Updated April 2022

Hampshire Pension Fund Statement of compliance with the UK Stewardship Code 2020

Purpose and Governance

Principle 1 – Signatories' purpose, investment beliefs, strategy, and culture enable stewardship that creates long-term value for clients and beneficiaries leading to sustainable benefits for the economy, environment and society.

Context

The Hampshire Pension Fund is part of the Local Government Pension Scheme (LGPS) and its mission is to provide an efficient and effective pension scheme for all employees and pensioners of all eligible employers in Hampshire, in accordance with the requirements of the legislation for the LGPS. There were approximately 178,000 members from over 340 employer bodies in the scheme at 31 March 2020.

The Pension Fund has defined the following investment beliefs:

Investment belief	Reasons why important
Clear and well-defined objectives are essential to achieve future success	To provide focus in achieving the aims of generating sufficient returns, understanding potential risks and ensuring sufficient liquidity to pay benefits to members
Strategic asset allocation is a key determinant of risk and return	An appropriate strategy is a key driver to future success and typically even more important than manager or stock selection
Funding and investment strategy are linked	Funding feeds into investment strategy decisions, including assessing what returns are required and by when
Long term investing provides opportunities for enhancing returns	The Pension Fund is less constrained by liquidity requirements and can better withstand short term price volatility, with the ability to tolerate periods of active manager underperformance when the manager's style is out of favour with the market.
The Panel and Board will take an appropriate level of risk[1]	There is a need to take risk to ensure the sustainability of the Fund whilst also continuing to be affordable to employers and members. However the level and type of risk must be aligned with long term objectives.

[1] The Panel and Board is responsible for the governance of the Pension Fund and its investments

Equities are expected to generate superior long-term returns	The Pension Fund will maintain a significant allocation to equities in order to support the affordability of contributions.
Government bonds provide liquidity and a degree of liability matching	These assets reduce the Pension Fund's funding risks and also reduce liquidity risk in time of market stress.
Alternative investments provide diversification	Diversification across asset classes can help to reduce the volatility of the Fund's overall asset value and improve its risk-return characteristics.
Fees and costs matter	This is about recognising the need to get value for money through minimising the negative impact of fees and costs whilst being willing to pay higher fees to access strategic opportunities or to achieve better or more consistent returns.
Market inefficiencies will provide opportunities to add value over time	Allowing specialist external investment managers the flexibility to take allocation decisions to take advantage of market opportunities.
Active management can add value	The selective use of active managers to target higher returns net of fees, using careful selection and monitoring of managers to minimise the additional risk.
Passive management has a role to play in the Fund's structure	Combining low cost passively managed investments alongside active management can have cost benefits and reduce relative volatility
Responsible Investment (RI) is important to the Panel and Board and can have a material impact on the long-term performance of its investments	Environmental Social and Governance (ESG) issues can impact returns meaning the Panel and Board needs to be aware of and monitor financially material ESG-related risks.

These beliefs are fundamental to the Pension Fund's investment strategy, as set out in its Investment Strategy Statement.

<u>Activity</u>

The Pension Fund Panel and Board holds four formal meetings per year in addition to receiving briefings from each of its appointed investment managers at least once per year. The Panel and Board has also constituted an RI sub-committee, which meets twice per year to provide greater capacity for the consideration of ESG issues and to enable additional scrutiny of investment managers.

Outcome

The Pension Fund's investment beliefs were key to the basis of the Fund's RI policy which was significantly revised in 2019. Since the redrafting of the policy the Pension Fund has seen an increase in the level of interest in several aspects of RI, in particular Climate Change. The revised policy has enabled the Pension Fund to articulate its position on RI more clearly and thoroughly when responding to its scheme members.

Whilst some of its interactions with a small number of scheme members have highlighted that the Pension Fund's RI activities have not gone as far as these members would like, particularly in relation to disinvesting from companies involved with producing fossil fuels. The Pension Fund Panel and Board supports the objectives of the Paris Agreement and believes that keeping a global temperature rise this century to well below 2ºC relative to pre-industrial levels is entirely consistent with securing strong financial returns but believes that disinvesting from fossil fuel companies at the current time is not the most appropriate action to transition to a low carbon economy. The Pension Fund has now published 3 years' worth of carbon footprint data for its investments, which shows a reduction since the original benchmark, following its five separate decisions to change the investment strategies or guidelines to reduce and limit the carbon output of five of its active and passive investment portfolios.

Principle 2 – Signatories' governance, resources and incentives support stewardship

Activity

The Hampshire Pension Fund is a part of the Local Government Pension Scheme (LGPS). The governance and management of the Fund is the responsibility of the Pension Fund Panel and Board. The Panel and Board oversees the appointment and ongoing scrutiny of external investment managers, to whom the day-to-day responsibility for implementing stewardship is delegated. This includes investment managers appointed through the ACCESS pool. The ACCESS pool comprises 11 LGPS local government administering authorities and was established in response to the UK government issuing its LGPS: Investment Reform Criteria and Guidance (2015). Through the Panel and Board, its RI sub-committee and the Deputy Chief Executive/Director of Corporate Resources and her officers, there is sufficient resource and capacity to monitor and support stewardship activities.

To ensure that the members of the Pension Fund Panel and Board have the required knowledge and skills to fulfil their role, they undertake an annual training programme based on requirements identified from CIPFA’s Knowledge and Skills framework. This includes training on RI; the Panel and Board have received training from the UN PRI, specialist RI consultants from MJ Hudson Spring and an officer from the Local Government Association.

