing investment stewardship, to better manage risk and generate sustainable, long-term returns. Financial and ESG analysis together identify broader risks leading to better informed investment decisions and can improve performance as well as risk-adjusted returns.

Investment stewardship includes active ownership, using voting rights, engaging with investee companies, influencing regulators and policy makers, and collaborating with other investors to improve long-term performance.

3. Governance and Implementation

Border to Coast takes a holistic approach to sustainability and as such it is at the core of our corporate and investment thinking. Sustainability, which includes RI, is considered and overseen by the Board and Executive Committees. Specific policies and procedures are in place to demonstrate the commitment to RI, which include the Responsible Investment Policy and Corporate Governance & Voting Guidelines (available on the **website**). Border to Coast has dedicated staff resources for managing RI within the organisational structure.

The RI Policy is owned by Border to Coast and created after collaboration and engagement with our eleven Partner Funds. The Chief Investment Officer (CIO) is accountable for implementation of the policy. The policy is monitored with regular reports to the CIO, Investment Committee, Board, Joint Committee and Partner Funds. It is reviewed at least annually or whenever revisions are proposed, taking into account evolving best practice, and updated as necessary.

4. Skills and competency

Border to Coast will, where needed, take proper advice in order to formulate and develop policy. The Board and staff will maintain appropriate skills in responsible investment and stewardship through continuing professional development; where necessary expert advice will be taken from suitable RI specialists to fulfil our responsibilities.

5. Integrating RI into investment decisions

Border to Coast considers material ESG factors when analysing potential investments. ESG factors tend to be longer term in nature and can create both risks and opportunities. It is therefore important that, as a long-term investor, we take them into account when analysing potential investments.

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The factors considered are those which could cause financial and reputational risk, ultimately resulting in a reduction in shareholder value. ESG issues will be considered and monitored in relation to both internally and externally managed assets. The CIO will be accountable for the integration and implementation of ESG considerations. Issues considered include, but are not limited to:

Environmental	Social	Governance	Other
Climate change Resource & energy management Water stress Single use plastics Biodiversity	Human rights Child labour Supply chain Human capital Employment standards	Board independence/ diversity Executive pay Tax transparency Auditor rotation Succession planning Shareholder rights	Business strategy Risk management Cyber security Data privacy Bribery & corruption Political lobbying

Whilst the specific aspects and form of ESG integration and stewardship vary across asset class, the overarching principles outlined in this policy are applied to all internally and externally managed assets of Border to Coast. More information on specific approaches is outlined below.

5.1. Listed equities (Internally managed)

Border to Coast looks to understand and evaluate the ESG-related business risks and opportunities companies face. We consider the integration of ESG factors into the investment process as a necessary complement to the traditional financial evaluation of assets; this results in a more informed investment decision-making process. Rather than being used to preclude certain investments, it is used to provide an additional context for stock selection.

ESG data and research from specialist providers is used alongside general stock and sector research; it is an integral part of the research process and when considering portfolio construction, sector analysis and stock selection. The Head of RI I works with colleagues to ensure they are knowledgeable and fully informed on ESG issues. Voting and engagement should not be detached from the investment process; therefore, information from engagement meetings will be shared with the team to increase and maintain knowledge, and portfolio managers will be involved in the voting process.

5.2. Private markets

Border to Coast believes that ESG risk forms an integral part of the overall risk management framework for private market investment. An appropriate ESG strategy will improve downside protection and help create value in underlying portfolio companies. Border to Coast takes the following approach to integrating ESG into the private market investment process:

- The assessment of ESG issues is integrated into the investment process for all private market investments.

- A manager's ESG strategy is assessed through a specific ESG questionnaire agreed with the Head of RI and reviewed by the alternatives investment team with support from the Head of RI as required.
- Managers are requested to report annually on the progress and outcomes of ESG related values and any potential risks.
- Ongoing monitoring includes identifying any possible ESG breaches and following up with the managers concerned.
- Work with managers to improve ESG policies and ensure the approach is in-line with developing industry best practice.

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5.3. Fixed income

ESG factors can have a material impact on the investment performance of bonds, both negatively and positively, at the issuer, sector and geographic levels. ESG analysis is therefore incorporated into the investment process for corporate and sovereign issuers to manage risk. The challenges of integrating ESG in practice are greater than for equities with the availability of data for some markets lacking.

The approach to engagement also differs as engagement with sovereigns is much more difficult than with companies. Third-party ESG data is used along with information from sources including UN bodies, the World Bank and other similar organisations. This together with traditional credit analysis is used to determine a bond's credit quality. Information is shared between the equity and fixed income teams regarding issues which have the potential to impact corporates and sovereign bond performance.

5.4. External manager selection

RI is incorporated into the external manager appointment process including the request for proposal (RFP) criteria and scoring and the investment management agreements. The RFP includes specific requirements relating to the integration of ESG by managers into the investment process and to their approach to engagement. We expect to see evidence of how material ESG issues are considered in research analysis and investment decisions. Engagement needs to be structured with clear aims, objectives and milestones.

Voting is carried out by Border to Coast for both internally and externally managed equities where possible and we expect external managers to engage with companies in alignment with the Border to Coast RI policy.

