

REPORT OF THE GROUP DIRECTOR, FINANCE AND CORPORATE RESOURCES		
STEWARDSHIP FRAMEWORK - ENGAGEMENT OVERLAY OPTIONS	Classification PUBLIC	Enclosures:
	Ward(s) affected ALL	
Pensions Committee 27th June 2017		

1. INTRODUCTION

- 1.1 The Fund currently places reliance on its fund managers to engage with companies whilst being mindful of the Fund's requirements as set out in the new Investment Strategy Statement. There are however a number of options available which the Fund could use to enhance its engagement with investee companies and these are considered in the report below.

2. RECOMMENDATIONS

2.1 The Pensions Committee is recommended to:

- **Approve the use of National Frameworks' Stewardship Framework to procure an engagement overlay service, pending further work by officers to establish the Fund's requirements and most appropriate service model.**

3. RELATED DECISIONS

- Pensions Committee (24th January 2017) – Voting and Engagement Overlay Services
- Pensions Committee (24th January 2017) – Investment Strategy Statement
- Pensions Committee (31st March 2015) – Stewardship Code

4. COMMENTS OF THE GROUP DIRECTOR, FINANCE AND CORPORATE RESOURCES

- 4.1 The exercise of voting rights and engagement with investee companies are a key part of the Fund's role as a long term steward of assets. Ensuring good corporate governance and the adoption of sustainable business models at the companies in which the Fund invests should over the longer term ensure that they are able to deliver superior returns to the Fund. Poor corporate governance and unsustainable business practices can impact on share prices and increases the risk that the Fund may experience a loss of value in its investments in the future.
- 4.2 The cost to the Fund for engaging a governance overlay service will vary depending on the services required. Whilst no procurement exercise has been conducted by the Fund to date, it is estimated that employing the services of such organisations could cost anywhere between £30k up to £100k depending on the level of engagement that the Fund wants to undertake.

5. COMMENTS OF THE DIRECTOR, LEGAL

- 5.1 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 Regulation 7 requires Administering Authorities to publish and maintain an Investment Strategy Statement which includes, amongst other items, details of:
- The authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments.
 - The authority's policy on the exercise of the rights (including voting rights) attaching to investments.
- 5.2 In addition, Government guidance on the preparation and maintenance of the Investment Strategy Statement states that Administering Authorities should explain their policy on stewardship with reference to the Stewardship Code, the seven principles of which apply on a 'comply or explain' basis.
- 5.3 The proposals outlined in this report would help to ensure that the Fund is able to demonstrate further its compliance with the LGPS Regulations and Statutory Guidance.
- 5.4 There are no immediate legal implications arising from this report.

6. BACKGROUND TO THE REPORT

- 6.1 The subject of voting and engagement has been considered by the Pensions Committee on a number of occasions. The Committee wishes to ensure that it is able to effectively express its views on ESG issues through the exercise of the Fund's voting rights, as well as enhancing the Fund's approach to engagement with its investee companies more generally. However, the rapid changes currently taking place across the sector have raised a number of questions about how voting rights, and Responsible Investment (RI) approaches more generally, can best be delivered through the new pooled structures.
- 6.2 The Fund currently delegates the exercise of its voting rights to its external equity managers, who are asked to comply as far as possible with the Fund's voting policies. As discussed at the January 2017 meeting of the Pensions Committee, the move to a pooled structure over the medium term would significantly impact this arrangement as voting rights would need to be exercised at pool rather than fund level. The Fund will therefore need to ensure that it works with other London funds as well as the pool itself to ensure that in the future it is able to effectively express its views through the exercise of voting rights. As such, the Pensions Committee have agreed that pursuing a fund-level voting overlay approach is likely to be ineffective at this time.
- 6.3 The Fund also currently delegates broader engagement with investee companies around ESG issues to its external managers. The Fund is also a member of the Local Authority Pension Fund Forum (LAPFF), which currently comprises 71 local authority pension funds with combined assets of £175 billion. The Forum exists to promote the investment interests of local authority pension funds, and in particular to maximise their influence as shareholders to promote corporate social responsibility and high standards of corporate governance amongst the companies in which they invest.

6.4 Whilst this arrangement could continue under a pooled structure, the Committee wish to ensure that this area of the Fund's RI approach is enhanced. The Fund wishes to remain a member of LAPFF, but potentially enhance its engagement approach through use of an overlay service rather than relying on delegation to fund managers.

7. OVERLAY SERVICE OPTIONS

6.5 A range of organisations offer engagement overlay services, ranging from asset managers, some with dedicated stewardship advisory functions, through to specialist research organisations. Price ranges vary widely, with services ranging from £30k through to approximately £100k. It is therefore essential that further work is undertaken by officers to establish the range of services required by the Fund, to ensure that any services procured represent good value for money and do not duplicate work already undertaken e.g. through LAPFF.

6.6 The Committee is recommended to approve the use of the National LGPS Framework for Stewardship Advisory Services to undertake a procurement exercise. The framework offers stewardship services across a range of lots, with Lot 2 dedicated to the provision of engagement overlay services. Use of the framework ensures an efficient tender process using a tried and tested approach, with a range of providers who have met the necessary quality thresholds to be appointed to the framework.

6.7 Providers available under Lot 2 of the framework are as follows:

- BMO Global Asset Management
- Ethical Investment Research Services Ltd (EIRIS)
- GES Investment Services AB
- Hermes Equity Ownership Services
- Pensions and Investment Research Consultants Ltd (PIRC)
- Robeco Institutional Asset management B.V.

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Background papers

None