

Report to: Pension Board
Date: 5 November 2018
By: Chief Finance Officer
Title of report: Responsible Investment Policy
Purpose of report: To consider the proposed Responsible Investment Policy before implementation.

RECOMMENDATION -

The Board is recommended to consider and comment on the report.

1. Background

1.1 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 require the Pension Fund Investment Strategy Statement (ISS) to include a policy on how social, environmental or corporate governance (ESG) considerations are taken into account; in the selection, non-selection, retention and realisation of investments.

1.2 The East Sussex Pension Fund's ISS sets out how social, environmental or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments, and it is recognised that ESG factors can influence long term investment performance and the ability to achieve long term sustainable returns. The Pension Committee considers the Fund's approach to responsible investment (RI) in two key areas:

- a) *Sustainable investment / ESG factors – considering the financial impact of ESG factors on its investments.*
- b) *Stewardship and governance – acting as responsible and active investors/owners, through considered voting of shares, and engaging with investee company management as part of the investment process.*

1.3 Responsible investing issues can have a material impact on investment risk and return in the long term and therefore should be considered within the Fund's investment strategy. In addition, as an asset owner, the Fund has a duty to ensure it carries out its stewardship duties effectively.

1.4 The RI policy seeks to ensure the long term RI risks to which the Fund is exposed are fully incorporated into strategic and operational (i.e. the investment manager's) decision making, and that the Fund carries out its duties as a responsible investor. The proposed RI policy is appropriate, proportionate and achievable to implement within the Fund's resources and governance framework.

2. Proposed Responsible Investment Policy

2.1 The proposed RI Policy is based on the framework that was debated at the Committee meetings and advice from both the Fund Independent and Investment Consultants. Care has been taken to ensure that the policy and actions required to implement it are appropriate, proportionate and achievable to implement within the Fund's resource and governance framework.

2.2 The policy set out the underlying beliefs on which the policy is based. It demonstrates how the Fund will implement these beliefs within its strategic and operational decision-making processes. It recognises that the Fund's integrated investment strategy will develop over time as the economic outlook and expected investment risks and returns vary, and therefore allows flexibility to manage RI issues within an evolving strategy, rather than be prescriptive. The objective should not be for the strategy to reflect every RI investment approach, but to ensure RI risks and opportunities are integrated into the Fund's strategic investment.

2.3 The Fund's approach aims to ensure that consideration of ESG/RI factors is embedded in the investment process, utilising the various tools available to manage ESG risks and to harness opportunities presented by ESG factors. The Fund's core principles of responsible investment are:

- We will apply **long-term thinking** to deliver **long-term sustainable returns**.
- We will seek **sustainable returns** from **well-governed assets**.
- We will use an **evidence-based** long term investment appraisal to inform **decision-making** in the implementation of RI principles and consider the costs of RI decisions consistent with our fiduciary duties.
- We will evaluate and manage **carbon exposure in order to mitigate risks to the Fund from climate change**.

3. RI Policy Implementation

3.1 Once the responsible investment policy has been agreed, the Fund's ISS will be amended to reflect the beliefs and policy framework. Some elements of the policy that are not already in place can be implemented fairly quickly with little resource or cost implications, whereas others may require longer term structural changes to the investments structure. Because of this, the implementation timeframe for any agreed policy is over the medium term and as such the policy should be viewed as a roadmap for future activity rather than an immediate mandate for wholesale change.

3.2 A key risk to the Fund is that if the investments fail to generate the returns required to meet the Fund's future liabilities. This risk will be managed via the Asset Liability Model, which determines the appropriate risk adjusted return profile (or strategic benchmark) for the Fund.

Responsible investing issues can have a material impact on investment risk and return in the long term and therefore should be considered within the ISS.

4. Pension Committee Approval

4.1 The Committee at its 26 November 2018 meeting will be requested to approve (including publication) the Pension Fund's Responsible Investment Policy, which is attached at Appendix 1.

5. Conclusion and recommendations

5.1 The cornerstone of the Fund's policy on ethical investment – as set out in its ISS – is its interpretation of the Fund fiduciary duty and legal position regarding its duty towards ethical investment. This is an area in which further work will continue to be undertaken over the coming months.

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BACKGROUND DOCUMENTS

None