Leicestershire County Council

LOCAL PENSION COMMITTEE – 3 MARCH 2023

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

OUTCOME OF CONSULTATION ON NET ZERO CLIMATE STRATEGY AND RESPONSIBLE INVESTING UPDATE

Purpose of the Report

1. The purpose of this report is to present to the Local Pension Committee the outcome of the consultation on the draft Net Zero Climate Strategy and seek approval of the revised Strategy and the associated implementation plan.

2. The report also provides an update on the Fund's quarterly voting and stewardship activities undertaken on its behalf via LGPS Central (Local Government Pension Scheme), LGIM (Legal and General Investment Managers) and the Local Authority Pension Fund Forum, as well as any current developments.

Policy Framework and Previous Decisions

3. The Fund must follow the law and statutory guidance for preparing and maintaining its Investment Strategy Statement and must take proper advice and act prudently when making investment decisions. Subject to this, the Fund should consider any factors that are financially material to the performance of its investments, including environmental, social and governance (ESG) factors. This includes considerations over the long term, dependent on the time horizon over which the Fund's liabilities arise.

4. The appetite of the Fund for taking risk when making investment decisions is ultimately for local consideration and determination by the Local Pensions Committee subject to the aim and purpose of the Fund. To maximise the returns from investment returns within reasonable risk parameters. It is not the role of the Fund to put non-financial beliefs, such as ethical or moral considerations above those of the employers funding the pension scheme.

5. Responsible Investment is an approach to investment that aims to incorporate environmental (including climate change), social and governance factors into

investment decisions, to better manage risk and generate sustainable investment returns, as set out in the Fund's Investment Strategy Statement.

6. The Local Pension Committee is asked to approve an annual Responsible Investment (RI) plan, the latest of which was approved in January 2023, which supports the above approach with a continual focus on raising RI standards.

7. In November 2021, the Local Pension Committee agreed the commencement of work to produce the Fund's first Climate Strategy, recognising the systematic impact climate change could have on the Fund. In June 2022 it was agreed to engage on proposed metrics that were in line with the Net Zero Investment Framework developed by the Institutional Investors Group on Climate Change, a group with over 375 investor members with more than £45trillion in assets.

8. In November 2022, the Local Pension Committee received the outcome of the engagement, and further agreed to consult on the draft Net Zero Climate Strategy.

Background

9. As set out in the Fund's Investment Strategy Statement, the Fund holds investments in various asset classes, which includes the world's biggest companies in sectors that include manufacturing, technology, and transport. Climate change is a systematic risk where the climate actions, or inaction, of companies can positively or negatively affect other companies, as well as the overall economy.

10. To date the Fund has made a number of investments with climate considerations in mind, whilst maintaining the Fund's targeted risk-return trade-off. These investments and commitments alone account for over £1billion of Fund assets, as at 31December 2022. This does not account for other investments that will also have climate positive investments within their portfolios.

    - Transitioned £770m into LGPS Central's All World Equity Climate Multi Factor fund (Climate MFF), as of 31 December 2022 this now accounts for £872m. This investment incorporates three key climate change considerations: carbon emissions, fossil fuel reserves and green revenues. To date the Climate MFF fund has demonstrated a record of accomplishment of generating better carbon metrics compared to the broad market indices. As of 30 June 2022, the weighted average carbon intensity of the fund is 62.5% lower than its corresponding broad market index.

- £55m committed to the Quinbrook Net Zero Power Fund. A Fund that invests in solar power with battery systems, both as part of the decarbonisation of the energy system, and as part of demand from data centres.

- £55m committed to the Stafford Capital Carbon Offset Opportunity fund, in addition to its existing investment in timberland. This fund looks to invest in sustainably managed timberland globally, provide a source of sustainable low carbon timberland materials, generate verified carbon offsets. In addition to the £139million already invested in Stafford Capital timberland funds.

- £100m committed the LGPS Central Core/Core+ Infrastructure Partnership which invests in infrastructure funds across the core/core plus space. To date this partnership has made several such investments which include UK focussed solar and battery storage, as well as social, renewables, transport, and utilities assets. Further detail is set out in paragraph 55.

- £56million invested in Aegon's Short Dated Climate Transition Fund, which manages climate transition risks and climate change in a fixed income portfolio.

11. In recognition of the risk climate change poses, the Fund has produced a Climate Risk Report annually since 2020. This report combines bottom-up and top-down analysis and is designed to give the Fund a view of the climate risk held throughout its entire asset portfolio, accompanied by proposed actions the Fund could take to manage and reduce that risk. This enables the Fund to analyse progress against the baseline of data from previous reports, reassess the Fund's exposure to climate-related risks and opportunities, and identify further means for the Fund to manage its material risks.

