Engagement Policy Implementation Statement 2021

Shanks Group Pension Scheme

Introduction

On 6 June 2019, the Government published the Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019 (the "Regulations"). The Regulations amongst other things require that the Trustees produce an annual implementation statement which outlines the following:

- Explain how and the extent to which they have followed their engagement policy, which is outlined in the SIP.
- Describe the voting behaviour by, or on behalf of the Trustees (including the most significant votes cast by Trustees or on their behalf) during the scheme year and state any use of the services of a proxy voter during that year.

This document sets out the details, as outlined above. The EPIS has been prepared by the Trustees and covers the Scheme year from 6 April 2020 to 5 April 2021.

Scheme Stewardship Policy Summary

The Trustee expanded the stewardship policy in September 2020. In summary, the policy in place from this date stated that the Trustee would review the Stewardship report and activities carried out by AIL on an annual basis. The Trustees expect AIL to carry out the following on their behalf;

- Ensure that (where appropriate) underlying asset managers exercise the Trustee's voting rights in relation to the Scheme's assets; and
- Report to the Trustees on stewardship activity by underlying asset managers as required.

The below bullet points summarise the Scheme Stewardship Policy in force over the majority of the reporting year to 5 April 2021. The full SIP can be found at https://www.psgovernance.com/communications/shanks-group.html

Extract from the SIP – Stewardship

As part of AIL's management of the Scheme's assets, the Trustees expects the manager to:

- *Ensure that (where appropriate) underlying asset managers exercise the Trustees' voting rights in relation to the Scheme's assets; and*
- *Report to the Trustees on stewardship activity by underlying asset managers as required.*

The Trustees will engage with their fiduciary manager as necessary for more information, to ensure that robust active ownership behaviours, reflective of their active ownership policies, are being actioned. This will take the form of annual reporting which will be made available to Scheme members on request.

Where possible, the transparency for voting should include voting actions and rationale with relevance to the Scheme, in particular where: votes were cast against management; votes against management generally were significant; votes were abstained.

Where voting is concerned we would expect our underlying asset managers, to recall stock lending, as necessary, in order to carry out voting actions.

Scheme stewardship activity over the year

Training

Over the year, the Trustees had a responsible investment training session with their investment advisor, which provided the Trustees with updates on the evolving regulatory requirements and the importance of stewardship activity and appropriate consideration of ESG factors in investment decision making.

Updating the Stewardship Policy

In line with regulatory requirements to expand the SIP for policies such as costs transparency and incentivising managers, the Trustee also reviewed and expanded the Stewardship policy in September 2020. The updated wording in the SIP illustrates how the Trustees recognise the importance of its role as a steward of capital, as well as indicating how the Trustees would review the suitability of the Scheme's investment managers and other considerations relating to voting and methods to achieve their Stewardship policy.

This has been made publicly available via the link noted earlier in this document.

Ongoing Monitoring

Investment monitoring takes place on a quarterly basis with a monitoring reports being provided to the Trustees by Aon. The reports include ESG ratings and highlights examples of where Aon Investments Limited, the Scheme's fiduciary manager, has engaged with underlying investment managers on the Trustees' behalf.

The ESG rating system is for buy rated investment strategies and is designed to assess whether investment managers integrate responsible investment and more specifically ESG considerations into their investment decision making process. The ESG ratings are based on a variety of qualitative factors, starting with a proprietary due diligence questionnaire, which is completed by the fund manager. Aon’s researchers also conduct a review of the managers' responsible investment related policies and procedures, including a review of their responsible investment policy (if they have one), active ownership, proxy voting and/or stewardship policies.

After a thorough review of the available materials, data and policies, as well as conversation with the fund manager, the lead researcher will award an ESG rating, which is subject to peer review using an agreed reference framework. Ratings will be updated to reflect any changes in a fund's level of ESG integration or broader responsible investment developments.

Engagement activity – fiduciary manager

Overview

The Trustees have appointed Aon Investments Limited (AIL) as their fiduciary manager, who they consider to be their asset manager. AIL appoints underlying asset managers to achieve an overall target return. The Trustees delegate the monitoring of ESG integration and stewardship quality to AIL.