The Pension Fund Panel and Board approves a budget each year that provides the appropriate resources; the officers responsible for the functions of the Pension Fund and means to commission external specialist support, for the management of the Fund, including its responsible investment activities. The Pension Fund’s officers participate in continuous professional development (CPD) as part of the County Council’s staff performance management process. The Pension Fund’s officers take advantage of training opportunities provided by investment managers and other providers, as well as the training provided to the Pension Fund Panel and Board, the content of each includes a significant amount of RI material.

Outcome

Routine written reports from investment managers on voting and engagement activity are received by the Pension Fund’s officers on a regular basis. In addition, each appointed investment manager reports annually to the Pension Fund Panel and Board including on their activity in these areas. At each of their meetings the RI sub-committee receive a report on the investment managers’ engagement and voting activity, highlighting where the investment managers have voted against company management or how they have voted on shareholder motions.

To supplement its internal resources the Pension Fund has commissioned external support from the specialist RI consultants MJ Hudson Spring to report on the Fund’s external investment managers’ RI capabilities and the ESG risk and exposure of each of the Pension Fund’s investment portfolios. This report has assisted in the monitoring and scrutiny of the Fund’s investment managers stewardship activities on behalf of the Pension Fund.

The County Council, responsible for the administration of the Pension Fund, has a corporate commitment to equality and diversity, and works to continue to build a workforce which reflects the diversity of the local community, encouraging applications from people of all ages, genders, sexual orientations and ethnic backgrounds. This is reflected in the team that delivers services for the Pension Fund.

Principle 3 – Signatories manage conflicts of interest to put the best interests of clients and beneficiaries first.

Activity

The Pension Fund’s approach to conflicts of interest in relation to stewardship is part of its RI policy and is as follows.

Conflicts of interest in relation to responsible investment and stewardship could arise when the ability to represent the interests of the Fund as a shareholder is hindered by other interests. These can arise within the Fund or within external service providers. Third party advisors and investment managers may perform roles other than which they are employed for and to that extent conflicts may arise. The Pension Fund expects the investment managers and advisors it employs to have effective policies addressing potential conflicts of interest, and for these to be publicly available on their respective websites. These are discussed prior to the appointment of a manager/advisor and reviewed as part of the standard monitoring process.

Pension Fund Panel and Board members may have other roles within or outside of the Administering Authority that may provide for conflicts unless they are identified and managed. An example may be the potential stewardship of any investment made by the Pension Fund that could be a direct benefit to wider Council policy. To manage and mitigate these potential conflicts Pension Fund Panel and Board have agreed a Conflicts of Interest Policy and are required to complete a conflicts of interests declaration for the Pension Fund year and are recorded in the Fund's Conflicts register.

Hampshire County Council, as the Administering Authority of the Hampshire Pension Fund, requires all members of the Panel and Board and officers to declare any pecuniary or other registerable interests, including any that may affect the stewardship of the Fund's investments. Details of the declared interests of Council members are maintained and monitored on a Register of Member Interests. These are published on the Council's website under each member's name and updated on a regular basis.

Outcome

Following the recommendation of ths Scheme Advisory Board's (SAB) Good Governance review, the Pension Fund Panel and Board have agreed a specific Conflicts of Interest Policy for the Pension Fund. The Pension Fund's approach to managing conflicts of interest has operated as intended. For example, when appropriate the Pension Fund has noted before considering the following relevant issues that its independent advisor is a member of the board of Aberdeen Standard Fund Managers and one of the co-opted members of the Panel and Board is a member of the Trade Union UNISON. There have been no additional conflicts recorded as part of the completion of conflicts of interest declarations by the Pension Fund Panel and Board.

Principle 4 – Signatories identify and respond to market-wide and systemic risks to promote a well-functioning financial system.

Activity

Risk is managed by setting investment beliefs, funding and investment objectives that are incorporated into the Fund's asset allocation it Investment Strategy Statement (ISS). The ISS is reviewed annually and a strategic review is undertaken after each triennial actuarial valuation of the Pension Fund.

The Pension Fund conducts a full risk assessment of its activities which is reviewed twice a year by the Pension Fund Panel and Board,as part of the Fund's Annual Report and in setting its Business Plan. The risk register includes the risk to the Fund's investments from market fluctuations, interest rates, currency, credit and failure by its investment managers or custodian. Risks are identified with the input of the Pension Fund's actuary and investment consultant, as well as the Pension Fund's officers, who stay abreast of current events and potential risks through discussions with investment managers and peers, and seminars and conferences they attend as part of their ongoing professional develoment. In addition, the Pension Fund recognises the risk to investments from ESG factors including the impact of Climate Change that could materially impact long-term investment returns.

The Pension Fund's foremost mitigation against market-wide and systemic risk is a well diversified investment strategy. At each of its meeting the Panel and Board receives a report on the allocation of investments and can take action to address any variances. Therefore, it is important the Pension Fund Panel and Board receives the appropriate training and commissions advice to be able to select from and monitor a wide variety of investments. The Pension Fund commissions investment consultancy advice for its strategic asset allocation and as a point of escalation if it has any concern over the performance of an asset class or one of its investment managers.