The monitoring of appointed managers will also include assessing stewardship and ESG integration in accordance with our policies. All external fund managers will be expected to be signatories or comply with international standards applicable to their geographical location. We will encourage managers to become signatories to the UN-supported Principles for Responsible Investment. Managers will be required to report to Border to Coast on their RI activities quarterly.

5.5. Climate change

Border to Coast will actively consider how climate change, the shifting regulatory environment and potential macroeconomic impact will affect its investments. These pose significant investment risks and opportunities with the potential to impact the long-term shareholder value of investments across all asset classes.

Climate change is a systemic risk with potential financial impacts associated with the transition to a low-carbon economy and physical impacts under different climate scenarios. Transition will affect some sectors more than others, notably energy, utilities and sectors highly reliant on energy. However, within sectors there are likely to be winners and losers which is why divesting from and excluding entire sectors may not be appropriate.

14 Risks and opportunities can be presented through a number of ways and include:

- Physical impacts – damage to land, infrastructure and property due to extreme weather events, rising sea levels and flooding
- Technological changes - technological innovations such as battery storage, energy efficiency, and carbon capture and storage will displace old technologies with winners and losers emerging
- Regulatory and policy impact - financial impairment due to policy and regulation changes such as carbon pricing or levies, capping emissions or withdrawal of subsidies.
- Transitional risk - financial risk associated with the transition to a low-carbon economy, also known as carbon risk. It may entail extensive policy, legal, technology, and market changes to address mitigation and adaptation requirements related to climate change, creating investment opportunities as well as risks.
- Litigation risk - litigation is primarily aimed at companies failing to mitigate, adapt or disclose.

Border to Coast is:

- Assessing its portfolios in relation to climate change risk where practicable.
- Incorporating climate considerations into the investment decision making process.
- Engaging with companies in relation to business sustainability and disclosure of climate risk in line with the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD)[1] recommendations.
- Encouraging companies to adapt their business strategy in alignment with a low carbon economy.
- Supporting climate related resolutions at company meetings which we consider reflect our RI policy.
- Encouraging companies to publish targets and report on steps taken to reduce greenhouse gas emissions.
- Using the Transition Pathway Initiative (TPI)[2] toolkit to assess companies and inform company engagement and voting.

[1] The Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) - The TCFD developed recommendations on climate-related financial disclosures that are applicable to organisations (including asset owners) across sectors and jurisdictions.
https://www.fsb-tcfd.org/publications/finalrecommendations-report/

[2] The Transition Pathway Initiative ('TPI') is a global initiative led by asset owners and supported by asset managers. Aimed at investors, it is a free-to-use tool that assesses how prepared companies are for the low carbon transition.

- Voting against company Chairs in high emitting sectors where the climate change policy does not meet our minimum standards, and/or rated Level 0 or 1 by the TPI, where there is no evidence of a positive direction of travel.
- Co-filing shareholder resolutions at company AGMs on climate risk disclosure after due diligence, that are deemed to be institutional quality shareholder resolutions consistent with our RI policies.
- Monitoring and reviewing its fund managers in relation to climate change approach and policies.
- Participating in collective initiatives collaborating with other investors including other pools and groups such as the Local Authority Pension Fund Forum (LAPFF).
- Engaging with policy makers with regard to climate change through membership of the Institutional Investor Group on Climate Change (IIGCC).
- Reporting on the actions undertaken with regards to climate change on an annual basis in its TCFD report.
- Key investment themes pursued by the private markets team include Energy Transition opportunities which support the move to a lower carbon economy.

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6. Stewardship

As a shareholder Border to Coast has a responsibility for effective stewardship of the companies it invests in, whether directly or indirectly through mandates with fund managers. It practices active ownership through the full use of rights available including voting, monitoring companies, engagement and litigation. As a responsible shareholder, we are a signatory to the UK Stewardship Code[3] and are committed to being a signatory to the 2020 Code; we are also a signatory to the UN - supported Principles of Responsible Investment[4].

6.1. Voting

Voting rights are an asset and Border to Coast will exercise its rights carefully to promote and support good corporate governance principles. It will aim to vote in every market in which it invests where this is practicable. To leverage scale and for practical reasons, Border to Coast has developed a collaborative voting policy to be enacted on behalf of the Partner Funds which can be viewed on our website at: Corporate Governance & Voting Guidelines. Where possible the voting policies will also be applied to assets managed externally. Policies will be reviewed annually in collaboration with the Partner Funds. There may be occasions when an individual fund may wish Border to Coast to vote its pro rata holding contrary to an agreed policy; there is a process in place to facilitate this. A clear rationale must be provided by the fund concerned for any divergence from the agreed policy.

6.1.1 Use of proxy advisers

Border to Coast appointed Robeco as Voting and Engagement provider to implement the set of detailed voting guidelines and ensure votes are executed in accordance with policies.

[3] The UK Stewardship Code aims to enhance the quality of engagement between investors and companies to help improve long-term risk-adjusted returns to shareholders.
https://www.frc.org.uk/Our-Work/CodesStandards/Corporate-governance/UK-Stewardship-Code.aspx
[4] The UN-supported Principles for Responsible Investment (PRI) is the world's leading advocate for responsible investment enabling investors to publicly demonstrate commitment to responsible investment with signatories committing to supporting the six principles for incorporating ESG issues into investment practice.

