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PENSIONS SUB COMMITTEE

26 November 2018

SECOND DESPATCH

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Enquiries to : Mary Green
Tel : 0207 527 3005
Email : democracy@islington.gov.uk
23 November 2018

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ISLINGTON

Finance Department
7 Newington Barrow Way
London N7 7EP

Report of: **Corporate Director of Resources**

Meeting of:	**Date**	**Agenda item**	**Ward(s)**
Pensions Sub-Committee	26 November 2018		n/a

Delete as appropriate	Exempt	Non-exempt

SUBJECT: DECARBONISATION POLICY AND INVESTMENT STRATEGY STATEMENT(ISS) REVIEW

1. Synopsis

1.1 This report and draft policy and ISS appendices–provides information on the Fund to review and update its ISS and to enable a better understanding to its exposure to climate risk and opportunities.

1.2 It also specifically focuses on developing a policy on decarbonisation across its entire investment assets and demonstrate a consistent approach.

1.3 Mercer, our investment advisors have prepared a draft decarbonisation policy document attached as Appendix 1 for discussion and agreement.

2. Recommendations

2.1 To receive and consider the draft decarbonisation policy document presented by Mercer, our investment advisors- attached as Appendix 1

2.2 To agree the draft decarbonisation policy document and approve its integration into the draft Investment Strategy Statement attached as Appendix 2 for information

2.3 As part of next steps of implementation to agree to:

- integrate ESG issues including climate change in investment policy
- consider positive allocations to sustainable opportunities
- formulate a regular monitoring and reporting regime on progress
- extend decarbonisation beyond listed equities over the next 4 years
- continue to engage and collaborate with relevant parties including the LCIV on responsible investment.

2.4 To agree to authorise officers, with Mercer to update the ISS document-Appendix 2 with the agreed changes and publish it.

3. Background

3.1 The Committee believes that Environmental, Social and Governance ("ESG") risks should be taken into account on an ongoing basis and are an integral part of the Fund's strategy and objective of being a long-term investor.

3.2 **Action to date**
Members agreed at November 2016 pension sub- committee meeting that the carbon footprint level of equities in the In-House UK Passive Fund be reduced with immediate effect, with 50% of assets allocated to Legal and General Investment Management's MSCI World Low Carbon Target Index Fund and the remaining 50% of assets managed in house to track the FTSE UK Low Carbon Optimised index and that officers investigate how a low carbon approach could be realised for the rest of the Fund, which does not comprise equities.

3.3 Officers implemented the low carbon indices for passive global and UK by May 2017, covering 25% of the whole fund. The existing active global equities managed by Newton and Allianz on the LCIV platform had a low carbon footprint and did not require amendments

3.4 Mercer has completed analysis to identify ways in which the Fund can reduce ESG risk and has conducted a review of ESG ratings for the Fund's underlying investment managers. Mercer's ESG ratings provide an assessment of the integration of ESG issues into the investment process and provides an overall rating – ESG 1 is the highest possible rating and ESG 4 is the lowest possible rating. As such, Mercer has provided the ESG ratings the Fund's 9 strategies across equities, fixed income, DGFs, property and private equity.

3.5 Members now want to extend decarbonisation across its entire investment assets and it is important that they define their beliefs and investment policy, take account of sustainable opportunities, and agree a monitoring regime and progress measurement.

3.6 Some of the issue that needs to be considered on implementing their policy include:

- Fiduciary duty to members of the scheme
- Defining carbon exposure and measuring a company's carbon reserve
- Investment risks of companies with high fossil fuel exposure
- The missed opportunities of total divestment during transitions of companies
- Collaboration and engagement with policy makers, industry initiatives and the LCIV

3.7 Members are asked to consider and agree the decarbonisation policy attached as Apendix1 and authorise officers and Mercer to integrate the agreed policy into the draft ISS document – Appendix 2 and publish it.

4. Implications

4.1 **Financial implications**

4.1.1 The cost of providing independent investment advice and transition cost is part of fund management and administration fees charged to the pension fund.

4.2 **Legal Implications**
The LGPS (Management and Investment of Funds) Regulation 2016, Regulation7 (1) requires an administering authority to formulate an investment strategy which must be in accordance with the guidance issued by the Secretary of State. The ISS must include:

The authority's policy on how social environmental or corporate governance considerations are taken into account in the selection, non- selection, retention and realisation of investments

The Sub-Committee holds a key fiduciary responsibility to manage the Fund's investments in the best interests of the beneficiary members and the council taxpayers, where the primary focus must be on generating an optimum risk adjusted return. It is vital that any investment decisions or strategies developed, such as a carbon strategy, must not negatively influence this primary responsibility.

