Report Title:	**Responsible Investment**
Contains Confidential or Exempt Information	No - Part I
Lead Member:	Councillor Simon Bond, Chairman Pension Fund Committee and Advisory Panel
Meeting and Date:	Pension Fund Committee and Advisory Panel – 18 September 2023
Responsible Officer(s):	Damien Pantling, Head of Pension Fund
Wards affected:	None

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Royal Borough of Windsor & Maidenhead

REPORT SUMMARY

This report aims to update the reader on the Fund's responsible investment activities and outcomes through presenting a Responsible Investment (RI) report and dashboard as aligned with the Fund's RI policy; – noting that climate change is one of the underlying priorities in the Fund's RI policy and thus carries material weight in this update. This report also seeks to provide the reader with a suite of key engagement activities undertaken on behalf of the Fund and the outcomes of these engagements.

In addition, this report seeks to build upon work undertaken previously on climate risk and scenario analysis, addressing key actions and limitations associated with this work.

1. DETAILS OF RECOMMENDATION(S)

RECOMMENDATION: That the Pension Fund Committee notes the report;

- **i) Approves the Fund's RI dashboard, RI report and Active Engagement report for publication;**
- **ii) Acknowledges the forward looking actions on climate risk assessment; and**
- **iii) Agrees to the re-establishment of a RI working group and full review of RI policy by end of 2023/24**

2. REASON(S) FOR RECOMMENDATION(S) AND OPTIONS CONSIDERED

2.1 Since December 2021, the Fund has reported publicly on its implementation and outcomes concerning responsible investment. The report and dashboard to Q2 2023 (or Q1 2023/24) are included respectively at Appendix 1 and Appendix 2 to this report.

2.2 Notably, the report and dashboard shows indicative "green/brown" portfolio exposures to all of the Fund's equity and equity-like assets (listed equity, private equity, and infrastructure) plus corporate bonds within fixed income. The key takeaways from this analysis are as follows:

2.2.1 Investments in brown sectors (extraction, transportation, storage, supply, and generation of energy from fossil fuels) make up just 1.98% of the portfolio.

2.2.2 Investments in green sectors (renewable energy generation, clean technology, and decarbonising activities) make up over 6.85% of the portfolio.

2.3 As illustrated above, the green exposure significantly outweighs the brown exposure by over 3x within the identified portfolio.

2.4 LPPI has published a net-zero roadmap (presented at the March 2023 meeting) and its net-zero targets for the LPPI Global Equity Fund, further work is being undertaken by LPPI in relation to Net Zero target setting for additional asset classes with targets for Fixed Income and Real Estate to be published in 2023/24 and shared with the Committee in due course though this quarterly report.

2.5 In addition, LPPI is currently undertaking a project to develop a Climate Solutions Fund with details to be shared in due course.

2.6 Whilst a separate RI policy is not compulsory for LGPS Funds under the Regulations, regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations (2016) requires that the Authority's Investment Strategy Statement (ISS) must include its "policy on how ESG considerations are taken into account in the selection, non-selection, retention and realisation of investments". The Fund's ISS defines that a separate RI policy shall be in place with detailed guidance on the points within the Regulations, and that implementation of said RI policy would be undertaken by LPPI.

2.7 The Fund's RI policy was last presented for approval by the RI working group (the task and finish group) and approved by the Committee in October 2022 along with a commitment to review regularly. One of the actions of this report concerns the re-establishment of the working group and set up of a project to review the RI policy again for presentation at the March 2024 Committee. This action includes procuring and engaging relevant expert support to enable this project.

2.8 Consideration of climate risk was an important part of the triennial valuation process and final valuation report which was signed off by the Committee in March 2023. Supplementary to the triennial valuation was a climate risk report which detailed the Fund's approach to measuring climate risk and ensuring it is accounted for in contribution setting and establishing the funding level. A climate risk training session was subsequently held on 19 June 2023 and the climate risk report providing further detail on the valuation process was presented for approval at the 19 June 2023 Committee meeting.

2.9 Officers took away several actions from the 19 March 2023 Committee meeting in relation to climate risk and these are addressed as follows:

2.9.3 It was noted that there are widely recognised limitations in the data used to measure climate risk when looking at both transition and physical climate risks and this should be considered further. Some of these limitations are already noted in the climate risk report and others in a recent publication by the Institute and Faculty of Actuaries (available in the background papers of this report), which specifically addresses the limitations of climate risk analysis in respect of the scenarios used by data modellers. This IFoA publication specially outlines that some of the more pessimistic and extreme scenarios (such as a zero-GDP economy) are not properly considered by climate risk analysis models.