AIL has confirmed that all equity and fixed income managers have been rated 2 or above on AIL’s four-tier ESG ratings system. This means that all the appointed asset managers are at least aware of potential ESG risks in the investment strategy and have taken some steps to identify, evaluate and potentially mitigate these risks.

The Trustees have reviewed the AIL Annual Stewardship Report and are content that AIL is using its resources to appropriately influence positive outcomes in the strategies in which they invest.

Engagement activity

AIL has undertaken a considerable amount of engagement activity over the period, some examples of which have been outlined within this statement. AIL held around 35 ESG specific “deep-dive” meetings in 2020 predominantly covering the equity and fixed income managers that are invested in by AIL across all delegated funds in which AIL’s clients invest. At these meetings, AIL was able to analyse and discuss the voting and engagement activities undertaken during calendar year 2019, highlighting areas of improvement and discussing manager strategy in the area of RI moving forward. Meetings have been ongoing through the beginning of 2021.

Aon Solutions UK Limited ("Aon") also actively engage with asset managers and this is used to support AIL in their fiduciary services. Over the period, Aon’s Engagement Programme maintained a dialogue with one of its leading global asset managers ('the manager') on behalf of many of their clients which invest with the manager. This culminated towards the end of 2020 in a discussion with their Global Head of Stewardship with respect to numerous areas of concern regarding stewardship, in particular the manager’s ability to demonstrate commitment to publicly stated climate change goals. Discussions were held regarding the following:

- Aon’s analysis of the manager’s voting actions over the period showed that the manager had not been voting in a manner consistent with its public pledges nor rhetoric on the importance of sustainability issues. The manager acknowledged that there was a disconnect between vote decisions made in the first half of 2020, but that it had markedly changed its voting policies in the second half of 2020, and reassured Aon that moving forward, vote decisions would better align with its stated positions on such ESG matters. Aon expect to see this reflected in voting actions by mid-2021.
- Aon expressed concern that given the level of potential influence the manager had, the manager was unable to bring shareholder resolutions to those companies with which it had reason to engage. Reasons for this are regulatory and concern its investor classification status. The manager acknowledged Aon concern and agreed to follow up with further detail. While its situation has not yet changed, it is possible that regulatory restrictions may be eased in the future allowing the manager to use shareholder resolutions as a tool. The manager has since stated its intention to use its vote for shareholder resolutions brought by other organisations, to greater effect.

The manager has since provided further information on how it is updating its policies in a manner consistent with its strategy of intensifying engagement on sustainability. For example, in areas such as the transition to the low carbon economy; diversity, equity and inclusion; voting on shareholders proposals.

Aon welcomes the improved stance on ESG issues from the manager and their proactive updating of their policies to more closely align with their responsible investment goals. Aon will continue to monitor and engage with the manager, scrutinising their voting and engagement actions. Aon is encouraged that the manager to strengthen their influence with invested companies to better effect, especially the changed stance around supporting appropriate shareholder proposals.

Stewardship activities – asset managers

Voting and engagement – equity investments

Over the year, the Scheme invested in the AIL Managed Growth Strategy Fund. The material equity investments held in the Scheme over the year was:

- Legal and General Investment Management (LGIM) Multi Factor Equity Fund

The Trustees consider a significant vote broadly as a vote which the respective manager deems most significant to the Scheme, or a vote where more than 15% of votes were cast against management.

LGIM Multi Factor Equity Fund ("LGIM")

Voting policy

LGIM makes use of the Institutional Shareholder Services (ISS)'s proxy voting platform to electronically vote and augment its own research and proprietary ESG assessment tools, but do not outsource any part of the strategic decisions. It has put in place a custom voting policy with specific instructions that apply to all markets globally, which seek to uphold what it considers to be minimum best practice standards all companies should observe. Even so, LGIM retains the ability to override any voting decisions based on the voting policy if appropriate, for example, if engagements with the company have provided additional information.