12. The latest Climate Risk Report sets out that since the Fund's baseline of 31 December 2019 the Fund has shown clear progress as of 31 March 2022. These results were presented to the Local Pension Committee on 18 November and highlighted:

- The carbon intensity of the Fund reduced by 26% across measurable investments.
- The Fund's exposure to companies that own fossil fuel reserves reduced from 8.57% to 6.79% of listed equity assets.
- Increased investment in companies whose products and services include clean technology (including alternative energy, green buildings, pollution prevention and sustainable water) from 34.16% to 38.24% within listed equity assets.

13. The Fund recently produced its second Climate Scenario Analysis, via the services of Mercer LLC that was also presented on 18 November 2022. The analysis estimated the effects on key financial parameters (such as risk and return) that could result from plausible climate scenarios. This took into account transition risk, and physical risk, over a range of plausible futures over 5 to 40 years under three scenarios, rapid transition, orderly transition, and failed transition. Assessing the Fund's resilience to different climate scenarios and consider the impact of their portfolios on future climate trajectories

14. The latest analysis on the Fund's asset allocation as of March 2022 predicted the Fund's returns are best protected in an orderly transition, in comparison to a failed transition being the worst outcome, which could result in cumulative losses around 32% of the portfolio's value relative to the baseline. For the Fund it is clear over the medium to long term a successful transition is imperative, which it intends to support through the Net Zero Climate Strategy.

Developing the Net Zero Climate Strategy

15. The NZCS outlines the Fund's strategic approach to managing climate risk, and proposed approach to achieving Net Zero by 2050, with an ambition for sooner.

16. Considerable work and engagement has been undertaken with the Local Pension Committee and has driven the development of the Net Zero Climate Strategy (NZCS). This included:

    a. Following the International Investors Group for Climate Change Net Zero Framework.
    b. 21 January 2022 Committee workshop on development of the Net Zero Strategy.
    c. 25 March 2022 Workshop session on targets and metrics that were proposed and a summary of other LGPS fund climate strategies.
    d. Advice from Hymans Robertson presented to the Committee in June 2022 which reviewed proposed targets and set out further detail on the approach to engagement and divestment following comments at the March 2022 meeting.
    e. Further analysis of other LGPS Fund management of climate risk and targets set.
    f. 13 October 2022 briefing following the engagement conclusion on targets and measure.
    g. The Climate Risk Report and Climate Scenario Analysis presented to the Committee in November 2022, alongside the draft NZCS.
    h. Officers ongoing dialogue with Pension Committee members when requested.
    i. Government commitments, with recognition of the ongoing consultation on governance and climate risks and opportunities for the LGPS.

17. The Strategy includes four key sections, further to the introduction, and general context on the Pension Fund. These sections relate to:

   - **Climate Change Risks and Opportunities**: how the Fund will further embed climate risk and opportunities considerations. This will include working with Investment Managers to ensure they have taken into account climate risks and opportunities
   - **Targets and Measures** - Net Zero by 2050, with an ambition for sooner, supported by interim and secondary measures to decarbonise the Fund's portfolio and increase investment in a range of climate solutions. This also sets out current coverage, and limitations facing the Fund.
   - **Decision Making:** How the Fund can integrate targets and measures alongside best practice within the Fund's annual Strategic Asset Allocation, the Investment Strategy Statement and any investment decisions taken. Recognising the Fund can consider a range of investment approaches to manage risk and opportunities related to climate change, where there is a credible financial basis.
   - **Stewardship Engagement and Divestment** - In line with the IIGCC the Fund believes that engagement will drive the transition for a low carbon economy. This sets out a four step plan of evaluation, engagement, voting and divestment.

18. The Committee considered the draft NZCS on 18 November. Following some clarification and slight amendment to the summary document that arose from the discussion, the draft was published for consultation.

<u>Local Pension Committee comments 18 November</u>

19. At the 18 November Committee meeting a number of comments were made in relation to the draft NZCS. Key points predominantly related to the following and reflected earlier discussions and viewpoints expressed.

   - That the Fund needed to clarify within the NZCS that integration of engagement and divestment was not either, or, and that both have complimentary roles in the Fund's Stewardship approach.
   - That the Fund should set out clear 'trigger points' to divest from laggards especially in reference to those involved in new fossil fuel development.

20. In response to the comments raised by the Committee the Stewardship, Engagement and Divestment approach was strengthened within the NZCS, reflecting that engagement and divestment is not either or, and both are necessary in an effective NZCS. As well as the importance of supporting investment managers investment in companies that are better aligned to decarbonise given Managers view of medium to long-term risk of companies., over those that they are considered laggards, all else being equal. These changes are highlighted in the table in paragraph 42.