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A proxy voting platform is used with proxy voting recommendations produced for all meetings voted managed by Robeco as the Voting & Engagement provider. Robeco's proxy voting advisor (Glass Lewis. Co) provides voting recommendations based upon Border to Coast's Corporate Governance & Voting Guidelines ('the Voting Guidelines'). A Robeco team of dedicated voting analysts analyse the merit of each agenda item to ensure voting recommendations are aligned with the Voting Guidelines. Border to Coast's Investment Team receives notification of voting recommendations ahead of meetings which are assessed on a case-by-case basis by portfolio managers and responsible investment staff prior to votes being executed. A degree of flexibility is required when interpreting the Voting Guidelines to reflect specific company and meeting circumstances, allowing the override of voting recommendations from the proxy adviser.

Robeco evaluates their proxy voting agent at least annually, on the quality of governance research and the alignment of customised voting recommendations and Border to Coast's Voting Guidelines. This review is part of Robeco's control framework and is externally assured. Border to Coast also monitors the services provided by Robeco monthly, with a six monthly and full annual review.

Border to Coast has an active stock lending programme. Where stock lending is permissible, lenders of stock do not generally retain any voting rights on lent stock. Procedures are in place to enable stock to be recalled prior to a shareholder vote. Stock will be recalled ahead of meetings, and lending can also be restricted, when any, or a combination of the following, occur:

- The resolution is contentious.
- The holding is of a size which could potentially influence the voting outcome.
- Border to Coast needs to register its full voting interest.
- Border to Coast has co-filed a shareholder resolution.
- A company is seeking approval for a merger or acquisition.
- Border to Coast deems it appropriate.

Proxy voting in some countries requires share blocking. This requires shareholders who want to vote their proxies to deposit their shares before the date of the meeting (usually one day after cut-off date) with a designated depositary until one day after meeting date.

During this blocking period, shares cannot be sold; the shares are then returned to the shareholders' custodian bank. We may decide that being able to trade the stock outweighs the value of exercising the vote during this period. Where we want to retain the ability to trade shares, we may refrain from voting those shares.

Where appropriate Border to Coast will consider co-filing shareholder resolutions and will notify Partner Funds in advance. Consideration will be given as to whether the proposal reflects Border to Coast's Responsible Investment policy, is balanced and worded appropriately, and supports the long-term economic interests of shareholders.

6.2. Engagement

The best way to influence companies is through engagement; therefore, Border to Coast will not divest from companies principally on social, ethical or environmental reasons. As responsible investors, the approach taken will be to influence companies' governance standards, environmental, human rights and other policies by constructive shareholder engagement and the use of voting rights.

The services of specialist providers may be used when necessary to identify issues of concern. Meeting and engaging with companies are an integral part of the investment process. As part of our stewardship duties we monitor investee companies on an ongoing basis and take appropriate action if investment returns are at risk. Engagement takes place between portfolio managers and investee companies across all markets where possible.

Border to Coast has several approaches to engaging with investee holdings: 14

- Border to Coast and all eleven Partner Funds are members of the LAPFF. Engagement takes place with companies on behalf of members of the Forum across a broad range of ESG themes.
- We will seek to work collaboratively with other like-minded investors and bodies in order to maximise Border to Coast's influence on behalf of Partner Funds, particularly when deemed likely to be more effective than acting alone. This will be achieved through actively supporting investor RI initiatives and collaborating with various other external groups e.g. LAPFF, the Institutional Investors Group on Climate Change, other LGPS pools and other investor coalitions.
- Due to the proportion of assets held in overseas markets it is imperative that Border to Coast is able to engage meaningfully with global companies. To enable this and complement other engagement approaches, an external voting and engagement service provider has been appointed. Border to Coast provides input into new engagement themes which are considered to be materially financial, selected by the external engagement provider on an annual basis, and also participates in some of the engagements undertaken on our behalf.
- Engagement will take place with companies in the internally managed portfolios with portfolio managers and the Responsible Investment team engaging directly across various engagement streams; these will cover environmental, social, and governance issues as well as UN Global Compact[5] breaches or OECD Guideline for Multinational Enterprises breaches[6]
- We will expect external managers to engage with investee companies and bond issuers as part of their mandate on our behalf and in alignment with our RI policy.

Engagement conducted can be broadly split into two categories: engagement based on financially material ESG issues, or engagement based on (potential) violations of global standards such as the UN Global Compact or OECD Guidelines for Multinational Enterprises.

When engagement is based on financially material ESG issues, engagement themes and companies are selected in cooperation with our engagement service provider based on an analysis of financial materiality. Such companies are selected based on their exposure to the engagement topic, the size and relevance in terms of portfolio positions and related risk.

[5] UN Global Compact is a shared framework covering 10 principles, recognised worldwide and applicable to all industry sectors, based on the international conventions in the areas of human rights, labour standards, environmental stewardship and anti-corruption.

[6] OECD Guidelines for Multinational Enterprises are recommendations providing principles and standards for responsible business conduct for multinational corporations operating in or from countries adhering to the OECD Declaration on International and Multinational Enterprises.

For engagement based on potential company misconduct, cases are selected through the screening of news flows to identify breaches of the UN Global Compact Principles or OECD Guidelines for Multinational Enterprises. Both sets of principles cover a broad variety of basic corporate behaviour norms around ESG topics. Portfolio holdings are screened on 1) validation of a potential breach, 2) the severity of the breach and 3) the degree of to which management can be held accountable for the issue. For all engagements, SMART[7] engagement objectives are defined.

