



# RESPONSIBLE INVESTMENT POLICY



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## 1) INTRODUCTION

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This framework defines the commitment of London LGPS CIV Limited (“London CIV” or ‘the Pool’) to responsible investment (‘RI’). Its purpose is to detail the approach that the Pool aims to follow in integrating environmental, social and governance (‘ESG’) issues in its investments.

We recognise that our clients have a fiduciary duty to act in the best long-term interests of their members. To do so properly requires us to recognise that environmental, social and governance issues can positively and negatively impact on the Fund Solutions provided by the Pool which should be considered in our investment strategies and decision-making processes.

London CIV has considered the guidance provided in the Ministry of Housing Communities and Local Government (‘MHCLG’) paper ‘Local Government Pension Scheme: Investment Reform and Criteria and Guidance’ in the establishing of this policy.

### 1.1 BELIEFS AND GUIDING PRINCIPLES

The Pool’s RI beliefs and guiding principles underpin its RI approach and are described below.

#### 1.1.1 Beliefs

- a) We believe it is important that we accept and exercise the responsibilities of ownership of all the assets we manage.
- b) We believe that communication and engagement are integral to responsible investment.
- c) We believe that we should hold all our suppliers to account over how they exercise our ownership rights.
- d) We accept that there can be a conflict between the ability to exercise ownership rights when working with other third parties; we will manage this through communication and engagement.
- e) Sometimes assets will be sold over ESG issues; however the LCIV or its partners will only do this on a case by case basis when considering all the facts.
- f) We believe pre-determined divestment on a rules-based approach is contrary to Government guidance and does not form part of this RI policy.
- g) We believe our voice for responsible ownership is loudest when we own an asset.

#### 1.1.2 Guiding Principles

- a) We should set out principles to which we aspire on subjects that all shareholders can agree, for example:
  - Human rights
  - Human slavery
  - Cluster munitions
  - Rule of law
  - Equality
  - Corporate governance
  - Sustainability
  - Climate change
  - Fossil fuel risk
- b) We will require all Investment managers to have an RI policy if the LCIV is to invest with them.
- c) We will make clear to investment managers our consensus views on these matters and ask them to consider incorporating them into their RI policies.
- d) We will ensure that all investment managers operate their RI policies effectively and hold them to account.
- e) An Investment Manager’s inability to operate effectively their RI Policy will be a factor in determining if the LCIV continues to use a manager.
- f) We will produce an Annual RI report for the London CIV.

- g) The Pool also requires investment managers to vote in accordance with the Local Authority Pension Fund Forum (“LAPFF”), other than in exceptional cases, in which case they should explain their reasons for not doing so, preferably in advance of the meeting. This is monitored on a regular basis.

### **1.1.3 ESG Integration**

The Pool believes that

- i) Investing responsibly and engaging as sustainable long term investors reduces risk over time and may positively impact the returns. The London CIV must encourage the underlying funds and companies to consider the long-term impacts of their actions.
- ii) A long time horizon requires that the team consider the impacts of its actions on future generations.
- iii) Effective management of financially material ESG risks should support the Pool’s requirement to protect returns over the long term.

The Pool considers RI to be relevant to investment performance across asset classes.

The Pool recognises the need to operate at a market-wide level to promote improvements that will help it to deliver sustainable long-term growth.

It is supportive of the UK Stewardship Code and is a Tier 1 signatory to the Code. The Pool encourages investment managers to sign up to the UK Stewardship Code and the United Nations Principles of Responsible Investment (UNPRI) where appropriate.

### **1.1.4 Engagement versus Exclusion**

Investee companies with robust governance structures should be better positioned to handle the effects of shocks and stresses of future events.

There is risk but also opportunity in holding companies that have weak governance of financially material ESG issues. Thus, the Pool has a policy of risk monitoring and engagement in order to positively influence company behaviour and enhance stakeholder value, influence that would be lost through a divestment approach. The Pool extends this principle of ‘engagement for positive change’ to the due diligence, appointment and monitoring of external fund managers who are at an early stage of developing their RI approach.

The Pool believes that it will improve its effectiveness by acting collectively with other like-minded investors because it increases the likelihood that it will be heard by the company, fund manager or other relevant stakeholder compared with acting alone. This extends to other LGPS pools and other public and private investors.

### **1.1.5 Fees and Incentives**

Managing fees and costs matter in low return environments. Fee arrangements with external fund managers – as well as the remuneration policies of investee companies – should be aligned with the participating funds’ long-term interests.

The Pool recognises that it is part of its fiduciary duty to ensure that there is appropriate alignment.