21. There are a number of factors to consider on these points. Firstly, the majority of the Fund's investments are held through investment managers and does not hold direct control over stock picking meaning the Fund is unable to divest from certain stocks (given managers will also have regard to the views of others invested within the Fund). Secondly, divestment alone would do little to effect real world emissions if other, less ESG minded investors, purchased the shares. As the Fund's portfolio would still be exposed to the global impact of climate change.

22. To manage the risk of 'stranded assets' the Fund will continue to reduce its exposure to fossil fuels. This will be enhanced through understanding investment managers approaches, and whether they complement the Fund's Net Zero Climate Strategy. The NZCS sets out the Fund's expectation that Managers should be considering climate risk on a case-by-case basis and, have the resource and capacity to scrutinise companies sufficiently.

23. This process is further set out within the associated Implementation Plan and manager questionnaire that will enable the Fund to challenge its existing managers and consider who could be considered 'laggards'. The Fund can then begin a dialogue with these managers, where the Fund does not consider them to be appropriately managing climate risk the Fund can choose to remove or reduce exposure to certain managers where possible. Where there are concerns more generally on certain asset sectors or geographies, they will be incorporated into future iterations of the Strategic Asset Allocation.

24. Given the discussion on 'trigger points' officers through LGPS Central questioned the underlying active equity managers to understand their investment processes in relation to development of new fossil fuel reserves, given unabated fossil fuel production will impair the world's ability to limit global warming to 1.5C. From the response it is clear that:

    - Many current active equity managers have their own 'house' restrictions on investments. For example, where companies generate more than a certain revenue (between 5-30%) in thermal coal/oil sands.
    - Managers that do not have exclusion thresholds or look at investing in companies under set revenue thresholds, still make investments decisions on a case-by-case basis integrating climate risk considerations into their investment process.
    - Managers recognise the importance of maintaining active and ongoing engagement in viewing company disclosures. It is difficult to quantifiably screen for companies' future investment plans as there will not be financial data to capture, until it arises as a cost or investment and ultimately in the company's financials. Managers should also have a detailed knowledge of investee companies which will include plans and attitudes towards climate change that should be assessed.

- Managers engage routinely with company management of the stocks they own or are considering within the portfolio. This includes assessment of climate-related factors. i.e., company targets, the management plans to achieve them and how the company is managing climate related risks. Any new capital expenditure plans should be highlighted within this process.

25. It is important to note that exclusions were not required or requested as part of investment manager selection. Instead, Central require the integration of ESG (including) risk and opportunities into investment processes as well as robust engagement. This provides a more nuanced and sophisticated approach to assessing ESG risks at company, regional and sector level given the different risks posed by climate change, other ESG factors, and reduction in managers investable universe. Any exclusions held by managers will be at their ‘house level’ and not part of the investment mandate. Manager selection would have been subject to Central’s selection and due diligence processes considering the managers commitment to ESG integration and engagement and the managers ability to deliver on those commitments.

26. Managers approaches will need to be scrutinised and will form part of long-term monitoring of managers, to ensure they consider climate risk and opportunity not only at a high level, but as part of all financial considerations. This will include understanding managers own commitments which the Fund must hold them to or engage with them to become more ambitious. This will be an ongoing and evolving process in line with best practice as it emerges. By challenging managers on these issues, the Fund can ensure they are appropriately considering climate risk on a case-by-case basis, rather than considering it as a ‘technical’ issue where the Fund expresses its own exclusion or trigger point list.

27. The Fund has set out explicitly within the Implementation Plan how it intends to monitor managers, in line with what was agreed as part of the 2023 Responsible Investment Plan.

28. At its meeting on the 18 November, the Committee agreed to the consultation subject to members consideration of the summary document. Following the meeting the documents were shared with members, some of whom fed back comments to officers which were taken on board and adjustments to the summary report were made, primarily related to areas where confusion could be created given lack of context from the wider NZCS. The changes did not substantially change the tone of the summary document.

<u>Findings of the Net Zero Climate Strategy Consultation</u>

29. The consultation ran from 21 November to 5 February 2023 using the County Council’s ‘Snap Survey’ tool. The consultation sought the views of a wide variety of stakeholders including scheme members (active, deferred and

retired), employers and investment managers. Responses were also received from other interested parties. A report of the outcome of the consultation is attached as Appendix C.

