Oxfordshire Local Government Pension Scheme

Pension Fund Committee Position on Responsible Investing, including matters relating to Climate Change

The formal position of the Pension Fund Committee on responsible investments is included the ESG Policy section of the Fund's Investment Strategy Statement, which is available on the Fund's website at:

https://www.oxfordshire.gov.uk/business/pensions/pension-fund/about-fund

and is repeated as an Annex to this paper. This document is reviewed annually, with a fundamental review undertaken every three years in line with the Triennial Valuation of the Fund and a review of the Fund's Asset Allocation. The next review is due to complete in March 2020. In line with the guidance, the views of interested stakeholders will be taken into account in completing the next review.

The current position, which explicitly recognises the financial risks associated with environmental, social and governance (ESG) issues including climate change, was developed with the support of the Chief Responsible Investment Officer at the Brunel Company and previously at the Environment Agency Pension Fund. She is internationally recognised as an expert in this field, and a regular award winner for her work in the area of responsible investment.

A key element of the current policy is to avoid blanket decisions, such as the disinvestment of all fossil fuel companies, but to make investment decisions on the merits of each individual case, and engage directly with companies to ensure they are acting to mitigate key risks. The Committee believes that such a policy both enables them to best meet their fiduciary duties, as well as contributing to the development of a sustainable future for all. The policy allows differentiation between those fossil fuel companies that are working hard to reduce their carbon emissions and switching to renewable sources of energy, and those that have failed to respond appropriately to the challenge.

The Committee has been challenged not only on its policy not to divest in all fossil-free companies, but also on why it doesn't make an allocation to the passive low-carbon and/or sustainable equity portfolios managed by Brunel. It is the Committee's view that it cannot meet its fiduciary duty by blanket decisions that all fossil fuel companies are bad, and all low carbon companies are good. Each investment is examined for investment potential and risks to achieving that potential. This allows the Committee to select those fossil fuel companies that are building a sustainable future through cleaning up their processes and increasing resources developing renewable alternatives. It also allows the Committee to avoid those low-carbon companies that are failing to manage other key ESG risks, including the wider risks associated with climate change. The ability to engage with companies as an active manager, with the ultimate sanction of disinvesting if the company fails to respond positively to the engagement is also seen as a key benefit of the current policy.

The main area the Committee wishes to develop is the reporting on company performance on ESG issues to enable it to validate its current policy and ensure that the Fund Managers are complying with the policy and that their engagement is effective. This work is being undertaken in conjunction with the Chief Responsible Investment Officer at Brunel, alongside the other Funds within the Brunel Pension Partnership, and it is hoped to have the first ESG report at portfolio level available as part of the quarterly performance report to 31 March 2019.

Annex – Extract from the Investment Strategy Statement
ESG Policy

The Committee recognises that environmental, social and corporate governance (ESG) issues, including climate change, can have materially significant investment implications. The Fund therefore seeks to be a responsible investor and to consider ESG risks as part of the investment process across all investments. The objective of responsible investment is to decrease investor risk and improve risk-adjusted returns. Responsible investment principles are at the foundation of the Fund’s approach to stewardship and underpin the Fund's fulfilment of its fiduciary duty to scheme beneficiaries.

The Committee’s principal concern is to invest in the best financial interests of the Fund’s employing bodies and beneficiaries. Its Investment Managers are given performance objectives accordingly. The Council requires its Investment Managers to monitor and assess the environmental, social and governance considerations, which may impact on financial performance when selecting and retaining investments, and to engage with companies on these issues where appropriate. The Council believes that the operation of such a policy will ensure the sustainability of a company’s earnings and hence its merits as an investment.

The Investment Managers report at quarterly intervals on the selection, retention and realisation of investments on the Council’s behalf and on any engagement activities undertaken. These Reports/Review Meetings provide an opportunity for the Council to influence the Investment Manager’s choice of investments and to review/challenge their stewardship activities but the Council is careful to preserve the Investment Manager’s autonomy in pursuit of their given performance.

Just because concerns have been registered about a company’s performance on ESG issues, doesn’t mean our fund managers will be instructed not to invest in that company. It is then through active ownership we aim to drive change. Where engagement is not seen to be resulting in sufficient progress, and so the risk associated with a holding is increasing or not reducing sufficiently, the Fund will consider divesting.