In addition, internal portfolio managers and the Responsible Investment team monitor holdings which may lead to selecting companies where engagement may improve the investment case or can mitigate investment risk related to ESG issues. Members of the investment team have access to our engagement provider's Active Ownership profiles and engagement records. This additional information feeds into the investment analysis and decision making process

We engage with regulators, public policy makers, and other financial market participants as and when required. We encourage companies to improve disclosure in relation to ESG and to report and disclose in line with the TCFD recommendations.

6.2.1. Escalation

Border to Coast believe that engagement and constructive dialogue with the companies in which it invests is more effective than excluding companies from the investment universe. However, if engagement does not lead to the desired result escalation may be necessary. A lack of responsiveness by the company can be addressed by conducting collaborative engagement with other institutional shareholders, registering concern by voting on related agenda items at shareholder meetings, attending a shareholder meeting in person and filing/co-filing a shareholder resolution. If the investment case has been fundamentally weakened, the decision may be taken to sell the company's shares.

6.3. Due diligence and monitoring procedure

Internal procedures and controls for stewardship activities are reviewed by Border to Coast's external auditors as part of the audit assurance (AAF) control review. Robeco, as the external Voting and Engagement provider, is also monitored and reviewed by Border to Coast on a regular basis to ensure that the service level agreement is met.

Robeco also undertakes verification of its active ownership activities. Robeco's external auditor audits active ownership controls on an annual basis; this audit is part of the annual International Standard for Assurance Engagements control.

7. Litigation

Where Border to Coast holds securities, which are subject to individual or class action securities litigation, we will, where appropriate, participate in such litigation. There are various litigation routes available dependent upon where the company is registered. We will use a case-by-case approach to determine whether or not to participate in a class action after having considered the risks and potential benefits. We will work with industry professionals to facilitate this.

[7] SMART objectives are: specific, measurable, achievable, relevant and time-bound.

8. Communication and reporting

Border to Coast will be transparent with regard to its RI activities and will keep beneficiaries and stakeholders informed. This will be done by making publicly available RI and voting policies; publishing voting activity on our website quarterly; reporting on engagement and RI activities to the Partner Funds quarterly; and in our annual RI report.

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We also report in line with the TCFD recommendations.

9. Training and assistance

Border to Coast will offer the Partner Funds training on RI and ESG issues. Where requested, assistance will be given on identifying ESG risks and opportunities in order to help develop individual fund policies and investment principles for inclusion in the Investment Strategy Statements.

The Investment Team receive training on RI and ESG issues with assistance and input from our Voting & Engagement Partner and other experts where required. Training is also provided to the Border to Coast Board and the Joint Committee as and when required.

10. Conflicts of interest

Border to Coast has a suite of policies which cover any potential conflicts of interest between itself and the Partner Funds which are applied to identify and manage any conflicts of interest.

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Corporate Governance & Voting Guidelines

Border to Coast Pensions Partnership

November 2020

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1. Introduction

Border to Coast Pensions Partnership believes that companies operating to higher standards of corporate governance along with environmental and social best practice have greater potential to protect and enhance investment returns. As an active owner Border to Coast will engage with companies on environmental, social and governance (ESG) issues and exercise its voting rights at company meetings. When used together, voting and engagement can give greater results.

An investment in a company not only brings rights but also responsibilities. The shareholders' role includes appointing the directors and auditors and to be assured that appropriate governance structures are in place. Good governance is about ensuring that a company's policies and practices are robust and effective. It defines the extent to which a company operates responsibly in relation to its customers, shareholders, employees, and the wider community. Corporate governance goes hand-in-hand with responsible investment and stewardship. Border to Coast considers the UK Corporate Governance Code and other best practice global guidelines in formulating and delivering its policy and guidelines.

2. Voting procedure

These broad guidelines should be read in conjunction with the Responsible Investment Policy. They provide the framework within which the voting guidelines are administered and assessed on a case-by-case basis. A degree of flexibility will be required when interpreting the guidelines to reflect specific company and meeting circumstances. Voting decisions are reviewed with the portfolio managers. Where there are areas of contention the decision on voting will ultimately be made by the Chief Investment Officer. A specialist proxy voting advisor is employed to ensure that votes are executed in accordance with the policy.

Where a decision has been made not to support a resolution at a company meeting, Border to Coast will, where able, engage with the company prior to the vote being cast. In some instances, attendance at AGMs may be required.

Border to Coast discloses its voting activity on its website and to Partner Funds on a quarterly basis.

We will support incumbent management wherever possible but recognise that the neglect of corporate governance and corporate responsibility issues could lead to reduced shareholder returns.

We will vote **For**, **Abstain** or **Oppose** on the following basis:

- We will support management that acts in the long-term interests of all shareholders, where a resolution is aligned with these guidelines and considered to be in line with best practice.
- We will abstain when a resolution fails the best practice test but is not considered to be serious enough to vote against.
- We will vote against a resolution where corporate behaviour falls short of best practice or these guidelines, or where the directors have failed to provide sufficient information to support the proposal.