The precise choice of investments can be influenced by ethical and environmental, social and governance (ESG) considerations, so long as that does not risk material financial detriment to the fund. Whilst deliberating on such issues, Queen's Counsel (Nigel Giffin) advice, commissioned by the LGPS Scheme Advisory Board and published in 2014, states that the administering authority may not prefer its own specific interests to those of other scheme employers, and should not seek to impose its particular views where those views would not be widely shared by scheme employers and members (nor may other scheme employers impose their views upon the administering authority).

4.3 **Environmental Implications**

None applicable to this report. Environmental implications will be included in each report to the Pensions Sub-Committee as necessary.

4.4 **Resident Impact Assessment**

None applicable to this report. The council must, in the exercise of its functions, have due regard to the need to eliminate discrimination, harassment and victimisation, and to advance equality of opportunity, and foster good relations, between those who share a relevant protected characteristic and those who do not share it (section 149 Equality Act 2010). The council has a duty to have due regard to the need to remove or minimise disadvantages, take steps to meet needs, in particular steps to take account of disabled persons' disabilities, and encourage people to participate in public life. The council must have due regard to the need to tackle prejudice and promote understanding.

5. Conclusion and reasons for recommendations

5.1 Members are asked to consider and agree the decarbonisation policy prepared by Mercer and agree to authorise officers to integrate the policy into our current ISS and publish the updated version.

Background papers:
None

Final report clearance:

Signed by:

Corporate Director of Resources Date

Report Author: Joana Marfoh
Tel: (020) 7527 2382
Email: Joana.marfoh@islington.gov.uk

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LONDON BOROUGH OF ISLINGTON PENSION FUND

DEVELOPING A DECARBONISATION STRATEGY FOR THE FUND - DRAFT

INTRODUCTION

In 2017, the London Borough of Islington Pension Fund (the "Fund") started the decarbonisation of its asset portfolio as part of its Environmental, Social and Governance ("ESG") integration activities. Specifically, the Fund transitioned its passive equity assets to lower carbon alternatives such that the passive UK and global equity portfolios now track the FTSE All Share Low Carbon Optimised index and the MSCI World Low Carbon Target index respectively.

Following discussion at the September 2018 Pensions Sub-Committee (the "Committee") meeting, it was agreed that in addition to the way in which the Fund already incorporates responsible investment considerations throughout its investment strategy, it wants to give specific focus to decarbonisation across all its investment assets, to demonstrate a consistent approach, and develop a policy to reflect this. In a press release "Islington Council's Pension Fund is coming out of carbon" dated Wednesday 12 September the Fund made a public commitment to:

"… remain in the vanguard of the worldwide decarbonisation movement. By continuing to reduce its investment in fossil fuels and its overall carbon intensity, the Fund will contribute to global efforts to keep the earth's temperature from rising by more than 2°C."

In light of this, we would propose that the Committee adopts the below objective (which is consistent with the current regulatory position laid out in the Department for Communities and Local Government guidance (July 2017)).

Objective: To develop and progressively implement a decarbonisation strategy that takes account of the risks and opportunities arising from climate change across all asset classes.

Definition of decarbonisation: A reduction or removal of exposure to carbon dioxide from fossil fuel energy sources and other greenhouse gases within the Fund's investment portfolio. This may mean reduction of carbon intensity (for example, as measured by the emissions per unit of sales or per unit of electricity generated) and/or reduction or removal of potential future emissions (for example, reducing exposure to proven and probable fossil fuel reserves). Decarbonisation also captures opportunities presented by the transition to a low carbon economy that enable the reduction or removal of carbon, either directly or indirectly.

As previously discussed with the Committee in 2016, decarbonisation can be achieved by a number of different approaches including “ESG integration” and “sustainability-themed investments”. We would recommend that the Fund achieves decarbonisation via both of these approaches.

- **ESG Integration** focuses on identifying, mitigating or avoiding financially material risks arising from ESG issues (including climate change) at the portfolio level, by capturing these issues within existing investment frameworks and all investment decision making processes (e.g. the idea generation and portfolio construction process for an individual strategy).[1] This can include the use of low carbon indices.
- **Sustainability-themed investments** focus on identifying growth opportunities in sectors and markets that are addressing global sustainable development challenges either via thematic investments (e.g. renewable energy, resource efficiency, clean water, health, education etc.) or via sustainability-themed core investments such as sustainable equity or fixed income funds.

This document that is for consideration by the Committee at the November 2018 meeting, presents the Fund with Mercer’s recommendation for policies that should be considered to be adopted (if not already in place) by the Committee and integrated within the Fund’s Investment Strategy Statement (“ISS”) to achieve the proposed decarbonisation objective. The ISS as “a living document” is a natural place to express a Fund-wide ESG and decarbonisation framework and to consider how these issues impact the Fund’s wider strategy and we believe this will be more effective than having a stand-alone policy. Updating the ISS is a crucial first step in achieving the decarbonisation of assets beyond listed equity. The proposed updated ISS is appended to this document.

