Subject	**The Authority's Approach to Investment Exclusions**	**Status**	For Publication
Report to	Authority	**Date**	18th December 2025
Report of	Director		
Equality Impact Assessment	Not Required	Attached	No
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1 Purpose of the Report

1.1 To allow the Authority to consider the approach to the exclusion of specific investments from the investment universe following discussion at the March meeting.

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2 Recommendations

2.1 Members are recommended to:

a. **Consider the issues and options outlined in the body of the report and provide guidance for officers.**

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3 Link to Corporate Objectives

3.1 This report links to the delivery of the following corporate objectives:

Investment Returns

To maintain an investment strategy which delivers the best financial return, commensurate with appropriate levels of risk, to ensure that the Fund can meet both its immediate and long-term liabilities.

Responsible Investment

To develop our investment options within the context of a sustainable and responsible investment strategy.

Effective and Transparent Governance

To uphold effective governance showing prudence and propriety at all times.

4 Implications for the Corporate Risk Register

4.1 The process of exclusion of specific investments could, depending on how it is applied have either a positive or negative impact on the identified corporate risks relating to investment returns and climate change.

5 Background and Options

5.1 At its March meeting the Authority resolved to request officers to “review the impact of SYPA advocating for active exclusion where engagement has demonstrably failed and provide the results in a report at the 18th of December 2025 Authority meeting.” This report responds to that resolution which followed discussion about the frustration felt by some members that the current situation leaves the Authority in an uncomfortable position seemingly unable to express its views on key issues through investment decisions.

5.2 In addition, at its meeting on 3rd September 2025 Sheffield City Council passed a motion which among other things “calls on South Yorkshire Pensions Authority (SYPA) to consult with their members on ethical investments and divesting from companies potentially complicit in war crimes and reflect members' views in investments made by SYPA and Border to Coast Pensions Partnership.” This report also responds to the issues raised by this motion.

5.3 Before addressing the detail of the resolution, it is important to understand how officers have understood what members have asked to be considered. The resolution refers to cases where engagement has “demonstrably failed”. As engagement takes place with individual companies this has been taken to mean that consideration is being given to the exclusion of individual companies rather than to the exclusion of whole classes of company such as tobacco companies. The Sheffield City Council motion also addresses the activities of individual companies. Officers have worked on this basis and have consulted with the Border to Coast operating company and other partner funds as well as reviewing the policies operated by a range of fund managers.

5.4 The approach taken by officers in producing this report has been:

a. To understand how a policy as suggested in the resolution might operate in simple process terms.
b. To consider how this might be translated into the investment process.
c. To consider whether there would be wider support for the adoption of such a process across the Border to Coast partnership, as this is not an approach that the Authority could implement in isolation.
d. To consider the wider implications for the Authority in the context of the Partnership if it were to actively advocate for such a course.

5.5 Taking the first aspect of this. The key to the suggested approach is to clearly define the “demonstrable failure” of engagement. Assuming this can be done, things become simple in process terms in that the relevant stocks would be sold. However, defining “demonstrable failure” is not easy and the definition would be different in relation to each engagement process undertaken, although it would be possible to set some criteria to define demonstrable failure at the beginning of each engagement process. Additionally, there will need to be a clear policy about the steps which would be taken in the event that the company changed its position in a way that meant the objectives of the engagement had been achieved. If this were to occur would the company be removed from the list of exclusions? This is certainly the position taken by several asset managers. It is also the case that timing the sale of stocks based on a determination of failed engagement may result in financial detriment to the Fund and scheme members. This would, if financially significant, run counter to the Authority's fiduciary duty.

5.6 More difficult is how this sort of approach fits into the investment process. Portfolio managers make decisions to buy, hold or sell stocks based on a wide range of considerations. It is important that the Authority does not substitute its own judgement for that of portfolio managers whose skills are ultimately what our fees are paying for. Doing so could be to the financial detriment of the Fund and therefore scheme members, and as set out above counter to the Authority's fiduciary duty.

5.7 It is recognised, however, that viewed from the outside, there appears to be no obvious relationship between:

- the very significant efforts made to engage with companies (which incur not inconsiderable cost);
- change (or lack of change) in the behaviour of those companies; and
- the decisions made by portfolio managers regarding those companies, which often seem to completely ignore the reputational damage their decisions may have on their clients.

5.8 There is also a further consideration, in relation to holdings within the Border to Coast equity funds SYPA invests in. As has been discussed previously, the pooled Border to Coast products have a series of risk parameters which constrain the degree to which portfolio managers can depart from the composition of the benchmark index in the construction of a portfolio. Broadly, for the funds in which SYPA is invested this means that to remain within these parameters the portfolio will look at pairs of companies within a sector, overweighting the one evaluated as the better of the pair and underweighting the worse of the two as a key part of the risk management approach.

5.9 Adopting a policy of exclusion related to failed engagement could potentially undermine this element of the investment process and, if such a policy affected a significant number of companies, it could change the risk dynamics of the product in a way that would not be in line with the Authority's risk tolerance, or the product prospectus which is subject to FCA approval. It could also require the making of fundamental changes to the investment process for what could be seen as non-investment reasons. Such changes are generally regarded as high risk and can undermine performance.