3. Voting Guidelines

Company Boards

The composition and effectiveness of the board is crucial to determining corporate performance, as it oversees the running of a company by its managers and is accountable to shareholders. Company behaviour has implications for shareholders and other stakeholders. The structure and composition of the board may vary between different countries; however, we believe that the following main governance criteria are valid across the globe. 14

Composition and independence

The board should have a balance of executive and non-executive directors so that no individual or small group of individuals can control the board's decision making. They should possess a suitable range of skills, experience and knowledge to ensure the company can meet its objectives. Boards do not need to be of a standard size: different companies need different board structures and no simple model can be adopted by all companies.

The board of large cap companies, excluding the Chair, should consist of a majority of independent non-executive directors although local market practices shall be taken into account. Controlled companies should have a majority of independent non-executive directors, or at least one-third independent directors on the board. As non-executive directors have a fiduciary duty to represent and act in the best interests of shareholders and to be objective and impartial when considering company matters, the board must be able to demonstrate their independence. Non-executive directors who have been on the board for a significant length of time, from nine to twelve years (depending on market practice) have been associated with the company for long enough to be presumed to have a close relationship with the business or fellow directors. We aspire for a maximum tenure of nine years but will review resolutions on a case-by-case basis where the local corporate governance code recommends a maximum tenure between nine and twelve years.

The nomination process of a company should therefore ensure that potential risks are restricted by having the right skills mix, competencies and independence at both the supervisory and executive board level. It is essential for boards to achieve an appropriate balance between tenure and experience, whilst not compromising the overall independence of the board. The re-nomination of board members with longer tenures should be balanced out by the nomination of members able to bring fresh perspectives. It is recognised that excessive length of tenure can be an issue in some markets, for example the US where it is common to have a retirement age limit in place rather than length of tenure. In such cases it is of even greater importance to have a process to robustly assess the independence of long tenured directors. Where it is believed an individual can make a valuable and independent contribution, tenure greater than nine years will be assessed on a case-by-case basis.

The company should, therefore, have a policy on tenure which is referenced in its annual report and accounts. There should also be sufficient disclosure of biographical details so that shareholders can make informed decisions. There are a number of factors which could affect independence, which includes but is not restricted to:

- Representing a significant shareholder.
- Serving on the board for over nine years.
- Having had a material business relationship with the company in the last three years.
- Having been a former employee within the last five years.

- Family relationships with directors, senior employees or advisors.
- Cross directorships with other board members.
- Having received or receiving additional remuneration from the company in addition to a director's fee, participating in the company's share option or performance-related pay schemes, or being a member of the company's pension scheme.

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Leadership

The role of the Chair is distinct from that of other board members and should be seen as such. The Chair should be independent upon appointment and should not have previously been the CEO. The Chair should also take the lead in communicating with shareholders and the media. However, the Chair should not be responsible for the day to day management of the business: that responsibility rests with the Chief Executive. The role of Chair and CEO should not be combined as different skills and experience are required. There should be a distinct separation of duties to ensure that no one director has unfettered decision making power.

However, Border to Coast recognises that in many markets it is still common to find these positions combined. Any company intending to combine these roles must justify its position and satisfy shareholders in advance as to how the dangers inherent in such a combination are to be avoided; best practice advocates a separation of the roles. A senior independent non-executive director should be appointed, in-line with local corporate governance best practice, if roles are combined to provide shareholders and directors with a meaningful channel of communication, to provide a sounding board for the chair and to serve as an intermediary for the other directors and shareholders. Led by the senior independent director, the non-executive directors should meet without the chair present at least annually to appraise the chair's performance.

Non-executive Directors

The role of non-executive directors is to challenge and scrutinise the performance of management in relation to company strategy and performance. To do this effectively they need to be independent; free from connections and situations which could impact their judgement. They must commit sufficient time to their role to be able to carry out their responsibilities. A senior independent non-executive director should be appointed to act as liaison between the other non-executives, the Chair and other directors where necessary.

Diversity

Board members should be recruited from as broad a range of backgrounds and experiences as possible. A diversity of directors will improve the representation and accountability of boards, bringing new dimensions to board discussions and decision making. Companies should broaden the search to recruit non-executives to include open advertising and the process for board appointments should be transparent and formalised in a board nomination policy. Companies should have a diversity policy which references gender, ethnicity, age, skills and experience and how this is considered in the formulation of the board. The policy should give insight into how diversity is being addressed not only at board level but throughout the company, it should reflect the demographic/ethnic makeup of the countries a company is active in and be disclosed in the Annual Report.

We support the government-backed Davies report, Hampton Alexander and Parker reviews, which set goals for UK companies regarding the representation of women and ethnic minorities on boards, executive teams and senior management. Therefore, in developed markets without relevant legal requirements, we expect boards to be composed of at least 30% female directors. Where relevant, this threshold will be rounded down to account for board size. Recognising varying market practices, we generally expect emerging market and Japanese companies to have at least one female on the board. We will vote against the chair of the nomination committee where this is not the case. 14

Succession planning

We expect the board to disclose its policy on succession planning, the factors considered and where decision-making responsibilities lie. A succession policy should form part of the terms of reference for a formal nomination committee, comprised solely of independent directors and headed by the Chair or Senior Independent Non-executive Director except when it is appointing the Chair's successor. External advisors may also be employed.

Directors' availability and attendance

It is important that directors have sufficient time to devote to the company's affairs; therefore, full time executives should not hold more than one non-executive position in a FTSE 100 company, or similar size company in other regions; nor the chairmanship of such a company. In the remaining instances, directors working as full-time executives should serve on a maximum of two publicly listed company boards.