[1] This idea can be illustrated with the following examples: A portfolio manager (PM) is evaluating two similar stocks, one with poor corporate governance and another with good / better governance, but comparable in all other ways. The PM may pick the stock with better governance as, all else equal, it represents a higher quality long-term investment. Alternatively, a PM may buy the stock with worse governance if they believe (a) they can influence the company to improve its governance processes and practices and (b) that these improvements will be recognised by the market. Both approaches fall within ‘ESG integration’.

MERCER'S RECOMMENDED POLICIES

Mercer's recommended policies ensure that the Fund's high level of historic commitment to responsible investment continue, which includes the management and monitoring of ESG risk as well as engagement, are outlined below**.** For completeness we have included an exhaustive list but note that in practice some of these are already adopted by the Committee (these have been highlighted). The Committee has a fiduciary duty in respect of ESG issues - including climate change.

Recommended policies:

- The Committee will set specific targets for decarbonisation and sustainability-themed investments.

- The Committee will annually review these targets.

  The Fund seeks to achieve the following targets by 2022:

  1) Reducing future emissions by focussing on absolute potential emissions (tons of CO2e), a reserves based measure that focusses on emissions that could be generated if the proven and probable fossil fuel reserves owned by the companies in the portfolio were burned, in the public equity allocation by XX per cent compared to the exposure June 2016 , the date of the Fund's latest carbon footprinting exercise.

  2) Reducing "exposure to carbon intensive companies" as measured by Weighted Average Carbon Intensity [2], an indicator of current climate-related risks facilitating comparison across asset classes and across industry sectors,in the public equity allocation by 40% percent compared to the exposure June 2016, the date of the Fund's latest carbon footprinting exercise.

  3) Will invest 15% per cent of the Fund in sustainability-themed investment - for example in climate change mitigation, low carbon technology, social housing, sustainable infrastructure, energy efficiency and other opportunities.

- The Committee is committed to extend decarbonisation of the Fund beyond listed equity within a set time period (we have used 2020 in the ISS) and develop a mechanism to measure progress.

- The Committee will consider financially material ESG factors on an on-going basis as this is an integral to the Fund's approach to investment as a long-term investor. *This has already been adopted and is incorporated within the ISS.*

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[2] Weighted Average Carbon Intensity (tons CO2e / $M sales). Calculated based on Scope 1 and 2 emissions. Does not relate to the Fund's ownership share and hence serves as an indicator of potential climate-related risks. Importantly facilitates comparison with non-equity assets. FSB Taskforce for Climate-related Disclosures (TCFD) recommended metric for asset owners indicating portfolios exposure to carbon-intensive companies.

- The Committee will ensure that the Fund's investment managers incorporate ESG risk considerations. *This has already been adopted and is incorporated within the ISS.*

- The Fund's investment managers should comply with UK Stewardship code. *This has already been adopted and is incorporated within the ISS.*

- The Committee will monitor manager ESG ratings (as provided by their Investment Consultant) at each Pensions Sub-Committee meeting. *This has already been adopted and is incorporated within the ISS.*

- The Committee will monitor ESG risks including managing climate change / carbon risks within its portfolio (for example bi-annual analysis of the Fund's carbon footprint and periodic climate change scenario analysis to support TCFD reporting (see the next below).

- The Committee will adopt the Task Force on Climate-related Financial Disclosures ("TCFD") guidance in reporting (where appropriate).

- The Committee believes that stewardship is important for the sustainability of investments in the long-run. *This has already been adopted and is incorporated within the ISS.*

- The Fund will engage and collaborate with relevant parties such as policymakers or industry initiatives on ESG matters such as the London CIV, likeminded Funds, the Local Authority Pension Fund Forum ("LAPFF"), the Institutional Investors Group on Climate Change (IIGCC). *This has already been adopted and is incorporated within the ISS.*

Important Notices

This does not constitute an offer or a solicitation of an offer to buy or sell securities, commodities and/or any other financial instruments or products or constitute a solicitation on behalf of any of the investment managers, their affiliates, products or strategies that Mercer may evaluate or recommend.

For the most recent approved ratings of an investment strategy, and a fuller explanation of their meanings, contact your Mercer representative.

For Mercer's conflict of interest disclosures, contact your Mercer representative or see www.mercer.com/conflictsofinterest.

Mercer's universes are intended to provide collective samples of strategies that best allow for robust peer group comparisons over a chosen timeframe. Mercer does not assert that the peer groups are wholly representative of and applicable to all strategies available to investors.

This does not contain regulated investment advice in respect of actions you should take. No investment decision should be made based on this information without obtaining prior specific, professional advice relating to your own circumstances.

Mercer
Tomi Nummela

November 2018

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INVESTMENT STRATEGY STATEMENT

LONDON BOROUGH OF ISLINGTON PENSION FUND – ~~MARCH 2017~~DRAFT NOVEMBER 2018

1. Introduction

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 require administering authorities to formulate and to publish a statement of its investment strategy, in accordance with guidance issued from time to time by the Secretary of State.

