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	23RD March 2021		n/a

Delete as appropriate		Non-exempt

SUBJECT: DECARBONISATION POLICY –UPDATE ACTION PLAN AFTER NET ZERO CARBON TRANSITION TRAINING

1. Synopsis

1.1 This report updates the action plan to keep the Fund on course to achieve decarbonisation targets by 2022 or earlier as per agreed monitoring plan of our decarbonisation policy and update of action agreed after training session in February on the principles and considerations for pension investments to transition to Net Zero Carbon.

2. Recommendations

2.1 To agree to note the action agreed at the training session in February to receive a report in June to review the current decarbonisation policy and reset targets the Fund can achieve in the medium to long term.

2.2 To agree to receive a report on more evolved and progressive responsible indices now available in the market for options on our passive equities.

2.3 To note the draft recommendations at the training session listed in paragraph 3.3.2 and to receive a briefing on considerations for the pension investments to transition to Net Zero Carbon transition to <2^0C.

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 **Progress to date**

3.2.1 Members agreed a decarbonisation policy as part of its Investment strategy statement and sets targets to achieve further decarbonisation across its entire investment assets. The policy defines the Committee's beliefs and takes account of sustainable opportunities, and agrees a monitoring regime and progress measurement.

The agreed targets are as follows:

The Fund seeks to achieve the following targets by May 2022 through:
1) Reducing future emissions by focussing on absolute potential emissions (tons of CO_2e), 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 more than three quarters compared to the exposure at June 2016, the date of the Fund's latest carbon foot-printing exercise.

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

3) Investing at least 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.

Measures agreed to monitor and guide decarbonisation and allocation to sustainability include:
1) The Fund adopting TCFD supplemental guidance for asset owners where applicable.

2) The Fund reviewing targets annually.

3) The Fund forming a view on decarbonisation of all asset classes beyond public equities by 2022 and will develop mechanisms to evaluate the progress.

4) The Fund monitoring ESG (including climate change) risks annually and set targets to mitigate these risks. Monitoring will include 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.

ESG ratings

3.2.2 Mercer conducted a review of ESG ratings for the Fund's 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. The average rating for the whole Fund has improved from 2.3 to 2.1.

Measuring carbon footprint of equities portfolio annually

3.2.3 The Fund's latest carbon foot printing exercise on the equity holdings as at 31st March 2020 showed that since 2016 the fund has achieved in its equities:

i) 72% of its target to reduce exposure to carbon intensive companies
ii) 73% of its target to reduce absolute emissions

3.3 **Transition to net zero carbon for pension investments**

The decarbonisation policy is a living document and Members have targeted decarbonisation across all asset classes of its pension investment where the funds' risk and return objectives are optimised. Any transition should still achieve the primary objective of paying benefits to pensioners and still affordable for employers.

3.3.1 At the December meeting, Members agreed to attend a detailed training arranged with Mercer to discuss the transition principles, objectives, framework and implication. The training session on 18th February 2021, was attended by members of the Pension board and Pension sub- committee as well as the Corporate Director of Environment and Regeneration.

3.3.2 The draft recommendations at the training session were that Islington adopt

- Science based: basing Islington decision on Intergovernmental Panel on Climate Change input
- Below 2^{0}C: in alignment with the Paris Agreement
- Unambiguous: (Net) Zero Emission 2050 -(2045)
- Base year: 2016 base year for monitoring (where applicable).
- Intermediate targets : Continue monitoring towards achieving 2022 targets
- Set a target review commitment and period for post 2022. "Next target period will run 2022-2026 and targets for the period will be set by the end of 2022"
- Optional: set a 2030 target (50-60% emissions reduction with a scope 3 caveat)
- Methodology: adopt TCFD (as per the current policy) to steer Islington climate action

Continue doing what we do well –be alert to climate change as an investment topic be willing to learn about new methodologies and developments

3.3.3 Members agreed to receive a report at the next June meeting to review the current decarbonisation policy and set new short and medium term targets to transition to a net zero carbon emission<2^{0}C.

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 and contribution to achieving a net zero carbon Islington by 2030:**

Environmental implications will be included in each report to the Pensions-sub committee as necessary. The current agreed investment strategy statement for pensions outlines the policies and targets set to April 2022 to reduce the current and future carbon exposure by 50% and 75% respectively compared to when it was measured in 2016 and also invest 15% of the fund in green opportunities. The link to the full document is https://www.islington.gov.uk/~/media/sharepoint-lists/public-records/finance/financialmanagement/adviceandinformation/20192020/20190910londonboroughofislingtonpensionfundinvestmentstrategystatement.pdf

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

4.4.1 An equalities impact assessment has not been conducted because this report is seeking opinions on an existing policy document and therefore no specific equality implications arising from this report.

5. Conclusion and reasons for recommendations

5.1 Members are asked to note the draft recommendations and agree to receive a report in June to review the existing targets and set new short to medium targets to enable the transition to net zero carbon emissions.

Final report clearance:

Signed by:

Corporate Director of Resources Date 15 March 2021

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