Parliamentary Contributory Pension Fund (PCPF)
UK Stewardship Report

Contents

Foreword

The year 2020 has been a challenging year for the Fund, with the pandemic leading to unprecedented changes made to the way we work. Despite that, as a Board of Trustees we have maintained our commitment to responsible investment and good scheme governance. Having developed a Responsible Investment policy in 2019, this continued to be a primary consideration throughout 2020 as we looked for opportunities arising from a greater understanding of Environmental, Social and Governance (ESG) factors.

We remain committed to responsible investment and responding to climate change risks to our assets, and as part of this work developed a Climate Risk policy which was approved during the year. This policy outlines our approach to addressing climate related risks within the Fund. We also adopted a sustainable and low carbon approach to our passive equity assets, made an investment in a renewable infrastructure fund and have agreed to allocate further assets to an additional environmental or social infrastructure fund during 2021. We believe these changes will reduce the portfolio's carbon emissions intensity by at least half, without negatively impacting performance.

It is vital that we continue to monitor the voting and engagement activities of our equity managers, and we do this on a quarterly basis, at our Investment Committee meetings. During 2019 concerns over the voting practices of one of our managers was identified and during 2020 we took the opportunity to challenge the manager and requested they provide justification on some of their individual votes.

As asset owners, we welcome the introduction of the Financial Reporting Council's new UK Stewardship Code and see this as an opportunity to improve the transparency of our stewardship of the Fund and improve standards over time. We hope the report sets out clearly the work we have done over the year to integrate stewardship into our investment strategies.

Sir Brian H Donohoe
Chair of the Trustees of the PCPF

Introduction

1. The Financial Reporting Council (FRC) is the UK's independent regulator responsible for promoting high quality corporate governance and reporting. The 2012 UK Stewardship Code, published by the FRC, calls for greater collective action among shareholders and outlines 7 Principles for good stewardship practice. The revised UK Stewardship Code (the Code) took effect on 1 January 2020, setting out 12 Principles for asset owners. The Code sets a new higher standard for stewardship reporting for those investing on behalf of UK savers and pensioners. It defines stewardship as the responsible allocation, management, and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.

2. Under the revised Code, signatories are required to submit an annual report on stewardship activities and outcomes. This stewardship report works through each of the 12 Principles of the revised code in turn. It firstly sets out the FRC's definition of the principle, before going on to demonstrate how the Parliamentary Contributory Pension Fund (the Fund, or PCPF) has sought to apply each of these 12 Principles during the period from 1 January 2020 to 31 December 2020.

1. Purpose, strategy, and culture

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, the environment and society.

3. The Parliamentary Contributory Pension Fund (the Fund, or PCPF) is a statutory scheme that is made up of the MPs' Pension Scheme which provides benefits for MPs and certain office holders, and the Ministers' Pension Scheme which provides benefits for paid Government Ministers and certain office holders. The benefit structure of the MPs' Pension Scheme is determined by the Independent Parliamentary Standards Authority (IPSA) and the benefit structure of the Ministers' Pension Scheme is determined by the Minister for the Civil Service (MCS). It is important to note that Members of Parliament, office holders and Ministers are not employees. The payroll for MPs and office holders is handled by IPSA. The payroll for Ministers is handled by Government departments.

4. Given the purpose of the PCPF, the Trustees believe that it is paramount that the Fund's strategy reflects clearly stated objectives, beliefs, and robust responsible investment policy that will stand up to scrutiny from various sources. The long-term vision and overriding objective of the Fund is to ensure that its assets are invested in a manner which meets the need to pay benefits to members as they fall due. The Fund's investment strategy is guided by a set of investment beliefs, as documented in the Fund's Statement of Investment Principles, which is published on the PCPF website.[1]

5. Below is a summary of the Fund's key investment beliefs, which create a framework for the Trustees' decision-making:

Belief	**Further information**
Clear and well-defined objectives are essential to achieve future success.	The Trustees are aware that there is a need to generate a sufficient level of return from the Fund's assets, while at the same time having a clear understanding of the potential risks and ensuring there is sufficient liquidity available to pay members' benefits as they fall due.
Strategic asset allocation is a key determinant of risk and return, and thus is typically more important than manager or stock selection.	The Trustees understand that having the appropriate strategy in place is a key driver of the Fund's future success. As a result, priority is given to more strategic investment matters.
Long term investing provides opportunities for enhancing returns.	The Trustees believe that investors with long term time horizons are able to better withstand periods of price volatility. As a long-term investor, the Fund may choose to gain additional compensation by investing in assets that are illiquid or may be subject to higher levels of

[1] PCPF website in this report refers to https://www.mypcpfpension.co.uk/investments/.

	volatility (a premium return is required for any such investments).
The strength of employer covenant allows the Fund to take a long-term view of investment strategy.	The Trustees believe that the strength of employer covenant (the UK Government) means that the Fund can take advantage of the benefits associated with a long-term investment horizon, as set out above.
Equities are expected to generate superior long-term returns.	The Trustees believe that, over the longer term, equities are expected to outperform other liquid assets, in particular government bonds. The Trustees are therefore comfortable that the Fund maintains a significant target allocation to equities
Alternative asset class investments provide diversification.	The Trustees believe that diversification across asset classes can help reduce the volatility of the Fund's overall asset value and improve its risk-return characteristics. The Trustees believe that investing across a range of asset classes (including but not restricted to) equities, government bonds, corporate bonds, infrastructure, and property) will provide the Fund with diversification benefits.
Fees and costs matter.	The Trustees recognise that fees and costs reduced the Funds investment returns. The Trustees monitor the fees and costs of its investment arrangements to ensure the Fund is getting value for money and to minimise, as far as possible, any cost leakages from its investment process. The Trustees have undertaken industry benchmarking of the Fund's investment management fees and the funds overall costs and will continue to review this on a regular basis.
Passive management has a role to play in the Fund's structure.	The Trustees recognise that passive management allows the Fund to access certain asset classes (e.g. equities and bonds) on a low cost basis and, have over time increased the proportion of assets managed on a passive index tracking basis within the Fund.
Active management can add value but is not guaranteed.	The Trustees recognise that certain asset classes can only be accessed via active management. The Trustees also recognise that active managers may be able to generate higher returns for the Fund (net of fees), or similar returns but at lower volatility, than equivalent passive exposure. By carefully selecting and monitoring active

	managers, the Trustees seek to minimise the additional risk from active management. The Trustees will monitor active managers to ensure their mandates remain appropriate for the Fund.
Environmental, social, and corporate governance ('ESG') issues can have a material impact on the long-term performance of its investments.	The Trustees recognise that ESG issues can impact the Fund's returns, and the Trustees aim to be aware of, and monitor, financially material ESG-related risks and issues through the Fund's investment managers.

6. Responsible investment is at the centre of the Fund's investment philosophy. The Trustees recognise that their duty is to act in the best financial interests of the Fund's beneficiaries and they believe that ESG risks can have a material impact on the long-term performance of the Fund's investments. The Trustees have developed a stand-alone Responsible Investment Policy which continues to be a primary consideration when forming their forward-looking business plan. The policy is published on the PCPF website and explained further in this report under Principle 7.

7. The Fund's commitment to responsible investment continued to develop during the reporting period. In November 2020, the Trustees formalised a Climate Risk Policy which outlines the Trustees' approach to addressing climate related risks within the Fund. Through the policy the Trustees reaffirm their view that the Fund's primary objective is to ensure assets are invested in a manner which meets the need to pay members' benefits as they fall due. The Trustees acknowledge that climate related risks may negatively impact their ability to meet this objective and are particularly relevant for investors with long-term time horizons such as the Fund. The policy sets out the Trustees' ambition for all PCPF investments to be compatible with net zero emissions by no later than 2050. The full policy is available on the PCPF website.

Trustee Board values

In line with their investment beliefs and funding objectives, the Trustees agree the following statement of their culture and values:

"As a Trustee Board we are responsible for ensuring that the Fund's assets are invested in a manner sufficient to meet our overriding objective, which is to pay member benefits as they fall due, we aim to do this by maintaining a funding level of as least 100%.

Our Board is an open, transparent and inclusive body, which actively promotes the principles of equality, diversity and inclusion. Diversity amongst Board members is highly valued, and we recognise that when the board is comprised of individuals with a complementary range of experience and individual skills, this helps to improve our decision making and leads to better outcomes for our members.

Responsible investment is at the forefront of our investment philosophy. We believe that investing in sustainable, well governed companies and practicing active stewardship will have a positive impact on returns in the longer term. We also value engagement, recognising that we can positively influence the behaviour and practices of our investment managers with regard to stewardship through ongoing and

forceful engagement, even where assets are invested through pooled funds. This is supported by our voting and engagement policy."

8. While the Trustees maintain overall responsibility for the management of the Fund, in practice they have appointed Officials from the Finance, Portfolio and Performance Team within House of Commons to provide a full secretariat and administrative service. Day to day management of the Fund is delegated to Secretariat officials.

9. The Secretariat staff are House of Commons (or 'House') employees and are therefore required to behave in line with House values. These values describe what House staff want their culture to be and help reflect how they work together to deliver a shared strategy and the vision 'Everyone has a voice'.

10. There are four values: Inclusive, Courageous, Trusted, and Collaborative. Each value is described by three supporting behaviour statements to expand on what they mean for how staff behave at the House of Commons.

Inclusive • We value everyone equally • We respect each other • We all have a voice	Trusted • We trust each other to do a good job • We are impartial • We build confidence in Parliament through our integrity
Courageous • We try new things • We own our actions and decisions • We learn from our mistakes	Collaborative • We share our knowledge and experience • We work towards a shared vision • We know we work better in partnership

11. All the above factors combined influence how the PCPF operates and feed into its business plan, which guides important decision-making such as choosing asset managers, setting stewardship expectations, and monitoring delegated activities (see Principles 7 and 8).

12. Below is a selection of activities that demonstrate how the focus on responsible investment is reflected in various aspects of the Fund's operation:

- Opportunities arising from a greater understanding of ESG factors (e.g., renewable infrastructure) are considered when setting investment structure.
- Responsible investment considerations are explicitly made for new mandates, including voting and engagement policies.
- Managers demonstrating weaker practices over sustained periods will not be considered for future appointments, and their appointment will be reviewed.

- Analysis of the Fund's carbon exposure and intensity will be considered where appropriate.
- The Annual Review includes an update on the Fund's stewardship and governance activities, including voting and engagement.

13. One example of integrating investment beliefs with investment decision-making are the steps taken by the Trustees to restructure the Fund's equity portfolio.

14. The Trustees carried out a review of the Fund's equity structure in 2020. As part of the review, the Trustees considered approaches expected to reduce the carbon emissions intensity of the equity portfolio, reflecting the Fund's objectives, beliefs and Responsible Investment Policy. After receiving training on alternative benchmark indices, presentations from industry partners and formal advice, the Trustees agreed to transition the Fund's index tracking regional equity portfolio to a sustainable multi-factor and low carbon index approach. This change is expected to reduce the carbon emissions intensity from the equity holdings by more than 50% relative to the current position. The transition is expected to be completed in early 2021.

15. To assess how effective the PCPF has been in serving the best interests of the beneficiaries, the Trustees regularly monitor investment outcome and measure success against the Fund objectives to:

- invest predominantly in long term growth assets reflecting the investment time horizon of the Fund
- achieve a rate of return over the long term that is at least equivalent to the assumed level of investment return used when calculating the long-term cost of the benefits
- maintain a funding level of at least 100% over the medium to longer term
- ensure that the Fund's assets provide sufficient liquidity to meet benefit payments as they fall due, and minimise the risk of forced selling
- manage the investments as efficiently as possible. It is anticipated that investment management costs (excluding performance related fees) should not exceed 0.4% of the Fund's assets
- have due regard to the risk of incurring large and sustained deficits in the future with resulting increases in contribution levels and reducing these risks where possible

16. The Fund's performance (net of fees) for the 3-year period to 30 June 2020 was 2.1% p.a. ahead of the assumed increase in long-term cost of benefits. The funding level as at 30 September 2020 was estimated to be 113.2% on the 2017 liability basis. With the exception of a 3-week period in March/April 2020, the funding level has remained above 100% since the 2017 actuarial valuation. The 3-week period where the funding dropped below 100% was driven by the extreme market volatility as a result of the COVID-19 pandemic. The proportion of income producing assets was increased in August 2020 with investment in a renewable infrastructure fund. The restructured equity portfolio increased management fees slightly but these remain below 0.4% of Fund assets.

17. The Trustees are satisfied that the Fund has been effective in serving the best interests of its beneficiaries and that the Fund's Responsible Investment Policy has been treated as a primary consideration throughout all relevant decision-making processes.

2. Governance, resources, and incentives

Principle 2 - Signatories' governance, resources and incentives support stewardship.

Governance structure

18. The PCPF is a funded, public service, trust based pension scheme, governed by a statutory framework under schedule 6 to the Constitutional Reform and Governance Act 2010 (CRaG). The rules of the Fund are set out in the following schemes made under that Act:

- an administration scheme, made by the Independent Parliamentary Standards Authority (IPSA),
- the MPs' Pension Scheme made by IPSA, setting out the benefits payable to and in respect of members of the House of Commons and certain officeholders, and
- the Ministers' Pension Scheme made by the Minister for the Civil Service (MCS), setting out the benefits payable to and in respect of Ministers and prescribed officeholders.

19. The provisions of CRaG prescribe various matters relating to the structure of the Trustee Board (such as the number and composition of Trustees), requirements for member-nominated Trustees and the Trustees' powers and procedures. In particular, it prescribes that the Trustee Board is made up of the following:

- 1 person appointed by IPSA, referred to as the "**IPSA Trustee**",
- 1 person appointed by the MCS, referred to as the "**MCS Trustee**", and
- 8 member-nominated Trustees.

20. Collectively, the ten Trustees of the Fund have a range of legal duties for the Fund as well as maintaining overall responsibility for the management of the Fund. It is the Trustees' fiduciary duty to oversee all aspects of the Fund to ensure that the Fund's assets are invested in a manner which meets their overriding objective to pay benefits to members as they fall due. The Trustee Board, supported operationally by the Secretariat, have oversight of, and overall accountability for, the Fund's effective stewardship.

21. The Trustee Board regularly meet for ordinary and for investment focused meetings to scrutinise how the Fund operates and address any emerging concerns. Since 2015 the Trustees have held three investment focused meetings per year, with an increased focus on investment stewardship. In 2019, the Trustees agreed to the Fund's Responsible Investment Policy, which sets out the Trustees' policy for incorporating responsible investment (including climate risk) considerations within the investment process. The policy also details the processes for reviewing the Fund's stewardship and investment policies (see Principle 5). Last year the Trustees made the decision to hold four investment focused meetings per year from 2021, which will further strengthen the focus on robust governance and active stewardship.

22. The Trustees recognise the importance of ongoing education on a broad range of investment matters, including responsible investment. Arrangements are in place to assess and address the ongoing training requirements of Trustees, to ensure that they keep up to date with new and current issues affecting the Fund's operations. Regular and relevant Trustee training sessions are arranged both during and outside of Trustee meetings. As part of their annual business planning, the Trustees ensure that at least one formal training session is directly focused on responsible investment. Training is sought from the Trustees' investment advisers, investment managers, legal advisers, external specialists and other

engaged pension funds to provide exposure to a range of opinions and approaches to effective governance. During the reporting period the Trustees focused their training on responsible investment. An ESG specific training session was held in January 2020. Other areas covered included changes to investment regulations and impact investing.

23. While the Trustees maintain overall responsibility for the management and stewardship of the Fund, in practice they have appointed Officials from the House of Commons to provide a full secretariat and administrative service. Support is provided through the Secretariat, part of the Members' Hub, within the House of Commons' Finance, Portfolio and Performance Team. The Secretariat team is led by Gurpreet Bassi, Head of Members' Hub, who also acts as Secretary to the Trustees.

24. The Trustees have a balance of powers document in place which sets out their responsibilities relating to the administration and governance of the Fund. The roles and responsibilities the Trustees have delegated to the Secretariat are set out in the Secretariat terms of reference.

25. The Secretariat report to the Managing Director of Finance, Portfolio and Performance. The Finance, Portfolio and Performance Team was created to support the House of Commons to be efficient, professional, and fit for purpose and is responsible for financial strategy and corporate business planning. Working in Finance, Portfolio and Performance is a natural fit for Members' Hub and has facilitated a closer working relationship between PCPF Secretariat and the Corporate Finance office, particularly the accounting team. This has increased in-House financial support and advice that is available to the Trustees.

26. Gurpreet Bassi is supported by two employees acting alongside the Secretary as the Secretariat team. Additional administrative support is provided by the wider team. In the past few years several non-pension functions previously held within Members' Hub were moved to other areas. This reduced remit allows the Head of Members' Hub to focus on the role of Secretary to the PCPF Trustees, a vital governance role in the Fund's structure.

27. The Trustees' Business Plan 2017-18 to 2019-20 sets out expected projects over three Fund years. During the reporting period, Trustees monitored regular reports provided by the Secretariat at Trustee meetings, on progress made in each area, including Secretariat performance. The new three-year Business Plan 2020-21 to 2022-23 was approved by the Trustees in March 2020. The focus of the new Business Plan is on improving service received by members, undertaking a governance review of Trustees' procedures and strengthening focus on investment stewardship and responsible investment.

<u>Resourcing/Incentives of stewardship activities</u>

28. The Trustees appoint professional external advisers to provide high-quality tailored investment and legal advice and services. Currently Hymans Robertson act as the Fund's investment consultant and Sackers its legal adviser. Their expert advice guides the Trustees' decision-making and covers a wide range of areas relating to pension schemes, including stewardship activities. Over the past year the advisers have been instrumental in supporting the Trustees with their expertise on key areas of stewardship such as:

- Drafting the Fund's new Climate Risk Policy;
- Guiding the Trustees in drafting and review of policies;
- Briefing Trustees on increased requirements of the new UK Stewardship Code;
- Recommending a restructuring to the Fund's equity portfolio in line with Trustees' responsible investment ambitions;

- Reviewing contractual terms and agreements in relation to the equity transition etc.;
- Discussing investment managers' quarterly voting and engagement reports with Trustees;
- Monitoring managers' adherence to Trustees' investment and stewardship policies and raising issues;
- Educating Trustees on recent responsible investment trends and drivers, ESG reporting/disclosure guidelines, and impact investing etc.