Over the last two years significant attention has been given to monitoring the ongoing risk of market volatility caused by COVID-19. Although equity markets have recovered a lot of the initial losses. The Fund's diversified portfolio helped cushion the initial impact of the pandemic in March 2019 and the Fund's valuation and funding level have both since risen above their pre-pandemic levels. The Pension Fund Panel and Board and Fund officers has focused on scrutinising the Fund's investment managers analysis of the risks of the impact of Covid, for example in reviewing the impact on the collection of rents of the Pension Fund's property assets.

Outcome

The following summary takes key risks from the Pension Fund's risk register covering market wide and systemic risks and the actions that have been taken in the last year to manage these risks:

- Employer risks – the covenant risk of the employers in the Pension Fund has continued to be monitored by the Pension Fund and its actuary, in the context of the Fund's Funding Strategy Statement that seeks to appropriately balance the risk of an employers failure and inability to continue to pay contributions with the rate of contributions they are required to pay. The Fund's officers and the actuary have responded to relevant market developments such as the impact of Covid and the extent that this has damaged the convenient of any employers in the Fund and changes in the UK gilt yields that have impacted the affordability of contributions for higher risk employers.
- Investment risks – the Pension Fund's officers continue to monitor the value of the Fund's investments on a monthly basis and these are reported to each quarterly meeting of the Pension Fund Panel and Board. Reports focus on both the investment performance of the Fund's investment managers and the implementation against the Fund's asset allocation. The Pension Fund's officers and Panel and Board have continued to engage with its investment managers, including through the ACCESS pool where relevant, to challenge and scrutinise investment managers. Discussions with investment managers focus on market wide and systemic risks such as inflation, unemployment, interest rates, government intervention in markets and other drivers of market sentiment. In the last year this engagement has heavily focused on the ongoing impact of the Covid-19 pandemic. In general the value of the Fund's assets have benefited from the recovery of asset values in the last year, which has lead to a significant rise in the overall value of the Fund.
- Liability and funding risks – the Pension Fund receives quarterly updates from its actuary on interim funding levels and on an exception basis can take action to change the contributions required from employers or the Fund's investment strategy. As described above in the last year given the improvements in the value of Fund's investments there has been a similar improvement in the funding level.
- Regulatory and compliance risks – the Pension Fund's officers and advisors have continued to monitor any developments from Government or regulators and will respond to any consultation when required. A number of pending developments are expected from Government but yet to received including; the McCloud remedy for age discrimination in previous pensions benefit reforms, implementation of the Good Governance outcomes from the Scheme Advisory Board review and the adoption of the Taskforce for Climate-related Financial Disclosure (TCFD) recommendations. Although the Government is yet make announcements in these areas, the Fund has sought to be proactive in undertaking the work adopt the outcomes of Good Governance and TCFD.
- ESG risk – a significant amount of the Pension Fund's attention has focused on the management of ESG risk, in particular the risk of climate change. Monitoring is undertaken through the regular engagement with the Fund's investment managers and is reported in a number of ways, including a

stewardship report that is made to each meeting of the Fund's RI sub-committee and an annual RI update made to the Fund's scheme members. In the last year the Pension Fund has continued working on the reporting in line with the TCFD recommendations, extending the investments that it is able to report carbon emissions on and then making further agreements with its investment managers on limits or caps to the carbon emissions in investment portfolios. In addition the Fund has undertaken a scenario analysis of the impact of climate change, based on the PRI's *inevitable policy response* scenario, which highlighted the Fund's investment managers varying ability to consider and answer this question. Finally the Pension Fund has commissioned GRESB benchmarking to measure the management of ESG for its direct property portfolio, which will be used on an ongoing basis prioritise investment in the property portfolio for the greatest ESG benefit.

Principle 5 – Signatories review their policies, assure their processes and assess the effectiveness of their activities.

<u>Activity</u>

The Pension Fund began a significant review of its RI policy in 2018 forming a working group of the Panel and Board that took advice from Dr Rupert Younger - Chair of Oxford University's SRI Committee. Following the agreement of the updated policy in 2019 and further external review was carried out in 2020 as part of the commissioning of the specialist external RI consultant MJ Hudson. Recommendations from MJ Hudson were accepted to make the RI policy more comprehensive and readable.

As already reported the Pension Fund's RI sub-committee receive a report to each meeting on the investment manager's engagement and voting activity, highlighting where the investment managers have voted against company management or how they have voted on shareholder motions. This report is part of the sub-committee's published agenda and demonstrates the assurance that the Pension Fund is seeking for the stewardship activities undertaken on its behalf by the Fund's investment managers.

<u>Outcome</u>

The 2019 review of the Pension Fund's RI policy began an emphasis from the Fund on engaging with scheme members and employers on RI. The RI sub-committee created in 2019 has specific actions in its Terms of Reference:

- to regularly review the Pension Fund's Responsible Investment Policy (contained in its Investment Strategy Statement), and practices relating to it, to ensure that ESG issues are adequately reflected;
- to provide a forum for considering representations to change this Policy and/or the Pension Fund's responsible investment practices relating to it;

- to engage directly and indirectly with scheme members and employers to hear representations concerning ESG as appropriate.
- to report annually on the Pension Fund's Responsible Investment to demonstrate progress to the Pension Fund's stakeholders.

The RI sub-committee's first Annual Report on RI was published in April 2020. Following feedback received, for the following years' reports the Pension Fund commissioned the Council's Communication and Marketing team to assist with the publication and improve the format and clarity of the report to make it more accessible to the Pension Fund's scheme members.

