



Report of: Corporate Director of Resources

Meeting of: Pensions Sub-Committee

Date: 3rd July 2023

Ward(s): n/a

Appendix 1 is exempt and not for publication as it contains the following category of exempt information as specified in Paragraph 3, Schedule 12A of the Local Government Act 1972, namely: Information relating to the financial or business affairs of any particular person (including the authority holding that information).

Subject: Decarbonisation Policy Monitoring- Carbon Footprint Results and Next Steps

1. Synopsis

- 1.1 This report discusses progress to date on the agreed monitoring plan on our decarbonisation policy and to note carbon footprint of our equity and credit holdings.
- 1.2 Mercer have undertaken a carbon foot printing measure of our equities and credit holdings and presented the results in a briefing as well as discussing next steps to achieving our net zero target, attached as Exempt Appendix 1

2. Recommendations

- 2.1 To note the carbon footprint of our public equities and credit
- 2.2 To note the fund's progress in reducing its exposure to carbon intensive companies since 2016 and absolute emissions as set out in Exempt Appendix 1.
- 2.3 To note that officers will continue to engage with our portfolio managers to improve ESG ratings and achieve the targets set in 2025 and long-term net zero target for the whole fund.

- 2.4 To consider next steps and training to adopt new metrics and reset medium to long term targets.

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. Members agreed a decarbonisation policy as part of its Investment Strategy Statement and set 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.
- 3.2 The Fund’s last carbon foot printing exercise on the equity and corporate credit holdings was 31st March 2022 and showed that since 2016 the fund had achieved, in its equities, a reduction of 34.6% in absolute emissions and a weighted average potential emissions of 67%.
- 3.3 Members agreed a transition of the In-House UK equity portfolio, as it was identified as one of the largest contributors to the overall carbon footprint of the Fund. Changing the index from the low carbon index to the third generation climate indices will enable achievement of our short to medium targets.
- 3.4 These indices are explicitly designed to measure initial and ongoing decarbonisation, consistent with the Intergovernmental Panel on Climate Change’s 1.5 degrees Celsius warming scenario. This is a key component to enable the Fund to achieve its net zero carbon emission target set to 2050.

Progress to date

3.4.1 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 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 affordability for employers.

Members agreed at the June 2021 meeting to adopt new decarbonisation targets for the short to medium term and a net zero carbon emission for the whole Fund by 2050.

The new targets are:

- i) Net zero emission target in 2050 including aligning with the 1.5-degree Celsius scenario
- ii) Investing at least 20% of the fund in sustainability themed investments (such as low carbon technology or green infrastructure) by the end of April 2026. *(March’23 results- 16%)*
- iii) Reduce carbon Intensity of all listed portfolios i.e., equities and credit by 49% by 2026 and 60% by 2030 against a baseline in 2016. *(March’23 results- 40%)*

3.4.2 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 2023 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 2°C to 4°C.

ESG ratings

3.4.3 Mercer conducted a review of ESG ratings for the Fund's underlying investment Managers in 2022. 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 of the Fund's 13 strategies across equities, fixed income, DGFs, property, private debt, infrastructure and private equity and this will be updated over the summer.

3.4.4 Measuring carbon footprint of equities and credit portfolio annually

The carbon footprint measure comprises of two elements; future emissions that is reserve based, and exposure to carbon intensive companies. The valuation of assets as 31st March 2023 was used for the exercise across our public equities and credit mandates.

3.4.5 Mercer have conducted the exercise to capture the equity and credit holdings of the fund and results are presented in Exempt Appendix 1. Members are asked to consider the individual portfolios and the total level of emissions and reserves for the fund and the next steps to achieve net zero carbon target for the whole fund.

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, Regulation 7(1) requires an administering authority, after taking proper advice, to formulate an investment strategy which must be in accordance with the guidance issued by the Secretary of State. The investment strategy 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 administering authority owes fiduciary duties both to the scheme employers and to the scheme members 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 opining on these issues, King'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).

The Pension Fund must take investment advice on investment decisions.

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/20192020/20190910londonboroughngtonpensionfundinvestmentstrategystatement.pdf>

4.4 **Equality 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 recommendation

5.1 Members are asked to note progress on carbon footprint results to March 2023 and continue to monitor climate risk and engage with our fund managers on governance and climate risk.

Appendix: Exempt Appendix1- Mercer presentation Carbon footprint results

Background papers:

None

Final report clearance:

Signed by:

Corporate Director of Resources

Date

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