With regard to non-executive directors, there can be no hard and fast rule on the number of positions that are acceptable: much depends upon the nature of the post and the capabilities of the individual. Shareholders need to be assured that no individual director has taken on too many positions. Full disclosure should be made in the annual report of directors' other commitments and attendance records at formal board and committee meetings. A director should attend a minimum of 75% of applicable board and committee meetings to ensure commitment to responsibilities at board level.

Re-election

For a board to be successful it needs to ensure that it is suitably diverse with a range of skills, experience and knowledge. There is a requirement for non-executive directors to be independent to appropriately challenge management. To achieve this, boards need to be regularly refreshed to deal with issues such as stagnant skill sets, lack of diversity and excessive tenure; therefore, all directors should be subject to re-election annually, or in-line with local best practice. As representatives of shareholders, directors should preferably be elected using a majority voting standard. In cases where an uncontested election uses the plurality[1] voting standard without a resignation policy, we will hold the relevant Governance Committee accountable by voting against the Chair of this committee.

Board evaluation

A requisite of good governance is that boards have effective processes in place to evaluate their performance and appraise directors at least once a year. The annual evaluation should

[11] A plurality vote means that the winning candidate only needs to get more votes than a competing candidate. If a director runs unopposed, he or she only needs one vote to be elected.

14 consider its composition, diversity and how effectively members work together to achieve objectives. As part of the evaluation, boards should consider whether directors possess the necessary expertise to address and challenge management on key strategic topics. These strategic issues and important areas of expertise should be clearly outlined in reporting on the evaluation. The board should disclose the process for evaluation and, as far as reasonably possible, any material issues of relevance arising from the conclusions and any action taken as a consequence. Individual director evaluation should demonstrate the effective contribution of each director. An internal evaluation should take place annually with an external evaluation required at least every three years.

Stakeholder engagement

Companies should take into account the interests of and feedback from stakeholders which includes the workforce. Taking into account the differences in best practice across markets, companies should have an appropriate system in place to engage with employees.

Engagement and dialogue with shareholders on a regular basis are key for companies; being a way to discuss governance, strategy, and other significant issues. Companies should engage with shareholders ahead of the AGM in order that high votes against resolutions can be avoided where possible.

Where a company with a single share class structure has received 20% votes against a proposal at a previous AGM, a comprehensive shareholder and stakeholder consultation should be initiated. A case-by-case approach will be taken for companies with a dual class structure where a significant vote against has been received. Engagement efforts and findings, as well as company responses, should be clearly reported on and lead to tangible improvement. Where companies fail to do so, the relevant board committees or members will be held to account.

Directors' remuneration

Shareholders at UK companies have two votes in relation to pay; the annual advisory vote on remuneration implementation which is non-binding, and the triennial vote on forward-looking pay policy which is binding. If a company does not receive a majority of shareholder support for the pay policy, it is required to table a resolution with a revised policy at the next annual meeting.

It must be noted that remuneration structures are varied, with not one model being suitable for all companies; however, there are concerns over excessive remuneration and the overall quantum of pay. Research shows that high executive pay does not systematically lead to better company performance. Excessive rewards for poor performance are not in the best interests of a company or its shareholders. Remuneration levels should be sufficient to attract, motivate and retain quality management but should not be excessive compared to salary levels within the organisation and with peer group companies. There is a clear conflict of interest when directors set their own remuneration in terms of their duty to the company, accountability to shareholders and their own self-interest. It is therefore essential that the remuneration committee is comprised solely of non-executive directors and complies with the market independence requirement.

Remuneration has serious implications for corporate performance in terms of providing the right incentives to senior management, in setting performance targets, and its effect on the morale and motivation of employees. Corporate reputation is also at risk. Remuneration policy should be sensitive to pay and employee conditions elsewhere in the company, especially when determining annual salary increases.

Where companies are potentially subject to high levels of environmental and societal risk as part of its business, the remuneration committee should also consider linking relevant metrics and targets to remuneration to focus management on these issues. The selection of these metrics should be based on a materiality assessment that also guides the company's overall sustainability strategy. If environmental or social topics are incorporated in variable pay plans, the targets should set stretch goals for improved ESG performance, address achievements under management's control, and avoid rewarding management for basic expected behaviour. Where relevant, minimum ESG standards should instead be incorporated as underpins or gateways for incentive pay. If the remuneration committee determines that the inclusion of environmental or social metrics would not be appropriate, a clear rationale for this decision should be provided in the remuneration report.

The compensation provided to non-executive directors should reflect the role and responsibility. It should be structured in a manner that does not compromise independence, enhancing objectivity and alignment with shareholders' interests. Non-executive directors should, therefore, not be granted performance-based pay. Although we would not expect participation in Long-term Incentive Plans (LTIPs), we are conscious that in some exceptional instances Non-executives may be awarded stock, however the proportion of pay granted in stock should be minimal to avoid conflicts of interest.

To ensure accountability there should be a full and transparent disclosure of directors' remuneration with the policy published in the annual report and accounts. The valuation of benefits received during the year, including share options, other conditional awards and pension benefits, should be provided. Companies should also be transparent about the ratio of their CEO's pay compared to the median, lower and upper quartiles of their employees.