This investment strategy statement (ISS) has been designed to be a living document and is an important governance tool for the Fund. This document sets out the investment strategy of the Fund, provides transparency in relation to how the Fund investments are managed, acts as a risk register, and has been designed to be informative but reader focused. This document replaces the Fund's Statement of Investment Principles.

This statement will be reviewed by the Pensions Sub-Committee ('the Committee') at least triennially or more frequently should any significant change occur.

Myners Principles

Although not specifically referenced in the Regulations, the ~~Pensions Sub-~~Committee feels that assessment of compliance with the Myners Principles is a valuable governance tool. A copy of the Fund's Myners Compliance Statement can be found in the Annual Report and Accounts and is attached as Appendix A

2. Investment Beliefs and Objectives

The Committee has adopted policies with the primary objective being to pay members benefits as they fall due and the secondary objective to achieve maximum growth of pension fund investments to reduce the burden of employer contributions. The target for real investment returns above CPI is set out in the Fund's Funding Strategy Statement.

The Fund has the following investment beliefs which help to inform the investment strategy derived from the decision making process.

- Funding, investment strategy and contribution rates are linked
- The strategic asset allocation is the key factor in determining the risk and return profile of the Fund's investments
- Investing over the long term provides opportunities to improve returns.

- Diversification across asset classes can help to mitigate against adverse market conditions and assist the Fund to produce a smoother return profile due to returns coming from a range of different sources.
- Managing risk is a multi-dimensional and complex task.
- Risk mitigation will be prioritised according to size of potential impact and risks will only be taken where they are expected to be rewarded.
- "Environmental, Social and Governance ~~are important factors for~~(ESG) issues can have a material impact on long-term risk and return outcomes and considering these issues is consistent with the ~~sustainability~~fiduciary duty of the Committee. In particular, the Fund recognises that climate change poses a systemic risk with potential long-term investment ~~returns over the long term. Value for money from investments is important, not just absolute costs.~~ risks and opportunities".
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2. Investment strategy and the process for ensuring suitability of investments.

As noted above, the Fund's objective is to pay benefits as they fall due and this requires the build-up of sufficient reserves in advance. The Fund is currently assessed to have a deficit in terms of the reserves needed and so the asset strategy is focused on achieving returns in excess of CPI inflation, without taking undue risk. ~~Having a thorough understanding of the risks facing the Fund is crucial and these are covered later in this statement.~~

The asset strategy, along with an overview of the role each asset plays in achieving the Fund's objectives is set out in the table below:

Asset class	Allocation %	Allowable ranges %	Role (s) within the strategy
Equity (developed, emerging and frontier markets)	46.0	+/-6.0	-Long term growth in excess of inflation expected
Private Equity	4.0	+/-2.0	-Additional returns in excess of public equity
Diversified Growth Funds	10.0		-Diversification (expected to outperform when the broader market falls)~~.~~ -Some inflation protection~~;~~ -Source of income
Property	~~15.0~~20.0	+/-2.0	-Diversification~~.~~ -Generates investment income~~;~~ -Returns expected to be inflation-sensitive -Exposure to Illiquidity premium

Corporate Bonds	~~10.0~~5.0	+/-2.5	-~~Diversified source of return from a range of sources.~~Access to credit risk premium. ~~Not specifically income generating-~~
Diversifying 'real' assets e.g. Infrastructure Social Housing	15.0		-Diversification~~.~~ -Generates investment income~~;~~ -Returns expected to be inflation-sensitive -Exposure to Illiquidity premium

The ~~Pensions Sub-~~Committee is responsible for the Fund's asset allocation which is determined via a triennial strategy review as part of the valuation process, but is kept under constant review; noting that strategic changes are an evolutionary process.

The triennial review looks at both qualitative and quantitative analysis, covering:

- The required level of return that will mean the Fund can meet its future benefit obligations as they fall due
- The level of risk that the Fund can tolerate in absolute terms, and in relation to its funding level and deficit
- An analysis of the order of magnitude of the various risks facing the is established in order that a priority order for mitigation can be determined
- The desire for diversification across asset class, region, sector, and type of security.

3. Risk measurement and management

The Committee assesses risks both qualitatively and quantitatively, with the starting point being the triennial strategy review. Risks are considered, understood and then prioritised accordingly – the Committee evaluates the Fund's risk attribution analysis as part of the investment strategy review following the actuarial valuation.

