Wiltshire Pension Fund

RESPONSIBLE INVESTMENT PLAN 2021/22

Introduction

1. Responsible investment is the strategy to incorporate ESG (environmental, social and governance) factors into investment decisions. The Fund's position regarding ESG issues is set out in the ISS (Investment Strategy Statement) as follows:

> The Committee believes that in order to carry out their fiduciary duty by acting in the interest of its members, that effective management of Environmental, Social & Corporate Governance management (ESG) issues, including climate change, which are financially material to the Fund is essential. In order to protect the Fund's investments into the future, the Fund supports a global warming scenario of 2°C or lower, and states an ambition to achieve net-zero carbon emissions across all investment portfolios by 2050.
> 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.

2. The Pension Fund's investment objectives are to achieve sufficient investment returns such that there are funds available to pay the pensions as they fall due, and to meet the liabilities over the long term whilst maintaining stable employer contribution rates.

3. Therefore, consideration of all factors (including ESG factors) which could affect the investment returns is a fundamental part of managing the investments. Responsible investment practices can both help mitigate risks and also enhance returns.

4. This Responsible Investment Plan 2021/22 sets out where the Fund is now, what has been done so far, and plans for developing the Fund's approach to responsible investment issues over the coming year.

Fiduciary Duty

5. The UNPRI (UN Principles for Responsible Investment) discusses a modern interpretation of fiduciary duty at the following link: https://www.unpri.org/fiduciary-duty/the-modern-interpretation-of-fiduciary-duty/6538.article

6. A quote from the link above states that "The integration of ESG issues into investment practice and decision making is an increasingly standard part of the regulatory and legal requirements for institutional investors, along with requirements to consider the sustainability-related preferences of their clients and beneficiaries, and to report on how these obligations have been implemented. Investors that fail to incorporate ESG issues are failing their fiduciary duties and are increasingly likely to be subject to legal challenge."

7. Wiltshire Council's in-house legal team have produced a memo which specifically addresses how climate change risk can be considered in the Fund's investment strategy, and which also tackles the broader issue of consideration of ESG factors in the investment strategy. The memo is attached in full as Appendix 2.

Wiltshire Pension Fund as an investor

8. As the Fund is open to new members, who will not be retiring for many years into the future, the Fund has a very ***long-term investment horizon***. The Fund therefore needs to consider long-term sustainability issues, and the importance of engagement with companies in which it is invested, in order to safeguard the investments into the future.

9. The Fund is a ***large, diversified investor***, with exposure to the global economy. The Fund therefore needs to invest in a way that contributes to the success of the global economy and society as a whole, as this will have a positive financial impact on the Fund's investments.

10. One of the Fund's investment beliefs, as set out in the ISS, is that "**Investing over the long term provides opportunities to improve returns**".

Business plan and risk register

11. Developing the Fund's approach to responsible investment is set out as a "High Priority" action in the Fund's Business Plan for 2020/21. This will have the expected service benefit of helping the Committee to understand and incorporate risks which could have a material financial impact on the Fund's future investment returns. This high priority action shows the strong commitment which the Committee has towards responsible investment, and the high importance of this area of work.

12. Climate change risk is included in the Pension Fund's risk register (risk PEN041) as a "High" priority risk ("Medium" residual risk after the controls in place to manage the risk are considered). Climate change is a key environmental risk which could have a material financial impact on the Fund's returns, and as such needs to be considered, managed and monitored as part of the Committee's fiduciary duty, to protect the investment returns of the Fund. Failure to embed climate change considerations in the investment strategy could cause a negative impact on investment returns over the long term.

What has been done to date

13. The Fund has historically demonstrated a strong approach to responsible investment. The following actions are a summary of recent work done by the Committee and officers, and build on the strong foundations laid over past years.

