

THE VIEW FROM THE FORUM

Pension Funds and Climate Change

New LAPFF Briefing for 'Trustees' on Current Developments and Policy

Climate change is a major risk for companies in the medium to long-term, but it also affords considerable opportunities for both companies and investors.

The Forum has recognised that in order for trustees to make informed investment decisions, or to opt for activism on climate change where this would enhance value, they will need to be aware of, and understand the relevance of the latest major developments in the area of climate change policy. The Forum has therefore produced a briefing on these issues for LAPFF members.

The purpose of the briefing is to provide trustees with information on the latest developments in the area of climate change policy. There is a growing consensus among government, scientists and business on the need to take action to address climate change, and businesses are increasingly facing both physical and regulatory risks due to climate change in the coming years. Policy initiatives currently in place and under development will present both business and investors with long-term risks and costs, but they will also present opportunities. Informed trustees will be in a better position to assess these risks and

opportunities and make decisions likely to enhance long-term value. The briefing to LAPFF members covers:

- The Kyoto Protocol and its mechanisms;
- Developments in emissions trading and the EU Emissions Trading Scheme, which is now underway;
- UK Government policy on climate change, including the implications of the recently released Energy Review; and
- On-going shareholder initiatives in the area of climate change.

As stated above, these developments will bring costs and opportunities to companies, and in turn may affect long-term value for investors. Accordingly the briefing advises trustees to:

- **Assess potential risks, costs and opportunities within their portfolio due to future climate change initiatives**
- **Consider engagement with companies in the areas of climate change disclosure, strategy, and actions taken to address risks, costs and opportunities.**
- **Consider investment in those companies that may stand to benefit from future climate change policy, including the Kyoto Protocol, emissions**

trading, and the UK Government climate strategy.

- **Consider collaboration with other institutional investors on climate change initiatives.**

At the October meeting of the Forum, it was agreed that more resources will be put into climate change facilitating more engagement with a greater number of companies, including overseas companies.

The Local Authority Pension Fund Forum (LAPFF) is a voluntary association of 39 public sector pension funds based in the UK, with assets of more than £70 billion. LAPFF exists to promote the investment interests of local authority pension funds, and to maximise their influence as shareholders in promoting corporate social responsibility and high standards of corporate governance amongst the companies in which they invest.

For more information about the Forum, contact Forum Officer, Keith Bray on 07811 800612. Alternatively, you can email postmaster@keithbray.plus.com or visit our website www.lapffforum.org

LAPFF Alerts - we review our procedures

LAPFF Alerts are issued where a company significantly fails to meet the Forum's standards of corporate governance (CG) and corporate social responsibility (CSR) best practice. The Forum's approach is set out in its policy statement 'Strategies for Shareholder Engagement', adopted in July 2004.

Analysis is provided by PIRC, as the Forum's research and engagement partner, drawing on their extensive company database, and highlighting the particular resolutions on the relevant company meeting agenda. A recommendation on voting for, against or abstaining is made on the particular resolution and the alert is then emailed to the LAPFF membership for consideration. The alerts focus on a range of best practice areas including:

- board composition;
- voting rights;
- compliance and internal control statements;
- greenhouse gas emission reporting;
- remuneration; and
- audit issues.

In seeking to improve our service to our members, we have reviewed the operation of our alerts system, based on data collected in the period running from 1 July 2005 to 30 June 2006, and our analysis has revealed the following:

- 23 alerts have been sent out over the year, alerting Forum members to concerns over practices at 101 companies, 35 of which are from the FTSE 100;
- The number of companies per alert is usually 2 on average. In the 'busy season', i.e. April and May, the number of companies per alert peaks at 10 – 16;
- The vast majority of companies had remuneration issues, followed by board issues and audit issues. A small number of FTSE 100 companies were identified that did not report their greenhouse gas emissions.

LAPFF alerts were originally designed to highlight the most egregious cases in terms of CG and CSR



performance. For remuneration, it was assumed that we would be focusing on approximately 15% of the FTSE 350. These have so far been identified on the basis of a small number of key indicators, such as 'excessiveness' and 'whether targets were challenging'. The number of companies included in LAPFF alerts as a result is slightly above target.

More recently however, PIRC has introduced a new weighted rating matrix, which gives greater weight to those issues that are considered to have a potentially greater impact on share value. We now propose to incorporate this new approach into our procedure, as it takes a greater number of issues into account and therefore allows for a more balanced assessment.

The case-by-case approach to exceptional concerns, which has been applied during the year, has worked well. We therefore propose to continue with this approach. In addition we believe it will be helpful to ascertain LAPFF members' views on the effectiveness of our alerts procedures. We will therefore be surveying our membership to establish exactly in what ways our members are currently using the LAPFF alerts, and seeking their views on areas for improvement.

Labour Standards in China – LAPFF Trustee Guide

The Forum has a longstanding interest in overseas employment standards and between 1999 and 2003 it ran a successful campaign to persuade UK companies, particularly in the retail sector, to adopt and implement codes of conduct in relation to their overseas supply chains. The Forum's second benchmark study in 2003 demonstrated that the FTSE 100 retailers covered by its survey were making genuine efforts, predominately amongst their direct suppliers, to translate their codes into business practice.

