Policy on responsible investment

November 2018

the people's pension

For people, not profit

Responsible investment

Our core belief

Investment decisions should reflect environmental, social and governance considerations

Policy statement

We aim to be responsible investors of our members' assets.

'Responsible investment' covers just about anything that presents a major opportunity – or a genuine threat – to members' interests that we should identify, understand and evaluate.

It's a broad term but, in the context of a pension scheme, responsible investment requires a long-term view on delivering capital and income to members in retirement.

We set an investment strategy in the interests of our members and consider responsible investment issues where they're material to those interests. We allocate an appropriate amount of time to assessing these issues and to the systematic, fact-based analysis that enables us to make high-quality decisions.

This fact-finding and analysis is delegated to B&CE and our independent investment advisers.

Moreover, the Trustee has an Investment Committee to govern the investments of The People's Pension, which considers responsible investment within its terms of reference.

> *Responsible investment is simply a set of tools to sort out environmental issues, social behaviours and governance practices in the companies we invest member money in.*

Process

For us, responsible investment means using three tools:

1. **Integrate:** Construct portfolios to reflect environmental, social and governance (ESG) factors that could positively or negatively affect investment returns.
2. **Screen:** Exclude companies from investment portfolios that do not meet certain minimum ethical criteria. Include companies and investments that are likely to have a positive impact on the wider society.
3. **Engage:** Work with companies in an investment portfolio about the issues that are likely to have a material impact (both positive and negative) on future returns.

These three elements guide us when we set and review investment strategy. For example, when we believe that an investment approach could impact our members' savings, we'll consider addressing this in our investment processes. And we'll do this by either excluding specific named companies or reshaping portfolios. When we feel strongly about an issue, but cannot alter our portfolios to benefit members, we engage with the relevant companies on these issues.

When we make decisions like this, we evaluate:

- the expected impact on investment returns
- the likelihood of the decisions having an impact on the issue in the wider society
- the cost, transparency and investment merit of the investment options available
- how it affects the governance of The People's Pension and its investments.

Sometimes our preferred course of action is not possible, because of scale and time. For example, we may not be able to take certain actions that might help reduce risk until we have a certain number of assets under management. This means that certain actions may not be appropriate, either now or in the foreseeable future.

But overall, we do believe that it's good governance to try, whenever we can, to:

- ensure our research process can identify investment approaches with a positive impact on both returns and, potentially, ESG issues
- focus on proposals from our advisers that specifically benefit our members and their needs, rather than other special interest groups
- test, challenge and (in some cases) research any new ideas or options to make sure they're fully appropriate for our members' needs.

We expect these principles to remain but we do recognise the need to be flexible. Any approaches we develop and implement now may be adjusted proportionately as The People's Pension grows and as the market develops. Greater scale may enable us to devote extra resource for engagement or to pursue alternative investment approaches. We will review this policy annually and communicate changes to our approach with members.

Definitions:

Responsible investment (or 'RI') helps ensure members' money is invested in the right way. We use the three tools (explained above): integrate, screen and engage.

Environment, social and governance (or 'ESG') refers to any issue not covered by traditional financial analysis that could impair or improve long-term investment returns. These issues can be split into a number of factors, which we list and explain on page 4. We also state our core beliefs about these factors on page 8.

Investee companies refers to the companies that issue the shares or bonds our fund managers invest our members' money in.

Corporate governance is the way in which companies are led, managed and structured – according to UK or other national law, regulations and official guidelines.

Decision-making process

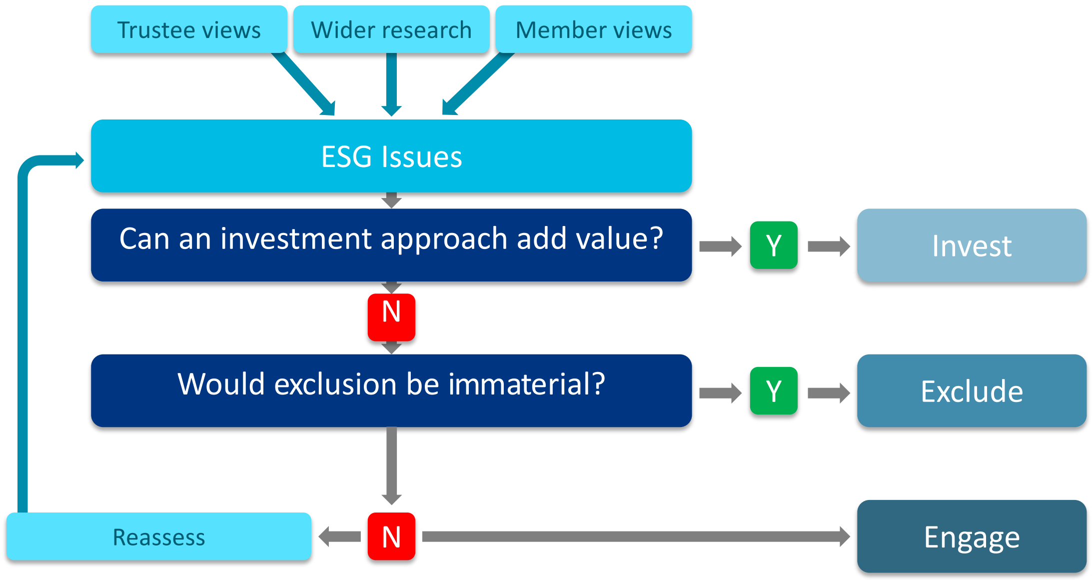
The People's Pension works with its founder, B&CE.