Principle 6 – Signatories take account of client and beneficiary needs and communicate the activities and outcomes of their stewardship and investment to them.

Context

The Hampshire Pension Fund is a part of the Local Government Pension Scheme (LGPS). It is a defined benefit scheme responsible for the pensions of over 178,000 scheme members across over 340 scheme employer bodies. Of the members, over 43,000 are currently in receipt of their pensions and the average pension paid in the 2019/20 year was £5,038. Of the members not yet in receipt of their pension, over 58,000 are active members with a further 75,000 deferred members. The average age of all scheme members as at the last triennial actuarial valuation was 51.8 years.

The majority of the employer bodies whose staff are members of the Pension Fund have strong covenants due to their status as public sector bodies. This means that the Pension Fund is able to take a long-term view when making investment decisions, helping the Pension Fund to achieve its investment aims. These aims include managing employers' liabilities to achieve long-term solvency by ensuring that 100% of liabilities can be met over the long term, but without creating volatility in primary contribution rates for employers (and therefore taxpayers) or taking excessive investment risk outside of reasonable risk parameters.

Activity

Following a re-drafting of the RI policy in 2019 the Pension Fund then undertook extensive consultation on the new draft policy by:

- creating a specific Responsible Investment section on the Pension Fund's website where the new draft policy was published, with an explanatory note;
- including details of the consultation in the employers' newsletter requesting that employers publicise this to their members;
- sending an email to a sample of 500 deferred scheme members;.
- inclusion details of the consultation in the newsletter that accompanies the pensioners' annual payslip;

- writing to Hampshire’s Director of Public Health;
- writing to the Pension Fund’s investment managers to ask for their views on the draft policy;
- sharing the draft policy with the other members of the ACCESS pool;

Following the agreement of the revised RI policy in 2019 the Pension Fund has maintained a greater focus on engagement with its scheme members on RI issues. The Pension Fund has maintained a specific RI webpage that it keeps up to date with relevant information to explain the Pension Fund’s approach to RI and provide details for stakeholders, including publishing the full voting records of the Fund’s equity investment managers. The Pension Fund is invested in many companies through its investment managers meaning that voting records may not feel sufficiently accessible to some scheme members and voting and stewardship examples are therefore highlighted in the regular reports to the RI sub-committee. The Fund also has a specific RI email address for scheme members to use to share their views on any aspect of RI. These contact details are published on the Fund’s website and are also shared with scheme members at other opportunities, such as in the publication of the annual RI update report.

The Pension Fund’s RI policy clearly states that the Panel and Board may also consider disinvestment from a particular stock, the exclusion of a particular type of stock or investment in specific ‘social’ investments where, based on an evaluation of ESG factors, it believes that the decision would be supported by a significant majority of scheme members and employers; the Panel and Board may take this approach so long as it does not result in significant financial detriment to the Pension Fund.

Outcome

The Pension Fund reports the allocation, investment value and performance in its Annual Report as at 31 March 2021 for scheme members, which is summarised below:

Asset class	Regional exposure	Actual allocation	Strategic allocation
Growth			
Active Equities*	Global	30.9%	25.0%
Passive Equities*	Global	15.9%	11.0%
Passive Equities*	UK	2.7%	0.0%
Private Equity	Global	4.9%	5.0%
		54.5%	41.0%
Income			
Multi-asset Credit	Global	9.4%	10.0%
Asset-backed Securities	Global	6.2%	2.0%
Private Debt	Global	2.4%	5.0%
Property	UK	6.0%	10.0%
Infrastructure	Global	3.0%	10.0%
		27.1%	37.0%
Protection			
Index-linked Gilts*	UK	17.4%	22.0%
Cash	UK	1.1%	0.0%
		18.5%	22.0%
Total		100.0%	100.0%

* invested via the ACCESS pool, which in total accounted for 67% of the Fund's investments

The Pension Fund records the engagement it receives from scheme members on RI matters. In meeting the RI sub-committee's action 'to engage directly and indirectly with scheme members and employers to hear representations concerning ESG as appropriate' the communication that has been received is reported to the RI sub-committee. The evaluation of the effectiveness of engagement with scheme members is through the volume of correspondence received and the topics covered.

The Pension Fund Panel and Board has agreed that it wants to increase the level of engagement that it has with scheme members further still and has agreed an additional budget of £20,000 for additional communications and is in the process of developing its communications strategy. In the last year the Pension Fund has reviewed its website and made the information on RI more prominent and accessible within it. The coverage of RI in its Annual Report for 2020/21 was also expanded as another means to publicise its activities to scheme members.

Since the Pension Fund's updated RI policy in 2019 the Pension Fund Panel and Board and RI sub-committee has received several deputations, prior to which it had not received any, all about disinvesting from fossil fuels. Although the Pension Fund has not gone as far as the suggestions put forward in these deputations, the Fund has taken several actions that address the issues expressed:

- The Pension Fund Panel and Board has made three separate decisions to change or set limits for three of its investment portfolios to reduce the carbon footprint of these portfolios.
- The Pension Fund publicly reports on the carbon footprint of its investments which show a reduction between the first and second year of reporting (and is aiming to benchmark itself in this regard against other LGPS funds where this data is available)
- The Fund has publicly reported against the Taskforce for Climate-related Financial Disclosure (TCFD) criteria.

Investment Approach

Principle 7 – Signatories systematically integrate stewardship and investment, including material environmental, social and governance issues, and climate change, to fulfil their responsibilities.