Following from that study the Forum decided that investment by UK companies in the rapidly expanding economy of the People's Republic of China provided an obvious progression of its work on labour standards. An Interim Report was published in November 2005 which presented the results of a survey commissioned

from PIRC on a range of knowledge-based industries – banks, pharmaceuticals and chemicals – that investigated how they are addressing and managing the risks related to operating in China, particularly with respect to labour standards.

This Final Report and Trustee Guide which recommends that any engagement programme be undertaken jointly with other investors is based on the Interim Report and outlines a process by which the Forum can now engage with companies in the chemicals, food producers, retail and oil & gas sectors.

Also in this context, at its October meeting, the Forum received a presentation 'Labour Standards in China: challenges and opportunities' from **Hilary Murdoch, Senior Project Manager, Impactt Ltd (Ethical Supply Chain Consultants)**

Company Workforce Practices

The Forum issued the initial LAPFF Trustee Guide on Company Workforce Practices in April 2005 with the aim of helping trustees in assessing the quality and effectiveness of investee companies' reporting of employment policies and practice. The proposed engagement approach is currently based on the following three-pronged objective:

- Require a minimum standard of reporting on employment practices applicable to all publicly quoted companies above a certain size;
- Identify material industry-specific employment risks and opportunities;
- Seek directors' views on the materiality of employment issues in the preparation and publishing of the Operating and Financial Review or similar reports.

LAPFF has over the last year actively engaged with four companies in the hotels/leisure sector and one in the food producer sector and the outcomes were assessed against these three objectives. We will now be revising the LAPFF Trustee guide to take account of the lessons learnt from our engagement activity.



Over the past 18 months, BP has been increasingly embattled over a number of health and safety incidents, causing heightened investor concern about health and safety management at the oil major.

In particular:

- a major blast at BP's Texas City refinery, which led to the deaths of 15 contractors and injury to 170;
- hurricane damage to the Thunder Horse production platform in the Gulf of Mexico;
- closure of 12 of its oil wells at Prudhoe Bay, Alaska following allegations of oil leaks from whistle-blowers.

Our representatives attended an analyst briefing by senior BP executives, facilitated by the Responsible Investor Network (RIN) on BP's Alaskan operations, and it has been agreed that we should continue to engage with the company regarding our concerns about health and safety.

LAPFF members' networking initiative - currency management

The Forum's members' networking initiative will be 'kicked off' at our January meeting by **Martin Spriggs from the London Borough of Brent**. Martin will give a short presentation setting out how the Brent Fund has approached **currency management** i.e. 'why and how they do it' – followed by a discussion session which will give LAPFF members the opportunity to compare different approaches to this very topical aspect of fund management. This will be the first of what we believe will be a very useful series of short presentations from our members, focussing on current issues and points of practice. We feel that by sharing practical experiences in this way we can all benefit on a wide range of subjects which in future might include topics such as:

- the structure of their fund i.e. the pros and cons of 'doing it our way';
- how the fund determines its strategic asset allocation;
- customised benchmark v peer group;
- communications with stakeholders;
- balanced v specialist or active v passive;
- a recent management experience, e.g. a fund manager selection process;
- or any other experience which any member fund cares to share with fellow members.

Membership in Wales hits 50%



STRONG HERITAGE | STRONG FUTURE
RHONDDA CYNON TAF
TREFTADAETH GADARN | DYFODOL SICR



Pensions • Pensiynau

Rhondda Cynon Taf Pension Fund, the largest local authority fund in the Principality, has decided to join the Forum following a presentation to the RCT Investment Committee in September by Forum Officer, Keith Bray. This means that four out of the eight funds in Wales are now Forum members – a particularly encouraging development, as there were no Welsh funds in the Forum just three years ago. In total our members now manage funds in excess of £70 billion.

LAPFF membership as at 30 September 2006

- Avon Pension Fund
- City of Edinburgh Council
- Clwyd Pension Fund
- Derbyshire CC
- Devon CC
- Dyfed Pension Fund
- Greater Gwent Fund
- Greater Manchester Pension Fund
- Lancashire County Pension Fund
- LB Brent
- LB Camden
- LB Croydon
- LB Hackney
- LB Hammersmith & Fulham
- LB Harrow
- LB Hillingdon
- LB Hounslow
- LB Islington
- LB Newham
- LB Southwark
- Lincolnshire CC
- London Pension Fund Authority
- Merseyside Pension Fund
- Norfolk Pension Fund
- Northamptonshire CC
- North Yorkshire CC
- Nottinghamshire CC
- Rhondda Cynon Taf Pension Fund
- Shropshire CC
- Somerset CC
- South Yorkshire Pensions Authority
- South Yorkshire Passenger Transport Authority
- Teeside Pension Fund
- Tyne and Wear Pension Fund
- West Midlands Pension Fund
- West Midlands PTA Pension Fund
- West Yorkshire Pension Fund
- Wiltshire CC
- Worcestershire

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