As a passive investor, the Fund accepts that it will hold companies of varying ESG quality due to the requirement to hold all securities in the target index. The committee believes that passive investing offers a number of benefits that need to be weighed against this and requires passive managers to demonstrate effective engagement, as is the case for active managers. It is important to note that ownership of a security in a company does not signify that the Oxfordshire Pension Fund approves of all of the company’s practices or its products

The Committee is open to investing in Social Investments; investments where social impact is delivered alongside financial return. The Committee further believes that the goal of social impact is inherently compatible with generating sustainable financial returns by meeting societal needs. The Fund has made investments in this area and will continue to review whether further opportunities are available that offer an appropriate risk/return profile. Stakeholders’ views are taken into account through the representation of different parties on the Pension Fund Committee, which includes a beneficiaries' representative, and the Local Pension Board, which consists of equal numbers of employer and member representatives.

The Fund will not use pension policies to pursue boycotts, divestment and sanctions against foreign nations and UK defence industries, other than where formal legal sanctions, embargoes and restrictions have been put in place by the Government.

One of the principal benefits, outlined in the Brunel Pension Partnership business case, achieved through the enhanced scale and resources as a result of pooling is the improved implementation of responsible investment and stewardship. Once established and fully operational the Brunel Company will deliver best practice standards in responsible investment and stewardship as outlined in the BPP Investment Principles.

Every portfolio under the Brunel Pension Partnership explicitly includes responsible investment and an assessment of how social, environment and corporate governance considerations may present financial risks to the delivery of the portfolio objectives. These considerations will therefore be taken into account in the selection, non-selection, retention and realisation of assets. The approach undertaken will vary in order to be the most effective in mitigating risks and enhancing investor value in relation to each portfolio and its objectives.

Policy on Exercise of Rights

As an investor with a very long-term investment horizon and expected life, the success of the Oxfordshire Pension Fund is linked to long term global economic growth and prosperity. Actions and activities that detract from the likelihood and potential of global growth are not in the long-term interests of the Fund. Since the Fund is a long-term investor, short-term gains at the expense of long-term gains are not in the best interest of the Fund. Sustainable returns over long periods are in the economic interest of the Fund.

The Fund recognises that encouraging the highest standards of corporate governance and promoting corporate responsibility by investee companies protects the financial interests of pension fund members over the long term. Stewardship activities include monitoring and engaging with companies on matters such as strategy, performance, risk, capital structure and corporate governance, including culture and remuneration.

The Fund's commitment to actively exercising the ownership rights attached to its investments reflects the Fund's conviction that responsible asset owners should maintain oversight of the way in which the enterprises they invest in are managed and how their activities impact upon customers, clients, employees, stakeholders, and wider society.

The routes for exercising ownership influence vary across asset types and a range of activities are undertaken on the Fund's behalf by Fund Managers including engagement with senior management of companies, voting of shares, direct representation on company boards, presence on investor & advisory committees and participation in partnerships and collaborations with other investors. Where the

Pension Fund invests in pooled vehicles it will seek to gain representation on investor committees if considered appropriate.

In practice the Fund's Investment Managers are delegated authority to exercise voting rights in respect of the Council's holdings. Voting decisions are fully delegated to fund managers, while recognising that the Fund maintains ultimate responsibility for ensuring that voting is undertaken in the best interests of the Fund.

The Fund will exercise its voting rights in all markets and its investment managers are required to vote at all company meetings where practicable. Market conventions in some countries may mean voting shares is not in the best interests of the Fund, for example where share-blocking is in operation.

The Fund has appointed an external company to monitor the Fund's proxy voting at the whole fund level. The Fund receives reports detailing where votes cast by Fund Managers differ to the template vote recommended by the provider. The monitoring service also includes the production of an annual report for the Fund summarising and analysing the voting activity for the Fund including at Fund Manager level. These reports are used to inform the Fund and to enable discussion with Fund Managers where appropriate.

Our approach to Stewardship, including the exercising of rights attached to investments is outlined above and is consistent with the requirements of the UK Stewardship Code. During 2017 we will develop this further by becoming signatories to the code and clearly demonstrating our position in relation to all seven principles. As part of the Brunel Pension Partnership (BPP) we are actively exploring opportunities to enhance our stewardship activities.