• **Annual bonus**

Bonuses should reflect individual and corporate performance targets which are sufficiently challenging, ambitious and linked to delivering the strategy of the business and performance over the longer-term. Bonuses should be set at an appropriate level of base salary and should be capped. Provisions should be in place to reduce or forfeit the annual bonus where the company has experienced a significant negative event. For large cap issuers, we expect the annual bonus to include deferral of a portion of short-term payments into long-term equity scheme or equivalent. We will also encourage other companies to take this approach.

• **Long-term incentives**

Remuneration policies have over time become more and more complex making them difficult for shareholders to adequately assess. Border to Coast therefore encourages companies to simplify remuneration policies.

14 Performance-related remuneration schemes should be created in such a way to reward performance that has made a significant contribution to shareholder value. The introduction of incentive schemes to all employees within a firm is encouraged and supported as this helps all employees understand the concept of shareholder value. However, poorly structured schemes can result in senior management receiving unmerited rewards for substandard performance. This is unacceptable and could adversely affect the motivation of other employees.

Incentives are linked to performance over the longer-term in order to create shareholder value. If restricted stock units are awarded under the plan, the vesting period should be at least three years to ensure that the interests of both management and shareholders are aligned in the long-term. Employee incentive plans should include both financial and non-financial metrics and targets that are sufficiently ambitious and challenging. Remuneration should be specifically linked to stated business objectives and performance indicators should be fully disclosed in the annual report.

The performance basis of all such incentive schemes under which benefits are potentially payable should be clearly set out each year, together with the actual performance achieved against the same targets. We expect clawback or malus provisions to be in place for all components of variable compensation. We encourage Executive Directors to build a significant shareholding in the company to ensure alignment with the objectives of shareholders. These shares should be held for at least two years post exit.

Directors' contracts

Directors' service contracts are also a fundamental part of corporate governance considerations. Therefore, all executive directors are expected to have contracts that are based upon no more than twelve months' salary. Retirement benefit policies of directors should not be excessive, and no element of variable pay should be pensionable. The main terms of the directors' contracts including notice periods on both sides, and any loans or third-party contractual arrangements such as the provision of housing or removal expenses, should be declared within the annual report. Termination benefits should be aligned with market best practice.

Corporate reporting

Companies are expected to report regularly to shareholders in an integrated manner that allows them to understand the company's strategic objectives. Companies should be as transparent as possible in disclosures within the Report and Accounts. As well as reporting financial performance, business strategy and the key risks facing the business, companies should provide additional information on ESG issues that also reflect the directors' stewardship of the company. These could include, for example, information on a company's human capital management policies, its charitable and community initiatives and on its impact on the environment in which it operates.

Every annual report should include an environmental section, which identifies key quantitative data relating to energy and water consumption, emissions and waste etc., explains any contentious issues and outlines reporting and evaluation criteria. It is important that the risk areas reported upon should not be limited to financial risks.

We will encourage companies to report and disclose in line with the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) recommendations, and the Workforce Disclosure Initiative in relation to human capital reporting.

Audit

The audit process must be objective, rigorous and independent if it is to provide assurance to users of accounts and maintain the confidence of the capital markets. To ensure that the audit committee can fulfil its fiduciary role, it should be established as an appropriate committee composition with at least three members who are all independent non-executive directors and have at least one director with a relevant audit or financial background. Any material links between the audit firm and the client need to be highlighted, with the audit committee report being the most appropriate place for such disclosures. Audited financial statements should be published in a timely manner ahead of votes being cast at annual general meetings.

FTSE 350 companies should tender the external audit contract at least every ten years. Reappointment of the same firm with rotation of the audit partner, will not be considered as sufficient. If an auditor has been in place for more than ten fiscal years, their appointment will not be supported. For the wider market, the external audit contract should be put out to tender at least every ten years. Where an auditor has resigned, an explanation should be given. If the accounts have been qualified or there has been non-compliance with legal or regulatory requirements, this should be drawn to shareholders' attention in the main body of the annual report. If the appropriate disclosures are not made, the re-appointment of the audit firm will not be supported.

Non-Audit Fees

There is concern over the potential conflict of interest between audit and non-audit work when conducted by the same firm for a client. Companies must therefore make a full disclosure where such a conflict arises. There can be legitimate reasons for employing the same firm to do both types of work, but these need to be identified. As a rule, the re-appointment of auditors will not be supported where non-audit fees are considerably in excess of audit fees in the year under review, and on a three-year aggregate basis, unless sufficient explanation is given in the accounts.

Political donations

There are concerns over the reputational risks and democratic implications of companies becoming involved in funding political processes, both at home and abroad. Companies should disclose all political donations, demonstrate where they intend to spend the money and that it is the interest of the company and shareholders. Where these conditions are not met, or there is insufficient disclosure that the money is not being used for political party donations, political donations will be opposed. Any proposals concerning political donations will be opposed.

Lobbying

A company should be transparent and publicly disclose direct lobbying, and any indirect lobbying through its membership of trade associations. We will assess shareholder proposals regarding lobbying on a case-by-case basis; however, we will generally support resolutions requesting greater disclosure of trade association and industry body memberships, any
14 payments and contributions made, and requiring alignment of company and trade association values.