~~[Risk Attribution Analysis (to be added in following strategy review) to show size / impact of main investment risks]~~

~~[Impact of falls in equity markets, rises in inflation, falls in interest rates and investment manager underperformance on the funding level (to be added in following strategy review).]~~

A Investment Risks

Equities – The largest risk that the Fund is running is in relation to its equity holdings. Should equity market conditions deteriorate significantly this will have a negative impact on the funding level. The Fund holds equities in order to provide the necessary returns to ensure that the Fund remains affordable. The Committee believes that the extra returns that are expected to be generated by equities compensates the level of risk equities bring to the Fund, but does believe in diversification, and looks to mitigate equity risk by investing significantly in other diversifying assets. The Committee will also consider the use of equity options where appropriate.

Inflation –The Fund's liabilities are impacted by inflation both explicitly and implicitly and the required return on assets is expressed in terms of inflation plus a premium. The Fund will seek to invest in a range of assets that provide returns in excess of inflation and in some cases provide an inflation-linked income, subject to a tolerable level of volatility.

Diversifying assets – The Fund has a significant amount of assets allocated to a range of non-equity, diversifying assets, with allocations to property, bonds, diversified growth and a plan to build allocations to real assets such as infrastructure and social housing. The risks that these investments bring at an individual level are not insignificant but the Committee believes that over the long term these assets will provide returns that compensate for the risks being run. Additionally the level of diversification the assets provide helps to reduce the Fund's reliance on returns from equities. Illiquid assets such as property are also a valuable source of income.

Active Manager Risk – Investment Managers are appointed to manage the Fund's investments on its behalf, a number of which are active managers. Active manager risk is small relative to other risks; the Fund still addresses this risk. Extensive due diligence is undertaken before managers are selected, with a number of different managers employed to prevent manager concentration risk The investment managers are also monitored regularly by the Committee and by the Fund's Advisors.

The Fund's portfolio is well diversified across asset classes, geography and asset managers. As different asset classes have varying correlations with other asset classes, the Fund by investing in a range of different investments can reduce the overall level of risk run to a degree.

B Demographic Risks

The Fund is subject to a range of demographic risks, but with particular reference to investment strategy, the Committee is aware of the potential for the Fund to mature over time as the pensioner liability increases. A mature pension fund is likely to take less investment risk over time and this is considered at each strategy review. The more mature a pension fund, the more likely it is that disinvestments would need to be made to pay benefits. The Fund is not in that situation at present as income from contributions and investments are greater than benefit payments. However, this situation is monitored regularly and formally as part of the actuarial valuation and strategy review.

C Cashflow Management Risks

The Fund is cash flow positive. However, this position will be reviewed regularly and is a factor that is incorporated into the Fund's investment strategy reviews with the long-term aim that a portfolio of income generating assets is built up over time.

D Governance Risks

The Committee believes that there is a benefit to the Fund to be gained from good governance in the form of either or both of an increased return and/or decreased risk. Poor governance can lead to opportunities and risks to be missed, and have a detrimental effect on the funding level and deficit.

Details of the Fund's governance structure can be found in the Governance Compliance Statement in the Annual Report found via https://www.islington.gov.uk/about-the-council/apply-for-a-job/council-pension-scheme useful documents. The ~~Pensions Sub-~~Committee members receive training on a regular basis as a group and attend individual training courses and seminars. Each member must attend the 3 Day Trustee Training organised by the Local Government Association.

E ESG Risks

The Committee believes that ESG (including climate change) risks should be taken into account on an ongoing basis. ESG considerations are an integral part of the Fund's strategy and objective of being a long term investor. The Committee expects its investment managers to include information on how carbon risk is being managed within their respective portfolios as part of regular reporting for the Fund.

The Fund encourages its underlying investment managers to comply with the UK Stewardship Code and will monitor progress, as well as monitor the ESG ratings of its Fund managers by way of an annual report from its Investment Consultant on the ESG credentials of its investment managers.

The Fund has committed to reduce climate change risk by decarbonising the Fund's portfolio. The Committee expects to continuously review further opportunities, across all asset classes, to reduce the Fund's reliance on carbon sensitive assets by considering the potential financial impacts of both the transition to a low-carbon economy and the physical impacts of different climate outcomes.

The Fund will monitor ESG (including climate change) risks annually and set targets to mitigate these risks. Monitoring will include bi-annual analysis of the carbon footprint of the Fund's portfolio, as well as conducting a periodic scenario analysis based on multiple climate change scenarios ranging from 2ºC to 4ºC.

The Committee accepts that engagement is key in relation to strong corporate governance, which in turn will ~~enhance returns. Details of the Fund's policies can be found later in this statement~~reduce ESG risks.

~~The Fund has made a commitment to reduce its exposure to carbon intensive companies and assets. After careful consideration, the Committee decided to change both the UK equity index benchmark for the Fund's internally managed passive equities and the global equity index benchmark for externally-managed passive assets, to low carbon variants of the standard index. As a result of these changes, the Fund will have a very much lower carbon footprint than a 'normal' equity portfolio, and therefore a low carbon footprint at the Total Fund level. The Pensions Sub-Committee expects to continue to review further opportunities, particularly in other asset classes, to reduce the Fund's carbon footprint further.~~

4. Approach to asset pooling

The Fund has formally joined the London Collective Investment Vehicle (CIV) as part of the Government's pooling agenda. The London CIV has been operational for some time and ~~is in the process of~~ has opened~~ing~~ a range of sub-funds covering liquid asset classes~~, with~~ and is in the process of opening less liquid asset classes ~~to follow~~.