30. The following steps were taken to ensure scheme members and Fund employers had sufficient opportunity to respond to the consultation:
    - Multiple emails to circa 40,000 scheme members (that the Pension Service held email addresses for) with a link to the consultation.
    - The consultation information was available via the Pension Fund's website and was highlighted on the main page.
    - All employers were sent Employer Bulletins highlighting the engagement and asking them to respond and share the consultation with their staff. They were also reminded as part of emails highlighting the Investment Strategy Statement and Funding Strategy Statement.
    - A presentation was provided as part of the Fund's Annual General Meeting.

31. The Local Pension Board considered the draft NZCS on 8 February 2023. Comments raised during the meeting related to:
    - Risk to the Fund and employers if it removed exposure to fossil fuel entirely, and the importance of the Fund maintaining appropriate diversification of its assets. Noting it was important to manage the transition in an orderly fashion.
    - Questions on how the Fund can monitor the financial impact from changes made in line with the NZCS, and impact on employer contributions. The Board were assured that this formed part of how the Fund regularly reviewed its Investment Strategy and Strategic Asset Allocation.
    - Contact Board members received with regard to the Fund's investment strategy, and the future ability to point people to the NZCS as a key document which would likely answer the majority of questions which arose.

32. While not part of the Fund's formal process, it is also worth highlighting that Climate Action Leicester and Leicestershire provided their own briefing materials, and briefing sessions to interested parties, as well as held stalls alongside UNISON, and an interview with Demon FM (De Montfort Universities student radio station). Points specifically raised by Climate Action Leicester and Leicestershire through their formal response have been referenced within the outcome report and fed into changes made to the NZCS alongside other consultation responses.

Responses to Consultation

33. Recognising feedback from the initial engagement undertaken in summer 2022 with regard to the complexity and length of the questioning, the consultation exercise was based on three key questions. In total 747 online

consultation responses were received, as well as one paper copy. The breakdown of responses is set out below, with further detail provided as Appendix C.

	Respondents	Organisation if applicable
Deferred	90	
Retired or dependant	296	
Active Member	337	
Employers	3	Leicestershire County Council, North-West Leicestershire District Council, and the Open Thinking Partnership
Resident of Leicester, Leicestershire, and Rutland	20	
Local business or organisation	1	UNITE Leicester City Branch
Other	1	
Total	**748**	

34. Climate Action Leicester and Leicestershire submitted separately their response which received support from 20 groups ranging from religious groups to trade union branches, and community/resident groups. They also submitted an open letter that had 120 (47 of which were scheme members) supportive signatures. Documents submitted by Climate Action Leicester and Leicestershire were considered and attached as part of Appendix C.

To what extent do you agree or disagree with the draft Net Zero Climate Strategy?

35. 748 responses were received, of these, 23 did not know, 92 neither agreed nor disagreed. 261 strongly agreed, 223 tended to agree, 37 tended to disagree and 114 strongly disagreed, which showed the majority of respondents agreed with the Strategy (65%), and 20% disagreed. Respondents were then able to expand on their view if they wished.

Why do you say this?

36. 433 individual comments were received. Each was reviewed and all the relevant comments were identified and recorded. The key themes are set out below, more detail on the Fund's response is set out in Appendix C, and within 'Changes to the NZCS' detailed elsewhere in the report. It is clear from these that while the majority support the NZCS, there are also polarised opinions that call for more ambition, or that climate change is not a relevant factor for the Fund to consider.

Theme	**Comments**	**Appendix C Reference**
Supportive Comments	214	1
That the NZCS should be more ambitious.	60 (including 29 referencing divestment)	1.1
Climate change is not applicable.	53	1.2
The Fund must protect investment returns as the key priority.	50	1.3
Limited by other factors (i.e., government commitments, lack of sustainable materials involved in the transition)	23	1.4
Did not know, felt they did not understand, or did not have a view.	20	1.5
Other comments were also received related to, offsets, local investment, diversification, and ethical investment.		1.6

<u>What if anything is missing from the Net Zero Strategy?</u>

37. 318 individual comments were received on this question, many of which were cross cutting and related to similar themes discussed above. The key themes are set out below, more detail on the Fund's response is set out in Appendix C, and within 'Changes to the NZCS' detailed elsewhere in the report.