Investments and strategy

i. **Passive Low Carbon Equities** – in December 2019, the Fund transitioned all of its passive equity exposure to a low carbon passive equities portfolio managed by Brunel. This was done following research to ensure that the risk and return profile of the portfolio would remain the same as the previous portfolios, but also delivered the benefit of reducing the Fund's exposure to carbon-intensive companies, therefore reducing the risk of exposure to stranded assets and reducing transition risk.

ii. **Climate change scenario modelling** – in the summer of 2020, the Committee commissioned Mercer (as the Fund's investment consultants) to carry out climate change scenario modelling, on both the existing strategic asset allocation, and one with a more sustainable tilt. In addition, Hymans (as the Fund's actuary) carried out modelling looking at different levels of policy response to climate risk. The results of these pieces of modelling work have been used to help the Committee understand the financial implication of climate change risk, and this has helped to develop the investment strategy, when considered in the round with other information including training and other professional advice from the Fund's independent adviser and investment managers. A summary of the modelling findings is in Appendix 1.

iii. **Including a new investment belief in the Investment Strategy Statement** – following on from the modelling work, the Committee debated and agreed a new investment belief: "**In order to protect the Fund's investments into the future, the Fund supports a global warming scenario of 2°C or lower, and states an ambition to achieve net zero carbon emissions across all investment portfolios by 2050**."

iv. **Setting a net zero by 2050 target** – the Committee approved a target of net zero by 2050 for the Fund's investment portfolios, based on the outcomes from the modelling work done, which showed that this was in the Fund's best financial interests.

v. **Publicly declaring the net zero target** – the Fund has signed a net zero by 2050 commitment through the IIGCC (Institutional Investors Group on Climate Change), and hopes to be involved in a round of publicity regarding the commitment in June 2021. The news has also been shared with the scheme membership via a newsletter.

vi. **Approving a budget to work with consultants to develop an action plan to deliver the net zero target** – the Committee has approved a budget for Mercer to help develop a plan to achieve the net zero target, showing a strong commitment to making good on the promises made.

vii. **Research into investing in sustainable equities** – the modelling work done by Mercer showed that the Fund may be able to realise a material financial benefit by taking advantage of the opportunity to invest in sustainable equities. This will also have the additional benefit of diversifying the Fund's investment strategy via exposure to different investment styles and sizes/types of company. The Committee has looked into initial information on Brunel's sustainable equities portfolio, and will make a formal decision in due course.

Reporting and disclosure

viii. **Enhanced voluntary disclosures in the Annual Report** – in the 2019/20 Annual Report, the Fund voluntarily included a section on climate risk and metrics, in order to communicate with stakeholders about the work which has been done, and to demonstrate transparency about the Fund's holdings and actions.

ix. **Carbon footprinting** – the Fund first commissioned carbon footprinting of its equity portfolios as at 31 March 2019, to develop an awareness of the starting point for ongoing monitoring.

x. **Commitment to delivering TCFD (Task Force on Climate Related Financial Disclosures) reporting in 2021** – the Committee is keen to demonstrate best practice, so the Fund will be reporting in line with TCFD in or alongside the 2020/21 Annual Report, in advance of any requirements on LGPS funds. It is anticipated that this will become mandatory in the next couple of years. This will explain the way that the Fund manages climate change risk, from a perspective of governance, risk management, strategy and reporting metrics.

xi. **Commitment to reporting in line with the Stewardship Code 2020** – the Committee has shown support of the updated Stewardship Code (the Fund was a signatory of the previous code), by committing to develop a plan to report in line with the new code. The plan will be put in place through 2021, ready for full reporting the following year.

Training and engagement

xii. **Dedication to Committee training** – the Committee has engaged with several training sessions on responsible investment in general, and climate change in particular, including topics such as embedding ESG issues within the investment process, impact investing, and what work is done by the Brunel pool on responsible investment.

xiii. **Strong programme of scheme employer and membership engagement** – the Committee has approved a plan for scheme membership engagement, which is included in the latest version of the ISS. Work done so far includes member and employer webinars on responsible investment matters, communication with the membership on the new net zero by 2050 target, development of the Fund's website, and a scheme membership survey on responsible investment, which generated a very high level of response and engagement. The results of the survey have been published online, and a section in the Annual Report for 2020/21 will highlight the key findings.

Where the Fund needs to be

14. There is no one framework for best practice regarding responsible investment in the LGPS. Each fund needs to decide the best approach individually, whilst operating in line with their fiduciary duty, and taking appropriate professional advice.