### **1.1.6 An Evolving and Flexible Approach**

The Pool recognises that RI in the market is changing. This framework will remain flexible and will evolve over time to reflect evolving market developments.

## **1.2 OVERSIGHT AND APPLICATION**

This policy will be reviewed at a minimum annually, or whenever they or the Pool proposes revised RI policies and procedure. The Chief Investment Officer is responsible for policy implementation.

## **1.3 CONTENT**

The RI framework is divided into sections:

- How ESG is interpreted by Asset Class
- What the Pool expects of itself, companies and investment managers with respect to RI.
- How the RI beliefs and guiding principles are implemented in practice.

Definitions are provided in Section 5.

## **2) ESG BY ASSET TYPE**

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### **2.1 LISTED EQUITIES**

Responsible investment allows listed equity investors to make better informed investment decisions by integrating all material factors, including material ESG factors, into investment analysis, valuations and decisions. Investment Managers should be voting all proxies and using their influence as owners of companies to ensure shareholder valuation is maximised through considering the impact of ESG factors (both positive and negative) on the value of the organisation.

### **2.2 FIXED INCOME**

ESG analysis provides fixed income investors with additional insight into issuer creditworthiness. Whilst governance influence over fixed income issuers can be less than in equity ownership, investment managers taking sizable positions in capital structures can influence behaviours including ESG factors.

### **2.3 PRIVATE EQUITY**

Responsible investment is naturally aligned to private equity through its long-term investment horizon and stewardship-based style. The Pool will incorporate ESG practices for the selecting, appointing and monitoring of investment managers and direct/co-invest portfolio companies.

### **2.4 PROPERTY**

Property is a long term asset class where ESG is centred on delivering sustainable, long term performance by considering ESG factors within investment decision-making and ownership practices, providing greater insight into potential risks and opportunities that will impact the value, performance and reputation of the investment.

### **2.5 INFRASTRUCTURE**

Long-term infrastructure investors should consider a broad range of possible ESG issues that infrastructure investments might face over the course of the assets' life, in the analysis and assessment of opportunities, and in the ongoing management of investments.

### **2.6 COMMODITIES**

Responsible investment in commodities allows investors to address risks such as: labour rights, human rights, land/resource rights, waste, water scarcity and pollution levels in assets, such as forests and agricultural land, and companies throughout the supply chain. Applying responsible investment to investments in commodity derivatives can address systemic issues such as volatile prices and unstable markets.

## **2.7 OTHER ALTERNATIVES**

The pool will working with investors, investment managers, industry associations and service providers to incorporate ESG factors into the investment decision-making process of all other alternative investments.

## **2.8 ENVIRONMENTAL & SOCIAL THEMED INVESTING**

Themed investing allows investors to address ESG issues by investing in specific solutions to them, such as renewable energy, waste and water management, sustainable forestry and agriculture, health products and inclusive finance.

## **3) RI EXPECTATIONS**

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### **3.1 POOL**

#### **3.1.1 General**

The Pool aims to:

- 1) Be aware of and monitor financially material ESG issues in the context of investment and manager selection. Depending on the asset class and nature of the proposed mandate or vehicle, the Pool will monitor:
  - ESG issues in relation to internally managed investments;
  - The extent to which the external managers incorporate ESG issues into their investment processes; and
  - Hold external managers to account for improvement in their ESG performance over a reasonable timeframe.
- 2) Seek to use pooling to facilitate implementation of the environmental, social and corporate governance policy, for example by sharing best practice, collaborating on social investments to reduce cost or diversify risk, or using their scale to improve capability in this area. It will make full use of its ownership rights, including voting and engagement activities. Either directly, collaboratively or through specialist service providers:
  - Hold constructive dialogue with listed companies;
  - Encourage the disclosure by companies of ESG issues; and
  - Participate in the development of public policy on ESG issues.
- 3) Disclose and maintain a policy for identifying and managing conflicts of interest with the aim of taking all reasonable steps to put the interests of participating funds' beneficiaries first.
- 4) Keep our stakeholders aware of our RI activities through:
  - making its RI policy documents public, e.g., voting policies, RI policy;
  - providing a summary of the Pool's RI activities for publication in participating funds' annual reports;
  - publishing aggregate voting and company engagement statistics on a quarterly basis

### **3.1.2 Fiduciary Responsibility**

The London CIV acknowledges a need to set out the extent to which social, environmental or corporate governance considerations are taken into account in the selection, retention and realisation of investments. This extends to the need to monitor environmental, social and corporate governance policies to provide a useful tool in managing financial risk, as they ensure that the wider risks associated with the viability of an investment are fully recognised.