2.9.4 Whilst the data and scenarios used by Barnett Waddingham (adopting an approach developed by the Bank of England) follows a generally accepted approach for institutional investors, it should be noted (based on the IFoA publication) that there is a potential for optimism in the results. In addressing this, officers took an action to undertake a cost benefit analysis on re-visiting climate risk report with alternative data and scenario approaches (considering both alternative data and the use of a bottom-up approach). the key advantages and disadvantages following this review are outlined in Table 1.

Table 1 – Cost-benefit analysis

Costs/Disadvantages	**Benefits/Advantages**
Based on quotes from third party providers, a top-down analysis similar to already undertaken but with alternative scenarios will cost in the region of £0.070m-£0.090m. A bottom-up report is likely to cost significantly more depending on the level of detail we require to be modelled. This is currently unbudgeted so should be set in 2024/25 and funded by other service efficiencies; – budget efficiencies will require careful consideration of their impacts on fund governance, resourcing and core operations.	Bottom-up analysis of the fund’s assets may lead to better visibility and understanding of how our existing assets will be impacted by both the transition and physical risks associated with climate change. This may create or enable us to identify opportunities.
Change of approach would involve going against the advice of our independent scheme actuary which may cause governance concerns. Implementing approach different to that already used in the valuation will lead to Berkshire being a LGPS outlier, which has been the cause of many legacy issues.	Top-down alternative data modelling and scenarios may give the Fund a more holistic picture of the risks of climate change, allowing the comparison and contrasting views of two data modellers.
If the results produce an alternative outcome to that of Barnett Waddingham’s analysis, a contribution review should be undertaken with the results impacting scheme employers.	Fund may be regarded as more forward-thinking and advanced on the climate change risk reporting agenda.
This may, to some extent, be duplicating work that will need to be undertaken as part of the mandatory TCFD reporting framework currently being implemented across the LGPS.	Time. Implementing a bottom-up approach, or using an alternative data provider for a top down approach would likely take considerable time to arrange and the results would not be available for immediate consideration.
If the analysis was re-modelled and instead relied on more extreme risk assumptions, similar critiques would still apply as those on the existing model; the results would still not produce a true picture of the likely, or plausible, reality as models today still can’t account for it accurately, and flaws in the models’ assumptions will still exist. Balancing pragmatism, it is best instead to recognise the early stage we are at and its widely understood shortfalls, committing to take account of these going forward, evolving the approach at future junctures.	

2.9.5 Considering the cost-benefit analysis undertaken by the Fund and summarised above, officers recommend that a bottom-up approach is postponed until the statutory implementation of TCFD (first report due by December 2025 at the earliest). LPPI have offered to assist the Fund in preparing for TCFD requirements which will provide an efficient and cost-effective solution compared to any alternative.

2.9.6 Regarding the use of alternative scenarios for top-down modelling, the Fund has aligned with the commonplace LGPS industry approach thus far to achieve some level of consistency and comparability across the asset owner community. This approach is aligned with TCFD Principle 5; "Disclosures should be comparable among organizations within a sector, industry, or portfolio". For that reason, officers do not recommend re-modelling scenarios at this point in time but do recognise the existing model's flaws and aim to continue to evolve its approach over time. Furthermore, work in this area is understood to be nascent, therefore, further work at this point might not deliver the intended benefit of a significantly greater degree of certainty and insight.

2.10 As detailed in the Fund's Responsible Investment policy, "the RCBPF considers engagement to be a route for exerting a positive influence over investee companies and encouraging responsible corporate behaviour." The Fund (via LPPI) has appointed an engagement partner to increase capacity for active engagement with companies across its credit and equity portfolios, seeking to improve a company's behaviour on ESG related issues. The Fund's active engagement outcomes are reported at Q2 2023 (or Q1 2023/24) on the Fund's website and noted in the background papers section to this report. The key parts of the active engagement report are summarised within the RI report attached at Appendix 1.

3. KEY IMPLICATIONS

3.1 A key implication of publishing this report is to actively put the Fund's RI outcomes and data in the public domain in advance of receiving FOI requests. Officers have thus far seen a significant reduction in the amount of time dedicated to addressing RI related FOI requests as a consequence of proactively publishing this report quarterly since December 2021.

3.2 The Fund seeks to achieve good ESG credentials whilst maintaining strong investment performance. Evidence[1] suggests these two are not mutually exclusive, therefore, the Fund seeks to achieve both over the long run provided it can meet its fiduciary responsibility to scheme members and employers.

3.3 Strong ESG credentials are positive indicators for sustainable companies. Therefore, incorporating material ESG considerations is an important part of both asset selection and active stewardship and is additive to the identification of long-term stable returns, thus assisting the Fund in meeting its fiduciary responsibility.