Context

As set out in its RI policy the Pension Fund's approach to RI, includes consideration of the Principles for Responsible Investment (PRI), a set of six principles that provide a global standard for responsible investing as it relates to ESG. The PRI provides the following examples of ESG factors:

- Environmental - climate change – including physical risk and transition risk, resource depletion, including water, waste and pollution, deforestation.
- Social - working conditions, including slavery and child labour, local communities, including indigenous communities, conflict, health and safety (including health inequalities), employee relations and diversity.
- Governance - executive pay, bribery and corruption, political or religious lobbying and donations, board diversity and structure, unjustifiable tax strategy.

Activity

The Pension Fund's RI policy sets out by asset class how it expects its investment managers to integrate RI and stewardship into their investment decisions as follows:

Passive investment managers

The Pension Fund accepts that in making investments through an index, passive managers are unable to actively take ESG factors into account in deciding to hold an investment. However, the Pension Fund does expect its passive investment managers to act in its best interests to enhance the long-term value of investments and support and encourage sound practices in the boardroom. As such the Pension Fund expects its passive investment managers to engage with companies within the index on areas of concern related to ESG issues and to also exercise voting rights particularly with regard to ESG factors, in a manner that will most favourably impact the economic value of the investments.

Quantitative investment managers

The Pension Fund will only utilise a quantitative investment manager if having taken advice it was appropriate for implementing the Fund's investment strategy and following a thorough assessment of the investment manager and their quantitative model, including the extent to which it can account for ESG factors. Similarly, to passive investment management the Pension Fund accepts that a quantitative investment manager cannot make stock specific judgements on ESG issues and therefore may not be able to take all ESG factors into account in their investment decisions. However, the Fund still requires the same level of engagement and exercise of voting rights (as described above) as with all other investment managers.

Active investment managers

The Pension Fund delegates responsibility for making individual investment decisions (non passive) to its active investment managers. In delivering their service to the Pension Fund, the Fund requires its active investment managers to pro-actively consider how all relevant factors, including ESG factors, will influence the long-term value of each investment. To ensure that ESG factors are considered in investment decisions, the Pension Fund uses the following framework of questions, which it requires its investment managers to be able to answer and uses these as a basis to scrutinise them.

For each investment has the investment manager assessed and concluded that the overall expected long-term financial return is mitigated from the risk of:

- Detrimental social impacts or increasing health inequalities from the company's products/services, such as armaments or tobacco.
- Negatively contributing to Climate Change or other environmental issues, such as pollution and the use of plastic.
- The impacts of Climate Change.
- Poor corporate governance, systems of control and a lack of transparency.
- A senior management pay structure that is biased towards managers making short-term decisions that aren't in the company's and investors long-term interests.
- The detrimental treatment of the company's workforce or workers in the company's supply chain on issues such as health and safety, gender equality and pay.
- Dangerous business strategies, such as the creation of monopolies, that may expose the company or wider economy to unacceptable risk.
- Any outcome damaging to human rights.

- Reputational damage to the company, the Pension Fund in relation to its beneficiaries, Hampshire residents, or the general principles of the UK Corporate Governance Code; as a result of its approach to any ESG issue.
- If the PFPB do not receive satisfactory responses to these questions they may undertake further engagement with investment managers (and possibly directly with investments) and/or consider directing the investment manager to not invest in the company/sector in question.

Closed-ended limited partnerships

The Pension Fund requires that its investment managers to integrate ESG considerations into their selection of these investments, which it believes will improve the long-term risk adjusted returns. Whilst the Pension Fund expects its investment managers to be able to influence the investment decisions of these partnerships, it accepts that once it has committed its investment it cannot control the investments that are made.

Direct property

The Pension Fund has made a strategic allocation to invest in UK commercial property, and therefore recognises that as a landlord it has an opportunity to affect to quality of the buildings that it owns. As part of the investment management contract that the Pension Fund has let for the discretionary management of its property portfolio, the Pension Fund expects its investment manager to consider improving the environmental impact of each of the properties it owns as part of the investment case for owning each property.

The Pension Fund tendered for a number of its investment managers from 2015 to 2019. These tenders considered various aspects of prospective investment managers capacity and ability to integrate ESG factors into their investment decisions and the commitment to RI through adherence to standards such as the UK Stewardship Code and UNPRI. The Pension Fund has only tendered for one new investment manager in the last 2 years. This procurement was for an investment manager for the Pension Fund's UK commercial property portfolio and external consultant advice was used to integrate the assessment of the management of ESG into the criteria for the selection of the investment manager and the appointed manager is now required to report against the GRESB benchmarking factors. This is particularly important given the relatively long term and illiquid nature of directly held property assets and reflects the need to consider ESG issues not just over the shorter term.