29. The Trustees require administrative support from the Secretariat team to ensure that the Fund is managed properly. Efficient operation of a pension scheme enables the Trustees to focus on the important issues, leaving sufficient time at meetings for key decision-making. As well as business as usual activity, there has been an increasing focus on strengthening scheme governance and enhancing active stewardship. Over the past few years, the level of engagement and external interest in the Fund and the Trustees' investments has increased , and this has had resourcing implications within the Secretariat team. To ensure that the team is appropriately resourced, a new role of Investment and Governance Specialist was appointed in May 2020 and has been a valuable resource to both the Trustees and the Secretariat. By increasing Secretariat support the Trustees have ensured that external advisers and suppliers are used in an efficient and appropriate manner, and that all parties are challenged if necessary. The new position also brings a level of investment expertise to the Secretariat and renewed focus on active stewardship.

30. The PCPF Trustee Board is made up of ten Trustees, eight are member-nominated Trustees, one appointed by IPSA, and one by the MCS. Currently three Trustees are serving MPs. All Trustees bring with them a breadth of knowledge and experience.

31. The Members' Hub has a diverse workforce and good female representation at management level. Gurpreet Bassi, Head of Members' Hub and Pension Scheme Secretary, is APMI qualified (Associate of the Pensions Management Institute). The team promote Continuing Professional Development (CPD) as part of ongoing personal development. The Secretariat team are members of industry-wide organisations such as the Pensions and Lifetime Savings Association (PLSA) and Pensions Management Institute (PMI), and are encouraged and supported by the management to participate in various industry forums, investment conferences, and e-learning to keep abreast of developments in areas such as stewardship and ESG. The team adopted the Coach and Focus approach launched by House of Commons in 2020 for performance and development. This new framework aims to reduce bureaucracy and put people before paperwork. Team managers look to nurture and retain talents through regular dialogues that are focused, unbiased, non-judgemental, committed and supportive.

<u>Effectiveness of governance, resources, and incentives</u>

32. The Fund's governance structure is explained under Principle 1.

33. The Fund's stewardship processes and commitments are reviewed regularly. In light of the increasing focus on investment stewardship, the Trustees have decided to increase the number of investment focused meetings from 2021.

34. The Trustees are supported by the Secretariat team within House of Commons. A robust governance and reporting structure exists between the Secretariat and senior management within the wider Finance, Portfolio and Performance Team. This arrangement is a natural fit and also facilitates a closer working relationship between the Secretariat and Finance professionals.

35. Overall, the Fund's governance structure has been effective in supporting active stewardship, with certain areas such as resourcing undergoing review and changes. As the PCPF is a taxpayer funded, public service Pension Scheme, the Trustees are careful in scrutinising their resourcing requirements. Resourcing papers are prepared and brought to ordinary Trustee meetings as and when business needs arise. Last year the Trustees made a decision to increase the resourcing of investment stewardship and appointed a PCPF Investment and Governance Specialist to provide additional support on investment matters, with a focus on ESG issues. This has been a valuable addition to the Secretariat team.

36. To continue to improve the Fund's governance framework, the Trustees aim to review services currently provided by their external advisers, including those in relation to stewardship, and examine whether certain activities are better carried out in-house. This will reduce external dependency, improve cost efficiency, and ensure that external advisers could be challenged where necessary.

3. Conflict of interest

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

37. The basic principle in relation to conflicts of interest is found in the High Court case of Re Thompson's Settlement [1986] where the Court held that: "…a man must not put himself in a position where duty and [personal] interest conflict or where his duty to one conflicts with his duty to another *unless expressly authorised"*.

38. The Fund encourages its investment managers to have effective policies that address potential conflicts of interest in relation to stewardship.

39. In respect of conflicts of interest within the Fund, The Trustees recognise that they need to be able to identify conflicts of interest, including those in relation to stewardship, and have procedures in place to manage and monitor them appropriately. The Trustees reviewed and updated PCPF Trustees' Policy and Procedure for Managing Conflicts of Interest, with effect from 16 January 2020, to manage potential or actual conflicts of interest that they may have in carrying out their functions in relation to the Fund. The policy is to be reviewed every three years and may be revised from time to time.

40. New Trustees are appointed under procedures that require them to disclose any conflicts of interest. New Trustees are also provided with a Trustee induction training pack which contains a copy of the Conflicts of Interest policy, as well as other information about the Fund and their new role as a Trustee.

<u>Background to the policy</u>

41. In preparing the Conflicts of Interest policy, the Trustees are mindful of the importance of effective and efficient pension scheme governance and in particular of recent developments in the context of managing conflicts of interest, including:

    - guidance issued by the Pensions Regulator - though the Fund is not regulated by it,
    - the requirements under the Public Service Pensions Act 2013 on certain other public service pension schemes to ensure that their pension board members do not have a conflict of interest - the Fund is not subject to the governance provisions of that legislation and the circumstances of the Fund differ in many respects from those other schemes, and
    - the principles set out in the UK Stewardship Code issued by the Financial Reporting Council

42. Although no new material conflicts of interest were declared by the Trustees during the reporting period, they have identified the below indicative examples of other roles and responsibilities, which may give rise to a potential conflict in relation to investment stewardship:

    - a Trustee may have roles or responsibilities from employment, private business or personal interests (outside of their membership of the Houses of Parliament),
    - a Trustee may have a financial interest in an existing or potential Fund investment or fund manager,
    - a Trustee may have views regarding the Fund's investments based on their personal beliefs.

43. In respect of other roles and responsibilities, individual Trustees may have obligations to declare and manage conflicts of interest. For example, Trustees who are members of the House of Commons must

comply with the Code of Conduct approved by the House which includes requirements for members to declare interests and to register certain financial interests (and that register is publicly available).

44. Where a Trustee is an active political campaigner, s/he may have a predetermined interest in the outcome of Trustee deliberations. If that is the case, s/he should consider whether there is a conflict of interest, and if there is make a declaration in line with the policy.

45. The Trustees understand that they are fiduciaries and as such have a duty to safeguard the interests of the Fund's beneficiaries. However, this does not preclude any of them from having other roles or responsibilities which may result in a potential or actual conflict of interest with their role as Trustees.

46. Although these do not apply to the Fund, the Trustees have endorsed the Pensions Regulator's guiding principles in relation to Trustees' own conflicts of interest, which can be summarised as requiring Trustees to:

- understand the importance of conflicts of interest, particularly the need to exercise independent judgement and to be perceived to be doing so,
- identify conflicts (potential and actual), including maintaining a record of each Trustees' relevant interests,
- implement procedures to evaluate, manage and avoid conflicts in a way that ensures decisions are not compromised by conflicted Trustees; encourage a culture of openness where conflicts are disclosed and appropriately managed rather than ignored, and
- agree and document a policy (or procedures) for identifying, managing, and monitoring conflicts.

Conflicts of Interest policy and procedures

47. The Trustees have agreed that they must:

- acknowledge any potential conflict of interest they may have,
- be open with each other on any conflicts of interest they may have,
- adopt practical solutions, and
- plan ahead and agree on how they will manage any conflicts of interest which arise.

48. With these objectives in mind, the Trustees have adopted the following procedure:

- at the commencement of meetings of the Trustees (or any sub-committees they establish), each Trustee is required to declare to the meeting any potential or actual conflict of interest that s/he may have in respect of the business of the meeting, and
- a record of Trustees' declared interests will be made in the relevant meeting minutes.

49. It is the responsibility of:

- each Trustee individually to consider whether, in carrying out any of their functions as Trustees, they may have a potential conflict of interest, and
- the Fund secretary, in consultation with the Fund's Secretariat, to seek to identify any potential conflicts of interest, particularly when preparing the agenda for Trustees' meetings.

50. In each case the person responsible must, where practical, advise the Chair of any potential conflict issues relevant to the business of the meeting (limiting detail if necessary, to avoid placing the Chair in a similar position of potential conflict) prior to any relevant meeting. If it is not practical to advise the Chair in advance, the person responsible must state the potential conflict issue clearly at the outset of the meeting itself. Where the Chair is advised of a potential conflict and the relevant person responsible does not state it at the relevant meeting, the Chair must disclose its existence to the Trustees.

51. It is for the Chair to decide on the action (if any) required to manage a potential conflict of interest and to advise the Trustees of any actions taken. In taking that decision, they may have regard to such factors as they consider relevant, including (but not limited to) the perception of Fund members or other Fund stakeholders.

52. Where a conflict is identified outside of a Trustees' meeting, the Chair will consult with the Fund Secretary or the Fund's Secretariat prior to making a decision. Where the conflict is identified at a Trustees' meeting, the Chair will consult with the other Trustees prior to making a decision. In either case, the Chair may additionally consult with any of the Trustees, the Fund secretary, the Fund's Secretariat, or any appointed professional advisers as s/he sees fit.

Managing a conflict of interest

53. Steps that may be taken to manage a conflict might include (but are not limited to): a decision being delegated to a sub-committee of the Trustees which does not include the conflicted Trustee; or the conflicted Trustee being required:

- to leave the meeting during, or refrain from contributing to, the discussion on the conflicted matter,
- to withdraw from voting on the conflicted matter, and/or
- to draw to the attention of the other Trustees that s/he holds information that may be confidential to another party that is relevant to the discussion or decision (without being required to disclose that information where the Trustee owes a duty of confidentiality in respect of that information or to that other party).

54. Where steps are taken to manage a conflict of interest, the existence of the conflict and the action taken will be recorded in the relevant meeting minutes.

Investments

55. The Trustees recognise that with an increased focus on responsible investment matters, there is a potentially greater scope for individual Trustee views regarding some aspects of the Fund's investments to conflict with Trustee fiduciary duties when setting the Fund's investment strategy and reviewing investment options.

56. Trustees should note that where there is a financial interest, they must declare a conflict of interest. However, Trustees may have an 'interest' other than financial gain which may need to be declared as a potential conflict of interest.

The IPSA Trustee and the MCS Trustee

57. The Trustees recognise that, for each of the IPSA Trustee and the MCS Trustee, the risk of a potential conflict of interest may be particularly acute. For example, a potential conflict may arise:

- in respect of the IPSA Trustee, given IPSA's obligations to determine MPs' pay and pensions; its oversight function in relation to the Fund; and its functions under the Fund's rules relating to its administration and management, and
- in relation to the MCS Trustee, given the powers exercisable by the MCS under the Fund's rules; and any knowledge of, or responsibility for, implementing Government policy relating to public service pension provision.

58. The following additional procedures therefore apply in respect of each of the IPSA Trustee and the MCS Trustee:

- where the Trustee wishes to speak from the view of IPSA or the MCS (as appropriate), s/he must state this clearly at meetings and have this recorded in the minutes, and
- the Trustee will not participate in voting or take part in decision-making where there is an actual conflict. An example would be voting in respect of a decision of the Trustees in the exercise of their functions as statutory consultees to an IPSA consultation relating to the MPs' Pension Scheme, where the IPSA Trustee is privy to information (that is not disclosed to the Trustees) about, or responsible in whole or in part for, the setting of IPSA policy in relation to the determination of MPs' pay and pensions.

4. Promoting well-functioning markets

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

59. The Secretariat maintain the PCPF Risk Register to help identify key risks the Fund is faced with, monitor their likelihood and impact, and document mitigations to be put in place. This includes market-wide and systemic risks. The Risk Register is updated quarterly and during the reporting year was taken to ordinary Trustee meetings for discussion.

60. As of December 2020, the two top residual principal risks (after mitigation efforts are taken into consideration) are failure to provide expected returns due to impact of climate change or other significant market uncertainties, and operational disasters such as the pandemic.

Response to COVID-19

61. The year 2020 has certainly been a challenging one for the Fund, as COVID-19 has changed the way we live and work. As soon as the pandemic was identified as a major systemic risk to the running of the Fund, the Trustees and Secretariat worked swiftly to ensure effective measures were taken to mitigate this risk.

62. In response to the additional operational risks posed by the pandemic, the Secretariat ensured that business continuity plans for staff, administrator and advisers were all reviewed. Up-to-date business resiliency programme is provided by the administrator annually. Other advisers were requested to provide individual business continuity plans on an ad hoc basis.

63. The Secretariat reviewed data access and data security as a matter of priority. PCPF Trustee Records are held on a secure Parliamentary Network which is Cloud based. Paper copies of signed minutes are held in Secretariat offices but electronic copies are also held online. The administrator's database is held offsite.

64. Certain administrative procedures were adapted promptly in view of remote working. For instance, scans of legal documents can now be accepted electronically. The Secretariat also made extra effort to ensure timely pay-out of benefits, by checking that member and the Treasury contribution to the Fund would continue to be paid on time.

65. The Secretariat were fully equipped for working away from the estate prior to the pandemic. The House of Commons provided extra support by sponsoring additional work equipment, facilitating individual desk assessment, and conducting staff surveys. The Trustees, Secretariat, external advisers, and investment managers all made the switch to working from home efficiently, without any significant operational issues. This ensured continued management of the Scheme. Since the pandemic, the Trustee Board have managed to hold all Trustee meetings and training workshops virtually and continued their work seamlessly.

66. Since the pandemic the Trustees were made aware of a dramatic increase in cyber-attacks. In particular, hackers use phishing campaigns with a coronavirus theme to trick people into clicking on links that contain malware which could cause damage to the computer or its user. The Trustees highlighted this risk in their annual review and have urged their members to be extra vigilant to these attacks.

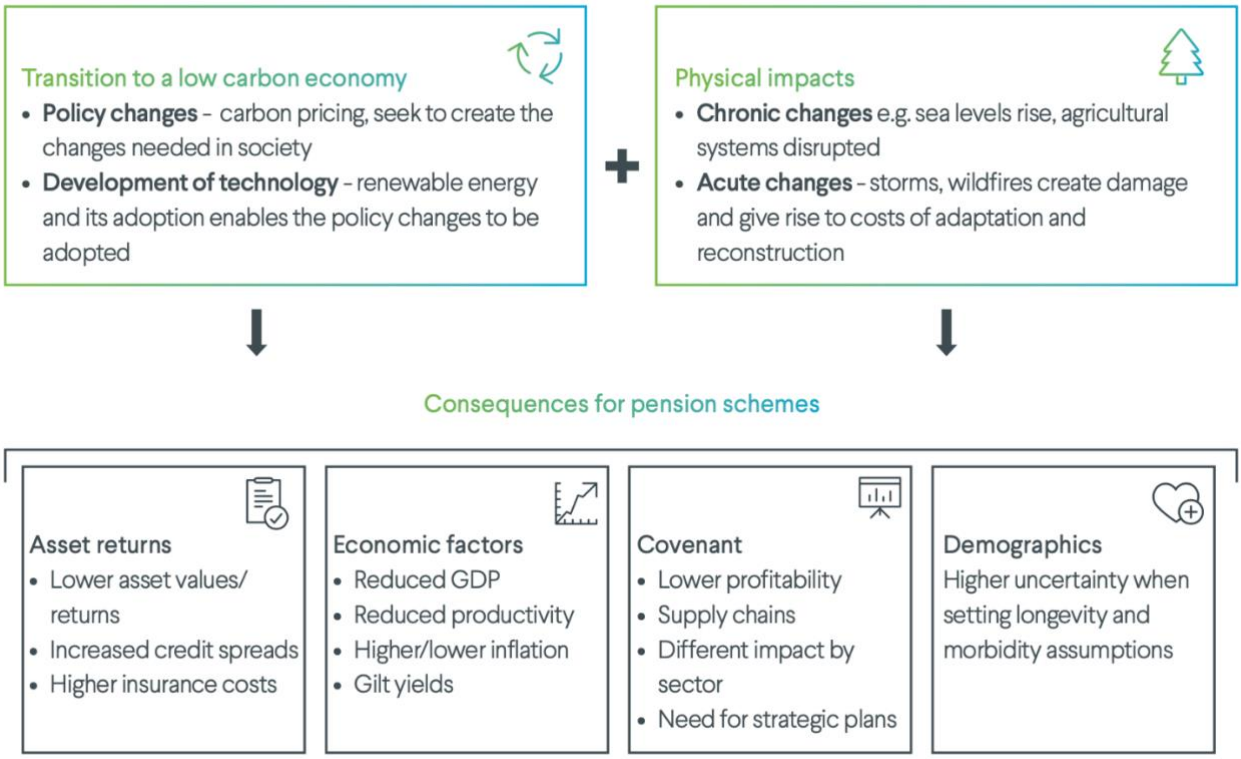
67. Through their advisers the Trustees have been actively monitoring the COVID-19 situation and its impact on market volatility and the value of the Fund's investments. The Trustees followed their

investment consultant's advice and stood by their strategic asset allocation, while postponing the planned equity portfolio transition until market conditions stabilise. The strategy to focus on a long-term horizon and ride out short-term volatility has paid off. Global equities rebounded strongly in Q2 and Q3 of 2020, and the Fund delivered a positive return of 13.3% over the six-month period to 30 September 2020, 1.6% ahead of benchmark return. With the exception of a 3-week period in March/April 2020 when market volatility peaked due to the pandemic, funding level has remained above 100% during the reporting period. The funding level as of 30 September 2020 was estimated to be 113.2% on the 2017 liability basis.

Response to climate risk

68. Climate change presents a systemic and material risk to the ecological, social, and financial stability of every economy and country in the world and is increasingly having a real impact on both Trustees and sponsors of defined benefit schemes. Guy Opperman, the Pensions Minister, wrote in an article on Pensions Age that climate change posed the 'largest risk' to pension schemes, highlighting that 'in reality it matters more than interest rates, exchange rates, company and sector performance and inflation'. [2] While climate change poses a key financial risk over the lifetime of schemes, it also provides opportunities for investors to positively impact the world that savers will retire into.

69. Through Hymans Robertson, the Trustees have identified two key areas in which climate risk may affect financial markets: the physical impacts that arise directly from a changing climate, and the transitory impacts that arise from the response of policy makers. Both can lead to uncertain economic outcomes, such as on GDP growth, inflation, and asset returns, as summarised in the diagram below:



[2] Source: https://www.pensionsage.com/pa/EXCLUSIVE-Climate-change-risk-largest-risk-to-pension-schemes-Opperman.php

70. The Trustees recognise that climate risk will impact us all for decades to come and that it is important to have a clear plan to address climate risks, and potential opportunities, given the likely material impact on investments and funding positions. During the reporting period the Trustees have continued to tackle climate change risk from various aspects.

Policy and strategy

71. The Trustees developed a stand-alone Responsible Investment Policy in 2019 to address the impact of Environmental, Social, and Governance (ESG) issues on the Fund. In November 2020 the Trustee Board examined climate change risk specifically and formalised a Climate Risk Policy, which outlines their approach to addressing climate related risks within the Fund. The full policy is published on the PCPF website.

