

Local Authority Conference 2011

A New Day

Local Authorities look to the future

The UK Stewardship Code

Howard Pearce

Environment Agency Active Pension Fund



Environment Agency Active Fund

- £1.7bn assets belong to 22,000 members.
- Current liabilities 94% funded – still need strong risk adjusted investment returns.
- Fund will pay benefits for at least 100 years.
- Current asset allocation 63% public equity, 27% fixed interest, 5% private equity and 5% property.



Global economy and natural resources

‘The time for delay is over. The time for denial is over. We all believe what the scientists have been telling us for years now, that this is a matter of urgency and national security and it has to be dealt with in a serious way. That’s what I intend my administration to do.’

U.S. President-elect Barack Obama, December 2008

‘What we cannot afford is more short-sighted approaches. The global economy needs more than a quick fix. It needs a fundamental fix. If we have learned anything from the financial crisis, it is that we must put an end to unethical and irresponsible behaviour and the tyrannical demand for short-term profit. The price of a global bail-out may seem high, but it will pale next to the enormous human and economic costs of delaying action on climate change. Continuing to pour trillions of dollars into fossil-fuel subsidies is like investing in sub-prime real estate. Our carbon-based infrastructure is like a toxic asset that threatens the entire portfolio of global goods – from public health to food security. We must direct investment away from dirty energy industries.’

United Nations Secretary-General Ban Ki-moon, May 2009



Our investment philosophy

“It is entirely consistent with this fiduciary duty for the fund investment strategy and fund managers to take into account financially material environmental risks like climate change (that could reduce investment returns) and opportunities like clean technology (that could generate higher investment returns). Ignoring or not taking into account these (and other) financial risks and opportunities in the fund’s investment strategy is a potential breach of this fiduciary duty.”

Environment Agency Pension Fund SIP



Leading consultancy firms views

“ESG issues ‘are’ financial risks for pension funds” Roger Urwin, Global Head of Investment, Towers Watson.

“The idea that responsible investment does not have to come at a cost to performance is becoming well established in the institutional investment industry. In fact, the ‘Shedding Light’ report further builds the already strong case that considering ESG factors can add real and measurable value to an investment portfolio”

Tim Gardener, global chief investment officer for Mercer’s investment consulting business.



Other stewardship frameworks

- UN Principles of Responsible Investment
- European Asset Managers
- Institutional Investors Group on Climate change
- Carbon-Water-Forestry Disclosure Projects
- LGPS/ UKSIF Self Assessment Framework



UK Code compatible with UNPRI

UNPRI Principles

1. We will incorporate ESG issues into investment analysis and decision-making processes.
2. We will be active owners and incorporate ESG issues into our ownership policies and practices.
3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.
4. We will promote acceptance and implementation of the Principles within the investment industry.
5. We will work together to enhance our effectiveness in implementing the Principles.
6. We will each report on our activities and progress towards implementing the Principles.

UK Stewardship Code

1. Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.
 2. Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.
 3. Institutional investors should monitor their investee companies.
 4. Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.
 5. Institutional investors should be willing to act collectively with other investors where appropriate.
 6. Institutional investors should have a clear policy on voting and disclosure of voting activity.
 7. Institutional investors should report periodically on their stewardship and voting activities.
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The UK Stewardship Code

- Financial Reporting Council keen to stress joint role between **asset owner** and **asset manager**.
 - “the responsibility for monitoring company performance does not rest with fund managers alone. Pension fund trustees and other owners can do so either directly or indirectly through the mandates given to fund managers. The FRC therefore encourages all institutional investors to report if and how they have complied with the Code.”



EAPF compliance statement

- Keen to signpost to other policies and statements
- Evidence published on our website, examples include
 - Corporate Governance and Environmental overlay policies
 - Responsible Investment Review
 - UNPRI statements
 - Voting policy and record on environmental resolutions
 - Research



Environment Agency Active Fund (EAPF) is fully committed to responsible investment. We believe there is a considerable body of evidence that well governed companies produce better and more sustainable returns than poorly governed companies. We also think investors, including pension fund managers and shareholders, could influence the Board/Directors of under-performing companies to improve the management and financial performance of those companies. A summary of our compliance with the UK Stewardship code, published in 2010, is detailed below.