<u>Outcome</u>

As explained above and in the Pension Fund's RI policy, all investment management activity is delegated to external investment managers. Focus on how the Fund's investment managers have incorporated ESG factors gathered through their stewardship activities, into investment decisions, is a significant part of the monitoring and discussion with the Fund's investment managers. Examples include:

- Barings (multi-asset credit) was approached in September 2021 to look at a new transaction for a healthcare company providing rehabilitation and mental health services. Barings' due diligence process had highlighted previous care quality issues at certain health facilities within the group. As such, the company had been rated poorly in the social category under Barings' internal ESG Ratings criteria. During the debt syndication process, the company intended to include sustainability KPIs into its finance terms in order to reduce interest costs on achievement of targets including reduced carbon emissions at facilities. Barings actively engaged with arrangers, senior management and the financial sponsor to push for the addition of KPIs linked to quality of patient care metrics given this was viewed as a key sustainability risk area. Ultimately, Barings was successful in achieving the addition of the requirement for independent third-party quality ratings on medical facilities to meet certain predetermined thresholds. A failure to meet targets would result in higher interest costs for the company.
- abrdn (private equity) co-investing in companies with strong ESG, for example Dott - a leading European micro-mobility focussed company, providing dockless e-scooters and e-bikes to cities across Europe. It also provides full stack operations, including maintenance, battery charging and swapping, ensuring availability at all times. Dott's mission is to provide a clean, sustainable transport option for all. Dott's operational model gives them control over the full lifecycle of their vehicles to ensure that they reuse, upcycle or recycle 100% of their used vehicles and parts, and can service their fleet with 100% electric vehicles powered by renewable energy. They take their ESG ambitions extremely seriously, putting in a place a public manifesto of goals, creating a Sustainability Committee, and continually tracking and reporting on their performance against the ambitious goals they have in place and against their competitors' performance.
- On behalf of investors in the ACCESS pool including Hampshire, Baillie Gifford have carefully considered an investment in U.K. Capital goods company in relation to its supply chain control and human rights issues. The company specializes in international distribution and services company and supplies a range of consumable products. The company's sustainability report states that 98% of its supply chain is in Asia where it has the largest proportion of supplies situated in countries identified by the Global Slavery index as high-risk for human rights issues. In 2020, the company conducted an audit and undertook remediation efforts to bring 61 suppliers up to required standards and are terminating contracts with 15 suppliers that failed to make progress. In addition to this Baillie Gifford asked the company to detail further its approach to forced labor and how it evaluates suppliers following contract termination. Several engagement activities were escalated and involved follow

up activities following initial lack of communication and action on providing for further detail about the company's approach to forced labour.
- Roundshield (private debt fund) has invested in opportunities with positive ESG credentials such as:
    - the construction of a biogas plant in Scotland, taking waste cheese from a nearby factory to generate energy.
    - financing a renewable energy from solar and wind in Northern Spain which has enabled the business to grow, and
    - taking a stake in a Spanish biofuels production plant

Principle 8 – Signatories monitor and hold to account managers and/or service providers.

Activity

The Pension Fund requires its investment managers to report to them on a quarterly basis and meet with them regularly including presenting to the Pension Fund Panel and Board at least once a year. In addition, the creation of the RI sub-committee gives the elected members responsible for managing the Pension Fund additional capacity for engaging with its investment managers and holding them to account, specifically on RI issues. Should the Pension Fund Panel and Board or the RI sub-committee feel that they have not received satisfactory responses from any of its investment managers, the Committees can invite the investment managers back to allow them the opportunity to present again and answer further questions until acceptable responses are received.

Outcome

As set out in the Pension Fund's RI policy and as above for Principle 7, the Fund sets out specific expectations for how its investment managers manage ESG factors according to the asset class that they manage. To date the Pension Fund has received satisfactory responses from its investment managers to demonstrate they have acted in accordance with the Fund's policy.

In addition, the Pension Fund has commissioned specific RI consultancy advice from MJ Hudson Spring on the capabilities of its investment managers in managing ESG issues and the ESG risks and exposures in each of the Fund's portfolios. This has given the Pension Fund better insight of which investment managers and portfolios they should give additional focus on to support their investment managers and ensure their policy is being adhered to.

As already reported the Pension Fund's RI sub-committee receive a regular stewardship report on the investment managers' engagement and voting activity, highlighting where the investment managers have voted against company management or how they have voted on shareholder motions. This report demonstrates that the Pension Fund's investment managers have met the Fund's requirement to vote as a shareholder on its behalf and tests that can provide a reasonable rationale for how their votes have been cast if they have not followed the Fund's policy. As shown in the examples in Principle 7 the engagement reports include all of the Fund's investments in different asset classes, not just equities.

Engagement

Principle 9 – Signatories engage with issuers to maintain or enhance the value of assets.

Activity

The Pension Fund's RI policy includes the instruction to its investment managers that they work in a consistent and transparent manner with companies they are invested in to ensure they achieve the best possible outcomes for the Pension Fund, including forward-looking ESG standards.

Outcome

As explained above and in the Pension Fund's RI policy, all investment management activity is delegated to external investment managers. Engagement activities are a regular feature of the monitoring of the Fund's investment managers by the Pension Fund Panel and Board, RI sub-committee and the Pension Fund's officers. Examples of stewardship activities that have been published and reported to the RI sub-committee are:

- Abrdn (private equity) have leveraged its longstanding relationship with Vespa (a General Partner investing in technology and healthcare companies) and worked with them from a position from not having an RI policy, to implementing a policy, employees undertaking ESG training and implementing an ESG reporting framework in 2021. Hampshire's two co-investments with Vespa are now monitoring Scope 1 and 2 carbon emissions at their main premises and reporting on the gender pay gap and employees earning a living wage.
- On behalf of the ACCESS Pool Baillie Gifford spoke to the chairman of CRH (building materials business) to discuss CRH's corporate governance and approach to sustainability. Two new board appointments incorporated feedback from shareholders, including Baillie Gifford, on adding industry experience to the board. Baillie Gifford have continued their dialogue on the company's efforts to improve efficiency and reduce its carbon emissions. In September, the Global Cement and Concrete Association, of which CRH is a member, announced a joint ambition to achieve carbon neutrality by 2050. Concrete is the world's most widely used material. It is essential to social and economic development and its production is carbon intensive. Accordingly, this ambition is important in addressing effects of climate change. Baillie

Gifford were encouraged to learn that CRH will not count offsets as part of its strategy to reduce its carbon footprint.