72. The policy sets out Trustees' longer-term ambition for 100% of the Fund's assets to be compatible with net zero-emissions by 2050 or earlier, in line with the Paris agreement. The Trustees believe that investing to support the Paris Agreement goals that deliver a below 2 Celsius temperature increase is consistent with securing long-term financial returns and is aligned with the long-term interests of the Fund's beneficiaries.

73. The Trustees have established a set of climate-related beliefs, which underpin their approach to incorporating climate risk considerations within the investment process. The Climate Risk Policy translates these beliefs into clear climate-related objectives and strategies. The Trustees' beliefs are as follows:

- Climate risk represents a material financial risk to the Fund's ability to deliver sustainable investment returns over the longer term;
- Climate-related risks are systemic risks which can impact on all asset classes and sectors to varying degrees;
- Investment solutions aimed at managing and mitigating climate-related risks can also provide opportunities to long term investors such as the Fund;
- Climate-related risks are best managed through a combination of active engagement and diversification of asset class and sector, rather than divestment;
- Investment managers appointed to the Fund are responsible for engaging with investee companies and issuers on climate-related issues, as well as other Responsible Investment issues that could have a material impact on performance;
- The Trustees believe that collaboration with other asset owners can be an effective method for engaging with investment managers and raising awareness of climate-related issues on a wider scale basis.

74. Recognising their current investment arrangements and governance budget, the Trustees' primary focus over near term will be on climate-related risk exposure within their equity and real asset holdings, these account for some 70% of the Fund's assets. The Trustees have agreed to reduce the carbon intensity of the Fund's equity portfolio by more than 50%. This will be achieved by switching from funds tracking traditional market indices to a combination of sustainable and lower carbon approaches. The Trustees also aim to consider climate-related risks in other asset classes where practical.

75. In accordance with their Responsible Investment Policy, the Trustees will consider opportunities in the development of their strategy/structure to make investments in assets that are expected to benefit from the transition to a low carbon economy.

76. The Trustees will also consider the merits of undertaking scenario analysis around the potential economic impact of climate-related risks, to inform their decision-making. The Trustees note that this is an evolving area, and such analysis is in its infancy.

Investment arrangements

77. In February 2020, the Trustees carried out a review of the types of assets the Scheme invests in, the mandates that are passively or actively managed, the benchmarks used, and considered the benefits of transitioning to a lower carbon intensity relative to the status quo, in line with their climate risk beliefs.

78. Prior to the review, the Fund had already committed 5% of assets to a Global Renewable Infrastructure strategy managed by BlackRock. The new strategy specialises in building the infrastructure required to generate renewable energy, such as Solar and Wind farms, and offers investment characteristics compatible with the Fund's investment objectives. the Trustees made their first investment into the fund when the manager called capital in August 2020. A second investment took place in December 2020.

79. Since the review, the Trustees took further steps to align Fund's investments with climate risk considerations so as to mitigate against material financial risks. The Trustees agreed to convert the Blackrock regional market-cap equity to Blackrock's low carbon approach. They have also agreed to allocate 30% of the existing equity structure to a global (sustainable) multi factor equity with Schroders. The equity transition is expected to take place in Q2 2021. Once completed, this change is expected to reduce the carbon emissions intensity from the Fund's equity holdings by more than 50% relative to the current position. The Trustees also agreed to allocate 5% of Fund assets to impact investment. It has been agreed that the impact investment will be made in an infrastructure fund with an explicitly stated objective to achieve a positive environmental or social impact, alongside generating a financial return. Following completion of a manager selection process, the Trustees expect to make this investment in 2021, funded from listed equity.

Engagement

80. One way to tackle the climate risk challenge is by engaging with investment managers and monitoring their voting and engagement approach. The Trustees expect their managers to engage with investee companies (see Principle 9-11) and exercise voting rights (see Principle 12) on their behalf, in line with the Fund's climate risk objectives.

81. The Trustees emphasise the importance of engagement on climate-related risks through dialogue with their investment managers. In particular, the Trustees encourage their managers to support engagement with investee companies on climate-related issues, including an increase in the disclosure on climate-related risks by companies to investors.

82. The Trustees monitor and ensure that their investment managers' climate change policies are aligned with Trustees' beliefs, and that the managers act in line with the Fund's stewardship policy in relation to climate change (see Principle 7 and 8).

83. The Trustees' approach to manager selection and assessment in relation to climate risk is set out in their Responsible Investment Policy. All active managers are expected to integrate the consideration of climate-related risks into their investment process and will be challenged to evidence their approach where appropriate during regular meetings. Should the Trustees be dissatisfied with the approach taken

by an investment manager, further action will be taken to understand the rationale for a particular course of action. Where the Trustees are not satisfied after a sustained period of monitoring and engagement, further action will be considered, including reviewing the manager's long-term role in managing assets for the Fund.

84. The Trustees understand that often the best strategy to drive change may be to exercise their 'voice' more as an investor in preference to simply exiting an investment. They believe that a partnership between trustees, asset managers, and companies such as fossil fuel groups will contribute to a well-functioning financial system, and ultimately a net zero carbon future, as these companies transform themselves into clean energy companies.

85. The Fund's asset managers have reported an increasing number of instances where shareholders worked in tandem to put pressure on fossil fuel companies to move towards more sustainable energy resources and to improve their reporting of climate change impact.

86. For example, BlackRock, who engage with underlying companies on behalf of the Fund, keep in regular contact with the higher carbon emitting companies. Engagement from BlackRock and other stakeholders over recent years has led to Royal Dutch Shell amending their climate commitments so as to pursue more aggressive carbon reduction (details available here).

87. Some companies with higher carbon emissions are also the companies leading change and are well placed for the transition to a low carbon economy. BP and Royal Dutch Shell are the UK's two largest providers of electric vehicle charging stations – utilising the infrastructure they already had in place for traditional filling stations. Both companies have also provided capital to support development and expansion of the electric vehicle charging network. A policy of engagement has meant that the Fund has supported this growth and also stands to benefit from the future profits of the investment.

Training and collaboration

88. The Trustees undertake training and education to ensure there is a clear understanding of the developing trends and regulatory changes in managing climate risk. They arrange at least one formal training session that is directly focused on ESG issues annually, and schedule workshops to dive deeper into key areas of opportunity or concern. The Trustees value their advisers' expertise on climate related risks and learn from the experience of their peers and other experts. For instance, the annual ESG training day, facilitated by the investment consultant, gave the Trustees an opportunity to hear from independent think tanks such as Carbon Tracker, and other pension funds such as the Environmental Agency Pension Fund (EAPF). Through these collaborations, Trustees were able to frame their decision-making based on in-depth analysis and industry best practice.

Next steps

89. The UK government has published proposals that will require larger pension schemes to report against the Taskforce for Climate-Related Financial Disclosures (TCFD) framework on an annual basis. Whilst the PCPF will not be directly impacted by these new requirements due to its current size, the Trustees are aware of the increasing pressure for pension schemes to ensure climate risk is managed effectively. The Trustees have expressed their ambition to report in future on actions undertaken to address climate risk in line with the TCFD framework and are looking to gain an understanding of the requirements through training.

90. The Trustees recognise that the monitoring and assessment of exposure to climate-related risks is developing and the metrics and tools available to them may evolve. The Fund's equity transition (see above) is expected to take place in early 2021 and is estimated to reduce the carbon emissions intensity

of the equity portfolio by more than 50%. The Trustees intend to instruct an independent carbon intensity review after the transition. The Trustees recognise that a single measure is unlikely to be sufficient to quantify climate-related risks for the entire Fund. Whilst it is anticipated that carbon intensity can be used as one such measure, they will also consider other measures in future depending on the availability of sufficient data and suitable analysis. The Trustees will monitor developments in this area to ensure that they follow the best practice as it evolves.

91. During the reporting period the Fund has had limited interaction with other stakeholders, such as other investors, issuers, policymakers, and not-for-profits, or participation in industry initiatives. This is partly due to time and resource constraints. However, the Trustees do understand that for society to achieve a net zero carbon future by 2050 or earlier, systemic change and collaboration in the investment community will be crucial. The Trustees are aware that many of their investment managers are signatories to, or active participants of, relevant industry initiatives such as ShareAction, Carbon Disclosure Project, and Climate Action 100+. The Trustees are keen to learn more about climate risk related initiatives and explore what role they may play in the future.

5. Review and assurance

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

92. The Trustees are responsible for reviewing the effectiveness of internal controls and assuring effective stewardship, undertaken directly or on their behalf. The Secretariat are tasked with the development and maintenance of the Fund's control framework. This includes a combination of internal controls such as senior management sign-off, Trustee Board oversight, and internal audit. All important policies and documents go through various stages of internal review and sign-off by authorised persons.

93. In authorising investment managers to make investments on their behalf, the Trustees receive sufficient information to make informed decisions and to understand the risks associated with those investments. Specifically, they take advice from Hymans Robertson, their investment consultant, and receive regular updates in relation to the investment managers' investment performance and stewardship activities.

94. The organisations that provide the Fund's custodianship and administration functions are subject to review by their respective internal audit units, which operate to relevant professional Internal Audit Standards. On behalf of the Trustees, the Secretariat review independent reports on internal operational controls for the custodian and the administrator where appropriate.

95. The Trustees set out in the Fund's Responsible Investment Policy their approach to enable effective stewardship, including policies and processes such as:

Explore the possibility of incorporating the United Nations' Sustainable Development Goals into their investment beliefs and broader policy.	Ongoing
Review the benchmarks of any index-tracking mandate. Seek input from advisers and investment managers to understand the potential implications and impact of ESG factors on different approaches.	At least triennially
Monitor investment managers' compliance with the PRI reporting requirements.	Annually
Monitor equity managers' records as set out in the Fund's policy on voting and engagement activities.	Quarterly
Request that investment managers provide details of any change in their house voting policy and review any changes against the ISS guidelines.	Annually
Monitor investment managers' adherence to this policy. Review annual compliance report submitted by equity and non-equity managers. Publish a summary of voting and engagement activity undertaken by managers and issues on which they have been challenged.	Annually
Aim to meet all investment managers on an annual basis. Managers are asked to address Responsible Investment matters as part of presentations to Trustees, setting out how these are incorporated within the investment process.	Annually

Monitor investment managers' compliance with the UK Stewardship Code and their track record of engaging with companies on issues such as climate change risk, fossil fuels, and broader ESG issues.	Ongoing
Consider analysis of the Fund's carbon exposure and intensity.	When appropriate
Complete a report on the Fund's Stewardship and Governance activities, including voting and engagement undertaken on behalf of the Fund, to be included in the Annual Review issued to all members of the Fund. Maintain transparency and accountability to stakeholders, and include disclosure of the Fund's top 20 equity holdings.	Annually
Review Trustees' own adherence to the policy and publish the results of this assessment as part of the annual stewardship and governance report.	Annually
Ensure ongoing Trustee education on a broad range of investment matters. Plan at least one formal training session that is directly focused on Responsible Investment.	Annually
Undertake a review to assess the investment adviser's performance against strategic objectives set by Trustees as per the Competition and Markets Authority (CMA) final order. Submit a report on the results.	Annually
Review the Responsible Investment Policy to ensure it remains appropriate and in line with the long-term objectives for the Fund, as well as broader industry developments.	Annually

96. As part of internal assurance, the Fund's policies are reviewed regularly and revised from time to time. For example, in January 2020, The Trustees updated their Conflicts of Interest Policy (see Principle 3) in light of an increased focus on responsible investment matters. The Trustee Board identified through internal review that as they prepared to update the Fund's Statement of Investment Principles and develop a Climate Risk Policy, there was a potentially greater scope for individual Trustee views regarding some aspects of the Fund's investments to conflict with Trustee fiduciary duties when setting the Fund's investment strategy and reviewing investment options. In particular, where a Trustee is a serving MP or active political campaigner, s/he may have a predetermined interest in the outcome of Trustee deliberations. To keep up with these emerging issues, the Trustees updated the policy, putting in place robust procedures to manage potential or actual conflicts of interest that they may have in carrying out their functions.

97. External assurance complements internal controls by helping the Trustees manage key risks and evaluate potential pitfalls. The Trustees use independent professional services provided by accountants, lawyers, and other professionals to assure the Fund's key documents, policies, and processes.

98. Audits are one example of services provided by such professionals to assure that stewardship reporting provided to members and the public is fair, balanced, and understandable. The National Audit Office (NAO) carry out independent audits on the Fund's Annual Report and Accounts and scrutinise

stewardship information included in the Implementation Statement to assure its accuracy and impartiality. The Implementation Statement is prepared by the Secretariat in accordance with the requirements of the Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019, and sets out in detail how the Trustees have complied with the Fund's stewardship policy during the scheme year.

99. The Trustees also seek advice from Sackers, their legal adviser, regarding any significant changes to the Fund's policies, including those in relation to stewardship practices, before sign-off. During the reporting period Sackers reviewed documents such as the updated Statement of Investment Principles and the Climate Risk Policy and assured the integrity and accuracy of information from a legal perspective.

100. As part of ongoing monitoring of investment managers' compliance with PCPF's stewardship polices, Hymans, the Fund's investment adviser, is asked to prepare independent voting and engagement reports every quarter, to be reviewed during Trustee meetings. This is to ensure that stewardship reporting is fair, balanced, and understandable and that Trustees can challenge managers where they fall short of expectations.

101. As mentioned under Principle 1, the Trustees reviewed the Fund's equity structure in 2020 and decided to transition the index tracking regional equity portfolio to a sustainable multi-factor and low carbon index approach. The transition is expected to take place in early 2021 and is estimated to reduce the carbon emissions intensity of the Fund's equity portfolio by more than 50% once completed. Prior to making their decision, the Trustees considered in-depth analysis by independent think tanks, such as Carbon Tracker, regarding the impact of climate change on capital markets. For comparison, the Trustees intend to instruct an independent third party to carry out a carbon foot-printing review to verify the effectiveness of this change.

102. During the reporting period, the Trustees have taken reasonable steps to review their policies, received internal and external assurance in relation to stewardship undertaken directly or on their behalf, and ensured their stewardship reporting is accurate and understandable.

103. The Trustees are satisfied that majority of the Fund's stewardship policies are up to date. With guidance from their investment adviser, the Trustees have started the process to review and update their investment objectives and beliefs within the Statement of Investment Principles in early 2021. Any changes will feed into the Fund's Responsible Investment Policy, which is next up for review.

6. Client and beneficiary needs

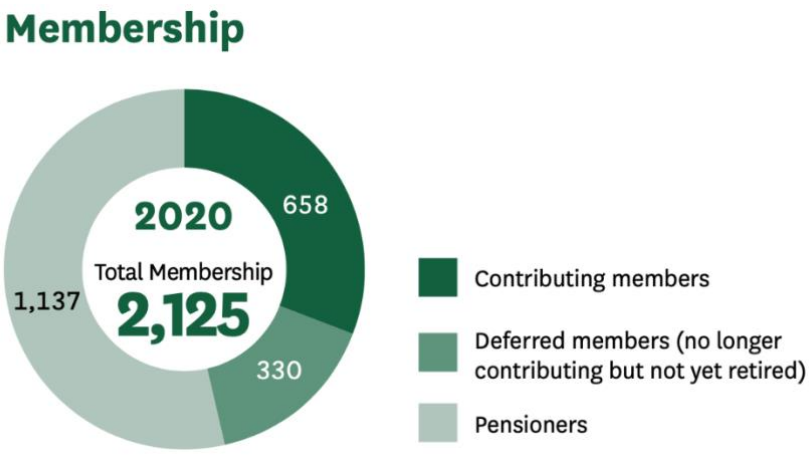
Principle 6 - Signatories take account of client and beneficiary needs, and communicate the activities and outcomes of their stewardship and investment to them.

104. The Fund is a contracted-out defined benefit pension scheme. Details on the background and structure of the Fund can be found under Principle 1 and 3.

105. A summary of the Fund's profile as of 31st March 2020 is as follows:

Total Assets:	Investments returned:	Total membership:
£638m	**-7.3%**	**2,125**
(down from last year's £733m)	(down from last year's 7.4%)	(up from last year's 2,006)

This information is taken from the draft Accounts for the year ended 31 March 2020, which as at time of printing have not been finalised. Once agreed, the accounts are published by the National Audit Office as a House of Commons paper, at which time a copy of the full report will be made available on the Scheme's website (**www.mypcpfpension.co.uk**).



106. Below is a summary of the age profile for each set of members as of 31st January 2021:

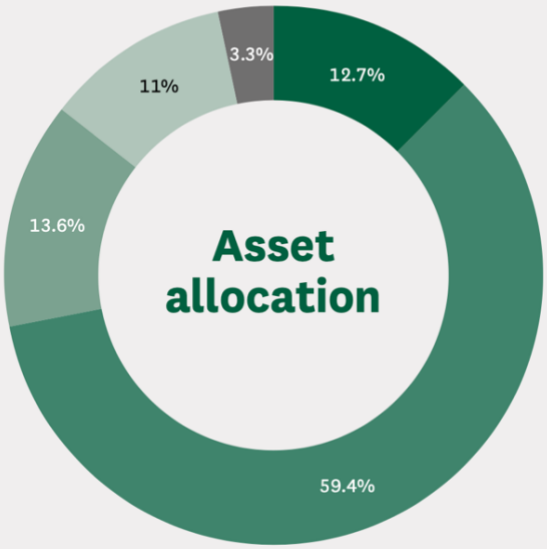
- Active – average age of 51 years
- Deferred – average age of 55 years
- Pensioners – average age of 75 years
- Spouses/Dependants – average age of 80 years
- Total membership – average age of 65 years

107. Due to the nature of the Fund and the strength of employer covenant (HM Treasury), the Trustees believe that the Fund can take advantage of the benefits associated with a long-term investment horizon. Investors with long term time horizons can better withstand periods of price volatility. As a long-term investor, the Fund may choose to gain additional compensation by investing in assets that are illiquid or may be subject to higher levels of volatility (a premium return is required for any such investments).

108. Below is an overall breakdown of assets under management across different asset classes and fund managers as of 31st March 2020:

Where were the assets invested on 31 March 2020?

