

Lancashire County Pension Fund

Pension Fund Committee

7th February 2020

Responsible Investment Report

Title of Paper	Quarterly Report on Responsible Investment (2019 Q3)
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Appendices	None

1. Executive Summary

This report provides members of the Pension Fund Committee of Lancashire County Pension Fund (LCPF) with a quarterly update on Responsible Investment (RI) matters.

2. Introduction

The Fund's approach to RI is articulated within an Investment Strategy Statement (ISS) which confirms that the objective of RI is to decrease investor risk, improve risk-adjusted returns and assist the Fund's adherence to the UK Stewardship Code. LCPF's ISS is supplemented by a Responsible Investment Policy which explains that the Fund's preferred approach to RI encompasses four main areas of activity:

- Voting Globally
- Engagement through Partnerships
- Shareholder Litigation
- Active Investing

Responsibility for the practical implementation of the Fund's approach to RI is devolved to Local Pensions Partnership Investments Ltd (LPPI) as LCPF's provider of investment management services. The report which follows provides the Committee with an update on RI activity during the period 1 July to 30 September 2019 plus insights on current and emerging issues.

3. Voting Globally

Through its investment in the LPPI Global Equities Fund (GEF) LCPF owns units in a pooled fund which invests in listed companies globally. Investors in the GEF delegate the control and exercise of shareholder voting to LPPI. This reflects that clients owning units in the GEF are beneficial owners in common but do not directly own shares in underlying companies.

LPPI exercises shareholder voting rights for the GEF centrally rather than delegating voting to individual asset managers and takes account of voting recommendations from an external provider of proxy voting and governance research (ISS) in accordance a Sustainability Voting Policy designed to ensure the consideration of ESG factors within analysis. LPPI reviews voting recommendations and takes the final decision on all voting.

In the third quarter of 2019 shareholder voting headlines for the GEF were as follows:

LPPI Global Equities Fund (GEF)

Total company meetings taking place	65
Total resolutions (management and shareholder proposals)	716
Total company proposals in the period	708
Total shareholder proposals in the period	8

The following table summarises resolutions by type and indicates where opposition voting was concentrated in Q3.

Proposals				
	For	Against	Withhold	Total
Antitakeover Related	10	0	0	10
Capitalization	71	2	0	73
Directors Related	327	36	4	367
Miscellaneous	7	0	0	7
Non-Salary Comp.	49	9	0	58
Preferred/Bondholder	2	4	0	6
Reorg. and Mergers	14	5	0	19
Routine/Business	167	1	0	168
SH-Dirs' Related	6	0	0	6
SH-Health/Environ.	1	0	0	1
SH-Routine/Business	0	1	0	1
Total	654	58	4	716

LPPI voted against or withheld support for management proposals in 62 instances (across 26 company meetings).

This included opposing or withholding support in 40 management proposals connected with the election / re-election of directors or with the appointment of statutory auditors.

Opposition voting commonly reflected concerns with the composition and independence of company boards, the independence of individual board members, and the over boarding (multiple other directorships) of individual board members.

Director Related

At AusNet Services Ltd (Australia: Electric Utilities) LPPI voted against the re-election of the independent chairman. The nominee was previously the chair of a financial services company where the Australian Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry found material failures of governance, stewardship, and risk oversight during his tenure (Result: 23.5% against).

At Yunnan Baiyao Group Co. (China: Pharmaceuticals) LPPI voted against the election of seven non-independent directors as the level of board independence falls below the regulatory requirement for more than one-third of the board to be independent directors. (Results: all seven directors received report of at least 95.8%).

At SBI Life Insurance Company Limited (India: Life & Health Insurance) LPPI voted against the re-election of a director due to failure to attend at least 75% of board and committee meetings with no satisfactory explanation. (Result: 10.0% against).

Non-Salary Compensation

Management proposals on compensation arrangements prompted nine opposition votes. These were in response to cases including a lack of transparency around performance conditions, poor alignment of performance conditions to shareholder interests, and instances where variable pay terms are considered to be excessive.

At Vista Outdoor Inc. (USA: Leisure Products) LPPI voted against the Advisory Vote to Ratify Named Executive Officers' Compensation. This reflected that despite the company's engagement with shareholders following the same proposal's rejection by shareholders (LPPI included) last year, underlying concerns are not yet considered sufficiently addressed. The company reduced target performance levels within the short-term incentive plan and achieved performance levels from 2018, resulting in above target pay-outs alongside declining financial performance. Additionally, key metrics in both the short-term and long-term incentive plans were not adequately disclosed. (Result: 59.9% against).