The Fund has already transitioned liquid assets into the London CIV with a value of £92m and will look to transition further liquid assets as and when there are suitable investment strategies available on the platform that meet the needs of the Fund in advance of April 2018.

The Fund holds £90m of its assets in life funds and intends to retain these outside of the London CIV in accordance with government guidance on the retention of life funds outside pools for the time being. The Fund agrees for the London CIV to monitor the passive funds as part of the broader pool.

A proportion ~~(currently 20%)~~ of the Fund is held in illiquid assets and these may remain outside of the London CIV pool where there is a strong business case. The cost of exiting these strategies early would have a negative financial impact on the Fund. These will be held as legacy assets until such time as they mature and proceeds re-invest through the pool assuming it has appropriate strategies available or until the Fund changes asset allocation and makes a decision not to reinvest.

The Fund will actively engage and seeks to work collaboratively with likeminded Funds, London CIV on climate change and ESG topics, including the provision of fund alternatives that will help

London CIV members to decarbonise, reduce ESG risks and invest in sustainably themed opportunities in their investment portfolios.

5. Social, environmental and corporate governance policy and policy of the exercise of rights (including voting rights) attaching to investments

The Committee has a fiduciary duty to invest Fund assets in members' best interests and so must ensure that assets are invested in an appropriate manner; as a result all material ESG considerations, including climate change, must be taken in light of expected risk and return implications.

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The Fund seeks to fully incorporate ESG (including climate change) risks and opportunities into its investment strategy and investment implementation, with a view to further a reduce or remove exposures to carbon dioxide from fossil fuel energy sources and other greenhouse gases and reduce ESG risks of the portfolio in line with stated objectives. In particular the Fund will seek to allocate investment to sustainability-themed investments, as well as uphold high standards of ESG incorporation the Fund.

With regard to ~~socially~~ responsible investment the Committee is mindful of the following legal principles, which are based on recent decisions in the courts and which apply to all pension schemes:

a. Administering authorities are free to adopt a policy of ~~socially~~ responsible investment, provided that they treat the financial interests of all classes of scheme members as paramount and their investment policies are consistent with the standards of care and prudence required by law.

b. Administering authorities are free to avoid certain kinds of investment, which they consider scheme members would regard as objectionable as long as they make equally financial advantageous and prudent investments elsewhere. They may also make "ethical" investments provided these are otherwise justifiable on investment grounds.

c. Administering authorities are not entitled to subordinate the interests of members to ethical or social concerns. The financial performance of the Fund consistent with proper diversification and prudence is paramount.

~~The London Borough of Islington Pension Fund wishes to promote a policy of dialogue on socially responsible investment issues, through the Fund Managers, with company management.~~

~~In the first instance, the Committee would like environmental issues, human rights, employment standards and modern day slavery to be raised with company management. Environmental issues could include issues such as reducing carbon emissions, conserving energy, promoting alternative energy sources, recycling, avoiding pollution and using environmentally friendly and sustainable resources.~~

~~Human rights could involve child labour issues in foreign subsidiaries of UK companies or operations in countries with oppressive regimes. Employment standards could relate to equal opportunities, health and safety, trade union recognition and employee participation.~~

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~~The Fund invests via pooled funds and is therefore prepared to subscribe to the policies of the individual fund managers. When monitoring investment managers, the Pensions Sub- Committee considers whether managers' actions and engagement activities have been appropriate and in keeping with London Borough of Islington Pension Fund policy.~~

It is proposed to monitor action by fund managers on a quarterly basis and further develop this policy on an annual basis on the basis of experience.

The Fund has joined the Local Authority Pension Fund Forum ("LAPFF") to promote best practice on corporate governance and SRI issues amongst the companies in which it invests, through cooperative action with other local authority funds. The Forum exists to promote the investment interests of local authority pension funds and to maximise their influence as shareholders in promoting corporate social responsibility and high standards of corporate governance amongst companies in which they invest.

With more than half of all local authority funds as members, the Forum can negotiate with companies with a single authoritative voice, impossible for smaller funds acting alone. The Forum is developing policy and carrying out research and engagement with companies on many issues, including environmental issues such as the climate change impact of the transport sector, and the impact of oil extraction from tar sands. Other initiatives include engagement with fund managers to try to improve transparency of proxy voting policies by the managers, and on corporate governance issues.