5.10 It should also be noted that divestment achieves no real-world impact - an oil company will still drill for oil if the stock is sold by Border to Coast, it is just that the stock may be bought by an investor less concerned about ensuring that the business has a sustainable future by moving away from fossil fuel production. So, exclusion presents a choice between making certain metrics for SYPA look better in isolation or seeking to move the dial on those metrics in aggregate in the real world. The Authority in determining its approach to exclusion needs to determine which of these choices it is seeking to prioritise.

5.11 There are fund managers who implement policies that involve divestment where engagement is seen to have failed although generally within investment products with different investment processes and risk tolerances to those of the Border to Coast funds in which the Authority is invested. Such products also tend to be marketed to a different investor base potentially with fewer fiduciary constraints than an LGPS fund.

5.12 In discussion on this issue as part of the annual review of responsible investment policies, Border to Coast have estimated that adopting such a policy would take something like 18 months to deliver a new policy and changes in the investment process together with additional resources in the Responsible Investment Team. The priority to be attached to such changes and additional resource requirements would need to be judged by shareholders in approving the budget alongside other resource requirements such as that required to facilitate the integration of the 7 new partner funds and the transition of legacy assets to pool management - the timescale for which is mandated by the Government. Therefore, from the overall point of view of the Partnership such a change if adopted would necessarily be a lower priority than addressing the requirements placed on the Partnership by Government.

5.13 Such an approach cannot be implemented by SYPA in isolation. To do so would require support across the Border to Coast partnership. While this is a debate that at least 3 of the current partner funds (including SYPA) are having at present it is not on the agenda for the others and the state of debate among the 7 new partners is not clear. This means that it is unlikely, given the other priorities outlined above, that there would be sufficient weight of opinion behind the issue to secure such a fundamental change of policy. However, there has been some development in the collective policy position following this year's annual review as set out elsewhere on the agenda for this meeting.

5.14 While there is no consensus on extending the use of exclusion currently it would be possible for SYPA to continue to advocate for such a position on an ongoing basis (for example as part of the annual review of Responsible Investment policies), in the same way that the Authority already advocates for gradual changes to policies in various areas. This would need to be handled very carefully to ensure that SYPA was not viewed as a fund obsessed with a single issue. If this were to be the case SYPA could be perpetually in a minority of one within the partnership making it more difficult to build alliances on a range of other issues because the Authority would be seen as an outlier and holder of views outside the mainstream.

5.15 In addition to these practical and partnership considerations, the Sheffield City Council motion asks the Authority to consult members on their views on divestment specifically related to the situation in Gaza. As members are aware, the Authority has already consulted scheme members on responsible investment issues generally, rather than on the specific issues associated with Gaza. In this survey, while a significant proportion of respondents felt that arms manufacturers were not an appropriate investment, this was not in the top 3 less acceptable investments and was deemed considerably more acceptable than the next ranked category of investment. It is acknowledged that this does not address the specific question of the situation in Gaza. However, Law Commission advice on fiduciary duty and the consideration of non-financial factors in investment decisions makes clear that the Authority is under no obligation to consult members on issues of this sort, as it is very difficult to ensure that the results of any survey are truly representative and the results of any survey cannot remove the obligation on members of the Authority acting as trustees to exercise their own judgement and act in what they consider is the best financial interests of scheme members. A further survey would therefore provide no additional benefit over and above the survey already undertaken and potentially incur unnecessary cost. In addition, a survey on a single issue such as this could easily be manipulated by lobby groups on either side of the debate undermining any value which its results might have.

5.16 Fundamentally the question facing members of the Authority is whether there is a desire to adopt a policy which cannot effectively be implemented and the adoption of which might distance South Yorkshire from its pooling partners making it difficult to achieve progress on other issues of importance such as local investment and the development of additional products which would allow the Fund to deliver its investment strategy more effectively. Alternatively, members have the option of retaining the stance of building alliances with partners to move the collective position across the pool in what SYPA would regard as a positive direction. This could be accompanied by the setting of clear goals for the use of such influence as part of the annual review of the Authority's own responsible investment policy framework, which is due to come to the Authority's March 2026 meeting, and on which consultation could take place with members prior to refining the proposed policies.

6 Implications

6.1 The proposals outlined in this report have the following implications:

Financial	There are no direct financial implications arising from this report. However, there is the possibility that a policy of exclusion as outlined in the report could result in micro-level decisions being made based on non-financial factors outweighing financial factors which could have a negative impact on the financial returns achieved by the Fund, and thus impact on the delivery of the Authority's fiduciary responsibilities.
Human Resources	None
ICT	None
Legal	The framing of any exclusion policy would need to be very carefully considered to ensure that its operation does not intrude upon the Authority's ability to exercise its fiduciary duty to scheme members and the duty of the pool operating company to treat clients fairly under the terms of its FCA authorisation.
Procurement	None

George Graham

Director

Background Papers	
Document	**Place of Inspection**
Results of the 2025 Responsible Investment Survey	Responsible Investment Survey Results