<u>Theme</u>	**<u>Comments</u>**	**<u>Appendix C Reference</u>**
Supportive comments or stating no/nothing is missing.	86	2.1
That the NZCS is fundamentally wrong by its existence due to not believing climate change is applicable to the Fund.	44	2.2
That the NZCS needs to be more ambitious. These comments were cross cutting and included points raised by Climate Action Leicester and Leicestershire. These are taken in turn below given some comments addressed multiple issues:	71 (25 specifically referenced divestment)	2.3
Too few specific requirements to stop investing in companies (fossil fuel producers, banks, and insurance companies) which persist in developing new fossil fuel reserves.	These make up the above referenced 71 responses, many of which are	2.4
Divest from companies (fossil fuel producers, banks and insurance companies) which persist in developing new fossil fuel reserves.		2.5
Lacking requirements for companies the Fund		2.6

invests in to need specific effective CA100+ measures, and clear escalation and actions the Fund will take if they fail to meet these requirements.	cross cutting.	
Use of the Fund's power to push government for effective climate legislation by public ending investment in fossil fuel companies, therefore removing social license/public support for the development of new oil gas and coal reserves.		2.7
Mechanism for local business and organisations to apply for investment in carbon reduction and fuel poverty reduction projects.		2.8
Other points related to setting more ambitious targets and measures, by time targeted or asset class coverage. Additional interim milestones. As well as reference to Climate Action Leicester and Leicestershire's submission as part of the July-September 2022 engagement.		2.9
Comments linked to specific investment points such as (20): • Investment returns should be the key focus for the Fund • Not investing in very risky low carbon projects • Identification of alternative energy sources for investment and new technologies as they become available	39	2.11
Other comments that related to aspects of the Strategy such as whether alternative options had been considered, the importance of a diversified approach. How the Fund would manage risks and impact on investment returns and how this would be reviewed.	44	2.12
Do not know, or did not know enough to comment, or felt that the NZCS needed to be simplified.	26	2.13

38. There were also some more specific comments concerning how the Fund will review, partner with others, take action give limitations, and other reference which were also considered as part of the review and changes to the draft NZCS.

Do you have any other comments or suggestions about the new Strategy?

39. 196 substantive individual comments were received in this question. Many of them reflect the previous question. The key themes are set out below, more

detail on the Fund's response is set out in Appendix C, and within 'Changes to the NZCS' detailed elsewhere in the report.

Theme	Comments	Appendix C Reference
That the NZCS should be more ambitious. Including those referencing CALL document.	45	1.1, 2.3, 2.4,2.5,2.6, 2.7,2.8, 2.9, 2.10 and 3.1
Supportive comments	29	3.2
Climate Change not applicable	38	1.2
Investment comments related to investment returns, specific investments in certain sectors, new technology and not making decisions to the detriment of the Fund.	36	3.4
Other comments on the Strategy including how Fund will review the NZCS, concerns related to offsetting, limitations on the Strategy, partnership working.	23	1.6, 2.12
Comments related to the need to simplify the NZCS	10	2.12

40. While not a point raised specifically within the online consultation replies it is worth responding to the view raised by Climate Action Leicester and Leicestershire that the NZCS discriminates against younger scheme members. The NZCS aligns with the Fund's Investment Strategy Statement in that it takes a long-term investment outlook and takes account of all risks in a managed way and to reduce key risks to the Fund over the long-term. Given advice received from Hymans Robertson, and the process of following best practice of the Institutional Investors Group for Climate Change the NZCS is considered to be in line with the Fund's fiduciary duty. The Strategy supports the Fund in ensuring employer contributions remain affordable. This is important given employers own work engaging in socially positive activities in Leicester, Leicestershire, and Rutland.

41. Regarding points raised regarding offsetting. Officers have rescheduled the presentation that was due to be considered by the Pension Committee in September 2022 (which was subsequently cancelled) to the meeting in June 2023. This presentation will contain information on how Stafford Capital receive assurance on the offsets given concerns in the media, around the concept of additionality of carbon offsets, and carbon offset standards.

<u>Summary of changes made to the draft Net Zero Climate Strategy</u>

42. The table below summarises the changes made to the draft NZCS in response to consultation responses set out within Appendix C.

43. In addition to the changes made, the Fund has produced an associated implementation plan, which includes the key questions that will be put to Investment Managers. These reflect the actions and approach to climate risk management set out in the NZCS. The plan is a live document which will be updated in line with developments of partners and best practice.

