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Responsible Investment News and Views

August 2021

Two issues have dominated conversations on stewardship recently: climate change and COVID-19. The former has hit news headlines with more extreme weather events, while pension funds are increasingly being challenged to do more, while the latter has highlighted the importance of the "S" in ESG, with diversity and working practices within firms coming under scrutiny.

Getting ready for TCFD

Regulation requiring pension schemes to embed climate governance and reporting requirements comes into force from October 2021 for the largest pension schemes, with the scope increasing to other pension schemes from October 2022 and LGPS funds also expected to fall into scope. Trustees shouldn't wait for the regulations to come into force to get ready for TCFD, and steps can be taken now to ensure that processes are properly embedded. Our interactive guide sets out the practical steps you can take to get your scheme ready for TCFD.

Understanding ESG and climate risks

Anyone involved in the management of pension schemes is usually well-versed in the traditional metrics used to understand the performance and risks of an investment. However, traditional metrics fail to adequately support decision-makers when considering the ESG and climate-related risks and opportunities within portfolios. With ESG and climate-related data increasingly available, you need to understand what this data is telling you and the actions you can take. Our paper, Climate Metrics: Chasing Rainbows, explains the benefits and limitations of monitoring climate metrics, and the actions that you can take to better understand your investments.

Engage your managers and make them more accountable

You may remember our practical guide to getting the most from your asset managers which set out a process you can follow to engage with your asset managers. We don't think engagement needs to be onerous – it can start with a simple question to help you understand your asset managers' processes. We think the best outcomes come from being specific in your questions and targeting individual assets or themes to build understanding. As implementation statements need to be published from 1 October 2021, and reports on significant votes and engagement activity need to be documented, we've highlighted some recent areas of interest in high profile companies around our core themes of climate change, working practices and diversity.

Support our Climate Impact Initiative

Hymans Robertson has developed and launched a new action group, the **Climate Impact Initiative**, to encourage pension providers to make climate friendly impact investment options available for all savers regardless of plan size. This initiative is aiming to grow the voice of asset owners and compel providers to address the needs of DC pension savers.

Supported by organisations including Make My Money Matter and Pensions For Purpose, the group is asking pension plan trustees and governance committees to register their support for the campaign to help make these positive, forward-thinking options available to their members. You can find out more details and sign up here.

Focusing on stewardship: Significant votes

Trustees need to consider what they regard as "significant votes" for the purposes of preparing their implementation statements, although there is a question mark over what counts as significant. For some trustees, the themes that they have set as part of their own responsible investment policy may be considered. Others may take guidance from their investment managers on what is relevant. Following our own key themes of climate change, working practices and diversity & inclusion, we summarise several key resolutions over Q2 and Q3 that could be considered by trustees:

Exxon: Director Elections (May 2021)
Engine No 1, a small activist investor, won three seats on the board of Exxon and intends to prepare the company for a more sustainable future, free from fossil fuels. The hedge fund, which owns a small stake in the oil major, launched a campaign in December 2020 and nominated four directors, aiming to add climate and low-carbon energy expertise to the board. This was the first climate-related proxy contest to oppose the incumbent board of a company and the election of three directors demonstrated shareholders' ability to influence how firms such as Exxon address climate risks. Read our blog post on this issue here.

Shell: Say on Climate (May 2021)
At its May annual meeting, Shell's controversial 'say on climate' vote, which sought approval of its climate transition plan, was approved by 88.7% of shareholders. Shell's climate transition plans have been criticised by groups such as ShareAction and Follow This, for being overly reliant on a significant scale-up of carbon capture and storage. Despite this approval, at the same meeting, a significant portion of voters also supported a shareholder resolution seeking revised emissions reduction targets due to their inadequacy. This target-related resolution received 30.4% support, over double the support it received at Shell's 2020 annual meeting.

Proposals calling for diversity disclosure
As You Sow, an activist NGO, filed proposals with 20 US companies calling for reporting on diversity and inclusion efforts and the effectiveness of diversity, equity and inclusion programmes. The proposals follow a study by McKinsey which shows companies with strong racial and ethnic diversity are more likely to have financial returns above their industry medians. Companies targeted include American Express, Berkshire Hathaway and Tesla. Proposals at two companies – American Express and Union Pacific – were passed with the resolution at Union Pacific receiving 81.4% support. A similar proposal will be voted on at Nike's September AGM. These proposals show the influence voting activity can have on the diversity of a company's entire workforce, which has been shown to improve ideas, staff retention and enable a company to achieve a broader consensus, which in turn improves corporate success.