Shareholder rights

As a shareowner, Border to Coast is entitled to certain shareholder rights in the companies in which it invests (Companies Act 2006). Boards are expected to protect such ownership rights.

- **Dividends**

Shareholders should have the chance to approve a company's dividend policy and this is considered best practice. The resolution should be separate from the resolution to receive the report and accounts. Failure to seek approval would elicit opposition to other resolutions as appropriate unless there is a clearly disclosed capital management and allocation strategy in public reporting.

- **Voting rights**

Voting at company meetings is the main way in which shareholders can influence a company's governance arrangements and its behaviour. Shareholders should have voting rights in equal proportion to their economic interest in a company (one share, one vote). Dual share structures which have differential voting rights are disadvantageous to many shareholders and should be abolished. We will not support measures or proposals which will dilute or restrict our rights.

- **Authority to issue shares**

Companies have the right to issue new shares in order to raise capital but are required by law to seek shareholders' authority. Such issuances should be limited to what is necessary to sustain the company and not be in excess of relevant market norms.

- **Disapplication of Pre-emption Rights**

Border to Coast supports the pre-emption rights principle and considers it acceptable that directors have authority to allot shares on this basis. Resolutions seeking the authority to issue shares with and without pre-emption rights should be separate and should specify the amounts involved, the time periods covered and whether there is any intention to utilise the authority.

Share Repurchases

Border to Coast does not necessarily oppose a company re-purchasing its own shares but it recognises the effect such buy backs might have on incentive schemes where earnings per share measures are a condition of the scheme. The impact of such measures should be reported on. It is important that the directors provide a full justification to demonstrate that a share repurchase is the best use of company resources, including setting out the criteria for calculating the buyback price to ensure that it benefits long-term shareholders. 14

Memorandum and Articles of Association

Proposals to change a company's memorandum and articles of association should be supported if they are in the interests of Border to Coast, presented as separate resolutions for each change, and the reasons for each change provided.

Mergers and acquisitions

Border to Coast will normally support management if the terms of the deal will create rather than destroy shareholder value and makes sense strategically. Each individual case will be considered on its merits. Seldom will compliance with corporate governance best practice be the sole determinant when evaluating the merits of merger and acquisition activity, but full information must be provided to shareholders on governance issues when they are asked to approve such transactions. Recommendations regarding takeovers should be approved by the full board.

Articles of Association and adopting the report and accounts

It is unlikely that Border to Coast will oppose a vote to adopt the report and accounts simply because it objects to them per se; however, there may be occasions when we might vote against them to lodge dissatisfaction with other points raised within this policy statement. Although it is a blunt tool to use, it can be an effective one especially if the appropriate Chair or senior director is not standing for election.

If proposals to adopt new articles or amend existing articles might result in shareholders' interests being adversely affected, we will oppose the changes.

Virtual Shareholder General Meetings

Many companies are considering using electronic means to reach a greater number of their shareholders. An example of this is via a virtual annual general meeting of shareholders where a meeting takes place exclusively using online technology, without a corresponding in-person meeting. There are some advantages to virtual only meetings as they can increase shareholder accessibility and participation; however, they can also remove the one opportunity shareholders have to meet face to face with the Board to ensure they are held to account. We would expect an electronic meeting to be held in tandem with a physical meeting. If extraordinary circumstances rule out a physical meeting, we would expect the company to clearly outline how shareholders' rights to participate by asking questions and voting during the meeting are protected. Any amendment to a company's Articles to allow virtual only meetings without these safeguards will not be supported.

Shareholder Proposals

We will assess shareholder proposals on a case by case basis. Consideration will be given as to whether the proposal reflects Border to Coast's Responsible Investment policy, is balanced and worded appropriately, and supports the long-term economic interests of shareholders.

14 Shareholder proposals are an important tool to improve transparency. Therefore, we will, when considered appropriate, support resolutions requesting additional reporting on material business risk, ESG topics, climate risk and lobbying.

Climate change

We expect companies with high emissions or in high emitting sectors to have a climate change policy in place, which at minimum includes greenhouse gas emission reduction targets and disclosure of Scope 1 and 2 emissions. We use the Transition Pathway Initiative (TPI)[2] toolkit to assess our listed equities investments. TPI enables assessment of how companies are managing climate change, the related business risk and the progress being made. Where a company in a high emitting sector receives a score of zero or one by the TPI, or fails to meet the expectations above, we will vote against the Chair of the board if we consider the company is not making progress.

Investment trusts

Border to Coast acknowledges that issues faced by the boards of investment companies are often different to those of other listed companies. The same corporate governance guidelines do not necessarily apply to them; for example, investment companies can operate with smaller boards. However, the conventions applying to audit, board composition and director independence do apply.

The election of any representative of an incumbent investment manager onto the board of a trust managed or advised by that manager will not be supported. Independence of the board from the investment manager is key, therefore management contracts should not exceed one year and should be reviewed every year. In broad terms, the same requirements for independence, diversity and competence apply to boards of investment trusts as they do to any other quoted companies.

We may oppose the adoption of the report and accounts of an investment trust where there is no commitment that the trust exercises its own votes, and there is no explanation of the voting policy.

[2] The Transition Pathway Initiative ('TPI') is a global initiative led by asset owners and supported by asset managers. Aimed at investors, it is a free-to-use tool that assesses how prepared companies are for the low carbon transition.

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