The ~~Pension Sub-~~Committee is a member of the Institutional Investors Group on Climate Change (IIGCC). The IIGCC seeks to promote better understanding of the implications of climate change amongst its members and other institutional investors. It also aims to promote a lower carbon economy by encouraging the companies and markets in which IIGCC members invest to address their approach to climate change issues.

~~There are no proposals to invest any part of the Fund exclusively in Socially Responsible Investments at the current time. Nor is it proposed that positive or negative screening should be adopted by the Fund on socially responsible issues.~~

As noted earlier, the Fund has made a commitment to reduce its exposure to carbon intensive companies and assets.

The Fund seeks to achieve the following targets by 2022:

1) Reducing future emissions by focussing on absolute potential emissions (tons of CO2e), a reserves based measure that focusses on emissions that could be generated if the proven and probable fossil fuel reserves owned by the companies in the portfolio were burned, in the public equity allocation by XX per cent compared to the exposure at June 2016, the date of the Fund's latest carbon footprinting exercise.

2) Reducing "exposure to carbon intensive companies" as measured by Weighted Average Carbon Intensity [1], an indicator of current climate-related risks facilitating comparison across asset classes and across industry sectors in the public equity allocation by 40% percent compared to the exposure at June 2016, the date of the Fund's latest carbon footprinting exercise.

3) Will invest 15% per cent of the Fund in sustainability-themed investment - for example in climate change mitigation, low carbon technology, social housing, sustainable infrastructure, energy efficiency and other opportunities.

In order to monitor and guide decarbonisation and allocation to sustainability, the Fund will adopt TCFD supplemental guidance for asset owners where applicable.

The Fund will review targets annually ~~to size them appropriately~~. The Fund will form a view on decarbonisation of all assets classes beyond public equities by 2020 and will develop mechanisms to evaluate the progress..

6. Policy of the exercise of rights (including voting rights) attaching to investments and stewardship

Voting:

The ~~Pensions Sub-~~Committee takes its responsibilities as a company shareholder seriously and exercises its votes at company AGMs/EGMs wherever practically possible. The ~~Sub-~~Committee uses the Corporate Governance Service provided by Pension Investments Research Consultants (PIRC), and casts votes at all UK, European and North American company AGMs in line with PIRC recommendations unless the Council decides otherwise.

[1] Weighted Average Carbon Intensity (tons CO2e / $M sales). Calculated based on Scope 1 and 2 emissions. Does not relate to the Fund's ownership share and hence serves as an indicator of potential climate-related risks. Importantly facilitates comparison with non-equity assets. FSB Taskforce for Climate-related Disclosures (TCFD) recommended metric for asset owners indicating portfolios exposure to carbon-intensive companies.

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The Fund's investments through the London CIV are covered by the voting policy of the CIV which has been agreed by the Pensions Sectoral Joint Committee. Voting is delegated to the external managers and monitored on a quarterly basis. The CIV will arrange for managers to vote in accordance with voting alerts issued by the LAPFF~~Local Authority Pension Fund Forum~~ as far as practically possible to do so and will hold managers to account where they have not voted in accordance with the LAPFF directions.

In addition, voting records are published in the year end annual reports and quarterly reports of voting actions are posted on the Fund's website https://www.islington.gov.uk/about-the-council/apply-for-a-job/council-pension-scheme useful documents. The Fund has not issued a separate Statement of Compliance with the Stewardship Code, but fully endorses the principles embedded in the 7 Principles of the Stewardship Code Or
The Committee will provide an annual report on how the Fund satisfies its UK Stewardship Code obligations requirements.

- Stewardship
-

The London Borough of Islington Pension Fund wishes to promote a policy of dialogue on responsible investment issues, through the Fund Managers, with company management. In the first instance, the Committee would like environmental issues, human rights, employment standards and modern day slavery to be raised with company management. Environmental issues could include issues such as reducing carbon emissions, conserving energy, promoting alternative energy sources, recycling, avoiding pollution and using environmentally friendly and sustainable resources. Human rights could involve child labour issues in foreign subsidiaries of UK companies or operations in countries with oppressive regimes. Employment standards could relate to equal opportunities, health and safety, trade union recognition and employee participation.

The Fund invests via pooled funds and is therefore prepared to subscribe to the policies of the individual fund managers. When monitoring investment managers, the Pensions Sub- Committee considers whether managers' actions and engagement activities have been appropriate and in keeping with London Borough of Islington Pension Fund policy.

Advice Taken

In creating this statement, the ~~Pensions Sub-~~Committee has taken advice from its Investment Consultant and independent Investment Advisor. Also, in relation to each of the constituent parts, such as the asset allocation and risk mitigation, the Fund has taken advice from its Investment Consultant, Mercer, and the Scheme Actuary, also Mercer. In providing investment advice, Mercer is regulated by the Financial Conduct Authority.