B&CE is a not-for-profit organisation that operates (like The People's Pension) in the best interests of its customers. It has a significant level of resource and it has responsible investment duties for assets sitting outside of The People's Pension.

B&CE and The People's Pension act in partnership on responsible investment and agree the broad research agenda together. However, we may take different views from each other on topics from time to time, recognising the different characteristics, membership and objectives we have.

B&CE conducts responsible investment research for The People's Pension and is a signatory to several industry groups and research organisations. B&CE experts use insight from these bodies and the wider market to form a better understanding of ESG topics and trends before raising them formally with the Trustee. We take independent advice over any investment process proposed by B&CE.

Our current responsible investment research process is described in the next section. Responsible investment, and our approach to it, is evolving so this policy is subject to change.



1. We identify and understand responsible investment issues

B&CE communicates with companies, regulators, non-governmental organisations (NGOs) and other organisations in the investment chain.

We do this to understand the following:

- The issues we need to prioritise for research – from an investment and ethical perspective
- The most efficient and effective ways to address these issues – and we do this by collaborating with a variety of organisations
- Best practice

This generates a list of issues which we then research and build into our investment process. The Trustee reviews this list and agrees what B&CE will research as a priority.

We recognise how detailed this approach is but we believe it is important because it enables us to identify and focus on key issues.

2. We assess issues

When we identify a responsible investment issue, B&CE goes through our responsible investment framework to determine the most effective method of addressing it. This involves the following:

- A formal assessment to determine whether an investment approach to altering our portfolios could improve member outcomes
- Determining the most appropriate approach to exclusion – one that looks at just the issue in question (narrow) or one that considers a whole range of different issues (wide) – more on this is our section on 'Exclusion and screening'.

Finally, for any priority ESG issue that our portfolios remain exposed to, we'll include the issue when we engage with investee companies and decide upon its prioritisation alongside other issues.

Here's how we assess which approach is appropriate.

2.1 Our investment approach

Any investment approach is primarily about improving risk and return characteristics.

B&CE works with asset managers and index providers to understand and assess how their insight could help us integrate ESG factors into our investment process. Most likely this means using ESG data to tailor the indices tracked by our funds to take account of the issue.

Once an approach is identified B&CE, will present evidence to the Trustee to demonstrate whether the stated approach is likely to:

- reduce exposure to the ESG issue, including how the approach affects wider ESG measures
- affect the risk and return characteristics of the portfolio.

If there's evidence that an approach will reduce exposure to an ESG issue and improve risk and return characteristics, we'll seek to include it in our portfolios as quickly as we can.

Where the approach reduces ESG exposure and has no apparent effect on portfolio characteristics, we would also consider including this approach. This may be an exclusion or a more complex process.

Where the approach harms risk and return characteristics, we would consider it within our exclusion process.

2.2 Exclusion and screening

If we can't address an issue through our approach to investment, we'll consider applying exclusion or screening to the portfolio.

This consideration is only relevant to issues that don't appear to improve risk and return characteristics. We're very aware that excluding investments can have a cumulative effect and result in a more concentrated portfolio.

We recognise two types of exclusion:

1. Narrow issues

2. Wide issues

2.2.1 Narrow issues

Some issues affect a small number of potential investee companies – and a wholesale exclusion from our portfolios might be suitable.

These narrow issues can have a material reputational impact and/or not comply with broad social norms. An example is 'controversial weapons', as identified by the UN Global Compact. A narrow issue can be considered as a stand-alone exclusion.