However the London CIV also appreciates, as the Law Commission emphasised in its 2014 report on the fiduciary duty of financial intermediaries, that the law generally is clear that schemes should consider any factors financially material to the performance of their investments, including social, environmental and corporate governance factors, and over the long-term, dependent on the time horizon over which their liabilities arise. The report went on to state that although schemes should make the pursuit of a financial return their predominant concern, they may take purely non-financial considerations into account provided that doing so would not involve significant risk of financial detriment to the scheme and where they have good reason to think that scheme members would support their decision.

As indicated in the DCLG document, the Government's intention is to issue guidance to authorities to clarify that such considerations should not result in policies which pursue municipal boycotts, divestments and sanctions, other than where formal legal sanctions, embargoes and restrictions have been put in place by the Government. Investment policies should not be used to give effect to municipal foreign or munitions policies that run contrary to Government policy. This guidance has since been challenged on legal grounds and is currently under review. The London CIV policy will reflect the Government guidelines when this has been finalised.

London CIV acknowledges this fiduciary responsibility of its members and will reflect this obligation in the investment selection process.

### **3.1.3 Carbon Footprint & Climate Change**

The Pool aims to, either directly or through specialist service providers:

- Encourage improvement in the level of disclosure by companies of material climate change impacts through collaborative initiatives;
- Review its fund managers to understand their approach to incorporating climate change considerations and encourage improvements in identifying and assessing the potential impact of climate change;
- Contribute to public policy with regard to climate change as it relates to investment considerations;
- Increase awareness of climate change as it applies to investment decision making through participation in relevant industry forums and collaborative initiatives; and
- Keep up to date on the latest research and thinking on the financial materiality and interconnectedness of climate change within and across asset classes

## **3.2 COMPANIES**

### **3.2.1 Governance Codes**

The Pool expects UK companies to adhere to the UK Corporate Governance Code on a comply-or-explain basis. Further, the Pool has bespoke UK corporate governance guidelines which aim to deal with issues that are either not covered by the Code, require greater emphasis or are specifically left open for shareholders to resolve with company boards.

The Pool expects companies outside the UK to adhere to international voting principles, recognising local application and development.

### **3.2.1 Environmental and Social Risks**

The Pool expects companies to manage and disclose its environmental and social risks to the extent required for an understanding of the development, position and performance of the company.

There are aspects of environmental and social reporting on which the Pool places particular value given their relevance across all sectors, its holistic approach to risk management, and the view that owners should not micro-manage companies. This is narrative reporting which:

- Sets ESG risks in the context of the whole range of risks and opportunities facing the company;
- Contains a forward looking perspective; and
- Describes the actions of the board in mitigating these risks.

In terms of the specific environmental and social issues to focus upon, the Pool takes a case-by-case sector based approach.

## **3.3 INVESTMENT MANAGERS**

The Pool expects company directors and asset managers to adopt measures to promote both stewardship and long-term decision making. In particular asset managers can contribute more to the performance of business through greater involvement in the companies in which they invest. Adopting such responsible investment practices will prove beneficial for investors and markets alike.

### **3.3.1 Due Diligence**

For each appropriate asset class, the Pool will ensure that managers selected for appointment have:

- An ESG Policy, appropriate policy addressing ESG issues.
- Where relevant managers should be demonstrating active ownership policies or equivalent, articulating how ESG factors are integrated into their investment process. This may include research, active ownership activities or other sources.
- Case studies or examples of where ESG issues have influenced an investment decision
- Where appropriate, information on the process for integrating any third party ESG data into their company financial models, investment strategies and portfolio construction
- RI reporting format
- Whether they are a signatory of the UN backed Principles for Responsible Investment (PRI) and Stewardship Code, copy of their PRI public report and annual assessment scores if applicable.

### **3.3.2 Appointment**

The Pool assesses the ESG capability of a fund manager as a factor within each of the people, process and performance categories. In its decision to appoint a fund manager, the Pool takes a balanced consideration of all relevant factors including ESG. However, the Pool will pay particular attention to adherence to relevant soft regulatory codes, notably the UK Stewardship Code, depending on the market in which it invests.

In practice, this means the Pool would be willing to hire a fund manager at an early stage of developing its RI approach so long as there is a demonstrable RI commitment and a willingness to improve in their approach over time. In alignment with our guiding principles on 'engagement versus exclusion', the Pool believes that there is added value in working with them to improve their approach.

### 3.3.3 Monitoring and Reporting

Each external fund manager is expected to review their ESG policy on an annual basis.