Field Code Changed

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APPENDIX A

Myners Investment Principles - Compliance Statement

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In accordance with regulation 9A(3A) of the LGPS (Management and Investment of Funds) Regulations 1998, as amended the Council is required to state the extent to which the administering authority comply with the ten principles of investment practice set out in the document published in April 2002 by CIPFA, the Chartered Institute of Public Finance and Accountancy, and called "CIPFA Pensions Panel Principles for Investment Decision Making in the Local Government Pension Scheme in the United Kingdom (Guidance note issue No. 5)"; and give the reasons for not complying where they do not do so. This CIPFA publication is based on ten principles proposed by the Myners review of Institutional Investment in the United Kingdom, and adopted by the Government as a model for best practice in 2001.

The Myners Principles were reviewed by the NAPF during 2008 and a revised set of six principles were issued in October 2008. CIPFA expect to issue a new publication based on the revised six principles in the near future.

Principle 1 - Effective decision-making

- Trustees should ensure that decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to take them effectively and monitor their implementation.
- Trustees should have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.

Comment

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The Fund is generally compliant with the requirements of this Principle. The Pensions Sub-Committee requires new members serving on the Sub-Committee to source appropriate training within six months of joining the Sub-Committee. The three-day course run by the Local Government Pensions Committee of the Local Government Association is recognised as particularly relevant training for new Members, but other routes and courses, and requisite experience are also recognised as appropriate. Where several new Members are appointed together, tailor-made training will be considered.

Principle 2 - Clear Objectives

- Trustees should set out an overall investment objective(s) for the Fund that takes account of the scheme's liabilities, the strength of the sponsor covenant and the attitude to risk of both the trustees and the sponsor, and clearly communicate these to advisers and investment managers.

Comment

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The Council seeks to undertake regular reviews of investment strategy, most recently in 2014, which took into account the scheme's liabilities, the strength of the employer covenant and the attitude to risk of both the trustees and the sponsor.

Principle 3 - Risk and Liabilities

- In setting and reviewing their investment strategy, trustees should take account of the form and structure of liabilities.
- These include the strength of the sponsor covenant, the risk of sponsor default and longevity risk.

Comment

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In setting the investment strategy, the Trustees have considered the form and structure of liabilities, along with the strength of the sponsor covenant, risk of sponsor default and longevity risk, taking advice from independent professional advisors where appropriate.

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Principle 4 - Performance Assessment

- Trustees should arrange for the formal measurement of the performance of the investments, investment managers and advisers.
- Trustees should also periodically make a formal policy assessment of their own effectiveness as a decision-making body and report on this to scheme members.

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Overall Fund performance and detailed portfolio performance is measured quarterly, annually and over longer periods by external independent measurement specialists BNY Mellon. Performance is also monitored against the local authority peer group of pension funds, also based on old State Street Company data but from 1April 2016 run by PIRC (for the local authority universe), although in line with the Myners Principles the peer group is no longer considered the benchmark for overall fund performance. The overall benchmark is specific and customised to the Fund's objectives based on the outcome of the successive asset/liability studies.

Performance of the Fund is also subject to annual review by external auditors and by internal audit through regular audits programmed into the Audit Plan.

Pension benefits administration performance is reported regularly to Pensions Board

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Principle 5 - Responsible Ownership

- Trustees should adopt, or ensure their investment managers adopt, the Institutional Shareholders' Committee Statement of Principles on the responsibilities of shareholders and agents.
- A statement of the scheme's policy on responsible ownership should be included in the Investment Strategy Statement Trustees should report periodically to members on the discharge of such responsibilities.

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The Sub-Committee uses the Corporate Governance Service provided by Pension Investments Research Consultants (PIRC), and casts votes at all UK, European and North American company AGMs in line with PIRC recommendations unless the Council decides otherwise.

The Fund encourages each active investment manager to take account of social, environmental and ethical considerations insofar as the manager believes such considerations will benefit performance and/or reduce risk.

For those assets of the Scheme managed in pooled funds, the Trustees accept that the assets are subject to the investment manager's own policy on socially responsible investment. The Trustees are satisfied that this corresponds with its responsibilities to the beneficiaries.

The Fund's attitude to and policies regarding responsible ownership are set out within the body of the its Investment Strategy Statement.

The Trustees issue member newsletters in which this discharge of responsibilities is noted.

Mercer has adopted the Institutional Shareholders' Committee Statement of Practice relating to investment consultants.

Principle 6 - Transparency and Reporting

- Trustees should act in a transparent manner, communicating with stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives.
- Trustees should provide regular communication to members in the form they consider most appropriate.

Comment

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The Council's SIP (and its replacement the Investment Strategy Statement from 1 April 2017) is currently published and available to scheme members on the Council website. Summaries of performance and monitoring of managers are reported in the Pension Fund Annual Report and available to all pensioners and employees each year. Further performance reporting is provided to contributors and pensioners at the AGM. The full Pension Fund Report and Accounts are published as part of the Council's overall Annual Report and Accounts and available to all members of the public.

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