At Mr. Price Group Ltd. (South Africa: Apparel, Accessories & Luxury Goods) LPPI voted against a resolution to approve the Remuneration Implementation Report. The company has not disclosed sufficient information around bonus performance targets and the departing CEO's leaving arrangements. (Result: 38.7% against).

At Berkeley Group (UK: Homebuilding) LPPI voted against a proposal to approve the Remuneration Policy. The reworked policy sought to extend the long-term incentive plan (positive) but its extension is considered to be delivering a relatively high quantum of reward without encouraging enhanced company performance. (Result: 43% against).

LPPI supported seven shareholder proposals across eight company meetings in Q3. Six of the eight resolutions related to the election of shareholder nominated independent directors and board supervisors at two Chinese companies. LPPI supported the proposals in all cases.

Two interdependent shareholder resolutions arose at Suncorp Group (Australia: Property and Casualty Insurance). The proponent sought support for amending the company's constitution to enable each shareholder to place resolutions on the agenda. LPPI voted against the resolution due to a lack of legal or regulatory supervision of potential shareholder proposals in Australia (concern that proposal could lead to, and because the text of the proposed amendment was considered too broad (Result: 95.8% against). The second resolution, which sought the introduction of Paris-aligned targets in Suncorp's lending and underwriting was withdrawn (could not be tabled at the meeting) because it was dependent on the first resolution passing. Had the second resolution been tabled, LPPI would have voted in favour.

4. Engagement through Partnerships

LPPI regularly participates in collaborations which aim to make progress on commonly held issues by co-ordinating the efforts of multiple investors. Key partners include the Local Authority Pension Fund Forum (LAPFF) the Pensions and Lifetime Savings Association (PLSA) the Principles of Responsible Investment (PRI) the Institutional Investor Group on Climate Change (IIGCC) the LGPS Cross Pool RI Group, and the UK Pension Scheme RI Roundtable.

LAPFF

LAPFF has long been LCPF's preferred engagement partner. The Fund is a long-standing member of the Forum and the Head of Fund and Chair of the Pension Fund Committee both currently sit on the LAPFF Executive.

LAPFF provide information on engagement activities undertaken on behalf of member funds by publishing Quarterly Engagement Reports (QER). Based on the content of these reports it has previously been possible to provide committee members with quantitative information on LAPFF

engagement activities. However, a “new look” QER has recently been introduced which places greater focus on narrative content and includes selective examples rather than the former range of summary metrics. For this reason, it is no longer possible to provide the familiar tables. To enable members to review the Forum’s full account of engagement activity in the period a link to the 2019 Q3 QER is provided below.

<http://www.lapfforum.org/wp-content/members-folder2017/2019/LAPFFQERQ3FINAL.pdf>

LAPFF have undertaken analysis of the voting records of asset managers managing LGPS assets and have reported back results which confirm a lack of disclosure by some (which hampers analysis) and some degree of misalignment between LAPFF voting alerts (and the recommendations they make to Funds) and the way in which fund managers voted. The LAPFF analysis did not include any tabulation of voting by LGPS pools despite a number overseeing voting centrally rather than delegating it to individual asset managers.

Shareholder voting for the LPPI Global Equities Fund through which LCPF invests in listed equities is overseen by the RI team and voting decisions incorporate recommendations from an external voting provider based on sustainability (ESG) focussed voting guidelines. Wider information is considered where pertinent and if LAPFF issues a voting alert which relates to a company in the GEF consideration is given to the points raised as part of reaching a final decision. A record of all voting decisions by LPPI is made publicly available via quarterly voting reports published on the LPP website.

PLSA

The Head of RI is a member of the Pensions and Lifetime Savings Association’s Defined Benefit Scheme Stewardship Advisory Group (SAG). This group meets quarterly to discuss developing issues and is a sounding board for the Association’s programme of work on stewardship.

SAG members have been approached to join a working group which will shape the 2020 version of PLSA’s annual [Corporate Governance Policy and Voting Guidelines](#). This guidance is published every January and provides practical guidance for schemes considering how to exercise their rights at AGMs in the next season. The guide is one of the PLSA’s most popular stewardship downloads.