Managers should report at agreed intervals to the Pool on how their RI activities are contributing to improved long-term risk adjusted returns. Examples of information that can be provided in aid of this objective include but are not limited to the following:

- The evolution of how the manager integrates the consideration of ESG issues into its investment and active ownership activities.
- How investment and active ownership function are combined to protect and/or enhance shareholder value in the case of equities including
  - How the manager exercised the Pool's voting rights.
  - Any outcomes arising from the manager's engagement with companies and their effectiveness.

## 4) RI IMPLEMENTATION

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The Pool's active ownership approach can be divided into three distinct areas: **voting globally**, **engagement through partnerships** and **shareholder litigation**. This section briefly outlines the Pool's processes for each.

### 4.1 VOTING GLOBALLY

Where practical, the Pool requires managers to vote in every single market in which it invests. The Pool will monitor IMs voting records and will expect that an appropriately critical approach is taken to company proposals.

Reference to the Pool's voting policies is provided in Section 2.2 under 'Company Expectations'.

#### 4.1.1 Securities Lending Programme

The Pool does not currently engage in direct securities lending.

### 4.2 ENGAGEMENT THROUGH PARTNERSHIPS

The Pool uses various engagement platforms to maximise its influence as an active owner in collaboration with other like-minded investors. Where it is possible and practical to do so, the Pool will engage with the other Pools to maximise the effectiveness and the influence of the LGPS assets as a whole. The Pool's primary engagement partnerships are highlighted below.

#### 4.2.1 Local Authority Pension Fund Forum

The Pool is a member of the Local Authority Pension Fund Forum (LAPFF). LAPFF is the UK's leading collaborative shareholder engagement group encompassing local authority pension funds from across the country. The Pool and its constituent funds are active participants in LAPFF's engagement programs. Membership of LAPFF provides the Pool with:

- 1) independent research and advice on the ESG risks of companies to inform further stakeholder engagement;
- 2) advice on the governance practices of companies;



- 3) A forum to engage with companies to improve governance practices; and
- 4) Proxy voting advice on high-priority issues for annual general meetings.

#### **4.2.2 Industry Engagement**

In collaboration with other like-minded investors, notably other LGPS investment pools, the Pool may engage with public policy makers, regulators, trade bodies, indexes and other players in the financial markets to achieve the aim of promoting sustainable growth. The London CIV is a signatory of the UNPRI. The Pool considers these initiatives on a case-by-case basis.

### **4.3 SHAREHOLDER LITIGATION**

The Pool may hold securities that are the subject of individual and class action securities litigation. There are a number of litigation options available when a company has violated securities laws that result in losses to participating funds.

For US based claims, the options would be to:

- remain in the class action and file proof of claim;
- participate as a lead plaintiff in a class action; or
- opt out and file a private action.

For non-US based claims, the options would be to join an existing group action or file a group action as a lead plaintiff.

The Pool takes a case-by-case approach in determining whether or not to join a class action but considers factors such as:

- advantages and disadvantages of the Pool becoming actively involved;
- relative size of the Pool's potential losses compared to other organisations;
- likelihood of success; and
- whether the Pool is fully indemnified against costs, expenses, counterclaims and any other losses.

Where external service providers are used for voting, engagement and shareholder litigation, the Head of Equities will be responsible for ensuring that the quality of service provision is kept under regular review, reporting concerns internally and following up with the supplier. This includes verifying that engagement and voting are undertaken in line with London CIV's agreed RI Framework.

## **5) DEFINITIONS**

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### **5.1 RESPONSIBLE INVESTMENT**

The integration of environmental, social and corporate governance (ESG) considerations into investment management processes and active ownership practices in the belief that these factors can have an impact on financial performance. The Pool also supports the PRI's definition of responsible investment which can be found here:

<https://www.unpri.org/about/the-six-principles>

### **5.2 ESG**

Environmental, social and governance factors which may impact on company performance and therefore investment returns. ESG factors encompass a broad range of issues to potentially consider alongside

traditional financial factors when assessing investments. No definitive list of ESG issues exists however some examples include resource management and pollution prevention, climate change impacts, labour management, product integrity, executive compensation, board independence and audit function.

### **5.3 GOVERNANCE**

The process and principles by which a company or organisation undertakes its business. For the Pool, governance includes how it undertakes both its operational and investment responsibilities on behalf of its members.

### **5.4 ACTIVE OWNERSHIP**

Refers to the responsibility of the Pool to participate, where appropriate, in the governance decision making of companies in which it invests by way of voting and by engagement with company management, either directly or via its fund managers. It also recognizes the relevance of engaging with regulatory bodies and other market players to support policies that promote long term sustainable growth.