4. FINANCIAL DETAILS / VALUE FOR MONEY

4.1 Budget and funding implications should be properly considered if the Committee intend on undertaking additional climate risk analysis work over and above the work already undertaken.

4.2 Re-establishment of the RI working group (task and finish group) may require additional consultancy and advisory costs, but these shall be met within existing service budgets.

[1] The Journal of Sustainable Finance & Investment (2015) Vol 5 (Issue 4)

5. LEGAL IMPLICATIONS

5.1 Reporting against RI metrics and making a net-zero commitment are not legal or regulatory requirements. TCFD reporting requirements, when published, will be a legal requirement and legislated by DLUHC (Department for Levelling up, Housing and Communities). These requirements will likely involve penalties and levies by tPR for non-compliance. TCFD requirements shall be implemented in due course and the Fund shall monitor these developments closely.

5.2 The Fund is compliant with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (Regulation 7) which requires that the authority's investment strategy statement (ISS) must include the authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments. The Fund's ISS (last approved by the Pension Fund Committee in March 2023) defines that a separate RI policy shall be in place with detailed guidance on the points within the Regulations, and that implementation of said RI policy would be undertaken by LPPI. The revised RI policy is this compliant with the regulations.

6. RISK MANAGEMENT

6.1 The Pension Fund Committee review and approve a risk register on a quarterly basis, prepared in line with CIPFA's guidance on "managing risks in the LGPS – 2018". The latest risk register (including relevant actions and mitigations) has been prepared alongside this report, with any relevant changes considered and documented as appropriate in the quarterly risk management report.

7. POTENTIAL IMPACTS

7.1 Failure to comply with pension legislation could result in the Administering Authority being reported to the Pensions Regulator where failure is deemed to be of a material significance.

7.2 Equalities. The Equality Act 2010 places a statutory duty on the council to ensure that when considering any new or reviewed strategy, policy, plan, project, service or procedure the impacts on particular groups, including those within the workforce and customer/public groups, have been considered. An Equality Impact Assessment (EQIA) screening exercise has been completed and approved in respect of this this report and shared with the RBWM Equalities team. It has been determined through the EQIA screening that a full EQIA is not required and is therefore not appended with this report.

7.3 Climate change/sustainability: This report is centred around the topic of climate change and sustainability and such impacts are documented in detail through the report and its appendices.

7.4 Data Protection/GDPR. GDPR compliance is included as a specific risk on the register in regard to processing and handling personal data, this is dealt with in the relevant risk report to the Committee along with the relevant mitigations.

8. CONSULTATION

8.1 The Fund's fiduciary Investment manager LPPI, independent advisors and independent scheme actuary Barnett Waddingham was consulted in preparing this report.

9. TIMETABLE FOR IMPLEMENTATION

9.1 Responsible investment outcomes are not subject to any specific timeline and are instead ongoing. Specific interim net-zero targets and plans are set out in the relevant appendices to prior Responsible Investment reports presented to the Pension Fund Committee.

10. APPENDICES

10.1 This report is supported by 2 appendices:

- Appendix 1: Responsible Investment Report Q2 2023
- Appendix 2: Responsible Investment Dashboard Q2 2023

11. BACKGROUND DOCUMENTS

11.1 This report is supported by two background documents:

- Responsible Investment Policy (October 2022) is available in the "policies and reports" section of the Pension Fund website
- Active Engagement Report (Q2 2023) is available in the "Investments" section of the Pension Fund website
- IFoA paper on limitations of climate scenarios Emperor's New Climate Scenarios – a warning for financial services (actuaries.org.uk)

12. CONSULTATION (MANDATORY)

Name of consultee	Post held	Date sent	Date returned
Mandatory:	*Statutory Officers (or deputy)*		
Elizabeth Griffiths	Executive Director of Resources (Section 151 officer)	**n/a**	**n/a**
Elaine Browne	Deputy Director of Law and Governance (Monitoring Officer)	**30/08/2023**	
Deputies:			
Andrew Vallance	Deputy Director of Finance (Deputy Section 151 officer)	**30/08/2023**	**01/09/2023**
Jane Cryer	Principal Lawyer (Litigation) and Deputy Monitoring Officer	**30/08/2023**	
Other consultees:			
Cllr Simon Bond	Chairman – Berkshire Pension Fund Committee	**30/08/2023**	
Alan Cross	Chairman – Local Pension Board	**30/08/2023**	

13. REPORT HISTORY

Decision type:	Urgency item?	To follow item?
Pension Fund Committee decision	~~Yes~~/No	~~Yes~~/No

Report Author: Damien Pantling, Head of Pension Fund