Related Theme	**Summary of changes made to NZCS**	**App C ref**
Ambition / Targets	a) Added Implementation Plan to set out key actions to be undertaken and timescale. Including plan to include future asset classes, and reference within NZCS. b) Added reference to the high level of support from the engagement on the targets and measures has been added to the foreword. c) Added current coverage of material companies with net zero targets, as well as requirement to set alignment targets to ensure companies are credibly aligning to their targets. d) Expanded text under financed emission alignment target to reflect the above importance of a classification system that can provide the best assurance that underlying companies are setting credible plans. As well as emphasis that the targets will help inform the approach to engagement and escalation. e) Inclusion of high-level progress on summary page.	1.1, 2.9
Monitoring progress, Reporting	f) Included reference on how the Fund intends to measure progress towards both financed emissions, and companies within material sectors alignment using best practice. g) Inclusion within the Implementation Plan of how the Fund intends to benchmark its managers. Further highlighted within the risk and opportunities section. h) Removal of image of indicators included in IIGCC framework (the CA100+ indicators), and inclusion of further expansion of the desire for the Fund to use best available information. i) Added wording that the climate snapshot does not take into account wider factors, that must be considered as part of wider approach to evaluation and confidence in managers climate risk approach.	2.6
Approach to Engagement, Stewardship and Divestment	j) Emphasised that the Fund views engagement and divestment as proven and necessary elements of an effective approach stewardship, and are not mutually exclusive. k) Clarified the Fund will look to use best practice in evaluating underlying companies. Including	1.1, 2.4,2.6

	supplementing data using alternative tools, that can report whether companies expected future emissions intensity pathways are credible. l) Emphasis of the importance of companies setting relevant targets, which are aligned to credible plans as part of the relevant targets and stewardship section. m) Strengthened approach to evaluating, engaging with Investment Managers. n) Expanded reasoning on why divestment of high carbon emitting companies alone would not impact real-world emissions. o) Expanded section on divestment and the approach the Fund will take in relation to its investment managers, consideration as part of the SAA, and expectations of managers where it holds material concerns. p) Inclusion of key points as part of implementation plan. q) Inclusion of the Fund supporting a just transition in line with the Glasgow Climate Pact.	
Climate Change not applicable to the Fund	r) Strengthened section on why climate risk is important for the Fund. s) Included action within Implementation Plan regarding improving communication to scheme members.	1.2
Investment points, such as investment return are the Fund's priority	t) Added further emphasis to the Fund's approach and reference to fiduciary duty and Investment Strategy Statement, throughout NZCS. u) Included within implementation plan purpose of review and considering any future triennial valuation. v) Included further reference to ensure scheme members that their benefits are not impacted by investment returns. w) Further emphasis on any investments made following due diligence and advice from Investment Advisor. x) Further reference of investment actions to be considered as part of implementation plan. y) Amendment of case studies of the Fund's investments in renewables and highlighting alternative investments the Fund will consider.	1.3, 2.11, 3.4
Limited by actions/inaction of other	z) Updated limitation section within NZCS, reflecting global limitations and the UK's position. aa) Further emphasised the need for partnership working. Including reference to consideration of joining appropriate groups as set out in RI Plan and included in the Implementation Plan.	1.4

Other	bb) Formatting and design changes to ensure document are legible and easy to navigate, including additional links to documents such as the ISS. cc) Reduced complexity where possible, and examples of actions that could be taken, such as with the Strategic Asset Allocation. dd) inclusion of implementation plan to show short term, medium term, and long-term actions, and grouped into clear sections on general actions, investment actions, stewardship actions. ee) Revamped glossary. ff) Updates to reflect completion of COP27, the outcome of the Fund consultation, latest Fund summary valuation, and that the Fund will take into account Government requirements on the LGPS that arise from the TCFD consultation late 2022.	1.5
Communication	gg) Added reference to communication of how the Fund manage climate risk, and performs against the Strategy to key stakeholders, including scheme members. Incorporated into implementation plan.	1.2,1.3, 2.11
Partnership working	hh) Extends reference to working with partners, or other external organisations, including specific partners such as LGPS Central, LAPFF, Investment Managers, Hymans Robertson. ii) Inclusion of partnership support within implementation plan where reliant on LGPS Central reporting, were work with investment advisor, other managers, or joining any appropriate group.	2.12

44. The resulting Net Zero Climate Strategy and Implementation Plan have been appended to this report as Appendix A and B respectively. The Implementation Plan sets out all the actions the Fund will undertake to achieve its goals. These are all actions that build on the NZCS, consultation responses, and Responsible Investment Plan 2023.

Next Steps

45. Subject to approval of the Strategy, officers will begin work on actions set out in the Implementation Plan. Key aspects include, but are not limited to:

- Requiring managers to complete the appended manager questionnaire as of 31 March 2023. This will enable the Fund to better understand which of its managers are managing climate risk well, and which require further discussion and engagement.

- Communicating the NZCS to key stakeholders. Including revamping the Summary version that was part of the consultation exercise.

- Working with LGPS Central to develop the current approach to reporting on climate risk in line with the NZCS. As well as engaging with Central to set its own operational Net Zero target.

- Working with Hymans Robertson to take into account key considerations of this Strategy in any new investment proposals to the Investment Subcommittee, and implementation within future work on the Strategic Asset Allocation.