- Insight (asset-backed securities) has been working with an originator of UK mortgages and following this engagement they have agreed to adopt a "rebate" mechanism for current and new borrowers that s the energy efficiency rating of their home by at least one notch. Insight and Hampshire believe this type of engagement is directly encouraging individual borrowers to improve the energy efficiency of their homes and directly aid the transition to a lower carbon economy.
- One of Hampshire's Private Debt funds – CarVal have invested in Intersect Power. CarVal aggressively pursued and approved Intersect's purchase of 2.4GW of solar panels from a source that did not use materials from the Xinjiang province. At the time of the order, this was one of the largest orders of solar panels globally and CarVal wanted to ensure they were sourced responsibly.
- Alcentra (multi-asset credit) engaged with a global chemical company to better understand their long-term climate strategy and management of hazardous chemicals. Alcentra spoke with the Head of Investor Relations and Group Technology Director, who provided assurance that hazardous chemicals are not a material business for the group. The company has identified their plans to phase out fluorinated chemicals that may be restricted or banned in the future. The company recently announced a number of low-carbon projects in Europe, including green hydrogen and carbon capture storage investments, which will assist in their greenhouse gas emission reduction efforts, with a goal of reaching net zero emissions by 2050. Alcentra will monitor the company's publication of their interim 2030 reduction targets and progress against these.

Principle 10 – Signatories, where necessary, participate in collaborative engagement to influence issuers.

<u>Activity</u>

As explained above and in the Pension Fund's RI policy, all investment management activity is delegated to external investment managers. As part of this delegation the Fund's investment managers are able to decide if collaboration with other investors will benefit the engagement activities they carry out of the Pension Fund's behalf.

Furthermore Hampshire is a member of the ACCESS pool, which it uses to access more than two thirds of its investments. The 11 partner funds in ACCESS have collectively pooled £34.5m. ACCESS are collaborating on RI activities through unified RI guidelines which set the framework for the investment managers and enable them to utilise the combined weight of capital of the ACCESS authorities to positively engage with the companies they invest with.

In addition the Hampshire Pension Fund is open to discussing any other forms of collective action with other investors and where appropriate will discuss with our investment managers how they can co-ordinate their voting activity with other shareholders.

Outcome

The Pension Fund monitors its investment managers engagement activities through regular reports and discussions and welcomes instances where it sees its investment managers working with other investors. Examples include:

- On behalf of investors in the ACCESS pool including Hampshire, Baillie Gifford have engaged with Rio Tinto (metals and mining company) and third parties on the Juukan Gorge disaster in 2020 and 2021. Following the interim parliamentary inquiry into the incident, Baillie Gifford engaged as part of the Investor Forum and attended the Australasian Centre of Corporate Responsibility's briefing in the fourth quarter of 2020. The inquiry identified failings which led to the destruction of the Juukan Gorge site. Baillie Gifford also spoke with the UK Investor Forum and the Australian Council of Superannuation Investors in the first quarter of 2021. The focus of Baillie Gifford's stewardship work has been to promote governance practices which support responsible operating behaviour and the creation of long-term stakeholder value.
- One of Hampshire's private debt investments ICG have been actively participating with other investors in the CDP pilot project for private markets. The purpose of this project is to shift the industry from using proxy emissions data to actual data from portfolio companies to further enhance the data they report. CDP is a global carbon disclosure framework and ICG have helped develop a concise reporting template for private companies. ICG have been actively engaging companies to report their climate data to CDP and a number of portfolio companies have taken part.
- On behalf of ACCESS and other investors, UBS-AM identified Equinor (Norwegian petroleum company) in February 2017 as one of the world's top 100 greenhouse gas emitters and was included in the engagement focus of Climate Action 100+. The company was identified for engagement for concerns over carbon emissions trends, fossil fuel exposure, weak disclosure levels, or the absence of climate change policies and targets. UBS-AM joined the Climate Action 100+ coalition to provide consistent and coherent messaging and committed to leading the Climate Action 100+ coalition for this company. UBS-AM portfolio managers, analysts and SI analysts have been in contact with company representatives, including Board members, in the context of investor and Climate Action 100+ meetings and have established engagement objectives. Equinor has now strongly committed to increase capacity and investments in renewables, hydrogen and CCSU and executive pay will be updated to include new climate targets. The company is gradually

undertaking a climate transition, complementing energy producing portfolios with renewable and other low-carbon energy solutions. It has already become the world's largest offshore wind operator.

Principle 11 – Signatories, where necessary, escalate stewardship activities to influence issuers.

Activity

The Pension Fund expects its investment managers to take the appropriate action when operating on its behalf engaging in stewardship activities, this includes actions to escalate their approach when appropriate.