B&CE uses ESG research from MSCI – one of the world leaders in this field – to identify and analyse a company's involvement in major ESG controversies. This assesses adherence to international norms and principles.

MSCI ranks companies using the following scale:

Red:	Orange:	Yellow:	Green:
Indicates that a company is involved in one or more very severe controversies	Indicates that a company has been involved in one or more recent severe structural controversies that are ongoing.	Indicates the company is involved in severe-to-moderate level controversies.	Indicates that the company is not involved in any major controversies.

Where an issue has been flagged as Red, we'll consider this as a ground for exclusion from the portfolio.

2.2.2 Wide issues

These are far-reaching and have an impact and exposure across many sectors and markets.

Current examples include pay inequality and gender diversity. Excluding companies with poor behaviour from our portfolios would result in us having a very small number of companies to invest in. Conversely, having a diversified pool of companies to invest in could limit the practicality of the a policy.

Our primary route for addressing wide issues is engagement, but we do believe in exclusion for the worst behaving companies on several issues. Here's how we make this happen.

MSCI has assessed 37 key ESG issues:

3 Pillars	10 Themes	37 ESG key Issues	
Environment	**Climate change**	**Carbon emissions*** Product carbon footprint	Financing environmental impact Climate change vulnerability
	Natural resources	**Water stress*** Biodiversity and land use	Raw material sourcing
	Pollution and waste	**Toxic emissions and waste*** Packaging material and waste	Electronic waste
	Environmental opportunities	Opportunities in clean tech Opportunities in green building	Opp's in renewable energy
Social	**Human capital**	**Labour management*** **Health and safety***	Human capital development Supply chain labour standards
	Product liability	Product safety and quality Chemical safety Financial product safety	Privacy and data security Responsible investment Health and demographic risk
	Stakeholder opposition	Controversial sourcing	
	Social opportunities	Access to communications Access to finance	Access to health care Opp's in nutrition and health
Governance	**Corporate governance***	**Board**** **Pay****	**Ownership**** **Accounting****
	Corporate behavior	**Business ethics*** **Anti-competitive practices*** **Tax transparency***	Corruption and instability Financial system instability

*Indicates 'universal' issue assessed for all companies in the MSCI World Index
**Board, pay, ownership and accounting carry weight in the ESG rating for all companies.

The MSCI ESG ratings address four key questions about the companies in which we invest – these are as follows:

1. What are the most significant ESG risks and opportunities facing a company and its industry?
2. How exposed is the company to those key risks and/or opportunities?
3. How well is the company managing key risks and/or opportunities?
4. What is the overall picture for the company and how does it compare to its global industry peers?

One of the key things in investment is weighting – which means devoting an appropriate amount of time to a given company or issue. It doesn't mean dividing time equally across a number of unequally sized companies. The MSCI ratings work in the same way. They look at how a company performs against the industry average, rating them somewhere between best (AAA) and worst (CCC) and this helps us build a picture of wide issues.

We use these ratings to exclude or reduce our exposure to companies with the worst ESG performance and therefore reduce our exposure to a wide number of financial and reputational risks.

This approach isn't perfect. ESG issues will still crop up in the companies we invest member assets in. But we're pragmatic – we address concerns about an issue in combination with other issues and acknowledge that it cannot be completely removed from a portfolio.

2.3 Engagement

When we can't address an issue by investment approaches or by excluding specific securities from the portfolio, then we remain exposed to it.

We're comfortable with this and handle the matter through our engagement and, where appropriate, voting with investee companies.

In practice, our engagement may take a wide variety of forms depending on how high a priority the issue is to us, the mechanisms available to engage on the issue and the views whether our investment managers believe it is a high priority issue.

In many cases, we expect and require our fund managers to vote and engage with companies across global markets to protect and promote good standards and practice. This helps to encourage behaviours that are capable of boosting the long-term economic value of our members' investments.

Sometimes we work with other organisations. This can help us be more effective. The best example is our support for the UN-backed Principles of Responsible Investment – the world's leading proponent of responsible investment – supported by thousands of pension schemes, investment groups and governments.

We support collaborative initiatives that are focused and well organised, and which add more power to our engagement approach.

3. Trustee review process

B&CE manages the majority of the day-to-day activity within this process, working with the Trustee to agree issues that are being worked on and strategies to address them.

We expect to work in full partnership with B&CE. But if there are any differences of opinion between the Trustee and B&CE, we'll make a note of that in our annual statements on this policy.