15. In order to ensure that all relevant risks are considered and acted upon, the Fund needs to integrate responsible investment issues across the whole investment process:
    i. **Investment Strategy Statement** – recently updated to include the new investment belief, and will be kept under review as part of the ongoing work in this area;
    ii. **Strategic Asset Allocation** – see comments below;
    iii. **Monitoring of managers and the pooling company** – ESG issues are a standing item in manager meetings and reporting. More detail on Brunel's role is below;
    iv. **Stewardship and engagement work** – more detail on Brunel's role below, but the Fund can improve its approach here by engaging with wider initiatives;
    v. **Internal reporting and accountability** – responsible investment is a standing item at quarterly Committee meetings;
    vi. **Reporting externally** – the Fund includes information in the Annual Report, and this will be developed further via TCFD reporting and Stewardship Code 2020 reporting;
    vii. **Stakeholder engagement** – the Fund includes a plan on scheme membership engagement as part of the ISS, and more detail on this topic is included below.

16. The Fund needs to refine the Strategic Asset Allocation to reflect the results of the climate change scenario modelling, in order to ensure the best possible financial returns for the Pension Fund's investments, and to mitigate risks. This will involve a review of all asset classes to ensure that climate risk and sustainability are being fully considered. Two specific areas are under current consideration:
    i. **Sustainable equities** – the modelling carried out by Mercer indicated that the Fund could benefit financially from taking the opportunity to invest more sustainably. Specifically, the modelling found that under a 2°C scenario returns could be enhanced by around 0.2% p.a. over the next 10 years by adjusting the current strategic asset allocation to be more sustainable. The biggest impact would come from making a specific allocation to sustainable equities, which under a 2°C scenario, would deliver 1.63% p.a. more than standard global equities over the next 10 years.
    ii. To put this into context, the Fund is currently valued at £3bn, and the long-term allocation to active global equities is 10% of the Fund. 1.63% p.a. over 10 years on a portfolio of £300m is equivalent to the Fund potentially benefitting to the tune of £53m, from making a switch into a sustainable equities portfolio.
    iii. This could be achieved by making a strategic allocation to sustainable equities, and then implementing this portfolio via Brunel.
    iv. **Protection assets** – the Fund is currently reconsidering the way that the protection assets part of the strategic asset allocation is implemented, and this provides an opportunity to introduce more sustainable investments to this part of the strategy, thereby providing additional protection as part of securing stable, long-term, inflation-linked, sterling returns.
    v. The Mercer modelling indicated that there could be financial benefits from investing more in renewable infrastructure. In this part of the portfolio, this could be

implemented via additional exposure to operational renewable infrastructure. Other asset classes which could be included here include affordable or social housing, which may also provide an opportunity to invest locally (once all risk and return objectives have been satisfied). Officers will work with the advisers to research all options, and will provide Committee members with training and recommendations on the best way forward for the Fund.

17. Officers plan to develop a dedicated Responsible Investment Policy in the autumn of 2021, for approval by the Committee. This will bring together the existing policies and beliefs in the ISS with the work which will be done alongside Mercer to develop a net zero by 2050 road map. Having this information in one place will be a helpful resource for stakeholders, and can be used as an engagement tool.

18. In order to support the new investment belief and help achieve the net zero by 2050 target, the Fund could make use of more widely available resources, by signing up to various responsible investment initiatives. This will have multiple benefits, for example communicating the Fund's position on responsible investment issues, opening up opportunities to get involved in shareholder initiatives to promote the Fund's investment goals, and providing officers and members with resources. A list of initiatives is included below in this plan.

Stewardship

19. Stewardship is defined by the PRI as "The use of influence by institutional investors to maximise overall long-term value including the value of common economic, social and environmental assets, on which returns and clients' and beneficiaries' interests depend". The Stewardship Code 2020 defines it as "the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society".

20. The Fund was a signatory to the original Stewardship Code, which was introduced in 2010 by the Financial Reporting Council (FRC). The FRC has now published a revised 2020 Code, to which the Fund plans to become a signatory. The 2020 Code is ambitious and has a focus on outcomes, not just policy statements. It will entail a significant amount of work to report on and comply with the new 2020 Code, and the Fund is working on plans to do this during 2021, so that reporting can begin next year. This is being done by carrying out a gap analysis on the current Annual Report format, and then full reporting will be developed, either as part of or alongside the Annual Report.