Outcome

The Pension Fund monitors its investment managers engagement activities through regular reports and discussions and expects its investment managers to take the appropriate action when operating on its behalf engaging in stewardship activities, this includes actions to escalate their approach when appropriate up to disinvesting from a position if engagement activities do not produce the desired result. Examples include:

- Barings (multi-asset credit) divested from an Indonesian coal miner after multiple engagements on the environmental risks within its coal business for which they didn't get any positive traction with management around measuring or setting targets for its scope 1,2 or 3 emissions or any clear plan regarding environmental risks.
- Through the ACCESS pool, Hampshire owned a US holdings company in Baillie Gifford's portfolio. In early 2020, Baillie Gifford engaged with the Compensation Committee on the issue of discretionary bonuses that were due to be paid to management, despite triggers from the company's own Long Term Incentive Plan not being met. Nevertheless the company pressed on and so Baillie Gifford voted against both the pay package and the re-lection of the Chair of the Compensation Committee. For Baillie Gifford this became a broader issue, of an organisational culture not aligned to the long-term interests of their clients and was one of the factors taken into account when they decided to sell the holding.
- On behalf of investors in the ACCESS pool including Hampshire, Acadian have engaged with a UK Capital goods company on supply chain control and human rights issues. The company specializes in international distribution and supplies a range of consumable products including food packaging, disposable tableware and catering equipment, cleaning and hygiene supplies, packaging to customer markets including grocery, foodservice, cleaning and hygiene. The company's sustainability report states that 98% of its supply chain is in Asia where it has the largest proportion of supplies situated in

countries identified by the Global Slavery index as high-risk for human rights issues. In 2020, the company conducted an audit and undertook remediation efforts to bring 61 suppliers up to required standards and are terminating contracts with 15 suppliers that failed to make progress. Engagement was escalated by asking the company to detail further its approach to forced labor and how it evaluates suppliers following contract termination.

- On behalf of investors including the ACCESS pool UBS-AM identified Exxon Mobile (oil and gas company) for its lack of commitment to transition away from fossil fuels towards a low-carbon business strategy, and that the track record of the company's management was below industry average. UBS-AM engaged with the company through the Climate Action 100+ investor coalition. UBS-AM set engagement objectives aimed at encouraging the company to develop a stronger sense of direction in terms of greenhouse gas reduction ambitions, the strategic impacts of climate change, and to develop an action plan for transition. At the end of 2020, the company announced greenhouse gas reduction targets to aim at decreasing carbon intensity of its upstream business. However, these targets were limited in scope and were weaker than most of its industry peers. UBS-AM noted that over the course of the engagement, the company was reluctant to address the key question of the changes it needs to make in order to reflect the pressures on its business model from climate change. As a result UBS-AM decided to exclude Exxon Mobile from its Climate Aware strategy, which Hampshire invests in having switched from a traditional passive equity index.

Exercising rights and responsibilities

Principle 12 – Signatories actively exercise their rights and responsibilities.

Context

The Pension Fund's RI policy includes its approach for exercising of rights attached to investments. This include the Fund's belief that if companies comply with the principles of the UK Corporate Governance Code published by the Financial Reporting Council, this can be an important factor in helping them succeed; but the Fund also accepts the need for a flexible approach that is in the common long-term interests of stakeholders including shareholders, company employees and consumers, and that the principles accepted as best practice in the UK may differ globally. The Fund's investment managers should cast their votes with this in mind.

In particular, the Fund's investment managers should cast their votes to ensure that:

- executive directors are subject to re-election at least annually
- executive directors' salaries are set by a remuneration committee consisting of a majority of independent non-executive directors, who should make independent reports to shareholders

- arrangements for external audit are under the control of an audit committee consisting of a majority of independent non-executive directors, with clear terms of reference – these should include a duty to ensure that investment managers closely control the level of non-audit work given to auditors, and should not significantly exceed their audit-related fee unless there are, in any investment manager's opinion, special circumstances to justify it
- in the investment managers' opinion, no embarrassment is caused to the Fund in relation to its beneficiaries, Hampshire residents, or the general principles of the UK Corporate Governance Code.

The Pension Fund's investment managers (both active and passive) are required to report to the Pension Fund on their engagement with company management and voting recording, highlighting any instances that they voted against company management or did not follow its policy.

Where investment managers were appointed directly by the Pension Fund to segregated mandates, the Pension Fund expected these managers to vote in line with its own voting policy or explain the rationale for doing otherwise. Similarly, for investments held through the ACCESS pool in a segregated sub-fund the expectation is that investment managers will vote in line with the pool's RI policy, whereas where investments are in a pooled vehicle the Pension Fund accepts the investment manager will vote in line with its own policy, however there is still a requirement for the investment manager to explain the rationale for its decisions and ultimately the Panel and Board has the option to disinvest if it is dissatisfied with the manager's decisions.

The Pension Fund allows its investment managers to conduct stock lending and has actively recalled lent stock for voting reasons on multiple occasions when advised by its investment managers.

Activity

The Pension Fund's policy includes requiring investment managers to exercise the Fund's responsibility to vote on company resolutions wherever possible. The full voting record of all of the Fund's investment managers are published on its website Responsible investment | Hampshire County Council (hants.gov.uk).

The voting and engagement report to the RI sub-committee includes rationales provided by the Fund's investment managers for where they have voted against company management or how they have voted on shareholder resolutions. This report is published with the committees agenda, the latest example is published here: 2022-03-04 PFRIS Stewardship.pdf (hants.gov.uk)

The Pension Fund needs to develop its approach to exercise the rights for its fixed income investments.

Outcome

The RI sub-committee has identified the need to develop the reports that they received on the investment managers’ voting and engagement to include the outcome of the resolutions that have been voted on.