

Bath & North East Somerset Council

MEETING:	AVON PENSION FUND COMMITTEE
MEETING DATE:	10 DECEMBER 2021
TITLE:	ANNUAL RESPONSIBLE INVESTMENT REPORT
WARD:	ALL
AN OPEN PUBLIC ITEM	
List of attachments to this report: Appendix 1 – Draft Responsible Investment Annual Report 2020/21 Appendix 2 – Draft Taskforce on Climate-related Financial Disclosures (TCFD) Report Appendix 3 – Mercer Responsible Investment Total Evaluation (RITE) Analysis	

1. THE ISSUE

- 1.1. The Fund has a Responsible Investing (RI) Policy in place to address the impact of risks arising from RI issues on the investments portfolio.
- 1.2. Given that transparency and disclosure of the RI policy and activities is an important element of being a responsible investor, the Fund publishes an annual report demonstrating how the policy has been implemented during the year. This year the report covers periods to September 2021 as significant RI work was undertaken in 3Q21 including the equity allocation review which saw the Fund adopt two new interim decarbonisation targets as well as a number of strategic asset allocation changes.
- 1.3. Brunel are our strategic partner for developing, implementing and monitoring our RI policies and priorities. For the year ending December 2020 Brunel have published their second Responsible Investing and Stewardship Outcomes Report – elements of this report have been incorporated into the Fund's Annual RI report which contains links to the full Brunel document.
- 1.4. Appendix 2 is the Fund's first TCFD report. The Report will form an appendix to the RI Annual Report and is designed for public consumption.
- 1.5. The Responsible Investment and TCFD report for periods up to and including 3Q21 will be published on the Fund's website once it has been approved by the Committee.
- 1.6. Appendix 3 is a climate change strategy peer group comparison prepared by Mercer. Mercer will present the analysis at the meeting.

2. RECOMMENDATION

- 2.1. **Approves the Annual Responsible Investment Report for publication.**
- 2.2. **Approves the Taskforce on Climate-related Financial Disclosures Report for publication.**
- 2.3. **Agrees the RI priorities for 2022/23.**

3. FINANCIAL IMPLICATIONS

- 3.1. The budget includes the costs of the carbon and environmental analysis provided by Brunel as an elective service.

4. RESPONSIBLE INVESTMENT REPORT

- 4.1. This is the ninth annual report on responsible investment prepared by the Fund. The aim is to bring together all the aspects of the Fund's policies and activities that contribute to its responsible investing objectives. The draft Report to be approved is in Appendix 1.
- 4.2. The report sets out the RI and Environmental, Social and Governance (ESG) issues that have been taken into account and how these were addressed through strategic decision making. The major strategic updates during the period covered by the report were as follows:
 - a) Successfully achieving one of the Fund's interim decarbonisation objectives (to be 30% more carbon efficient than the benchmark) two years ahead of plan.
 - b) Setting additional absolute emissions reductions targets.
 - c) Implementing a revised strategic equity allocation designed to help the Fund move toward its 2050 net zero goal by (1) removing the dedicated emerging market listed equity allocation and increasing the allocation to global developed and sustainable equities, and (2) switching the legacy low carbon passive equities into a new Paris-aligned benchmark.
 - d) The submission of the application to become a signatory to the 2020 FRC Stewardship Code.
 - e) To produce a report in line with the recommendations of the TCFD.
 - f) Continued collaborative work with strategic partners including LAPFF, ClimateAction100+ and IIGCC, which saw the Fund participate in high profile engagements, shareholder resolutions and policy advocacy work calling on domestic and international governments to increase their nationally defined contributions (NDCs) ahead of COP26.
- 4.3. The Fund participated in over 3,500 shareholder meetings and engaged with over 600 companies in its active equity portfolio on a range of ESG issues. In general terms, there was an increase in environmental-related proposals winning voter support, with companies increasingly setting carbon reduction targets. The so-called 'say-on-climate' resolution which calls for companies to disclose emissions on an annual basis and publish a plan to manage those emissions which shareholders can then vote on, gained traction. In the UK and US markets executive remuneration and board structure continued to be a focus for shareholder resolutions.
- 4.4. The Fund is 30% less carbon intensive on a Weighted Average Carbon Intensity (WACI) basis than its benchmark. The year-on-year improvement in carbon metrics is due to a combination of factors including decarbonisation of the underlying portfolios (driven by investment managers allocating capital to less carbon intensive sectors and/or companies) and the Fund's own strategic asset allocation; principally the replacement of the oil & gas heavy UK equity allocation (and reduction in global equities) with the allocation to the Brunel global sustainable equity portfolio - which as can be seen from the report - has a nil exposure to future emissions from reserves. Future analysis will highlight the