UK bonds	12.7%
Global equities	59.4%
Fixed income	13.6%
Property	11%
Cash	3.3%



Fund managers

The manager proportions and mandates at the year-end (31 March 2020) are shown in the table below:

Manager	Mandate	Holding as at 31/03/2020	Target Allocation
BlackRock Advisors (UK)	Passive Global equities	41.8%	44.0%
MFS International (UK) Ltd	Active Global equities	17.6%	16.0%
M&G	European Loans	8.7%	10.0%
M&G	Illiquid credit	4.9%	5.0%
Multi-managers	Property	11.0%	10.0%
PIMCO Europe Ltd	UK bonds	8.4%	7.5%
BlackRock Advisors (UK)	UK Gilts	4.3%	7.5%
Cash*	Cash	3.3%	-
Total		100.0%	100.0%

*Cash balances include balances held by Fund's custodian, Northern Trust, and the balance of the Trustees' bank account. A higher proportion of cash was being held at the year end to continue to support payment of benefits following the Election in December 2019.

109. The PCPF Annual Review is the Trustees' main formal communication to beneficiaries about all scheme matters including stewardship activities and investment outcomes.

110. Given the membership turnover that is unique to this Fund, with new members joining and active members moving to deferred or pensioner status at each General Election, the Fund may experience heavy windfalls of queries from time to time. This may lead to additional engagement from members and pose additional questions for the Trustees (for example in relation to liquidity as Transfer activity increases) that often go beyond the scope of the Annual Review.

111. The Trustees recognise the importance of ensuring our members have all the information they need and a forum to express their views. Therefore, regular members' surgeries are held, typically once or twice a year, and after General Elections, for active members to meet the Chair in person, ask questions, and express opinions. The last members' surgery was held on 25th February 2020 following General Election. Due to COVID-19, the Trustees have had to postpone further in-person sessions. A virtual surgery is scheduled for March 2021, after the Annual Review is issued, to update members on scheme matters.

112. The Trustees also receive ad-hoc correspondence from scheme beneficiaries expressing views on various aspects of the Fund. The Trustees are aware of the scrutiny under which the Fund operates and are mindful of this when considering members' views. The Trustees recognise that with an increased focus on responsible investment matters, there is potentially greater scope for individual member's views regarding certain aspects of the Fund's investments to conflict with Trustees' fiduciary duty to safeguard the interests of the Fund's beneficiaries. The Trustees strive to manage any potential conflicts of interest and adopt a balanced approach when taking members' views into account. Details on the Trustees' conflicts of interest policy are addressed under Principle 3.

113. Beneficiaries' views are also sought informally. There are currently three serving Members of Parliament who sit on the Trustee Board. Scheme members who are serving MPs often engage with their MP colleagues who are Trustees to express views in relation to the Fund.

114. The above methods combined have been effective in enabling the Trustees to understand the views of the beneficiaries. While the Trustees respect certain moral/ethical views that could be held by individual members, they have a duty to balance the interests of all members and to act fairly when making investment decisions. Given the nature of the Fund, it has not always been possible to act on individual member's views. However, in considering these views and making decisions the Trustees have taken a fair and balanced approach and have ensured that their fiduciary duty is always given the utmost priority.

115. For instance, the Trustees acted in line with many members' views and formulated a Climate Risk Policy in 2020 as this is aligned with their investment beliefs. However, the Trustees have not made a decision to back campaigns such as fossil fuel divestments in the Fund's positioning due to potential conflicts of interest with their overriding fiduciary duty to invest in the best financial interests of the members. Through engaging with their investment managers, the Trustees have seen ample evidence that often the best strategy may well be to exercise their 'voice' more as an investor in preference to simply exiting an investment (see Principle 9-12). The Trustees believe that exploring how to further stewardship and engagement activities should be a precursor to any divestment decisions.

116. The Trustees recognise that the frequency and method of communication with beneficiaries may be an area for improvement or review. They intend to consider making use of additional tools to improve in-year communication with members in the future.

7. Stewardship, investment and ESG integration

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

117. The Trustees are responsible for ensuring that the Fund's assets are invested in a manner which meets their overriding objective to pay benefits to members as they fall due. The Trustees recognise that responsible investment considerations pose a financially material risk to the Fund. Responsible investment is considered to be those investment practices where Environmental, Social and Governance (ESG) issues are explicitly or implicitly integrated into investment management processes and asset ownership practices. The Trustees go through regular training on ESG related issues to ensure they are fully aware of the implications ESG factors can have on the Fund's investments.

118. The Trustees acknowledge that there are a broad range of ESG risks which operate over different timeframes with differing potential degrees of impact on the Fund. Of these risks, the Trustees have identified that climate risk warrants more detailed scrutiny given the potentially widespread and uncertain impact on financial, economic, and demographic outcomes. The Trustees also regard executive remuneration as a material governance-related risk and support the mitigation of this risk predominantly through active engagement by investment managers.

119. A stand-alone Responsible Investment Policy was agreed in July 2019 and sets out the Trustees' policy for incorporating responsible investment (including climate risk) considerations within the investment process. These factors are integrated into each stage of the investment decision-making process: assessing investments prior to holding, monitoring through holding, and exiting investments. The Trustees work closely with the Fund's investment managers to help support good corporate behaviour. The Fund's Responsible Investment Policy enables the Trustees to document their position and expectations for their fund managers and to hold managers accountable for the decisions they make.

Setting investment strategy/structure

120. The Fund's investment strategy represents the broad balance between different asset classes such as equities, debt and real assets. The Trustees frame their investment strategy by reference to long-term risk and return assumptions which make implicit allowance for operational and many systemic ESG risks. The Fund's investment structure represents the allocation to different mandate types within each broad asset class. In addition, the Trustees consider opportunities arising from a greater understanding of ESG factors, such as investment in renewable energy infrastructure, when setting their investment structure.

121. The Fund's investments are held either directly or through pooled arrangements and both active and passive strategies are used. The Trustees recognise that in practice the means of their engagement with ESG issues will vary depending on how the assets are held and managed, and that the integration of stewardship and investment differs across different types of funds and asset classes. The Trustees recognise the influence of benchmarks on the selection of assets by investment managers, particularly within rules-based or index-tracking mandates. Prior to entering into such mandates, the Trustees take into account their ESG characteristics and actively consider alternative approaches in their decision-making. The Trustees review the benchmarks of any index-tracking mandate on at least a triennial basis. As part of this process, the Trustees seek input from their advisers and investment managers to understand the potential implications and impact of ESG factors on different approaches. For active investment mandates, the Trustees expect their managers to take account of ESG-related risks and

issues as part of their investment analysis. The Trustees engage with their active managers to understand how ESG-related risks are considered in the decision-making process, and to determine that this is consistent with the Fund's policy.

Setting expectations and monitoring compliance

122. In selecting new investment managers for the Fund, where relevant to the investment mandate, the Trustees explicitly consider potential managers' approach to responsible investment and the extent to which managers integrate ESG issues in the investment process as a factor in their decision-making. The Trustees impose minimum standards for all managers and monitor compliance with these standards on a regular basis. When appointing new managers, the Trustees will consider ESG issues in setting benchmarks, performance criteria, and manager remuneration.

123. The Trustees expect all their investment managers to be signatories to the UN-sponsored Principles of Responsible Investment (PRI) or to be able to provide an explanation as to the reasons for not signing. The Trustees aim to monitor their investment managers' compliance with the PRI reporting requirements annually.

124. The Trustees support the FRC UK Stewardship Code and believe that, where relevant, the Fund's investment managers should be signatories to the Code. The Trustees monitor the investment managers' compliance with the UK Stewardship Code and their track record of engaging with companies on issues such as climate change risk, fossil fuels, executive remuneration, and broader ESG issues on an ongoing basis.

125. The Fund's investment managers are expected to incorporate ESG-related issues into their regular reporting. This includes information on voting and engagement, in addition to details on how they are assessing and managing ESG-related risks in relation to their respective mandates.

Voting

126. During the reporting period, the Trustees have investment in listed equity assets through two different mandates, managed by MFS (active equity) and BlackRock (passive equity portfolio). The Trustees believe that failing to exercise voting or other rights attached to shares could be contrary to the interest of the beneficiaries of the Fund. They have therefore instructed the investment managers to take this into account in exercising such rights on their behalf. The Trustees have instructed the managers to provide them with a statement on their corporate governance and voting policy, and to report on their voting record in each of these mandates on a quarterly basis.

127. The Trustees have adopted the voting guidelines issued by Institutional Shareholder Services (ISS) as the basis against which they will judge good voting practice.

- For segregated mandates, the Trustees have instructed their managers to adopt the ISS voting guidelines. Where a manager does not vote in line with the ISS guidelines, this will be reported to the Trustees and explanation will be required.

- For pooled mandates, the Trustees will review the policies employed by the manager against the ISS guidelines and where appropriate request that the manager take account of the ISS guidelines in the execution of voting policy.

128. The Trustees seek to ensure that their managers are exercising voting rights and where appropriate, to monitor managers' voting patterns. The Trustees require that their active managers provide an explanation where votes have not been cast in accordance with the Fund's policy. The Trustees review

managers' voting activities on a regular basis and challenge managers on voting practices during regular review meetings. The Trustees also monitor investment managers' voting on particular companies or issues that affect more than one company.

129. On an annual basis and where relevant, the Trustees request their investment managers to provide details of any change in their house voting policy and review any changes against the ISS guidelines.

130. In making any future manager appointments, the Trustees will assess the manager's voting policy as part of the due diligence process.

Engagement

131. The Trustees believe that their investment managers are accountable to them for all engagement activity and should be able to demonstrate, when challenged, the reason for any engagement activity, the objectives of the engagement activity, the approach taken to achieve the objectives, the timeframe over which the engagement is expected to take place, and the consequences should engagement be unsuccessful. The Trustees believe that engagement activity may differ across mandate types and asset classes and is not limited to listed assets.

132. In appointing new managers, the Trustees assess the prospective manager's approach to engagement to ensure consistency with the Trustees' own policies and reporting requirements. The successful candidates are expected to demonstrate that their approach is consistent with the Fund's policies and in line with developing best practice.

133. The Trustees adopt an evidence-based approach to assessing engagement activity by managers. The Trustees receive regular quarterly update on their equity managers' engagement activity. The Trustees recognise the difference in how investment managers carry out engagement activity for non-listed assets such as private debt and real estate assets, and request that their non-equity managers complete annual compliance reporting providing specific examples of engagement. Where appropriate, the Trustees challenge their investment managers on actions taken. The results of the compliance reporting are compiled and published annually on the PCPF website.

Stewardship and decision-making

134. The Trustees believe that they can influence the behaviour and practices of their investment managers with regard to stewardship through ongoing and forceful engagement, even where assets are invested through pooled funds.

135. Where the practices adopted by their investment managers differ from the Trustees' policy, the managers will be challenged on their approach. Managers exhibiting weaker practices over a sustained period will not be considered for future appointments to the Fund and their appointment will be reviewed.

136. Below example demonstrates how the Trustees have made use of information gathered through stewardship activities to monitor investment managers and guide decision-making.

Timeline	Meeting Subject	Action and Outcome
November 2019	Review meeting with manager.	Trustees identified responsible investment as potential area for improvement.
January 2020	Responsible investment follow-up, to discuss manager's voting record on	Trustees challenged the approaches taken and questioned how progress/success was

	climate change and executive compensation, following review meeting.	measured. Manager provided case studies and rationale for key votes. Trustees decided to monitor progress and invite manager back in 2020/21.
June 2020	Update from manager's stewardship team regarding measures of engagement activities.	Investment consultant and Secretariat questioned rationale for different engagement approaches and measure of success. Manager highlighted progress made to improve transparency on engagement activities, e.g., a dedicated stewardship website, automated quarterly reports etc. Manager confirmed understanding of Trustees' expectations. Secretariat agreed to continue monitoring.

8. Monitoring managers and service providers

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

Monitoring investment consultant

137. The Competition and Markets Authority (CMA) published its final order in 2019 following a review of the investment consulting and fiduciary management markets. The order made it a regulatory requirement for pension fund trustees to set objectives for their investment consultants.

138. The Trustees set strategic objectives for their investment consultant, review their performance against these objectives as part of ongoing good governance, and submit a CMA compliance statement annually. This is in line with guidance from The Pension Regulator which suggests performance is monitored annually, with a detailed review every three years.

139. Hymans Robertson, the Fund's investment consultant, create and update workplans to translate strategic objectives set by the Trustees into short-term and mid-term tasks and milestones. These workplans are taken to each investment focused Trustee meeting for discussion and approval. As part of ongoing assessment, the Secretariat ensure that Trustees' feedback, outcome of the discussion, and agreed actions are documented and agreed by all parties.

140. The Trustees adopt an evidence-based approach when assessing their investment consultant's performance against objectives. Progress made against the workplans forms the basis of ongoing evaluation. In addition, at the end of the year, Hymans are asked to provide evidence with example measures of success alongside each objective and are assessed accordingly. During the reporting period Hymans were able to demonstrate with quantifiable measures and specific examples that the services have been delivered to meet the objectives. For example, the Fund's performance (net of fees) for the 3-year period to 30 June 2020 was 2.1% p.a. ahead of the assumed increase in long-term cost of benefits. The funding level as of 30 September 2020 was estimated to be 113.2% on the 2017 liability basis. The restructured equity portfolio increased management fees slightly but these remain below the Fund's target of 0.4% of Fund assets.

141. The Trustees conduct an annual peer review with an independent partner at Hymans to ensure thorough, fair and transparent evaluation of performance. This was postponed last year due to the imminent investment consultancy tender which was issued in December 2020. Hymans have been reappointed through a competitive tender process and the practice of annual peer review will now continue.

142. The Trustees provide regular feedback to their investment consultant about the services they deliver and are vocal about any potential areas for improvement. While there is a formal policy for escalation, the Trustees have been able to address any minor issues through their regular engagement with Hymans.

Monitoring investment managers

143. The Fund's investment structure represents the allocation to different mandate types within various asset classes. When appointing new investment managers for the Fund, where relevant to the mandate, the Trustees set comprehensive investment guidelines including benchmarks, performance criteria, manager remuneration, and responsible investment expectations. The Trustees impose minimum standards for all managers and monitor their performance on a regular basis.

144. The Trustees have delegated voting and engagement activity in respect of the underlying assets to the Fund's investment managers. It is critical that the managers take an active role in the supervision of the companies in which they invest, both by voting at shareholder meetings and engaging with the management on issues which affect a company's financial performance.

145. The Trustees are supported by Hymans, their investment adviser, in developing stewardship practices to monitor the investment managers. The investment consultancy team at Hymans include a senior consultant specialised in responsible investment. The team have been instrumental in guiding the Trustees as they develop robust procedures to ensure their managers are held to account. Hymans also prepares quarterly voting and engagement reports to help monitor equity managers' adherence to the Fund's stewardship policies.

146. The Trustees' Voting and Engagement Policy, available on the PCPF website, sets out the Trustees' approach to:

- the exercise of voting rights attached to assets; and
- undertaking engagement activity, including how the Trustees monitor and engage with their investment managers and any other stakeholders.

147. In addition, a stand-alone Responsible Investment Policy was published in July 2019 setting out further details on the Trustees' voting and engagement expectations.

148. The Trustees value regular dialogue with their managers regarding investment performance and stewardship activities, undertaken in conjunction with their investment adviser. They meet regularly with their managers and consider how expectations have been met both during these meetings and through reporting provided by their investment adviser. Hymans are required to provide input and analysis to assist the Trustees in evaluating asset managers' performance. They prepare quarterly investment monitoring reports and discuss with the Trustees market outlook, asset allocation, manager performance, and manager ratings. The Trustees use these findings to identify any potential issues and inform their decisions regarding any further engagement with the managers.

149. As mentioned under Principle 7, the Trustees seek to ensure that their managers are exercising voting rights and where appropriate, to monitor managers' voting patterns. The Trustees have asked MFS and BlackRock, their equity investment managers, to report on how votes are cast on a quarterly basis. The results are analysed by Hymans and taken to Trustee meetings for discussion. The Trustees also scrutinise significant votes, identified within the Responsible Investment Policy as votes on issues that are of particular concern, i.e., climate change and executive remuneration.

150. The Trustees monitor the managers' voting records and challenge their decisions where appropriate, in particular, where there is a vote against shareholder resolutions, a vote that is not in line with voting policy, or where the two managers' opinions differ.

151. For example, the equity managers reported a significant vote regarding Walt Disney's proposal to ratify executive remuneration in Q1 2020. The Trustees compared the votes and asked for clarification as to why their votes were different. The equity managers then provided justification below:[3]

- **MFS** - voted against the Walt Disney proposal to ratify executive remuneration.

A vote AGAINST this proposal is warranted. Although meaningful improvements were made to address shareholders' concerns, including the elimination of certain compensation increases the CEO would

[3] Source of information: quarterly voting and engagement reports.

otherwise be contractually entitled to, there remain significant concerns regarding CEO pay magnitude and structure. Specifically, the CEO's base salary is more than double that of company peers at $3 million. The CEO's target and maximum annual incentive pay opportunities remain set at $12 million and $24 million, which is 400 percent and 800 percent of base salary, respectively. This resulted in an annual incentive award for 2019 that exceeded the CEO total pay peer median.

- **BlackRock** - voted for the proposal and in line with the management recommendation.

BlackRock engaged with The Walt Disney Company regarding its executive compensation plan, political spending and lobbying disclosure. The Board was responsive to shareholder feedback on both matters. As noted in the “Fiscal 2019 Shareholder Engagement” section of the company’s 2020 proxy statement, “In light of investor feedback, the Compensation Committee discussed with Mr. [Bob] Iger, and he agreed to, adjustments in Mr. Iger’s contractual compensation on three separate occasions.” The Compensation Committee reduced CEO Mr. Iger’s annual compensation and refined the related performance criteria, increasing the rigor of the measures and improving alignment with shareholder interests. We will continue to assess executive compensation at The Walt Disney Company, particularly in light of recent management changes. Where companies are making progress on key corporate governance issues, BlackRock will generally support the board and management in those efforts. BlackRock determined that The Walt Disney Company’s current level of disclosure, following the changes discussed above, is in line with the best practices detailed in BlackRock’s Investment Stewardship team’s commentaries on executive compensation and on corporate political activities.

152. Despite the constraint posed by lockdowns, the Trustees and Secretariat have held virtual meetings with various managers during the reporting period to address different topics such as manager ethos/style, market overview, portfolio positioning, performance review, and ESG integration. For example, during the meeting with MFS, the Secretariat noted that the fund was underperforming and questioned its positioning around the tech sector. The manager stood by their strategy despite the setback since COVID. They were able to provide rationale and justify fund positioning in line with their beliefs in sustainable growth and reasonable valuation. During the meeting with PIMCO, the manager shared specific examples of ESG integration in the Fund’s investments. They also highlighted that as a major bond investor PIMCO have influence over issuers through frequent interactions despite not having voting rights.