21. Voting and engagement activities on the Fund's equities portfolios are carried out through the Brunel pool. As part of owning publicly listed companies, Brunel, on behalf of its clients, will have the opportunity to vote at company meetings (AGM/EGMs). To provide guidance, Brunel has a single voting policy for all assets managed by Brunel in segregated accounts.

22. Brunel has appointed Federated Hermes EOS as the engagement and voting services provider. The appointment enables a wider coverage of assets and access to further expertise across different engagement themes. For full transparency, the Fund publishes its voting and engagement activities on its website on a quarterly basis.

Wider Initiatives

23. The following is a list of organisations and/or initiatives which the Fund either already supports, or which is it recommended that the Fund signs up to support. Some of these come with a cost, which is detailed below, and some also come with requirements on the

Fund to deliver reporting. All will deliver the maximum benefits if the Fund is able to engage fully, which with the added resource in the investments and accounting team should now be possible.

i. **The Brunel pool** – the Fund is a shareholder and client of the Brunel Pension Partnership. The Fund is able to be involved in setting portfolio specifications, approving manager selection, and monitoring ongoing performance of portfolios. Responsible investment is completely embedded and considered at each of these stages of the process. The Fund also engages through the client group, the responsible investment sub-group, and ad hoc communications from Brunel on responsible engagement initiatives, for example engagement and voting matters.

ii. **LAPFF (Local Authorities Pension Fund Forum)** - The Fund is also a member of the LAPFF, to enable it to act with other local authorities on corporate governance issues. LAPFF's mission is to protect the long-term investment interests of beneficiaries by promoting the highest standards of corporate governance and corporate responsibility amongst investee companies. Details of their activities can be found on the following link: http://www.lapfforum.org/about-us

iii. **TPI (Transition Pathway Initiative)** – The Fund publicly supports TPI, which is a is a global, asset-owner led initiative which assesses companies' preparedness for the transition to a low carbon economy. The TPI tool assesses progress against companies and sectors to measure the level management quality and carbon performance, to aid in risk assessment. More information can be found here: https://www.transitionpathwayinitiative.org/

iv. **PRI (UN supported Principles for Responsible Investment)** - the Fund supports Brunel as a signatory to the PRI. Asset managers and asset owners who are signatories to PRI support the six Principles for Responsible Investment, which are a voluntary and aspirational set of investment principles that offer a menu of possible actions for incorporating ESG issues into investment practice. More information can be found here: https://www.unpri.org/. It is recommended that the Fund sign up to PRI in its own right. There is a small cost of £3,069 to join. There are numerous benefits including access to resources and guidance, and the ability to engage in collective action with other signatories. There is an administrative burden in reporting, but this will help hold the Fund to account against its objectives.

v. **IIGCC (Institutional Investors Group on Climate Change)** – it is recommended that the Fund join this initiative, as it will help deliver the Fund's net zero by 2050 target. There is an annual membership fee of £2,460. Faith Ward, Brunel's Chief Responsible Investment Officer, is the Chair of the IIGCC, and it is well supported by other Brunel funds. The Fund has already made a public net zero commitment through the IIGCC. More information can be found here: https://www.iigcc.org/

vi. **Climate Action 100** – this is an investor-led initiative to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change. Is it recommended that the Fund sign up to this initiative, as it will help to deliver the Fund's net zero by 2050 target. This initiative would enable the Fund to support and/or take part in engagement activities with companies it is invested in. It is not possible to sign up to Climate Action 100 without also being a member of PRI or IIGCC. More information is available here: https://www.climateaction100.org/

vii. **Just Transition** – a just transition means not transitioning to a low carbon economy at any cost, but doing so whilst also ensuring that this is done in a socially responsible way. The Grantham Research Institute on Climate Change and the Environment at the London School of Economics and Political Science have put together a comprehensive guide as to what this means for investors, and what action can be taken. It is proposed that the Fund signs a statement of support, and uses the guide to help embed this goal within the Fund's policies, and help hold our investment managers to account. More information is available at the following link: https://www.lse.ac.uk/granthaminstitute/investing-in-a-just-transition-global-project/