impact of recent asset allocation changes and how the Fund is progressing towards its aim of reducing carbon intensity of the equity portfolio over time.

- 4.5. The RI report explains how Brunel and its third-party providers have delivered against policy. Among other things, the report includes engagement highlights, examples of policy advocacy work that Brunel has either led or participated in and voting data generated by Federated Hermes.
- 4.6. The Fund's RI priorities for 2021/22, contained in the final section of the report, have been updated to ensure consistency with Brunel's seven priority themes as all these topics remain relevant from a strategic perspective to the Fund. In addition to these themes the Fund works with Brunel and the other partner funds to identify emerging themes such as sustainable land use, biodiversity and fast fashion that are fed into EOS at Federated Hermes' annual engagement plan. The Committee are asked to agree these priorities:
 - a) Climate change including pollution, waste and plastics
 - b) Human capital
 - c) Diversity and inclusion
 - d) Cyber security
 - e) Cost and tax transparency
 - f) UK policy frameworks
 - g) Supply chain management

5. DRAFT TCFD REPORT (Taskforce on Climate-related Financial Disclosures)

- 5.1. The TCFD was established in 2015 by the Financial Stability Board (FSB), a body set-up by the G20 to monitor and make recommendations about the global financial system. It was created following a review into how the financial sector can take account of climate-related issues and the need for better information to support informed investment.
- 5.2. In 2017 the TCFD issued initial recommendations for reporting to help stakeholders in financial markets understand their climate risks and opportunities. This covers the areas of Governance, Strategy, Risk and Metrics & Targets and Avon Pension Fund has now adopted this guidance and set out its own disclosures.
- 5.3. Although not yet compulsory for Local Government pension funds, the Fund is a strong supporter of these disclosures. This critical framework not only helps us to deliver on our own climate change objectives but is also a way of signalling to investee companies, managers, partners and pension fund members how important climate risk transparency is if the Fund is to achieve real world emission reductions.
- 5.4. This is the first time the Fund has reported against these standards and reporting has been completed to the fullest extent we are able. While data is not always available in the quantity or quality desired, through lack of scope 3 emission information or due to the difficulty of reporting against certain asset classes, this should become more readily available over time. It is hoped that the level of detail and number of areas covered can increase with each future reporting period as the industry makes positive steps forward and as more disclosures become mandatory.
- 5.5. This report covers work undertaken outside of the financial year including the outcomes of the most recent equity allocation review. The Report will form an

appendix to the RI Annual Report and is designed for public consumption. The draft report to be approved is in Appendix 2.

6. RISK MANAGEMENT

6.1. Responsible investing issues can have a material impact on investment risk and return in the long term. The Fund's Responsible Investment Policy seeks to ensure the long-term RI risks to which the Fund is exposed are fully incorporated into strategic and operational (i.e. the investment manager's) decision making, and that the Fund carries out its duties as a responsible investor and shareholder.

7. EQUALITIES

7.1. A proportionate equalities impact assessment has been carried out using corporate guidelines and no significant issues have been identified.

8. CLIMATE CHANGE

8.1. The Fund is implementing a digital strategy across all its operations and communications with stakeholders to reduce its internal carbon footprint in line with the Council's Climate Strategy. The Fund acknowledges the financial risk to its assets from climate change and is addressing this through its strategic asset allocation to Paris Aligned Global Equities and renewable energy opportunities. The strategy is monitored and reviewed by the Committee.

9. OTHER OPTIONS CONSIDERED

9.1. None

10. CONSULTATION

10.1. The Council's Monitoring Officer and Section 151 Officer have had the opportunity to input to this report and have cleared it for publication.

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Background papers	None
Please contact the report author if you need to access this report in an alternative format	