- Review relevant strategies and Fund documentation including the Risk Register to align with the NZCS and entrench the approach throughout all Fund actions.

46. Progress will be monitored on a regular basis, including a commitment to continue to produce annual public reports on the Fund's Climate Risk and what it is doing with its partners such as LGPS Central, the Local Authority Pension Fund Forum, Hymans Robertson and Investment Managers to address risks and opportunities.

47. The Fund will review the NZCS and targets at least every three years and monitor progress annually as part of the Climate Risk Report. This will be supported through other Fund documents such as the Strategic Asset Allocation, Investment Strategy Statement, Funding Strategy Statement and risk register.

Responsible Investment Plan 2023

48. As per the Responsible Investment plan agreed January 2023, the Fund will report quarterly on voting and engagement.

49. The Fund has a longstanding policy of delegating voting and stewardship activities to its investment managers, with the view that well run companies protect and increase shareholder value by engaging on a range of financially material Environmental, Social and Governance (ESG) investment factors.

50. This is implemented through the Fund's equity managers LGPS Central (in contract with EOS at Federated Hermes) and Legal and General Investment Manager. As well as the Local Authority Pension Fund Forum (LAPFF) a group comprised of 85 funds and seven pools with combined assets of over £350billion, which is consequently able to exert significant influence over companies in which funds are invested. Some highlights are included below.

Voting

51. Appendix D includes the Fund's voting report covering the period October to December 2022. A brief breakdown is included below:

i. The Fund made voting recommendations at 761 company meetings, 5810 resolutions.
ii. At 373 of these company meetings, the Fund opposed one or more resolutions.
iii. The Fund voted with management by exception at six meetings and supported management on all resolutions at the remaining 380 meetings.
iv. The majority of votes where the Fund voted against management, or abstained on resolutions (3126) were related to board structure (44%), renumeration (17%), audit and accounts (10%), capital structure and dividends (10%)

Engagement

52. Voting is just one of the tools available to the Fund to encourage better corporate behaviour on environmental, social and governance factors. Which often goes hand in hand with stewardship. The Fund's approach to engagement takes a long-term perspective, a highlight of some of the latest actions and outcomes are set out below. The full report is appended accordingly.

	Company	**Theme**	**Action**	**Outcome/Next Steps**
LAPFF	Renault	Responsible Mineral Sourcing	Engagement with electric vehicle manufacturers to gain a better understanding of how they are addressing the risks associated with sourcing the minerals they need to produce the batteries for their vehicles.	Met with Renault for the first time, which covered an overview of Renaults work on risk assessments for the minerals it sources, and contingent reporting was discussed, including raising potential benefits of membership of Initiative for Responsible Mining Assurance.
LGPS Central (App E)	Barclays	Climate Change	Letter explaining why voted against their Climate Strategy as May 2022 AGM. Further engagement alongside other investors.	Commitment to prepone the deadline to phase out financing of US thermal coal power generation from 2035 to 2030. To take effect at the time of their year-end climate update and aligns approach to UK and EU. Central will continue engagement on climate transition, and targets to reduce absolute emission in the period to 2030.
LGIM	Capricorn	Climate, Governance and M&A	Direct Communication with Capricorn Management following announcement Capricorn were looking to merge with other energy companies. Raising concerns above	LGIM asked detailed questions regarding process. Capricorn initially proceeded with the merger, before a decision was taken to abandon it citing concerns about market conditions and external factors.

			governance and decision-making process, given it did not seem to advance the energy transition, and increased financial leverage and elevate climate transition risks.	

Current Developments

53. **Say on Climate**: Ahead of the 2023 AGM season LAPFF, alongside others wrote to chairs of all FTSE listed companies (excluding investment trusts) requesting that companies allow for a shareholder vote on their greenhouse gas emission reduction strategy. This aims to enhance transparency and accountability on one of the most financially material risks facing investee companies. The letter further urged all companies to disclose their transition plans aligned to 1.5C and allowing investor oversight on the robustness of plans through a vote on the strategy and any associated capital expenditure requirements.

54. **Shell Derivative Action:** As mentioned by LGPS Central at the January 2023 meeting Central had considered joining the derivative action brought forward by Client Earth on behalf of shareholders of Shell, to argue alleged breaches of duty by the Board.

    Following a thorough assessment of potential risks and benefits of supporting the claim, meeting with Client Earth, Shell, external managers, and pension fund peers, they subsequently decided not to join the action. Instead considering the significant overlap between the points raised in the Client Earth claim, and Central's own engagement objectives with Shell, Central have supported the claim through offering a copy of a recent engagement with Shell to the Court as evidence of Central's concerns. This was submitted in acknowledgement of the alignment between the fundamental objectives of the claim and LGPS Central's and partner funds own engagement expectations for Shell.