153. The Trustees believe that they can influence the behaviour and practices of their investment managers through ongoing and forceful engagement. The example under Principle 7 demonstrates how the Trustees took steps to challenge an investment manager about their voting record and engagement activities, through identifying the issue, following up to drive change, and escalating with the stewardship team for further action.

154. Trustees will challenge their managers if they fail to manage the assets in line with the Fund’s investment and stewardship strategy. Managers exhibiting weaker investment performance or stewardship practices over a sustained period will not be considered for future appointments to the Fund and their appointment will be reviewed.

155. The Trustees monitor their investment managers’ performance on a regular basis and have been able to address any minor issues through regular engagement with the managers. The Trustees are satisfied that the Fund’s investment and stewardship policies have been followed during the reporting period.

9. Engagement

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

156. The Trustees believe that successful engagement with investee companies can protect and enhance the long-term value of the Fund's investments. Day-to-day responsibility for managing the Fund's holdings is delegated to the appointed investment managers.

157. The Trustees consider that, in most cases, its managers are best placed to engage with investee company management due to (a) the practical constraint of investment in pooled funds which limits their own ability to make alternative directions, (b) the resources available to these managers, which are funded by the investment management fees paid by the Trustees, and (c) the existence of relationships between investment managers and the underlying investee companies.

158. The Trustees expect their investment managers to monitor investee companies, engage with company management where necessary, and report on voting, governance, and engagement activity. Reports from investment managers on voting and engagement activity are reviewed on a regular basis.

Passive equity manager

159. During the reporting period the Fund's target allocation to an index tracking equity portfolio was 44%. BlackRock manages this portfolio by investing in a range of passive funds as selected by the Trustees of the PCPF.

160. While index-tracking funds cannot exit holdings in specific companies, BlackRock believes this is precisely the reason engagement with investee companies is so important.

161. As part of their fiduciary duty, BlackRock's Investment Stewardship team (BIS) advocates for sound corporate governance and business practices that are aligned with long-term sustainable financial performance. This objective underpins all engagements and votes at company meetings. BIS engages company leadership on key topics emphasising governance practices including management of environmental and social factors that potentially have material economic, operational, or reputational ramifications for the company. BlackRock determines engagement priorities based on observation of market developments and emerging governance themes and evolve them year over year as necessary.

162. The BIS team's key engagement priorities include:

- Board quality
- Environmental risks and opportunities
- Corporate strategy and capital allocation
- Compensation that promotes long-termism
- Human capital management

163. Over the reporting period BlackRock carried out a total of 2,854 engagements with 1,733 individual companies for the passive equity portfolio. Below is an overview of the engagement metrics.

Engagements by region[4]	Number	%
Americas	1269	44%
EMEA	751	26%
APAC	834	29%
Engagement themes	**Number**	**%**
Governance (G)	2657	93%
Social (S)	1214	43%
Environmental (E)	1667	58%
Engagement topics	**Number**	**%**
E- Climate Risk Management	1273	45%
E- Environmental Impact Management	732	26%
E- Operational Sustainability	1180	41%
S- Human Capital Management	969	34%
S- Social Risks and Opportunities	688	24%
G- Board Composition & Effectiveness	1416	50%
G- Business Oversight/Risk Management	981	34%
G- Corporate Strategy	1385	49%
G- Executive Management	415	15%
G- Governance Structure	768	27%
G- Remuneration	1072	38%

164. BlackRock is committed to enhancing the transparency of their stewardship practices. Where the manager believes it will help investors understand certain voting decisions at shareholder meetings, a Voting Bulletin is published to explain the rationale for how BlackRock has voted on select resolutions, and (where relevant) provide information around engagement activity with the issuer. This could include interim or final outcomes of such engagements – depending on whether the engagement has concluded – and any escalation undertaken, including any voting action as a result.

165. Below is a selection of case studies to illustrate the details of such engagement activity.

[4] Engagements include multiple company meetings during the year with the same company. Most engagement conversations cover multiple topics and are based on BlackRock's vote guidelines and engagement priorities found at: https://www.blackrock.com/corporate/about-us/investment-stewardship#engagement-priorities

Case study 1: Royal Dutch Shell[5]

The shareholder proposal (Item 21) at the Annual General Meeting (AGM) held on 19th May 2020 requested that Shell set and publish targets across Scope 1, 2 and 3, aligned with the Paris Agreement.

The proponent argued that Shell's ambition to reduce its net carbon intensity by 50% by 2050 in a growing energy system would not ultimately lead to the level of absolute emissions reduction necessary to achieve the goals of the Paris Agreement. The proponent asked for more "aspirational" targets.

Since the submission of the shareholder proposal, Shell has updated its climate commitments to more aggressively reduce its carbon footprint, and to become a "net-zero emissions energy business" by 2050 or sooner. This commitment now includes:

Scope 1&2: net zero on all emissions from the manufacture of all products by 2050;

Scope 3: reducing the Net Carbon Footprint of its energy products by around 65% by 2050 (up from a previous target of around 50%), and by around 30% by 2035 (up from a previous target of around 20%), both now consistent with the Paris Agreement goal to limit the average temperature rise to 1.5 degrees Celsius;

A transition towards serving businesses and sectors that by 2050 are also net-zero emissions.

The Department for Business Innovation and Skills (BIS) has been engaged with Shell on its climate commitments for a number of years and was engaged with the company throughout the process of this latest upgrading of its commitments. Most of Shell's Scope 3 emissions are the Scope 1 emissions of their customers. Because no single oil & gas company is fully in control of the global energy mix, Shell's Scope 3 commitments will only be achievable if key stakeholders such as policymakers, businesses and consumers accelerate the development and use of low-carbon technologies, incentivize more energy efficiency, reduce demand for fossil fuels, and remove emissions from the atmosphere.

We understand from our engagement with the company that the recently revised targets will be kept under review, with a view to evolving them even further if possible. We will be monitoring closely the delivery against the targets set out to date. We will hold the management and board directors to account for lack of progress on their delivery through future voting on director elections. For now, we note that Shell's existing disclosure of 3-year net carbon footprint targets already makes the company a sector leader in the global oil & gas industry. Given the company's progress towards aligning its reporting with Task force for Climate Related Financial Disclosure (TCFD) recommendations, which has been one of BIS' key requests of large carbon emitters, and its responsiveness to shareholder engagement on portfolio resilience and reduction of scope 1, 2, and 3 GHG emissions, we are supportive of management for the time being. For these reasons, BIS voted with management on all resolutions at the AGM. We will continue to engage with the company on its governance practices, reporting on material factors including the alignment with the Sustainability Accounting Standards Board (SASB) guidelines, and on the development of its plans to achieve its ambitious climate commitments.

[5] For full disclosure please see Voting Bulletin at https://www.blackrock.com/corporate/literature/press-release/blk-vote-bulletin-shell-may-2020.pdf

Case study 2: Facebook[6]

BIS regularly reviews Facebook's governance structure and risk profile. In prior engagements with the company's board and management, we have discussed a range of material issues driving long-term shareholder value, including corporate governance practices, privacy issues, sustainability, and human capital management.

During our most recent engagement, we addressed several topics including director compensation, efforts to increase transparency and enforce their policies. Although the pay outcomes under the proposed director compensation plan are at the high end, they are within the range offered in its peer group. Facebook has increased transparency regarding its policy enforcement by publishing reports such as its Community Standards Enforcement Report and Ad Library.

We recognize that our vote in support of the shareholder proposal to introduce a one share, one vote capital structure is not likely to effect a change in approach by the company given our vote is diluted under the current dual class structure. Nonetheless, we believe it is important to send a clear signal that proportionate voting rights are, in our view, integral to good governance and accountability.

We will continue to engage with the company regarding the governance of and reporting on material business risks and opportunities. We will monitor closely the company's progress on independent board leadership and policy enforcement, amongst other factors critical to Facebook's ability to generate sustainable long-term returns. If the company's progress falls short, we will signal our concerns in future voting on management and shareholder proposals.

Case study 3: Amazon[7]

BIS regularly reviews Amazon's governance structure and risk profile. In prior engagements with the company's board and management, we have discussed a range of material issues driving long-term shareholder value, including corporate governance practices, sustainability efforts, enterprise risk management, and human capital management.

During our most recent engagement, in addition to discussing human capital management, we discussed the topics raised in the shareholder proposals to be voted on at the annual meeting and the company's oversight and management of those issues that are relevant to their business model. This included the company's plans to improve its disclosure on food waste and food diversion management and its efforts to monitor the use of certain technologies and enforce compliance with its product policies. Amazon has demonstrated a commitment to adopting best practices in corporate governance (e.g., 90% board independence, 50% board gender diversity, and balanced board tenure). As a result of past engagements, the company has agreed to enhance its governance policies, as noted by management's proposal to lower the threshold for shareholders to request a special meeting.

[6] For full disclosure please see Voting Bulletin at https://www.blackrock.com/corporate/literature/press-release/blk-vote-bulletin-facebook-jul-2020.pdf

[7] For full disclosure please see Voting Bulletin at https://www.blackrock.com/corporate/literature/press-release/blk-vote-bulletin-amazon-jul-2020.pdf

9.2. Active equity manager

166. The Fund has a 16% target allocation to an active global equity mandate, managed by MFS.

167. MFS undertakes a broad range of engagement activities with investee companies on behalf of clients. These engagements can take varying forms, such as formal proxy voting lead engagements, informal investment team engagements, more formal investment team engagements and other collective forms of engagements. Additionally, MFS participates in various industry working groups and organisations that seek to develop thought leadership on emerging proxy voting issues.

168. MFS' engagement discussions cover a broad range of topics including but not limited to climate change and the environment, remuneration, diversity, gender pay gap, board composition and labour practices. The goals when engaging are to exchange views on environmental, social and governance topics that represent material risks or opportunities for companies or issuers and to effect positive change on such issues.

169. Currently MFS does not have a systematic way of capturing all engagements for reporting purposes. However, the manager is committed to increasing the level of transparency and data provided to clients.

170. During the 2020 calendar year, at a firm wide level MFS was eligible to vote on 22,976 ballot items at 1,992 shareholder meetings across 60 markets. MFS voted shares at approximately 99% of these meetings, with the remaining meetings not voted due to share blocking concerns (nine meetings), late receipt of ballots (one meeting) or market-specific voting impediments (thirteen meetings).

171. MFS has provided examples of engagement activity during 2020.

Example 1: Waters Corporation

In July 2020, our US-based ESG analyst and the covering industry analyst engaged with the board chair of US health care company Waters Corporation in a discussion of issues relating to board structure and corporate culture, including excessive board and C-Suite tenure — both of which could create a culture of complacency versus innovation, especially when competition appears to be increasing. Coming out of the discussion it was clear that the board required a refresh and changes were imminent. These changes would likely cause some short-term disruption, but could be positive in the long run. We plan to continue monitoring the evolution of the board and company culture.

Example 2: Honeywell International Inc.

In September 2020, members of our proxy and investment teams engaged with senior representatives of Honeywell International Inc., including the chair of the board's Corporate Governance and Responsibility Committee, to discuss the company's response to COVID-19, including the outreach and support provided for company employees along with various board- and governance-related matters. Preservation of shareholder accessibility at the company's 2020 virtual meeting included a live Q&A period, responses via email to all unanswered questions, and public disclosure of the meeting transcript. We discussed board refreshment and the evaluation process. We noted the addition of two women to the board in the past two years, increasing female representation to 31%.

In light of Honeywell's appointment of a new lead independent director (LID) in 2020, we also discussed the structure of a combined CEO/chair role and the importance of the LID role to understand how they provide robust,

independent oversight of the board. Additionally, we note that the company has adopted reporting in line with the TCFD and SASB frameworks. Finally, we continue to engage with the company on political and lobbying disclosures to monitor alignment of such contributions with the company's stewardship commitments. Honeywell continues to improve related disclosures by publishing a list of contributions made above $50,000 to trade associations.

Example 3: Abbott Laboratories

In December 2020, our proxy team sent a formal engagement letter to the Abbott Laboratories board of directors regarding a shareholder proposal at their most recent annual shareholder meeting, which received support from a majority of shareholders. The proposal requested that the company eliminate the supermajority vote requirement. We shared our belief that the voting results signal a significant level of concern from shareholders, and requested that the board of directors provide shareholders with a thoughtful and meaningful response to the vote results prior to the company's next annual shareholder meeting. This letter was part of the proxy team's ongoing letter writing initiative that focuses on encouraging our portfolio companies to respond to particular areas of concern for shareholders.

Credit/Private debt manager

172. The Fund has a 15% target allocation in credit/private debt, spread across the M&G European Loan Fund and M&G Illiquid Credit Opportunities Fund.

M&G Illiquid Credit Opportunities Fund

173. The M&G Illiquid Credit Opportunities strategy follows a buy and hold approach, with the majority of returns derived from received coupon income over the life of the funds. This means that ESG engagement and analysis is primarily from a risk mitigation perspective and conducted with a view to ensuring that the asset is able to fulfil its payment obligations throughout its life and avoid default or covenant breaches. M&G's analysts conduct engagement at the research and due diligence phase of the asset, and this engagement will involve ensuring any material ESG issues are raised.

174. The subject of the engagement will naturally vary depending on the sector/industry of the borrower. As sector specialists, the analysts are well placed to ensure that ESG engagement is conducted on the issues most material to long-term financial performance. In order to create a robust structure to engagement practices across the firm, M&G has adopted the SASB framework for public side analysts. This allows their engagement to be more targeted.

175. On the private side, disclosure tends to be worse and therefore this can create challenges in certain aspects of engagement. However, M&G's private analysts are looking to implement the SASB principles over the next 12 months in order to mitigate these. Whilst it is difficult to track the effect that individual engagements have on the financial performance of an asset, as often the sole lender in private debt transactions, M&G is able to exert a greater influence on company management than public bonds.

176. The manager does not track data on engagement activity systematically at present but is in the process of developing tools to do so.

M&G European Loan Fund

177. The team's approach is to utilise M&G's status as a very large, private-side lender and exploit the lobbying and engagement opportunities that this affords. M&G engages with both company management and, where relevant, company owners and participate actively in market initiatives.

178. The manager has a regular calling-programme with Private Equity sponsors to review and appraise their ESG policy implementation which forms part of the investment decision.

Engagement examples

179. M&G provided examples of engagement undertaken for assets held within these two strategies to demonstrate the approach taken by the investment teams.

COMPANY SUMMARY Recruitment receivables
BACKGROUND Debt facility provided to a company providing operational and financing solutions to recruitment agencies. Structured as an Asset Based Lending facility secured on invoices payable by companies employing temporary workers.
ENGAGEMENT STATUS Ongoing **OBJECTIVE FOR ENGAGEMENT** Improvement of governance and risk controls. **ACTION** Despite initially declining the investment, we continued our dialogue with the borrower. We made recommendations with regards to the issues surrounding governance/risk controls, which were implemented. A new Chief Risk Officer was appointed to oversee these changes. Post implementation we monitored the company for approx. 9 months. **OUTCOME** We initially declined the investment due to inadequate risk control framework in the company, as well as governance issues. After a satisfactory monitoring period, we invested in the company. The period from initial engagement to investment was 18 months. We continue to focus on risk and the company is aware that this is important to us. We continue to have ongoing dialogue with the company.

COMPANY SUMMARY Privately placed (PP) note issuance for offshore windfarm refinancing
BACKGROUND Communication flow between the Borrower and the Lenders has been poor since closing the deal, with information often being delivered late and with insufficient detail. Major changes were being made to the assumptions that underpin the financing, with Lenders being notified late, with limited scope to discuss in detail.
ENGAGEMENT STATUS Complete

OBJECTIVE FOR ENGAGEMENT To ensure improved communication flow and better quality analysis from the Borrower. **ACTION** M&G worked over the past year to raise such concerns with other co-lenders, to help drive appropriate engagement from the lender group and strengthen our position in getting these governance issues resolved. Consistent requests for a management call were finally met with a one-to-one call with each investor. The call took place on Friday 11th December with participation from the Borrower and the Sponsor/Operator. The team provided a helpful update on the project's performance, and provided M&G with the opportunity to raise our concerns. **OUTCOME** Management has committed to a one-to-one update every six months, which we believe will help address the said governance issues and encourage better dialogue. We have now established a direct line of communication with the management team (rather than via the Agent) which provides for an escalation route, if issues are not being addressed in the future. We directly provided the team with a list of outstanding issues that need to be addressed (which were previously provided to the Agent as well).

Real estate managers

180. During the reporting period, the Trustees have investment in real estate assets through three funds, which collectively accounts for 10% of target allocation:

- Schroder UK Real Estate Fund
- UBS Triton Property Fund
- BlackRock UK Property Fund

181. These managers invest directly in real estate assets (and under certain circumstances, other real estate funds) rather than in listed companies, therefore their engagement activity is predominantly focused on occupiers, third party managers and suppliers, community, and investors, which is summarised below:

Schroders	Schroder Real Estate seeks active engagement with tenants to ensure a good occupational experience to help retain and attract tenants. Schroders' occupier engagements include regular tenant meetings, the use of online occupier portals, tenant satisfaction surveys, and annual newsletters. Examples of ESG matters discussed include: a new food waste system at a retail and leisure scheme, and trials for changes to the operational times of a building management system for a multi-tenanted office. Schroders has produced a Sustainability Fit Out Guide for Tenants to highlight why sustainable and healthy fit out is important, and guide them through how to implement, for example energy efficient lighting, indoor air quality, and biophilia.

	Schroders' community engagement is dependent upon the type of asset and how it and its users relate to the local community. With a shopping centre there may be communications to help determine local attitudes to the centre, amenity, safety and security, access and open space as well as support opportunities for recruitment. For a fully let office building examples may include sponsorship for a street festival and a youth centre.
UBS	UBS recognises that standing investments – offices, shopping centres, industrial estates – benefit local communities even though it may not be obvious at first sight. In order to assess the social value of investments, UBS has worked with tenants and its property and facilities management teams onsite to understand and measure things such as local employment levels, traineeships, jobs for young offenders, community events held at the property, and volunteering. UBS aims to prompt conversations with occupiers and suppliers, using these assessments to benchmark value and help connect interested parties at properties with the ultimate aim of further enhancement.
BlackRock	BlackRock's real estate portfolios strive to actively engage with tenants to further communicate and progress sustainability performance across assets. The range of activities often include a combination of campaigns, activities and events that address sustainable best practice, such as energy and resource efficiency. BlackRock also explores opportunities to participate in tenant meetings and conduct annual tenant surveys and questionnaires that address ESG factors, such as environmental improvement, energy efficiency and occupier health and well-being, as well as a broader array of questions focused on facilities management, property maintenance, security, housekeeping, and satisfaction with property management services.