Responsible Investment Road Map

Q2 2021 -

Investments and strategy: decision on sustainable equities

Reporting & disclosure: TCFD reporting

Training and engagement: Training on impact investing and affordable housing

Q3 2021 -

Investments and strategy: proposals for protection assets, develop and publish Responsible Investment Policy, including climate statement and action plan

Training and engagement: Develop plan for Stewardship Code reporting

Q4 2021 -

Investments and strategy: begin work to implement proposals for protection assets, begin reviewing potential work on other asset classes with respect to climate change and sustainability

Reporting & disclosure: sign up to wider initiatives

Training and engagement: hold membership webinars and develop the information shared on the Fund's website

Q1 2022 -

Investments and strategy: update Investment Strategy Statement

Reporting & disclosure: develop plans for reporting the year's progress in the Annual Report

Resourcing

24. Work done on responsible investment issues is largely resourced by officer time. The investments and accounting team has recently expanded by one FTE, and part of this additional resource will be used to help implement the responsible investment plan.

25. A huge amount of responsible investment work is carried out by the Brunel pool, which has a dedicated team of staff who are widely regarding as being market leading. This resource is a real benefit of pooling, as the Fund would be unable to carry out this level of work independently.

26. Clients engage with Brunel on responsible investment issues regularly – one of the ways this takes place is through the responsible investment sub-group, which Wiltshire officers regularly attend. This group learns about engagement case studies, helps to develop reporting, and sets the responsible investment agenda at the pool in line with client needs.

27. Through the Brunel pool and a wider network of contacts, officers regularly share responsible investment knowledge, ideas, progress, updates etc. with other LGPS funds.

28. The Scheme Advisory Board has recently launched a website resource on responsible investment, which is being further developed over time to add relevant case studies. This is available via the following link: https://ri.lgpsboard.org/items

29. The Fund's investment adviser, Mercer, have allocated a specialist responsible investment adviser to work with the Fund. This continuity of specialism will benefit the Fund as the approach is further developed.

30. The Fund has access to information through the various initiatives it has signed up to (and plans to sign up to), including reading materials, relevant data, and access to training.

31. Training is available for Committee members and officers, including but not limited to conferences, Brunel investor days, and internal training days. The next internal training opportunity will be a half-day in July 2021 which will cover impact investing and affordable housing.

Scheme membership engagement plan

32. The Pension Fund considers that transparency on its actions, particularly with regard to responsible investment issues, is important, and engagement with the scheme employers and membership is a key part of this. The topic of investments is quite technical, and responsible investment issues can be nuanced, so it is important to educate members as well as asking for opinions.

33. There are a range of ways that members can be engaged with:
    i. **Informing –** the Fund seeks to keep members and the general public informed via a section of the annual report which reports on climate change risk and actions. The Fund also published a press release about the transition to low carbon equities, and engaged in publicity to communicate the net zero by 2050 commitment.
    ii. **Educating –** the Fund held a dedicated responsible investment webinar as part of the annual member conference in November 2020. This covered the responsible investment framework, actions taken already, and plans for the future. The Fund has now launched a dedicated responsible investment page on its website, which will be further developed and will be used to keep members up to date on progress.

iii. **Consulting –** in order to incorporate the views of the employers, the Fund consulted with employers on the amended ISS.

iv. **Actively seeking views –** the Fund launched a responsible investment survey in early 2021, the results of which are published online at the following link: https://www.wiltshirepensionfund.org.uk/media/6555/Responsible-Investment-Survey-Report/pdf/Responsible_Investment_Survey_Report.pdf?m=637559931407900000. A summary of highlights from the survey will also be published in the Annual Report 2020/21. The views of the scheme membership cannot solely be used to drive the strategy, but the exercise provided a useful piece of information to help Committee members consider the full picture, alongside professional advice. It was also be an effective way to engage with the scheme membership on these issues. The survey received 2,251 responses, and gave a strong steer that members of the Fund put a high priority on sustainable issues, and would welcome further information and engagement.