Worthington Industries: Say on climate (Sept. 2021)
At the company's September meeting, a shareholder proposal will ask the US metals manufacturer to adopt "say on climate". The proposal asks the company to issue a report evaluating whether and how they intend to revise policies to be fully responsive to Climate Action 100+'s Net Zero Company Benchmark. This benchmark outlines metrics that create climate accountability for companies and transparency for shareholders on greenhouse gas emissions and targets, climate governance and climate related financial disclosures.

Tesla: Resolution on arbitration
Tesla shareholders are asking the company, which currently requires employees to arbitrate employment-related claims, to prepare a public report on the impact of mandatory arbitration on Tesla's employees and workplace culture. The report will evaluate the impact of Tesla's use of arbitration on the prevalence of harassment and discrimination in its workplace and on employees' ability to seek corrective action when needed. Mandatory arbitration limits an employee's ability to act against wrongdoing, creates a culture of tolerated discrimination, reduces workforce effectiveness and creates risks to a firm.

Our engagement: focusing on working practices

Over the last quarter, we have had discussions with various equity asset managers on the issue of child labour in the cocoa industry. This engagement followed a lawsuit against several chocolate manufacturers. We concluded that while there was some evidence that managers had engaged on child labour issues, our interactions highlighted that disclosure is perhaps the primary risk management tool employed by asset managers to assess risk within supply chains. Engagement by managers is therefore most likely to be focused on boosting reporting and encouraging transparency, thereby allowing the broader scrutiny of corporate practices. Watch our short video on this subject for more information.

ESG snippets

Roadmap to net zero

The International Energy Agency ('IEA') published a landmark report in May setting out a roadmap for the global energy sector on what needs to be done, and when, to limit global temperature rises to 1.5 degrees Celsius and avoid the worst effects of climate change. Identifying over 400 milestones over the next 30 years, the report is a stark reminder of the systemic changes that are needed to meet global climate goals. Read our blog on this report here.

Why not ask your asset managers for their thoughts on this net zero scenario and the actions they are taking to position portfolios for change?

Consultation overload?

The financial services industry has seen a further influx of consultations as regulators and others seek to catch-up and get ahead of the significant industry focus on ESG and climate change issues.

The FCA published new proposals for climate-related disclosure rules for listed companies and regulated firms. The proposals seek to introduce TCFD aligned climate-related disclosure requirements for asset managers, life insurers, and FCA-regulated pension providers. They will also extend the application of the FCA's TCFD-aligned Listing Rule to issuers of standard listed equity shares.

Separately, The Pensions Regulator is consulting on draft guidance covering its approach to regulating the recently introduced governance requirements. The PLSA has also published proposals for a new "Responsible Investment Quality Mark" on which it is seeking views.

While regulation matters, there is a clear opportunity here for standardisation of approaches and language within the industry, rather than the proliferation of different standards and terminology which has plagued the responsible investment industry in the past. We will be reflecting this message in our own responses.

Collaboration for better stewardship

In July, the government announced the launch of the Occupational Pensions Stewardship Council ('OPSC'), set up off the back of 'Recommendation 16' within the Asset Management Taskforce's report, Investing with Purpose, which states a need for a dedicated council of UK pension schemes to promote and facilitate high standards of stewardship across pension scheme assets.

The OPSC, which is open to all UK pension schemes, intends to be a vehicle for setting stewardship best practice standards, working in alignment with the UK Stewardship Code's principles, and strengthening the voice of pension scheme trustees and scheme managers across the market. It will facilitate knowledge sharing across its members and enable collaboration stewardship with a long-term focus.

While the launch of the OPSC is a welcomed development, the message for trustees and other asset owners is clear: improve standards of stewardship and seek guidance on what can be done. *Have you considered how effective your own stewardship activity has been and what more you can do?*

Focusing on biodiversity

Looking beyond climate risks, biodiversity loss and ecosystem collapse are also seen as material financial risks and are rated within the top five risks over the next 10 years by the World Economic Forum. The Taskforce on Nature-related Financial Disclosure ('TNFD') was formally launched in June.

Building on the work of the TCFD, this initiative goes further by addressing other nature-related risks, including plastics in the oceanic food chain and loss of soil fertility. The TNFD will design a disclosure framework to help organisations address biodiversity-related risks and opportunities, aiming to complement the TCFD framework.

Is biodiversity a priority for you? If so, watch this space for more on what can be done.