Amazon

In May 2020, LGIM supported 10 out of 12 shareholder proposals put forward against the management of Amazon, the largest number of shareholder proposals put on the table for any US company this proxy season. Two resolutions were in relation to governance structures that benefit long-term shareholders, and the remaining eight were in relation to disclosure to encourage a better understanding of process and performance of material issues. The resolutions received between 1.5% and 30% support from shareholders, meaning they were not passed.

Despite shareholders not giving majority support to the raft of shareholder proposals, the sheer number and focus on these continues to dominate the landscape for the company. LGIM's engagement with the company continues as they push it to disclose more and to ensure it is adequately managing its broader stakeholders, and most importantly, its human capital.

Pearson

In September 2020, LGIM voted against a remuneration policy put forward by an investee company Pearson. Pearson issued a series of profit warnings under its previous CEO. Despite this, shareholders have been continuously supportive of the company, believing that there is much value to be gained from new leadership and a fresh approach to their strategy. However, the company decided to put forward an all-or-nothing proposal in the form of an amendment to the company’s remuneration policy. This resolution at the extraordinary general meeting (EGM) was seeking shareholder approval for the grant of a co-investment award, an unusual step for a UK company, yet if this resolution was not passed the company confirmed that the proposed new CEO would not take up the CEO role.

This is an unusual approach and many shareholders felt backed into a corner, whereby they were keen for the company to appoint a new CEO, but were not happy with the plan being proposed. However, shareholders were not able to vote separately on the two distinctly different items, and felt forced to accept a less-than-ideal remuneration structure for the new CEO.

LGIM spoke with the chair of the board earlier this year, on the board’s succession plans and progress for the new CEO. They also discussed the shortcomings of the company’s current remuneration policy.

LGIM spoke with the chair directly before the EGM, and relayed their concerns that the performance conditions were weak and should be re-visited to strengthen the financial underpinning of the new CEO’s award. LGIM also asked that the post-exit shareholding requirements were reviewed to be brought into line with expectations for UK companies. In

the absence of any changes, LGIM took the decision to vote against the amendment to the remuneration policy.

33% of shareholders voted against the co-investments plan and therefore, by default, the appointment of the new CEO. While this resulted in the plan being passed, it highlighted concerns around governance, which LGIM has stated will need to be addressed through continuous engagement going forward.

Engagement policy

LGIM has a six-step approach to its investment stewardship engagement activities, broadly these are:

1. Identify the most material ESG issues,
2. Formulate the engagement strategy,
3. Enhancing the power of engagement,
4. Public Policy and collaborative engagement,
5. Voting, and
6. Reporting to stakeholders on activity.

More information can be found on LGIM's engagement policy here: https://www.lgim.com/landg-assets/lgim/_document-library/capabilities/lgim-engagement-policy.pdf

Engagement example

An example of engagement over 2020 was with Proctor and Gamble (P&G). P&G uses both forest pulp and palm oil as raw materials within its household goods products. A key issue identified was that the company has only obtained certification from the Roundtable on Sustainable Palm Oil for one third of its palm oil supply, despite setting a goal for 100% certification by 2020. Furthermore, two of their Tier 1 suppliers of palm oil were linked to illegal deforestation.

Following a resolution proposed by Green Century that P&G should report on effort to eliminate deforestation (that was voted on in October 2020), LGIM engaged with the P&G, the resolution proponent, and with the Natural Resource Defence Counsel to fully understand the issues and concerns.

Through this round of engagements, LGIM decided to support this resolution as although P&G has introduced a number of objectives and targets to ensure their business does not impact deforestation, LGIM felt it was not doing as much as it could. LGIM has asked P&G to respond to the CDP Forests Disclosure and continue to engage on the topic and push other companies to ensure more of their pulp and wood is from FSC-certified sources. More detail on this stewardship example can be found here: https://www.lgim.com/landg-assets/lgim/_document-library/capabilities/cg-quarterly-report.pdf

Summary

Based on the activity over the year by the Trustees and their service providers, the Trustees are of the opinion that the stewardship policy has been implemented effectively in practice. The Trustees note that most of their applicable asset managers were able to disclose strong evidence of voting and engagement activity.