

Climate Change Policy

South Yorkshire Pensions Authority's primary responsibility is to deliver the returns needed to pay scheme members' pensions, whilst maintaining stable and sustainable contribution rates. The Authority is a long-term investor and as such has to ensure that its investments are sustainable. In doing so it actively considers how environmental, social and governance (ESG) issues can be taken into account when managing investment portfolios.

The Authority has a fiduciary duty to consider ESG issues where it is considered that they could have a material financial impact on the Fund's performance. This is supported by the 2014 Law Commission's review which concluded that ESG factors should be taken into account where Trustees think that issues are financially material to the performance of an investment. The applicability of this approach to the Local Government Pension Scheme was confirmed in the Supreme Court's 2020 judgement in the Palestine Solidarity Campaign case. The Pensions Regulator also issued guidance in 2017 for Defined Benefit schemes, stating that ESG factors need to be taken into account if they are deemed to be financially significant and the regulations for trust based pension schemes have been updated to require trustees to set out their approach to ESG issues. The Local Government Pension Scheme Regulations also require the Authority to set out its position in relation to the consideration of ESG issues as part of its Investment Strategy Statement. The greatest potential environmental risk, indeed the greatest single risk, without qualification, to the Authority's investments is climate change, where the associated risks and opportunities may have a material financial impact across all asset classes. The systemic nature of climate change risk has the potential to reduce returns across all asset classes and will have a macro-economic impact that could affect the entire Fund. Equally, however, the need to transition to a low carbon economy and the innovation which that will require presents a number of potential investment opportunities. Risks and opportunities can be presented in a number of ways and include:

- physical impacts,
- technological changes,
- regulatory and policy impacts,
- transitional risk and
- litigation risk.

The Authority will therefore consider climate change issues across the Fund in order to minimise financial risk and maximise long-term opportunities.

In December 2015 the G20 finance ministers and Central Bank governors asked the Financial Stability Board (FSB) to review how the financial sector can take account of climate related issues. Such information is needed by investors, lenders and insurance underwriters in order to be able to assess climate related risks and opportunities. This led to the Task Force on Climate-related Financial Disclosures (TCFD) being established. Its remit was to develop a set of voluntary climate-related disclosures, which would assist in understanding the associated material risks of climate change. The final report with recommendation was published in June 2017, and can be accessed through the TCFD

website here:

<https://www.fsb-tcf.org/>

Supplemental guidance has been developed for financial and non-financial organisations which includes guidance for asset owners. The recommendations were based around four pillars;

- governance,
- strategy,
- risk management and
- metrics and targets.

The TCFD framework is widely recognised as the best practice guide against which investors' actions will be assessed. This Climate Change Policy will therefore be structured around these four themes, and the Authority will commit to reporting in line with this framework each year as part of its annual report and accounts.

Governance

The Climate Change Policy is owned and approved by the Authority with implementation and oversight of the Policy being by the Director; it will be reviewed as necessary, but as a minimum every two years.

The Authority is required by the LGPS Investment Regulations to invest its assets through one of the LGPS investment pools, in this case the Border to Coast Pensions Partnership, however, the responsibility for responsible investment and ensuring the appropriate consideration of ESG issues remains with the Authority. The Authority expects Border to Coast to implement this policy on its behalf across all its investments; it will monitor implementation and require reports from the Company at least annually in order to fulfill its obligations under the LGPS Investment Regulations.

While the Authority will aim to work collaboratively with the other funds within the Border to Coast Partnership to achieve collectively agreed goals, given that it retains responsibility in this area it reserves the right to act independently should collective action not result in the delivery of its objectives in terms of ESG issues and in the context of this policy climate change in particular.

Strategy

Climate change is an issue of greater significance than other ESG issues. It has the potential to impact returns across all asset classes (not just individual companies or sectors), and therefore has very material financial implications. The Authority will therefore expect Border to Coast to:

- be aware of the investment risks and opportunities associated with climate change;
- incorporate climate considerations into the investment decision making practices and processes; and
- monitor and review fund managers in relation to their climate change approach

and policies.

- engage with companies in relation to business sustainability and climate risk disclosure and to encourage companies to adapt their business strategies to support the transition to a low carbon economy.
- recognise that while active shareholder engagement should be the first option, the Authority encourages Border to Coast (and other fund managers) to consider actively reducing exposure to high-carbon intensity companies that fail to respond to engagement by not demonstrating a decrease in carbon intensity or carbon risk.
- support climate related resolutions at company meetings when deemed appropriate, and
- consider co-filing shareholder resolutions at Annual General Meetings (AGMs) on climate risk disclosure, transition plans, science based targets and related issues, such as trade association lobbying after engagement with its Partner Funds.