In January 2019 the guidelines were updated to cover changes to the UK Corporate Governance Code and highlight some of the key developments in UK corporate governance policy and practice. For 2020 the intention is a further thorough review. The update is in the context of renewed regulatory requirements and an increasing scrutiny of how pension schemes are fulfilling the responsibilities of asset ownership through stewardship actions.

The Head of RI has agreed to participate as a member of the Working Group (which had its first meeting in central London in early November). The outcome of the review will be a revised guide, details of which will be shared with the committee in due course.

Transition Pathway Initiative

LPP has agreed to become a Strategic Asset Owner Partner to the TPI.

This followed an approach proposing a more formal step in our continuing support for the initiative. Becoming a strategic partner entails providing funding support and being represented on the TPI Steering Committee. Members of LPP’s Stewardship Committee met with TPI representatives in September to discuss the proposal, provide feedback on our experience/impressions of the current tools and share insights from manager feedback.

Following the meeting it was agreed that LPP will provide financial support for 4 years (2020- 2024) and explore how we can add value through representation on the TPI Steering Group and through constructive

challenge/feedback which reflects our use of the toolkit as part of portfolio and manager monitoring and engagement.

5. Shareholder Litigation

LPPI employs Institutional Protection Services (IPS) as an external provider of litigation monitoring services to ensure shareholder litigation cases affecting securities owned by the GEF are known about, claims are filed in a timely way and progress is monitored and followed up with Claims Administrators. In addition, IPS monitor cases relating to shares held by LCPF in the period before the Fund pooled its listed equity investments from November 2016. Litigation can arise quite some time after shares have been sold and monitoring new cases and referring back to historic records to establish rights of ownership is an ongoing task.

IPS provide LPPI with monitoring information on a quarterly basis detailing the number of cases investigated. The monitoring report for Q3 2019 confirms that 3 new potential cases have been identified where the Fund may have an entitlement to join a class action and eligibility is being assessed, there are a further 11 cases where eligibility has been confirmed and a claim filed. In Q13 the Fund received a disbursement of monies relating to two claims that had reached settlement.

6. Active Investing

The LCPF Responsible Investment Policy describes active investing as the search for sustainable investments which meet LCPF's requirements for strong returns combined with best practice in ESG and corporate governance. The Fund has not set allocations for investments within specific sectors or identified impact themes but in general favours investments with positive social outcomes and has expressed an interest in understanding where current investments are delivering social benefits in addition to generating investment returns. Examples of socially positive investments are available from across the asset classes the fund invests in.

Infrastructure

In the period since the committee last met an infrastructure investment in Rock Rail East Anglia (through GLIL) has received positive media coverage related to the launch of a new fleet of passenger trains which are serving the Greater Anglia region.

A press release on the initiative produced by GLIL provides further detail on the benefits provided by the Rock Rail partnership and records a positive reception for the launch of the first cohort of new trains.

<https://www.glil.co.uk/assets/Greater-Anglia-has-formally-launched-its-new-fleet-of-regional-trains-with-special-runs-between-Lowestoft-and-Norwich.pdf>

The development of a website by GLIL <https://www.glil.co.uk/> has enabled information about the infrastructure partnership (origination, history to date, delivery aims and current portfolio) to be publicly available and details are now accessible on individual investments made to date by what is now a £1.275 billion alternative investment fund targeting core infrastructure opportunities (predominantly in the United Kingdom).

Current investments in which the Fund has an interest through GLIL (and which are having positive economic, employment and social benefits within the UK) include the supply of renewable power (wind and solar) and bio-energy (generating electricity and heat from waste), specialist logistics via one of the UK's largest port groups, and a portfolio of 92 operational assets supporting service provision within healthcare, education, accommodation, transport, community health, prisons, and utilities.

Additional Resources

LPPI has significantly increased the resources being dedicated to Responsible Investment through appointments to 3 new Analyst posts over the summer. This investment in expanding current capacity reflects the importance LPP places on RI and investment stewardship.

The new posts report to the Head of RI, are members of the Investment Strategy Team and create a split site RI Team of 4fte which has a presence in both London and Preston offices (which makes it better able to support the activities of asset class teams). Priorities include further developing policy and procedures which integrate ESG into decision-making, facilitating LPPI's participation in collaborative initiatives and identifying and using data to identify, map and quantify risks through models which will support monitoring, help to prioritise stewardship activity and increase the availability of information for enriching client and external reporting.