<p>Principle 1 Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.</p>	<p>Our Fund fully follows this principle</p> <ul style="list-style-type: none"> • The EAPF has a comprehensive suite of published policy documents which define how we discharge our Stewardship responsibilities, including but not limited to our Statement of Investment Principles, Corporate Governance and our Environmental Overlay Strategy. • All new Investment Management Agreements (IMAs) include requirements to observe the FRC's UK Corporate Governance Code and UK Stewardship Code.
<p>Principle 2 Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.</p>	<p>Our Fund fully follows this principle</p> <ul style="list-style-type: none"> • Declaration of conflict of interests is a standing agenda item at the start of all Pensions Committee and Investment Sub-Group meetings. A public register of Pension Committee members declaration of interests is also maintained and audited annually. • The need to avoid conflicts of interest is also highlighted in our Investment management agreements (IMAs) and contracts with external parties.
<p>Principle 3 Institutional investors should monitor their investee companies.</p>	<p>Our Fund fully follows this principle</p> <ul style="list-style-type: none"> • We include our Corporate Governance policy and ESG reporting requirements in all our IMAs with all our fund managers and Service Level Agreement (SLA) with our equity engagement overlay provider. • Monitoring of specific investee companies is detailed in our quarterly reports and discussed regularly at fund manager review meetings.
<p>Principle 4 Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.</p>	<p>Our Fund fully follows this principle</p> <ul style="list-style-type: none"> • Our Corporate Governance Policy and Environmental Overlay Strategy details of our engagement policies. • During quarterly review meetings with our fund managers we review their engagement activity and planned escalation of activity.
<p>Principle 5 Institutional investors should be willing to act collectively with other investors where appropriate.</p>	<p>Our Fund fully follows this principle</p> <ul style="list-style-type: none"> • We actively work with other pension funds, asset managers and other organisations to promote responsible investment. These include but are not limited to the UNPRI, IIGCC, NAPF and UKSIF. • All our managers work collaboratively with other parties. Collaborative engagements, research and advocacy work is detailed in our quarterly and annual reports.
<p>Principle 6 Institutional investors should have a clear policy on voting and disclosure of voting activity.</p>	<p>Our Fund fully follows this principle</p> <ul style="list-style-type: none"> • We detail on what basis our votes are cast and the guidelines we direct our managers to use in voting in our Corporate Governance policy. We publish all the votes on environmental resolutions. • All our equity manager have voting policies and most are publicly available. Similarly, our larger managers publish voting records on their website and others on request.
<p>Principle 7 Institutional investors should report periodically on their stewardship and voting activities.</p>	<p>Our Fund fully follows this principle</p> <ul style="list-style-type: none"> • We include a comprehensive annual review of our activities in our Annual Report and Accounts and Fundfare. A more detailed review is provided in our periodic Responsible Investment Review.

eapf.org.uk

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Our response, our managers and suppliers

- Co-signed a Joint letter of support to FRC.
- Published our own statement September 2011.
- We asked our 8 UK FSA registered managers to be explicit in their plans to produce a statement before FRC requirement.
- By early December our UK FSA managers had produced a statement.
- Our other 3 EEA registered managers have provided evidence to support their own compliance and agreement in principle to sign a European code in due course.
- Our advisors - Mercer, Rathbones, Hermes, Hymans Roberston provide supporting statements linked via FRC website.



LGPS asset owners with compliance statements

- Avon Pension Fund
- Bedfordshire Pension Fund
- Environment Agency Active Pension Fund
- Greater Manchester Pension Fund
- London Borough of Ealing Pension Fund
- Lothian Pension Fund
- Merseyside Pension Fund
- North East Scotland Pension Fund
- Northern Ireland Local Government Officers' Superannuation Committee
- West Midlands Pension Fund

Source FRC website April 12th 2011



How we are taking it forward 2011-12

Manager Selection

- Built into tender requirements and all new IMA's:
“Manager shall observe the Client's Corporate Governance and Environmental Overlay Strategies and Policies and the UK Financial Reporting Council's Stewardship Code and, in respect of investments in the United Kingdom, have due regard to the UK Corporate Governance Code and in respect of overseas investments have due regard to relevant recognised standards as agreed with the Client....”

How we are taking it forward 2011-12

Manager Monitoring

- UK Stewardship explicitly included in annual manager review and assessment.
- Quarterly reporting of all engagements, voting and ESG assessment.
- Required to provide evidential documents to support statement.



Discussion points

- Should the principles be used by all LGPS funds ? and in fund manager procurement across LGPS ?
- How can we use the code to progress stewardship?
 - Independent monitoring and benchmarking
- How to developing the code itself?
 - Applicability to all asset classes
 - Voting rights for beneficial owners in relation to pooled funds
 - Wider application in EU and overseas to improve transparency of voting



Questions ?

More information on our websites

www.environment-agency.gov.uk/pensions

www.environment-agency.gov.uk/environmentalfinance

www.eapf.org



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