182. The managers are also requested to provide specific examples to demonstrate compliance with the Fund's Voting and Engagement Policy as part of ongoing monitoring. For instance, BlackRock provided a case study on Birmingham Business Park detailing sustainable campaigns and tenant engagement, with outcomes:

ESG Case Study

Sustainable campaigns and tenant engagement at Birmingham Business Park

Programme Summary

Sustainability campaigns have been implemented at various properties across the BlackRock UK Property Fund to engage with tenants on a range of sustainability topics; from energy efficiency and carbon reduction, to sustainable transport and travel, waste management and recycling, wildlife conservation, and health and well-being.

Key Programmes and Campaigns

BBP is a large office campus comprising over 1.7m sq ft of office space, spread across 148 acres of mature parkland, and with over 130 occupiers, including Rolls Royce, IMI and Goodyear. Ongoing sustainability campaigns, together with quarterly 'Sustainability Week' events are now held at BBP and are open to all occupiers, as well as the wider local community. Campaigns and initiatives have included:

- The establishment of three on-site bee hives. The 'BBP Honey' generated by the bees is sold on-site to tenants and visitors, with all proceedings going to local charities.
- On-site pond dipping, woodland walks and 'wildlife awareness' talks at lunchtimes and after hours.
- The provision of 'Pool Bikes', together with on-site cycle storage facilities, for the use of all tenants.
- The establishment of a Community Cycling Club that holds guided cycle rides twice a week. The rides are open to all levels and championed by fully experienced riders from some of the on-site occupiers.
- Energy 'Switch-off' weeks, including internal competitions between tenants to be the 'Super Saver'.
- Waste awareness and recycling weeks in association with our appointed waste contractors.
- The establishment of Community Allotments which are sponsored and used by Park occupiers. In addition, two vegetable beds are dedicated to Age UK, who bring Solihull residents to nurture and for outdoor exercise.
- Supporting Marston Green Junior School with careers mentoring and activities and the sponsorship of the Junior Football Club
- Establishment of weekly well-being activities including yoga, pilates, tai chi, Nordic walking and meat free Mondays
- Further awards include: International Gold Corporate Social Responsibility Award, Silver Corporate Social Responsibility Award, Gold Green Apple Award – Community Cycling Club, Gold Green Apple Award – bi annual sustainability weeks, Silver Cycling Score

Key Outcomes

BBP was awarded the Transport for West Midlands Top Cycling Award and Top Walking Award in 2017 in recognition of the efforts to encourage more sustainable modes of transport for all occupiers and tenants.

Source: BlackRock as at 30 September 2020

Bond manager

183. The Fund has a 7.5% target allocation to the GIS Global Libor Plus Bond Fund managed by PIMCO.

184. While ESG-focused engagement is not a requirement of the Fund, the GIS Global Libor Plus Bond Fund indirectly benefits from the intensive engagement work pursued in PIMCO's ESG dedicated portfolios, given that issuers may be held in both strategies and there is often an overlap of issuers between strategies should PIMCO have a positive credit view on the specific issuer.

185. PIMCO conducts engagement based on opportunities that they believe will have the most significant impact unique to each issuer and encourages alignment of business activities with the Sustainable Development Goals (SDGs), including via green / sustainable bond issuance and track progress over time.

186. The broad engagement metrics of PIMCO's engagement activity is summarised below:

- The portfolio has engaged with 253 corporate issuers over the course of 2020
- It represents 15.9% of the holdings (and 64.3% of the corporate bond holdings) of the portfolio as of 31 December 2020

187. PIMCO's credit research analysts engage regularly with the issuers that they cover, for example in the corporate space discussing topics with company management teams related to corporate strategy,

leverage, and balance sheet management, as well as ESG-related topics such as climate change targets and environmental plans, human capital management, and board qualifications and composition. For portfolios like the PIMCO GIS Global Libor Plus Bond Fund, this engagement is focused on material ESG issues that can have significant impacts on the credit profile of the issuer.

188. PIMCO demonstrated how outcomes of engagement have informed investment decisions (buy, sell, hold) in the fund, with case studies:

Lloyds Banking Group

Lloyds is the UK's largest commercial bank, with a dominant position in retail

- Lloyds has limited direct exposure to transition risks
- Lloyds has started undertaking climate risk scenario analysis as per the TCFD recommendations From a social perspective, Lloyds was the first FTSE company to set diversity targets, and proactively engaged employees to enhance its human capital management

Engagement:

- PIMCO engaged Lloyds for a refresh of their latest ESG data and development
- We hold ongoing discussions on their progress and plans on climate risk assessment, Paris alignment, sectoral policy, human capital support towards digitalization and how ESG is reflected into employee performance assessment.
- PIMCO aims to maintain the dialogue for follow-up discussion on these areas moving forward

Avoid specific sector

As part of our broader ESG framework, engagement is particularly important to PIMCO's investment analysis

Example:

- For example, our healthcare team included the ESG engagement analyst on a call with a pharmaceutical company to evaluate and underscore its oversight of material product risk factors where the focus of the issuer's reporting was traditionally on operational resource efficiency (emissions, water) only.
- Opioid litigations have been impacting our views on individual issuers in this sectors and led to underweight recommendations by our Credit Analyst team for all our portfolios

189. PIMCO provided below examples of engagement, with mixed outcomes:

Case study: Sumitomo Mitsui

Year engagement was initiated	2020
Objectives	Lending policy could be improved along ESG lines. Moreover, the issuer's green bond reporting was not fully aligned with industry best practices.
Who has led the engagement	The credit analyst covering this issuer who is responsible for the interaction with the company alongside our ESG team
Final outcome	PIMCO engaged on their Green bond program, environmental impact method and reporting to align to industry best practices. In addition, PIMCO discussed our

	view on potential improvement in their lending policies, commitment to align to the Paris Agreement, and linking ESG metrics to management performance review. Ultimately, the company published a sustainability report and recently initiated further green bond issuance

ASIAN ELECTRIC UTILITY

- **Background:** Our ESG assessment identified a lack of alignment between the firmwide climate strategy and the environmental objectives of its green bond, specifically the pace and visibility of its transition from coal to low-carbon sources of energy.
- **Engagement:** We engaged in 2019 to highlight the importance of setting goals in line with the Paris Agreement***.
- **Outcome:** While the information provided along with its inaugural green bond issuance did not meet our expectations, we will continue to monitor the company's progress on setting concrete targets for phasing out coal generation or greenhouse gas emissions.

10. Collaboration

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

190. The Trustees are willing to act collectively with other investors and expect their managers to collectively engage with other investors, where appropriate. They encourage their investment managers to actively participate in collaborative engagements with other investors, fund managers, and organisations where this is deemed to be in the best interests of the Fund. The Trustees will consider opportunities to collaborate with other stakeholders and industry bodies, bearing in mind the resources available to support the Fund.

Passive equity manager

191. BlackRock engages the global investment and corporate community to promote a sustainable financial system through a number of coalitions and shareholder groups. Industry affiliations provide important forums in which to advocate for BlackRock's views on a variety of corporate governance and sustainability topics, as well as listen to the views of peers.

192. BlackRock has been a signatory to the United Nations supported Principles for Responsible Investment (PRI) since 2008. The six aspirational statements of PRI provide a framework in which ESG issues can be taken into account in investment decision-making and engagement with investee companies, clients, and other stakeholders. As a signatory, BlackRock commits to upholding all six principles. In 2019, BlackRock's Investment Stewardship function received A+ scores in Strategy & Governance and Listed Equity Active Ownership. Notably, for direct active ownership score for listed equity, BlackRock exceeded many other institutional manager respondents placing in the top 17% of 512 investment managers (83rd percentile) for collaborative engagement.[8]

193. BlackRock joined Climate Action 100+ (CA 100+) in January 2020, a natural progression to advance corporate reporting aligned with TCFD. CA 100+ is a group of investors that engages with companies to improve climate disclosure and align business strategy with the goals of the Paris Agreement. Prior to joining, BlackRock was a member of the group's five partner organisations.

194. An example of a recent collaborative engagement is BlackRock's work as a member of CA 100+'s Asia Advisory Group, and the Asia-region sponsoring organisations. BlackRock seeks to provide the group with strategic insight into the characteristics of local Asian markets to help inform engagements. Together with Cathay Financial, the manager has taken on the role of lead investor in engagement with China Steel, a Taiwanese company. In this engagement, BlackRock encourages China Steel to enhance its climate disclosures and to pursue more ambitious targets and investment plans to transition its business in line with a lower than 2-degree Celsius scenario.

195. BlackRock also provided a case study on Total to illustrate collaborative engagement.

[8] Source: BlackRock Investment Stewardship, at https://www.blackrock.com/corporate/literature/publication/blk-profile-of-blackrock-investment-stewardship-team-work.pdf

Case study

Total

BIS engages independently with CA 100+ focus company.

Total is a French oil and gas energy company. BIS has engaged extensively with Total over many years on climate risk and the implications for its long-term strategy. Earlier this year our engagement intensified to encourage the company to pursue more ambitious greenhouse gas (GHG) emissions reductions targets. Other CA 100+ members also engaged with Total over that same period. On May 5, the company issued a joint statement with members of the CA 100+ collaborative effort announcing new net zero emissions ambitions for parts of its business and more aggressive 2050 targets for reductions in the carbon intensity of its energy products used by its customers.

Because of this progress, BlackRock and many other members of CA 100+ declined to support a shareholder proposal seeking enhancements to the company's long-term targets, since the company, through its own actions (as reflected in the joint Total-CA 100+ statement), had already substantively met the request made in the proposal.

Active equity manager

196. At this time MFS does not have a systematic way of capturing all collaborative engagements for reporting purposes, and will continue to improve tracking.

197. During Q3 2020, MFS, along with other investors, joined **Fidra** (a UK-based non-profit) to draft a joint letter to a number of supermarkets, food-to-go, packaging and fast-moving consumer goods companies requesting that they entirely remove per- and polyfluoroalkyl substances (PFAS) from their food packaging products. This chemical is known to be hazardous and may cause cancer. Several companies responded positively, including one company that committed to eliminate PFAS from their food packaging entirely. MFS investment team members will ask corporate management teams about their stance on PFAS in food packaging in upcoming engagements with the goal of getting these target companies to consider removing these hazardous chemicals.

198. Last year, **ShareAction**, an industry group that promotes responsible investment, evaluated the 75 largest global asset managers — a group that includes MFS — across four key areas: responsible investing governance; climate change; human rights; and biodiversity. The results of the survey indicated a strong preference for detailed and proactive policies around each of these areas. This gave MFS the opportunity to engage with ShareAction and exchange views on sustainable investing best practices, which has helped MFS enhance its approach and provided the group with insights that may impact its future work. During these discussions, MFS learned about, and subsequently became a signatory of ShareAction and now participates in their **Workforce Disclosure Initiative** (WDI). The goals of the WDI are to improve corporate transparency and accountability on workforce issues, provide companies and investors with comprehensive and comparable data and help increase the provision of good jobs worldwide. This work is highly aligned with areas of particular focus for the MFS investment team. MFS believes workforce, supply chain, diversity, wage, and other employment data is material information that is important to active investors and generally poorly disclosed.

199. During the fourth quarter, MFS became a signatory to **Climate Action 100+**, an investor-led initiative to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change.

Climate Action 100+ focuses on engaging with 167 companies that are critical to the net-zero emissions transition. Investor members are responsible for driving engagement and developing and implementing company-specific engagement strategies. As part of being a signatory, MFS joined three company engagements — **Lockheed Martin**, **Rolls Royce** and **Duke Energy**. Through these engagements, MFS hopes to encourage these companies to implement a strong governance framework on climate change, take action to reduce greenhouse gas emissions across the value chain and provide enhanced corporate disclosure.

200. Finally, MFS is signatory to a number of collaborative investor statements. The firm signed several investor letters, including:

- a letter to the United Nations calling for urgent action on the stranded seafarer crisis,
- a letter in support of living income and living wages in agricultural supply chains, and
- a letter calling for improved transparency into the supply chains and ESG due diligence in the luxury fashion sector.

Credit/Private debt manager

201. As part of ongoing active memberships of the Investment Association, UNPRI, the Investor Forum and Institutional Investors Group on Climate Change (IIGCC), among others, M&G participated in a number of meetings and discussions around a variety of ESG topics during the reporting period, such as the Investment Association (IA) Remuneration and Share Schemes Committee, the IA Stewardship Committee, and the Institutional Investors Group on Climate Change (IIGCC) AGM.

202. In December, M&G became one of the 30 signatories to the 'Net Zero Asset Managers initiative' (NZAM), launched on the fifth anniversary of the Paris Agreement. Signing up indicates acknowledgement of the urgent need to accelerate transition towards global net zero emissions and the role that asset managers have to play in that process. A commitment to support the goal of net zero GHG emissions by 2050, in line with global efforts to limit warming to 1.5 deg. C - and to support investing aligned with net zero emissions – is made. Specifically, this means working in partnership with asset-owner clients on decarbonisation goals, setting interim targets for progress by 2030, consistent with a 50% global C02 reduction - and reviewing them every five years – as well as implementing a stewardship and engagement strategy across all assets under management that is consistent with the stated ambition.

203. Specific to Leveraged Finance, M&G was part of the roundtable discussions with issuers, hosted by European Leveraged Finance Association (ELFA), a buy-side committee that seeks to lobby for positive change in market practice, and the Principles for Responsible Investment (PRI), with a view to promoting consistent and improved disclosure of pertinent sectoral ESG risks. M&G also consulted with company owners (private equity sponsors), facilitated by ELFA and PRI, as a prelude to the issuance of some sector-specific and general ESG disclosure guidelines for their advisers.

204. M&G is part of the ESG subcommittee of ELFA, and have been actively involved in the preparation of an 'ESG factsheet' which will be used to lobby borrowers/issuers for better disclosure of ESG matters in the new-issue process. The manager is also a long-standing board member of the Loan Market Association which jointly issued the above with ELFA.

205. M&G chairs the loan committee of the ELFA and contributed to a publication to highlight the (mis)use of 'Covid adjustments' to 'earnings before interest, taxes, depreciation, and amortization' (EBITDA) via utilisation of grey areas in documentation (see below response to Principle 12). M&G supported the group

in publicising their collective displeasure at such action, the initiative also receiving support from the International Organization of Securities Commissions (IOSCO).

206. M&G is also founding signatories of Climate Action 100+, working with other major investors globally to push for improved transparency and reduced GHG emissions at companies operating in high carbon industries.

207. The manager provided an example of engagement activity where a borrower in the chemical industry was motivated by M&G's participation in Climate Action 100+.

- We have communicated to the Company, M&G's participation in the Climate Action 100+ which confers a responsibility of increasing requirements from our clients with regard to our actions and processes in assessing ESG standards of our investee companies, and our thinking around active engagement with investee companies who are exposed to high ESG risks.
- We have also provided guidance on the desired level of disclosure that we encourage the Company to incorporate, including science-based targets and defined operational Key Performance Indicators. Disclosure to CDP is also highlighted as an important way for investors, like M&G, to engage with the Company and the rest of the industry. Other reputable benchmark organisations we recommend the Company to consider, include the Transition Pathway Imitative (TPI) and the Task Force on Climate-Related Financial Disclosures (TCFD).
- Our feedback and recommendations were well received by the Company.

Real estate managers

208. The managers recognise the importance of industry engagement, the contributions they can make to progress the real estate sector, and the value that such engagement can bring to their own investment strategies and methodologies.

209. Schroders, for instance, sees climate change as a key area for collaborative engagement. Schroders has written to the companies in the FTSE 350 index, asking them to publish detailed and fully costed transition plans on climate change. Schroder Real Estate signed the Better Building Partnership (BBP) Members Climate Change Commitment, which recognises the significance of buildings in relation to carbon emissions and the role that landlords should play in driving energy reductions and efficiencies and potential for renewables. Alongside other BBP Members, Schroder Real Estate made the commitment to achieve Net Zero Carbon by 2050 and published their Net Zero Carbo Pathway in December 2020.

210. BlackRock also regularly engages with the global investment and corporate community with a view to promoting best practice and further progressing their approach to real assets sustainable investing and ESG integration. BlackRock participates in, and works closely with, a number of leading industry bodies and reporting frameworks and networks that promote sustainable and responsible investment, including the United Nations Principles for Responsible Investment and GRESB (formerly the Global Real Estate Sustainability Benchmark).

Bond manager

211. As one of the world's largest bondholders PIMCO has a large and important platform with which to engage issuers to drive meaningful change on sustainability dimensions. The manager aims to have an industry leading engagement program among fixed income asset managers. By investing across a

diverse asset class and group of issuers - including corporates, municipalities, sovereigns, and others - PIMCO is ideally positioned to drive greater change than through exclusions or evaluations alone.

212. PIMCO has reported that their collaborative engagement approach has the potential to result in tangible, positive changes in certain companies given the strength and history of their platform. For example, PIMCO co-led the engagement below along with other investors to encourage the company to set ambitious carbon emission reduction targets:

U.S. INDEPENDENT POWER PRODUCER (VISTRA ENERGY)

- **Background:** The issuer has a leading presence in the U.S. residential market. While its installed capacity and energy mix are dominated by fossil fuels, notably gas and coal, it had not set a carbon emission reduction target and advanced energy transition plan at the time of the release of its 2018 Sustainability report.
- **Engagement:** In the context of the CA100+ initiative**, PIMCO co-led the engagement with the issuer along with other investors to encourage the company to set ambitious carbon emission reduction targets and align its disclosure with the TCFD recommendations.
- **Outcome:** The company unveiled a long-term carbon emission reduction target and fleshed out its climate governance and support for carbon pricing. We will continue to follow up regarding the opportunity for a more detailed climate risk disclosure and ambitious strategy in the future.