    It is with this that Central hope that given the increasing urgency of developing and committing to meaningful transition strategies, that the significance of the escalation will be recognised and stimulate a genuine improvement in transition strategies both at Shell, in the oil and gas sector more broadly, and in the wider market across sectors. The full press release is available here: https://www.lgpscentral.co.uk/an-engagement-update-from-lgps-central-shell/

55. **LGPS Central Core/Core+ Infrastructure Partnership**: The Fund committed £100m to the LGPS Central Core/Core+ Infrastructure Partnership which invests in infrastructure funds across the core/core plus space. As of the most

recent update the Partnership has made a number of such investments which include:

- A global fund focussing on core renewable and energy transition assets with a view to accelerating the world's transition to net zero greenhouse gas emissions.
- A UK focussed solar and battery storage assets developer.
- A fund focussed on investing in core UK infrastructure specifically targeting social, renewables, transport, and utilities assets.
- A global open-ended infrastructure fund targeting a diversified portfolio of critical OECD based core infrastructure investments.
- A fund focusing critical core infrastructure investments through an open-ended structure with a buy and hold strategy delivering returns substantially through long-term income generating assets.
- A global fund focussing on availability based Public Private Partnerships, renewable energy investments, energy transition assets and utilities.
- A European and North American focussed infrastructure fund focusing on brownfield infrastructure companies within energy & utilities, digital and transport & logistics sub-sectors.

56. Officers are aware that on 22 February 2023 Hinckley and Bosworth Borough Council voted in favour of a motion calling for the Fund to divest from fossil fuel companies by 2030. Following formal receipt of the motion, and the conclusion of this meeting, the Director of Corporate Resources will respond, following consultation with the Chairman. The supporting information included within the motion did not provide any new information requiring any changes to the Net Zero Climate Strategy.

Recommendations

It is recommended that:

a) The outcome of the public consultation on the draft Net Zero Climate Strategy (NZCS) be noted;
b) The amended NZCS be approved;
c) Subject to b) above, the associated implementation plan and manager questionnaire be approved;
d) It be noted that the Director of Corporate Resources may use his existing delegated authority to make minor amendments to the Strategy and associated documents in order to ensure the documents remain fit for purpose;
e) The update on the Responsible Investment Plan 2023, including update on voting and engagement, be noted;
f) It be noted that the Director of Corporate Resources, following consultation with the Chairman, will respond to Hinckley and Bosworth Borough Council's motion calling for the Fund to divest from fossil fuel companies by 2030.

Background Papers

26 November 2021 – Local Pension Committee - Responsible Investing Update

25 March 2022 – Local Pension Committee – Responsible Investing Update

10 June 2022 – Local Pension Committee – Responsible Investing Update

18 November 2022 – Local Pension Committee - Outcome of Engagement on Net Zero Climate Strategy Targets and Draft Strategy and Responsible Investing Update and Climate Risk Report 2022

20 January 2023 – Local Pension Committee - Responsible Investment Plan 2023

Equality and Human Rights Implications

The NZCS is a high-level strategic document and there are no direct Equality and Human Rights implications. The Fund takes into account issues around Equality and Human Rights as part of its whole approach to responsible investment and environmental, social and governance factors in all investment decisions. The Fund will not appoint any manager unless they can show evidence that responsible investment considerations are an integral part of their decision-making processes. This is further supported by the Fund's approach to stewardship and voting through voting, and its approach to engagement in support of a fair and just transition to net zero.

Environmental Implications

The Net Zero Climate Strategy outlines the high-level approach the Fund is taking to its view on Climate Risk. This will align with the Fund's Responsible Investment approach as set out in the Principles for Responsible Investment. As set out above the Fund is committed to supporting a fair and just transition to net-zero.

Appendices

Appendix A – Draft Net Zero Climate Strategy

Appendix B – Implementation Plan and Manager Questionnaire

Appendix C – Net Zero Climate Strategy Consultation Outcome

Appendix D – Voting Report

Appendix E – LGPS Central Stewardship Update

Officers to Contact

Mr C Tambini, Director of Corporate Resources

Tel: 0116 305 6199 Email: Chris.Tambini@leics.gov.uk

Mr D Keegan, Assistant Director Strategic Finance and Property

Tel: 0116 305 7668 Email: Declan.Keegan@leics.gov.uk

Mr B Kachra, Senior Finance Analyst - Investments

Tel: 0116 305 1449 Email: Bhulesh.Kachra@leics.gov.uk

This page is intentionally left blank