Responsible investment membership engagement plan for Wiltshire Pension Fund:

- Continue to develop and expand upon the information published in the annual report;
- Develop the responsible investment webpage, to contain more data and resources, news and updates;
- Deliver a webinar on responsible investment issues at the member conference in the autumn to inform members about the responsible investment framework, policies and actions;
- Consult with employer organisations on revisions to the ISS;
- Communicate major responsible investment related decisions via press releases and member and employer newsletters;
- Consider further options for engagement with the scheme membership.

Appendix 1 – Summary of Climate Change Scenario Modelling Results

Mercer's Modelling

1. Mercer's scenario modelling looked at the climate change impact on return for the current strategic asset allocation, and one with a more sustainable tilt (i.e. higher exposure to sustainable infrastructure and global sustainable listed equity), in the context of various different climate change scenarios. The analysis covered 2°C warming, 3°C warming, and 4°C warming scenarios over various timescales up to 2100 (all compared to pre-industrial times).

2. The Mercer report gave compelling evidence that the Fund had scope to further reduce the exposure to climate change risk and increase its exposure to opportunities, and that not doing so could financially harm the Fund's investments.

3. A key finding was that keeping warming to 2°C or below was essential to protect the Fund's investment returns – this scenario is best for most investors and asset classes. Under scenarios with higher warming (3°C and 4°C), there was poorer performance across most asset classes.

4. It was found that in moving towards a higher weighting in sustainable assets, the Fund would be able to take advantage of more opportunities in a 2°C scenario, and that the Fund would be marginally better protected in a 3°C scenario. Both asset allocations modelled generate similar returns under a 4°C scenario as risks scale up towards the end of the century.

5. This finding is illustrated in the outcomes from the modelling, shown below:

		CURRENT SAA	SUSTAINABLY TILTED AA
		Climate change impact on return (% p.a.)	
2°C	2030	0.18%	0.37%
	2050	-0.01%	0.12%
	2100	-0.06%	-0.01%
3°C	2030	-0.02%	0.00%
	2050	-0.08%	-0.05%
	2100	-0.12%	-0.10%
4°C	2030	-0.08%	-0.08%
	2050	-0.15%	-0.15%
	2100	-0.20%	-0.20%

≤ -10 bps   > -10 bps, < 10bps   ≥ 10 bps

6. As well as addressing the risks, the modelling found that the Fund was currently not best positioned to capture the potential upside. Under a 2°C scenario, there was significant opportunity to invest in companies and assets which would benefit from the transition to a low carbon economy. These could be accessed through allocations to renewable infrastructure and sustainable equities.

7. Specifically, the modelling found that under a 2°C scenario returns could be enhanced by around 0.2% p.a. over the next 10 years by adjusting the current strategic asset allocation to be more sustainable. The biggest impact would come from making a specific allocation to sustainable equities, which under a 2°C scenario, would deliver 1.63% p.a. more than standard global equities over the next 10 years. However sustainable infrastructure would also offer a material "low carbon transition premium" under this scenario as well.

Hymans' Modelling

8. Hymans' modelling looked at the potential effects on the funding level. This modelling examined scenarios where policies were rapidly changed to respond to the threat of climate change, where nothing is done at all, and something in-between. Hymans explores the issue of climate risk from a purely financial perspective. The Institute and Faculty of Actuaries has identified climate change as a risk which needs to be addressed, as it is a financially material factor. In addition, GAD (the Government Actuary's Department) has very recently set out that climate change modelling is now mandatory as part of the 2022 triennial LGPS valuation cycle.

9. As with other responsible investment issues, climate change is a long-term issue. Hymans' modelling looked at a 10-year time horizon. The modelling showed that the Fund would be in a substantially better place under a "green revolution" scenario, i.e. one where there is a strong policy response and a transition to a low carbon economy. Investment returns (and the funding level) were significantly higher. This would be slightly dampened by increased liabilities resulting from improved longevity, but this does not alter the conclusion.

10. The following graph is an extract from Hymans' modelling. It shows the potential effects on the funding level from the different scenarios of policy response (green revolution (green) = immediate policy change, challenging times (yellow) = no immediate action followed by a catch up, head in the sand (red) = limited policy response). This chart only looks at changes from investment returns, and does not include other factors, and is only to be taken as a broad view to illustrate the potential magnitude of the issue of climate change.