213. In order to drive a more globally ESG effort, PIMCO collaborates closely with key industry groups, for example:

- PRI Bondholder Engagement Working Group: This group is comprised of around 15 asset owners and managers who support the Principles for Responsible Investment (PRI) by sharing their knowledge and experience in using bondholder engagement as a tool to help investors manage and mitigate investment risks related to ESG factors. Role includes exploring, defining, and identifying trends in bondholder engagement, and publishing guidance for investor implementation.
- Climate Bonds Initiative (CBI): CBI is a leading organization focused on fixed income and climate change solutions. CBI has been instrumental in supporting more robust data and standards to propel the green bond market, and remains heavily involved in shaping new green bond-related regulations. Partnering with CBI is an exciting development in the context of PIMCO's efforts to promote robust and innovative investment criteria and products to help advance the Paris Agreement on climate change.
- International Capital Market Association (ICMA): PIMCO has a seat on the Green Bond Principles (GBP) and Social Bond Principles (SBP) Executive Committee that helps shape the evolution of the green bond and social bond markets.

214. PIMCO also partners with and supports other initiatives, including Climate Action 100+, Task Force on Climate-related Financial Disclosures (TCFD), Carbon Disclosure Project (CDP), Institutional Investors Group on Climate Change (IIGCC), and Transition Pathway Initiative (TPI).

11. Escalation

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

215. Responsibility for day-to-day interaction with issuers is delegated to the Fund's investment managers, including the escalation of engagement when necessary. Managers are expected to disclose escalation activities as part of their annual statement of compliance with the Fund's stewardship policy.

Passive equity manager

216. Through engagement BlackRock seeks to build an understanding of a company's approach to governance and sustainable business practices, and communicate their views to ensure companies understand investors' expectations. However, despite repeated engagement efforts there are instances where escalation has been necessary.

217. BlackRock's sustainability report[9] details decisions to vote against a number of companies due to sustainability concerns and to put a number of companies "on watch" ahead of the 2021 voting season if progress is not delivered in line with expectations. Various published Voting Bulletins also illustrate cases where engagement has resulted in escalation (votes against).

Example 1: BlackRock's approach on climate engagement

We have been engaging for several years with companies – particularly those in carbon-intensive industries – regarding the need to enhance disclosure of climate risks and how they will impact business models over time. We began this process with a series of letters in 2017 and 2018, prioritizing companies with the most carbon-intensive business models where BlackRock's clients collectively were significant shareholders.

Our objective was to bring the final recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) to the attention of company leadership and ask them to consider reporting in line with the TCFD framework. This past January, we elevated our request, explicitly asking companies to report in line with TCFD standards.

In our direct dialogue with company leadership, we seek to understand how a company's strategy, operations and long-term performance would be affected by the transition to a low-carbon economy and other climate risks. Broadly, we aim to ensure that companies are effectively managing the risks and opportunities presented by climate change and that their strategies and operations are aligned with the transition to a low-carbon economy – and specifically, the Paris Agreement's scenario of limiting warming to two degrees Celsius or less, which is laid out in the 'Metrics and Targets' pillar of the TCFD framework. Such engagement can help inform the approach taken by corporate leadership as they advance their sustainability practices and disclosure.

Our approach employs a natural escalation process. If we are not satisfied with a company's disclosures, we typically put it 'on watch' and give the company 12 to 18 months to meet our expectations. (The complexity of many sustainability issues may necessitate detailed reviews of operations by the company if it is to make substantive disclosures that inform investors.) If a company

[9] BlackRock: Our Approach to Sustainability, at https://www.blackrock.com/corporate/literature/publication/our-commitment-to-sustainability-full-report.pdf

has still failed to make progress after this timeframe, voting action against management typically follows.

Example 2: BlackRock holding companies accountable when they fall short of expectations

Since the beginning of the COVID-19 pandemic, we have engaged with more than 380 companies across all 11 GICS sectors and 29 countries globally to understand how they are balancing short-term pressures created by the COVID-19 crisis with efforts to oversee long-term material financial and operational performance.

In particular, we have focused on how the crisis has impacted companies' commitment to sustainable social practices – that is, the compensation, employee development and advancement, working conditions for employees and suppliers, local community outreach, and other measures companies put in place to build a diverse, engaged workforce and a strong corporate culture within supportive local communities.

Because COVID-19 poses an existential threat for many companies, it is also straining the social contract between companies and their employees and other stakeholders. As companies reduce staffing levels and restart post-lockdown, for many workers, the promise of decent work in safe conditions feels increasingly remote. In some countries, the resultant economic dislocation has heightened economic, gender and racial inequality. As long-term investors, we believe that companies forced into difficult choices affecting employees, suppliers and local communities – especially those companies receiving government financial support – need to make prudent, balanced decisions about executive and board compensation and allocation of capital.

Where we are unconvinced that companies are preserving their social license to operate – whether in the context of the pandemic or more broadly – we may take voting action.

For example:

- We voted against management at Tyson Foods, a U.S. packaged food company, by supporting a shareholder proposal on supply chain due diligence because we were not satisfied with the company's disclosures and practices around sustainable working conditions.
- We voted against the re-election of a director at McKesson, a U.S. pharmaceutical company, for the company's failure to take adequate remedial action for their role in the U.S. opioid crisis.
- We supported a shareholder proposal at financial services company Santander Consumer USA where we were concerned that the risks of racial discrimination in lending practices were not being managed in a transparent and effective manner.
- We supported a shareholder proposal at U.S. technology company Fortinet that demanded greater disclosure around the company's diversity and inclusion efforts.
- And we voted against management at Ocado, a UK online grocery retailer, over concerns that the board did not exercise appropriate oversight of executive compensation given the current economic environment, potentially harming its relationship with consumers.

We believe issues that could threaten a company's license to operate will become even more acute in the wake of the COVID-19 crisis.

Active equity manager

218. At this time MFS does not have a systematic way of capturing all escalation of engagements for reporting purposes, and will continue to improve tracking.

219. While part of the engagement covers the reporting period, as long-term shareholders, MFS views engagement as an ongoing discussion aimed at producing outcomes over the long term. Escalation may begin within MFS' engagement process with increased discussions with management and board members, formal letters sent from the investment team, exercising the right to vote against management on proxy votes, trimming positions or divestiture. Below is a case study provided by MFS to demonstrate their approach to escalation.

Case study: EssilorLuxottica SA

EssilorLuxottica SA designs, manufactures, and markets a range of lenses, frames, and sunglasses to improve and protect eyesight. The company is the largest player in the global eyewear market. The 2017 merger agreement between Essilor (France) and Luxottica (Italy) created an evenly divided board for the new entity, EssilorLuxottica, on a joint basis until 2021. However, a dispute between the two parties was revealed in March 2019 when the controlling shareholder alleged that Essilor violated the merger agreement. This dispute highlights the risk in not having independent senior leadership on the board, as there was no one in a position to resolve the disagreement internally as the board was split evenly between both parties. It also prevented the board from focusing on its duties to all stakeholders to ensure the long-term sustainability of the company, and it is also likely to have impacted management's ability to maintain daily operations.

In 2019, as part of ongoing engagements with the company, MFS had conversations with management regarding governance and culture at the combined company. A settlement was reached before the 2019 AGM with both sides agreeing to end legal proceedings and resolve the company's governance issues. Aware of these issues, MFS voted in favour of both shareholder proposals regarding the proposed addition of new, independent board members[10].

Throughout 2020, MFS had many engagements with different parties at the company to escalate concerns, including the Chairman of the board. As a result of these discussions, which did not satisfy the manager's concerns, in strategies with larger positions MFS trimmed back positions in the company, while maintaining some of the smaller positions. As the three-year merger agreement expires this year, a new board of directors will be proposed to shareholders and voted on at the May 2021 AGM, after which a new CEO is expected to be nominated. This is widely thought to be the turning point for the integration to start in earnest (the two companies seem to still be run in parallel to a large degree) and for synergies to be delivered from the completed merger.

Despite these governance concerns, MFS continues to believe that this company has a defensible competitive position, reasonable valuation and that the potential for positive governance changes to occur in 2021 will provide a strong unpinning to the security's share price. The synergies being created from the combined company and its clear leadership position within a fragmented industry support this investment thesis.

[10] PCPF did not hold EssilorLuxottica SA at the time of the 2019 AGM.

Credit/Private debt manager

220. M&G provided a summary of activity and outcomes of escalation undertaken for the two funds that they manage on behalf of the PCPF during the reporting period, with examples.

Examples:

- Despite having a proven track record in the sector (ground mounted solar plants), the sponsor failed to provide the level of reporting required by the financing documents. Our ability to monitor ongoing performance of the plants was materially diminished due to the quality of the data provided. We escalated the issue and granted the sponsor sufficient time to rectify the situation; however, the poor quality of the reporting continued to hinder our ability to monitor the investment. The inability to manage such issues meant we were uncomfortable with the governance at the sponsor. We ultimately sought early repayment which was achieved ahead of legal maturity, and with no loss to investors. We also declined to engage in discussions with them on a long-term refinancing of those same assets.
- In 2020, we were uncomfortable with the fast acquisitive expansion of one of our portfolio companies and what the impact it would have on its governance structure. We were unsatisfied with the answers provided at the all-lender call and decided to follow-up with the management team separately (see case study below).
- We contacted a chemical company in relation to a press story that Co2 emission data had been under-reported at one of its petrochemical plants. We were comforted by the attitude taken to carbon reduction and environmental responsibility by the company and to the reminder that improving publication of their emissions and targets is a goal. We continue to have discussions with the borrower on this topic.
- We engaged with a chemical company and a health service company to encourage them to disclose their carbon emissions to the Carbon Disclosure Project (CDP). CDP is a not-for-profit charity that runs a global disclosure system for investors, companies, cities, states, and regions to manage their environmental impacts.
- We petitioned the top 27 emitters in our loan portfolios for better carbon disclosure.

Case study[11]:

COMPANY SUMMARY

The Company is a global petrol forecourt retailer.

BACKGROUND

- The company has grown rapidly via debt-funded acquisitions in recent years.
- The company announced that it had appointed a new external auditor, the company hosted a call to provide an update.

OBJECTIVE FOR ENGAGEMENT

To improve the corporate governance of the Company specifically via expanded board composition, improved oversight of internal controls and fuller disclosure so that we are comfortable that the company is managing these

[11] Please note this case study has been edited by M&G to preserve confidentiality.

material ESG risks and acting responsibly as risks around governance and controls arise naturally when a company has been on a highly acquisitive path at a fast pace.

ACTION

M&G reached out to the Group CFO and the Head of IR for a 1-1 engagement meeting, together with M&G's Head of Stewardship, Leveraged Loan fund managers and credit analysts.

KEY TAKEAWAYS FROM ESG ENGAGEMENT

- the Company are clearly cognisant of the value of good governance and the increasing scrutiny from its investor base over ESG risks.
- There is a clear intention to expand the board by injecting additional skillsets and further improving internal controls within a reasonably short timeframe. Actions have been taken in pursuit of a Chairman and Independent Directors as well as in setting up an internal audit function.
- While aware of the risks, we should continue to monitor the Company to ensure it continues to work towards improving corporate governance, particularly in the area of board composition and internal controls.

FOLLOW UP

- With the external auditor being newly installed, and with the Company taking action to recruit additional board members, we have requested to be informed on any new observations and recommendations from the auditor with regard to the control environment as well as to be updated with regard to progress in the board's expansion and composition. We also followed up the meeting with a recommendation to appoint a non-executive director who could chair an audit committee.

ESG ENGAGEMENT

We asked questions in relation to the change of auditors, board compositions and financial integrity. For confidentiality reasons, we are unable to disclose the details of the interview.

Date of Meetings	Company	M&G	Outcomes / follow up
20 October 2020 1-1 meeting with management	Group CFO Head of IR and Financial Projects	Rupert Krefting Fiona Hagdrup Michael George Adam Koller Yuqi Wang	The Company became increasingly aware of the value of good governance. M&G have been offered future opportunity to follow up with the group CFO regarding future queries/updates. We became more comfortable that the company is making progress towards the right direction. ACTION: review the situation in 3 months to identify whether progress has been made. For now, fund managers are comfortable with their holding. HOLD.

Real estate managers

221. The managers have commented that escalation (with issuers) in the traditional sense does not apply to funds investing directly in UK real estate. However, engagement, and escalation where appropriate, form part of the property manager and vendor monitoring process.

222. For instance, BlackRock has a formal process to request and review relevant policies associated with all suppliers and vendors, including appointed property managers. All new suppliers and vendors must complete a formal questionnaire that encompasses various key topics, including control documents, legal, health and safety, environmental and insurance. Existing suppliers and vendors must also complete the questionnaire to update their answers annually. As part of this process, they are asked to provide

copies of their Environmental Policies, as well as additional information pertaining to their environmental management, compliance and operating permits and licenses.

223. Where appropriate, BlackRock may also review the implementation of relevant vendor environmental policies. Meetings may also be held between the investment manager and key property managers to ensure that they are meeting their environmental obligations and objectives, and that any issues are escalated.

Bond manager

224. PIMCO views stewardship and engagement as a long-term and dynamic process that evolves over several years. While changes may take time to materialise, PIMCO analysts reinforce and follow up on ESG engagement objectives as part of their regular interactions with issuers. PIMCO has found incorporating sustainability issues into this regular dialogue across multiple touchpoints to be a highly effective method of steering for long-term improvement. Progress is assessed by both the interim steps taken by issuers and the level of effective communication. If there is a need for accelerating progress, PIMCO focuses on potential break-through points via constructive dialogues. While the manager is unable to disclose specific engagements where progress may be slower than desired, any lack of progress or response is taken into consideration.

225. For example, ongoing and constructive dialogue has proven to be crucial in the engagement with a large energy company. PIMCO maintains regular dialogue with the issuer as part of the Climate Action 100+ engagement initiative. After several meetings with the investor relations and sustainability teams, PIMCO met with the CEO of the company to emphasise best practices in terms of climate strategy and disclosure, including the importance of ratcheting up their carbon target and elaborating on their shift away from fossil fuels and their governance for climate change. PIMCO believes that the elevated discussion helps the issuer's management better understand the rationale behind their engagement objectives and has contributed to the positive changes made by the issuer later in 2020. The issuer tightened their GHG target, added a long-term net zero ambition for 2050 and outlined incremental measures for a low-carbon transition.

12. Exercising rights and responsibilities

Principle 12 - Signatories actively exercise their rights and responsibilities.

226. The Fund has delegated to its investment managers the responsibility for voting and engagement in relation to the investments that they manage on the Fund's behalf. Failure to exercise voting or other rights attached to the assets could be contrary to the interest of the beneficiaries of the Fund. The Trustees expect their investment managers to take this into account in exercising such rights on their behalf.

227. The Trustees have a commitment to monitoring the adherence of the managers to their voting policies and has instructed its equity managers to provide reports on voting and engagement activity on a quarterly basis. The quarterly reports on voting and engagement activity of the Fund's investment managers can be found on the PCPF website.

Passive equity manager

228. BlackRock uses voting as an important tool to hold companies accountable when they fall short of expectations. There are two main categories of voting actions: holding directors accountable and supporting shareholder proposals. Both can be valuable tools in the stewardship toolkit. Shareholder proposals, while often non-binding and less common outside of the U.S., can garner significant attention and send a strong public signal of disapproval. BlackRock typically uses votes against directors more frequently since they are a globally applicable signal of concern; additionally, significant votes against directors register strongly with both the individual director and the full board, and, importantly, failure to win a substantial majority frequently results in a director stepping down before the next annual meeting.

229. In certain European markets, concerns about a board's performance may be reflected by a vote against the approval (or 'discharge') of a board's actions over a year. Electing directors is a fundamental shareholder right in the vast majority of the markets in which BlackRock invests on behalf of clients, with elections held annually at most companies. As such, it is an effective, globally applicable tool to hold companies accountable for poor governance practices in general, and for lack of progress on sustainability issues more specifically.

230. Voting on shareholder proposals offers another way to express targeted disapproval of a company's policies or practices. BlackRock may support shareholder proposals that address issues material to a company's business model, which need to be remedied urgently and that, once remedied, would help build long-term value. BlackRock may support proposals seeking enhanced disclosure if the information requested would be useful to investors and if management has not already substantively provided it.

231. Below is an overview of voting metrics in relation to the passive equity portfolio based on BlackRock's Vote Summary Report for the year 2020.

Summary Voting Statistics	Number	%
Votable Meetings	721	
Meetings Voted	714	99.03%
Votable Ballots	1217	
Ballots Voted	1205	99.01%
Votable Proposals	**Number**	**%**
Total	10474	

Proposals Voted	10341	98.73%
FOR Votes	9799	93.56%
AGAINST Votes	457	4.36%
ABSTAIN Votes	88	0.84%
WITHHOLD Votes	0	0.00%
Votes WITH Management	9831	93.86%
Votes AGAINST Management	515	4.92%
Management Proposals	**Number**	**%**
Total	10426	
Proposals Voted	10293	98.72%
FOR Votes	9782	93.82%
AGAINST Votes	425	4.08%
ABSTAIN Votes	88	0.84%
WITHHOLD Votes	0	0.00%
Shareholder Proposals	**Number**	**%**
Total	48	
Proposals Voted	48	100.00%
FOR Votes	17	35.42%
AGAINST Votes	32	66.67%
ABSTAIN Votes	0	0.00%
WITHHOLD Votes	0	0.00%

232. BlackRock publishes vote bulletins[12] detailing the analysis, engagements, and votes in relation to a small number of high-profile proposals at company shareholder meetings, so that interested clients and others can understand the rationale behind BlackRock's votes.

233. A selection of case studies of stocks held in the passive equity portfolio is included below to illustrate how BlackRock has exercised voting rights on behalf of the PCPF.

Case study

Air Liquide

Voted against director and raised governance concern.

At Air Liquide, a French gas technologies and services company, we voted against the independent non-executive director standing for re-election as the board does not require annual elections of directors. Our vote signaled our concern about the company's lack of progress on TCFD-aligned disclosures. In our engagement, we encouraged the company to move to annual election of all directors (rather than staggered elections).

[12] See website: https://www.blackrock.com/corporate/about-us/investment-stewardship#engagement-and-voting-history

Case study

ExxonMobil

Voted against directors due to significant concerns about climate risk management; supported a shareholder proposal on governance.

We have engaged with ExxonMobil for several years on the issue of climate risk management. In 2020, we expressed to Exxon that we have continued to see a gap in the company's disclosure and action with regard to several components of its climate risk management.

We have centered our engagements with Exxon around our request to companies to align their reporting with the recommendations of the TCFD and SASB, which is particularly urgent for carbon-intensive companies such as Exxon.

These disclosures would allow shareholders to better assess how the company is considering climate-related risk in its strategy and how its portfolio aligns with the transition to a low-carbon economy. In response to an investor vote, Exxon released its Energy and Carbon Summary in 2018, which partially follows the four pillars of the TCFD framework. However, despite yearly incremental adjustments, we do not believe that full adherence with TCFD standards has been achieved.