The Authority will engage with both the Border to Coast operating company and the other funds within the Partnership to ensure this approach is taken both with internally managed assets and appointed external managers.

The Authority will look to consider climate change when reviewing investment strategy with its investment consultants and how this will impact future asset allocation decisions. This will include modelling the impact of differing climate scenarios on both the Fund's assets and liabilities.

The Authority expects those managing money on its behalf to actively consider environmental, social and governance factors, and in this context specifically climate change, into account in selecting stocks in which to invest which is likely to result in investments not being made in companies which are not actively addressing the need to move to a low carbon economy. However, in light of the significant potential financial impacts of climate change, carbon risk and stranded assets, it has made the decision not to invest in pure coal and tar sand companies.

The Authority will encourage Border to Coast to consider how it manages carbon risk and exposure across its various portfolios, and as stated above will seek the agreement of partner funds to reduce exposure to high carbon intensity companies that fail to respond to engagement on climate change related issues and to adopt means to create portfolios structured in a way that supports the low carbon transition.

There are a limited range of low-carbon related investments in quoted markets, with more opportunities existing within the private equity and alternative investment asset classes. The investment strategy which is being put in place to provide further diversification and reduce volatility of expected future returns, has resulted in a reduction in equities and a move into alternatives. This has therefore increased SYPA's exposure to assets that may be less sensitive to climate change risks, and/or support the transition to a low carbon economy.

The Authority's property allocation is mostly through direct property; and a standalone

statement relating to responsible commercial property investing, details the approach taken. It takes into account current best practice regarding social and environmental considerations when managing its property portfolios and determining the selection, retention and realisation of investments. The Authority's aim is to reduce its impact on the environment and maintain a positive relationship with its customers, tenants and suppliers.

Risk Management

The Authority will look to measure and manage the risk of climate change, carbon exposure and stranded assets to the Fund. It will measure and manage climate risk across portfolios by monitoring carbon intensity (where possible) and expects Border to Coast as its principal investment manager to provide data on the carbon intensity of its listed asset portfolios on an annual basis, and to develop similar measures in relation to private market investments. It will take appropriate action to identify such risks by increasing internal knowledge and understanding of scenario and risk analysis tools available, and being aware of ongoing climate change policy discourse. The Authority's preferred approach is with Border to Coast to identify ways of structuring the various investment portfolios to secure carbon reduction across portfolios and ensure that they are prepared for the transition to a low carbon economy.

The Authority believes that collaboration with other like-minded investors leads to greater shareholder power to influence company change and behaviour. It will therefore, look to work in partnership with Border to Coast and other groups such as LAPFF, the Institutional Investors Group on Climate Change (IIGCC) and Climate Action 100+ to ensure there is appropriate engagement with companies on climate related issues, including business sustainability and disclosure of climate risk, in line with TCFD recommendations.

Governments' climate change policies are unpredictable leading to public policy uncertainty. Investors are lobbying policymakers to accelerate the development of a realistic carbon price. Carbon pricing is vital for businesses and investors to properly incorporate climate related risk into investment decision-making. The Authority will, therefore, actively engage with policy makers through its membership of IIGCC.

Metrics and Goals

The Authority's Goal is that its investment portfolios should be "net zero" in terms of carbon emissions by 2050 in line with the UK's obligations under the Paris Agreement which have been incorporated into UK law. A plan to progress towards this goal will be agreed with Border to Coast and the other funds within the partnership.

The Authority will, where possible, report progress in line with TCFD recommendations; this Climate Change Policy has been structured around the TCFD's reporting themes. The TCFD believes that asset managers and asset owners, including public- sector pension funds, should implement its recommendations with disclosures made in annual public financial reports.

The Authority will measure its portfolios' exposure to carbon-intensive companies, where

possible through requiring Border to Coast to provide an annual carbon audit in line with the TCFD recommendations. However, the Task Force recognises the challenges and limitations of current carbon footprinting metrics, but sees it as a move towards developing investment decision-useful, climate-related risk metrics. This information will be used to highlight specific risks and inform company and fund manager engagement.

The Authority will seek to use its influence within the wider Border to Coast Partnership to secure the agreement of appropriate goals for reducing the carbon intensity of portfolios and the identification of ways of structuring the various portfolios so that they are prepared for the transition to a low carbon economy.

It will also report on additional metrics which will include company engagement meetings, both direct and collaborative. It will request that Border to Coast integrates climate risk and opportunities into the investment decision making process for both internal and external mandates, and for the private market structures.

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