We continue to have several areas of significant concern: Exxon's failure to have clear, long-term greenhouse gas reduction targets; the company's lack of disclosure around the degree of warming it expects under its stated strategy; and a lack of evidence that the board is fulfilling its duties of independent oversight and leadership.

Since there was not a relevant shareholder proposal on climate risk disclosure, the best path to express our disapproval was voting action against directors. BIS voted against the lead independent director as well as the chair of the relevant committee responsible for disclosures and climate policy oversight. Further, we voted in favor of a shareholder proposal asking the company to commit to separating the roles of chair and chief executive when the current chair/CEO vacates the role. The latter vote reflects our view that the board has not been responsive to shareholder feedback and concerns regarding climate risk management.

Case study

Fortum

Voted against directors; abstained from shareholder proposal.

Fortum is a Finnish electricity generation utility company. In early 2020, it undertook a transaction that significantly increased its exposure to coal-fired power generation and therefore the carbon intensity of its business. BIS considered this a retrograde step not aligned with long-term shareholders' interests. We held the board and president accountable by voting against their discharge. There was also a shareholder proposal for Fortum to specify an alignment of business operations with a target of limiting global warming to 1.5 degrees Celsius by amending the company's Articles of Association. We believe that amending the articles is not the most suitable tool to address climate-related matters, but we agreed with the proposal's overall goals of climate risk preparedness, and so we abstained from this proxy item rather than voting for or against.

Case study

Woodside

Publicly raised concern about insufficient progress on climate risk and reporting.

Woodside is an Australian oil and gas energy company. BIS has engaged with Woodside leadership over several years on climate risk and reporting. While we agreed with the intention of a shareholder proposal submitted to the company's 2020 shareholder meeting, we were concerned that the proposal bundled a request for public targets aligned with the Paris Agreement for Scope 1, 2 and 3 emissions by 2021[2]. Calculating targets for Scope 3 emissions is an evolving practice and we did not believe it appropriate to require the company to publish this information within such a short time frame. Nonetheless, we publicly stated that we expect Woodside to continue to review and set ambitious emissions reductions targets as the natural gas sector improves its ability to understand and manage Scope 3 emissions.

Active equity manager

234. As requested by the Trustees, MFS votes all proxies in line with the recommendations of ISS.

235. For accounts where clients have given MFS the authority to vote proxies, MFS analyses all proxy voting issues within the context of the MFS Proxy Policies, which are developed internally and independent of third-party proxy advisory firms. MFS uses a proxy advisory firm (ISS) to perform various proxy voting–related administrative services, such as vote processing and recordkeeping. While MFS also receives research reports and vote recommendations from multiple proxy advisory firms, such reports are just one input in their comprehensive analysis, which includes other more important sources of information (e.g., proxy materials, engagement, other third-party information, etc.), to determine the votes that are in the best long-term economic interest of the clients. MFS has due diligence procedures in place to help ensure that the research received from proxy advisory firms is accurate and to reasonably address any potentially material conflicts of interest of such proxy advisory firms.

236. Below is a summary of overall metrics provided by MFS in relation to the voting activity during 2020:

How many meetings were you eligible to vote at?	104
How many resolutions were you eligible to vote on?	1,443
What % of resolutions did you vote on for which you were eligible?	100%
Of the resolutions on which you voted, what % did you vote with management?	93.07%
Of the resolutions on which you voted, what % did you vote against management? *	6.93%
Of the resolutions on which you voted, what % did you abstain from voting?	1.11%
In what % of meetings, for which you did vote, did you vote at least once against management?	30.77%
* Abstentions are counted as votes against management	

237. MFS highlighted votes during the reporting period that they considered most significant for the Scheme, including:

SIGNIFICANT VOTES FOR THE SCHEME	VOTE 1
Company name	The Walt Disney Company
Date of vote	11/03/2020
Summary of the resolution	Advisory Vote to Ratify Named Executive Officers' Compensation
How you voted	As requested by the client, MFS voted in line with ISS recommendations: Against Management. For those accounts voting in line with MFS' policies, MFS voted Against Management.
Rationale for the voting decision	As requested by the client, MFS voted in line with ISS recommendations, which may be supported by rationale different than that of MFS. As it relates to accounts that vote in line with MFS' proxy voting policies, MFS voted against the executive compensation proposal due to concerns around the structure and magnitude of the executive pay program. While we have observed positive changes in recent years in response to shareholder feedback, we continue to have concerns with the pay structure.
Outcome of the vote	46.2% Shareholder Support (Votes with Management)
Implications of the outcome e.g., were there any lessons learned and what likely future steps will you take in response to the outcome?	Through our engagement efforts with the company over the past couple of years, we have expressed our concerns with the proposed remuneration scheme. The company has been receptive to shareholder feedback and has made some changes to the overall plan. However, concerns still remain. We will continue to communicate concerns with the remuneration scheme to the company and provide feedback that we believe is in the best long-term interest of the company's shareholders.
On which criteria have you assessed this vote to be "most significant"?	Ongoing engagement priorities around executive compensation and linking executive pay to long-term performance.

SIGNIFICANT VOTES FOR THE SCHEME	VOTE 2
Company name	Aptiv PLC
Date of vote	23/04/2020
Summary of the resolution	Elect Director Paul M. Meister

How you voted	As requested by the client, MFS voted in line with ISS recommendations: With Management. For those accounts voting in line with MFS' policies, MFS voted Against Management.
Rationale for the voting decision	As requested by the client, MFS voted in line with ISS recommendations, which may be supported by rationale different than that of MFS. As it relates to accounts that vote in line with MFS' proxy voting policies, MFS voted against the nominee as they serve on what we consider to be an excessive number of public company boards.
Outcome of the vote	16.50% Shareholder Support (Votes Against Management)
Implications of the outcome e.g., were there any lessons learned and what likely future steps will you take in response to the outcome?	Continue to monitor board service and discuss our concerns and voting approach with the company.
On which criteria have you assessed this vote to be "most significant"?	Linked to engagement activity, and director serves on what we consider to be an excessive number of public boards.

SIGNIFICANT FOR THE SCHEME	VOTE 3
Company name	United Parcel Service, Inc.
Date of vote	14/05/2020
Summary of the resolution	Report on Climate Change
How you voted	As requested by the client, MFS voted in line with ISS recommendations: Against Management. For those accounts voting in line with MFS' policies, MFS voted Against Management.
Rationale for the voting decision	As requested by the client, MFS voted in line with ISS recommendations, which may be supported by rationale different than that of MFS. As it relates to accounts that vote in line with MFS' proxy voting policies, MFS voted in support of the proposal as we felt shareholders would benefit from additional information on how the company plans to manage its GHG emissions as well as climate related risks and align its operations with the Paris Agreement goals.
Outcome of the vote	28.9% Shareholder Support (Votes Against Management)

Implications of the outcome e.g., were there any lessons learned and what likely future steps will you take in response to the outcome?	MFS generally supports proposals that request disclosure on the impact of environmental issues on the company's operations, sales, and capital investments. Supporting reasonably crafted shareholder proposals on climate change initiatives allows us as shareholders to better understand how the companies manage their GHG emissions and climate related risks.
On which criteria have you assessed this vote to be "most significant"?	Understanding the company's oversight and management of climate-related risks is an area of focus for our ESG team.

Credit/Private debt manager

M&G Illiquid Credit Opportunities Fund

238. Investments made for the Illiquid Credit Opportunities strategy will include a variety of financial covenants which are designed to monitor financial performance. They will comprise a number of triggers for any material underperformance against the manager's original expectations and are monitored by the analyst who initially structured the deal and is involved in the transaction throughout its life. Covenants provide M&G with a high degree of protection from adverse changes in a company's structure of financial position.

239. M&G's aim is to develop relationships with the management teams of the investee companies to promote greater engagement on financial and non-financial performance and to ensure there are no surprises in published results.

240. In addition to the covenant compliance submissions M&G also receives other information on a regular basis, such as audited final and interim financial statements as well as in certain circumstances management accounts and forecasts. Performance trends, including covenant headroom, are monitored to ensure M&G begins the conversation with management at an early stage in an effort to mitigate potential problems before they fully materialize. Where assets are underperforming M&G will seek to engage with these early to ensure any potential financial impact is mitigated. Throughout 2020 the Covid-19 pandemic has undoubtedly placed great strain on some of the investee companies. M&G has included examples below where analysts have sought to amend covenants and documents in order to mitigate some of this strain.

- For one of our direct lending assets, in the case of a (confidential) waiver request from a borrower, in return for short term renegotiation of leverage covenants and provision of liquidity to the borrower, we included a number of backwards-looking and forward-looking liquidity covenants, and restricted permitted payments out of the borrowing group. We increased the frequency and the detail of information reporting requirements.

- For one of our direct lending assets, in the case of a (confidential) waiver request, we negotiated to allow the company their request to postpone a number of principal repayments, but in turn reprofiled the loan amortisation schedule to ensure a constant maturity date, whilst keeping interest payments current.

- For one of our CMBS assets, in light of the severe cash disruption caused by Covid-19 (which had a direct impact on the ability of the borrower to collect rents) and the knock-on effects on asset values, we waived two financial covenants for two consecutive quarters in 2020 (Debt Yield Covenant and Loan to Value Covenant) in order to stabilise the structure.

M&G European Loan Fund

241. Loan documentation contains bespoke and pre-agreed financial and other terms that frequently need to be amended in a loan's life, requiring lender approval. Consequently, while lenders are not shareholders with a vote, they *can* have influence when consulted on waiver requests for amendments.

242. In 2020, the manager's focus was on the impact of Covid and the degree to which companies were availing themselves unreasonably of nuances in the loan documentation (which naturally could not have contemplated the impact of a pandemic). The aim was to ensure that no untoward largesse with interpretation was being taken e.g., covenant calculations using inappropriately adjusted EBITDA to manufacture illusory headroom. The investment team called out their displeasure on a few occasions at the use of documentation loopholes in defining EBITDA for covenant calculation purposes for adding back Covid-related losses to earnings, so-called 'EBITDAC'. This allows companies potentially to incur indebtedness against backward-looking metrics, stripped of the effects of the pandemic, potentially leveraging it to a degree that is inappropriate for an uncertain, post-Covid level of earnings and cashflow. Instead, they should look at covenants in the spirit in which they were drafted and, if additional funding is needed, all stakeholders should be consulted. M&G has provided some examples from the reporting period.

- In the case of a (confidential) waiver request, we managed to negotiate to remove flexibility to manipulate earnings for the addition of arbitrary 'Covid addbacks' to create flattered financial ratios.

- In 2020, we received 15 covenant waiver requests across our portfolios requesting relief relating to Covid-19. Out of 15, two of them were declined, one was due to the lack of transparency. The other one was in relation to the extension of an interest period beyond that permissible in the credit agreement and (in our view) reasonable.

Real estate managers

243. The real estate managers do not invest in any listed companies and as such exercising voting rights in the traditional sense does not apply. However, they do recognise that there are other forms of rights and responsibilities in this asset class.

244. In terms of responsibilities, UBS sees climate change, energy needs, and water scarcity as among the biggest challenges of the century. UBS acknowledges that real assets such as properties contribute significantly to CO2 emissions and the consumption of natural resources.

245. UBS also believes that responsible ownership and operation of real property can have significant social value and provided a case study to demonstrate this:

246. "In 2020 we had planned to continue the rollout of assessing the social value of our assets. While environmental considerations have started to become mainstream in assessing real estate and infrastructure, the "'S" in ESG has been traditionally harder to measure. We recognise that standing investments – offices, shopping centres, industrial estates – benefit local communities even though it may not be obvious at first sight. We commissioned an external specialist, the Social Value Portal, to collect the data from which they were able to calculate – in monetary terms – a social value for each property, which is then mapped to the UN's Sustainable Development Goals. We worked with tenants and our

onsite property and facilities management teams to understand and measure such categories as local employment levels, traineeships, jobs for young offenders, community events held at the property, and volunteering. During the 2019 calendar year, we undertook assessments from a sample of Triton's portfolio: Springfields Outlet Shopping Centre in Spalding (Retail Warehouse), Knollys and Stephenson House in Croydon (Office), Imperium in Reading (Office), and Stakehill Industrial Estate in Manchester (Industrial/Logistics). The total social value created by these assets against three of the seventeen UN Sustainable Development Goals is GBP 7.9 million. Unfortunately, in 2020, as a result of the pandemic our plans to continue the assessment of other assets within the portfolio had to be put on hold due to lockdowns and other mitigating factors. Towards the end of 2020, we were able to resume data gathering for the assessments and look to continue the rollout of the programme into 2021. Our ambition remains to have a social value for the whole portfolio."

247. BlackRock considers the management of environmental, social and governance risks key to exercising their rights and responsibilities as a real estate manager, as these factors may have material economic consequences throughout the investment life-cycle.

248. ESG risks and opportunities are comprehensively analysed for all new acquisitions and are further factored into BlackRock's investment decision and business plan processes for holding, disposal and asset management strategies. ESG issues that are considered include, but are not limited to, energy and water efficiency, energy and water supply, waste management, biodiversity and the local environmental, contaminated land, climate risk, flood risk, health and safety factors, and local community impact. Opportunities for third party green building certifications and/or sustainability labels and standards will also be considered.

249. BlackRock has developed and implemented a proprietary Investment ESG Questionnaire which must be completed by investment teams for all new acquisitions across their global real estate and infrastructure equity investment platforms. The ESG Questionnaire provides a comprehensive framework to assist with identifying and collating information on material ESG risks associated with any new investments.

250. The Questionnaire asks a number of questions on the various environmental, social and governance risks, and opportunities, that should be considered as part of the wider due diligence being undertaken by the investment teams. The findings of the Questionnaire help identify any key risks associated with each investment and enable greater due diligence, and ultimately improved, and increasingly responsible, investment decision making across BlackRock's global platform. The Questionnaire also enhances the transparency and documentation of ESG Integration across investment activities.

251. Key findings from the Questionnaire, including any issues identified as 'medium' or 'high' risk, and associated commentary on each issue, are captured within an ESG Summary Table. Key findings, including the ESG Summary Table, must be included within the Investment Committee Papers for all new acquisitions.

<u>Bond manager</u>

252. PIMCO believes that for financial markets to prosper over the super secular horizon, growth cannot come at the cost of society. The economic disruption from poorly managed ESG risks is already being felt and the winners and losers of the transition to a net zero carbon economy are emerging. This is particularly relevant for bond investors, as ratings agencies increasingly report on bond issuers' ESG risks in a way that affects their cost of capital.

253. The long-term challenge of decarbonizing the economy certainly comes with risks, but it also offers opportunities for active investors. PIMCO recognises that ESG factors are increasingly essential inputs

when evaluating global economies, markets, industries, and business models. Material ESG factors are important considerations when evaluating long-term investment opportunities and risks for all asset classes, public and private markets.

254. PIMCO believes that fixed income markets play a critical role in the ability to finance a more sustainable future and that bondholders should exercise their rights and responsibilities by using their voice to drive change. PIMCO believes fixed income is an ideal asset class to drive meaningful ESG change. The global bond market is almost double the size of the equity market ($114 trillion vs. $69 trillion[13]), and unlike equity securities which are in perpetuity, bonds mature and companies need to refinance. By engaging with companies when they need to fundraise, investors can help push for sustainability commitments and accelerate change. PIMCO believes effective engagement will help achieve a voluntary agreement around a common goal that benefits all parties involved.

255. PIMCO's goal is not just to find the best opportunities in the market, but to create them for investors by engaging
with issuers. PIMCO highlights that their engagement activity and sizable active holdings have influence on the scope or timing of the commitments made by issuers as well as the disclosures that those issuers will report to investors. For instance, through new bond issuance PIMCO encourages corporate and sovereign issuers to advance their efforts by issuing a green bond or a bond linked to the United Nations' Sustainable Development Goals (SDGs).

256. One example issuer is ENEL, a European utility company that has demonstrated a clear focus on renewables. PIMCO engaged with this company through the UN Global Compact (UNGC) for several years on their commitment to renewables and more recently through their participation in the UNGC symposium on SDG bonds – hosted at PIMCO's Newport Beach offices to encourage companies to issue SDG-linked bonds. At the end of 2019, the company issued a 5-year "General Purpose SDG-linked Bond" in U.S. dollars (followed, later in the year, by a multi-tranche bond of the same type in Euros) – a first of its kind instrument where proceeds are used for general corporate purposes and future coupon payments are linked to their renewable growth strategy (25 basis point (bps) coupon step-up if targets are not achieved).

Renewable Infrastructure

257. The Fund has committed 5% of assets to the Global Renewable Power Fund managed by BlackRock. The position is being built gradually, funded from listed equity, as and when the manager calls capital. The Trustees made their first investment into the Fund in August 2020. A second investment took place in December 2020.

258. As a manager in renewable infrastructure, BlackRock takes environmental, social and governance factors seriously and demonstrated through case studies how they exercised their rights and responsibilities through due diligence and sustainable investment.

[13] Source: Haver Analytics as of 30 September 2019.

Environmental, Social & Governance

ESG related matters as part of Phoenix Investment

As part of the due diligence and investment in Phoenix, the following occurred (not limited to):

- 12 hectares of land are currently being cultivated to accommodate wildlife in the form of different corridors between the crops.
- Two ponds near the site of the wind turbines that provide habitat for the crested newt, an amphibian that is threatened by habitat loss and farming practices, have been revitalised. This involved the ponds being deepened and their contours cleaned.
- One of the wind turbines is located near a small wood that is attractive to bats. In order to reduce the risk collision for bats, the wind turbine is stopped at night under specific weather conditions.
- Local schools in the region tour the sites to learn about the wind farm and its construction.

ESG related matters as part of Neptune Investment

As part of the due diligence and investment in Neptune, the following has been noted:

- As part of their development process, New Green Power (NGP) will conduct a community survey prior to signing the lease agreement.

Local school visiting the construction site (Gesves).

- Many of their projects include Environmental and Community Impact plans, including plans to introduce public walkways lined with trees, cycling paths, bird watching platform and annual excursions for local schools.
- NGP as a company has implemented a number of policies to conserve energy and water, including changing all the lighting in their public areas and parking lots into LED lighting, installing motion sensors to control lighting, limiting the use of AC in non-frequented area and installing water-saving toilets etc.
- From a governance perspective, BlackRock are currently working with NGP to enhance their Health and Safety policy. Additionally, we are introducing an Escalation policy for any reportable events to be aligned to our standard Real Assets policy.