4. Ongoing diligence and review

The responsible investment landscape is continually changing and more research is constantly published on many ESG issues. The way we prioritise issues and risks enables B&CE to focus on the most important ones – but we can change those priorities at any time in response to new evidence.

Similarly, we might conclude that a given issue can only be dealt with as part of our wider exclusions and engagement activity. But, even where this is the case, we'll re-assess ESG issues every 3 years to help us ensure we draw the right conclusions.

Appendix 1: Passive management – engagement principles

We measure our managers against the following principles.

We're an increasingly active owner – influencing both investee companies and the policies our asset managers use.

We expect our managers to...

- **be transparent and accountable by**
  - engaging in dialogue, honest evaluation, continuous enhancement and increased transparency of their stewardship practices.
- **enhance and evolve ESG practices in markets by**
  - applying higher voting standards where governance practices do not meet global investor expectations
  - identifying clear engagement priorities that focus on sector, thematic and/or market specific issues
  - collaborating with other investors when collective action is needed.
- **Develop long-term partnerships with companies and guide them through the evolution of ESG practices by**
  - engaging constructively with management/boards to bring about change in investee companies
  - publishing thought-leadership papers to inform directors on changing ESG practices
  - communicating clearly our expectations and vote rationale during engagement.

Given our commitment to high standards, we also expect our fund managers to have signed our Policy on responsible investment and to comply with the UK Stewardship Code (and relevant international equivalents, where applicable).

State Street Global Advisors (SSGA)

We have agreed with SSGA, the scheme's core passive investment manager, that strong relationships with boards and management teams of investee companies together with the monitoring of their performance, can enhance the long-term value of our members' investments.

On behalf of the Trustee, the Chief Investment Officer has evaluated (and will continue to evaluate) the breadth and capability of SSGA's function, in line with the above principles.

SSGA has a team of asset stewardship professionals who help it to carry out its duties as a responsible investor. These duties include researching companies, identifying issues and then engaging with them as necessary. SSGA voting and engagement focuses on a range of themes, including the following:

- Election of Directors and Boards
- Accounting and audit related issues
- Capital structure, reorganisation and mergers
- Compensation
- Environmental and social issues

As we invest in funds alongside other investors, we recognise that SSGA's prioritisation of issues for engagement and voting may not always be identical to ours. But we do our utmost, through regular contact with them and a formal annual engagement process, to make sure SSGA is as aligned as possible with us – now and in future.

Monitoring and reporting on responsible investment

We receive, review and publish reports on SSGA's:

- voting activity on our behalf
- engagement activity on our behalf.

We're also looking into ways to measure ESG risk across all of our assets under management – rather than on a case-by-case basis. Our new scoring system will enable us to report on how elements of our investment approach reduce ESG risks relative to market averages.

We provide copies of this policy, our voting and our engagement records on our website.

In 2019, we'll produce a responsible investment report that will include the following:

- How ESG and responsible investment principles have been integrated into our investment approach.
- Ownership of activities (voting, engagement, and/or policy dialogue),
- The outcome of our responsible investment research and the steps we're taking as a result
- What we're working on or discussing with other stakeholders in the interests of members.

We are working on ways to allow our members to highlight or endorse ESG issues.

Investment options

We recognise that member attitudes and view on responsible investment varies. For example, we may not engage with companies that members with money in our Ethical Fund may prefer to exclude. This fund invests passively in the MSCI World ESG Universal Index which is made up of companies that demonstrate a robust ESG profile and a positive trend in improving that profile.

Appendix 2: The People's Pension proxy voting and engagement principles

The People's Pension expects its fund managers to vote and engage with companies in global markets. This protects and promotes good standards and practice and helps to safeguard long-term economic value for our members.

Principally, we believe the primary responsibility of the board of directors of each of the underlying companies held by our funds, is to preserve and enhance shareholder value and protect shareholder interests.

The most likely areas we expect our fund managers to engage with companies on are the structure of company boards, audit-related issues, capital structure, remuneration, environmental, social and governance-related issues.

Directors and boards of investee companies

We believe that a well-constituted board of directors, with a good balance of skills, expertise and independence, provides the foundations for a well-governed investee company.

Director independence and succession planning, board diversity, evaluations and refreshment, and company governance practices are all useful measures of board quality. We expect our managers to vote for the election/re-election of directors on a case-by-case basis after considering these factors.

We also expect boards of FTSE-350 listed companies to have at least one female board member.

In principle, we believe independent directors are crucial to good corporate governance and help management establish sound corporate governance policies and practices. A sufficiently independent board is better placed to effectively monitor management and perform the oversight functions necessary to protect shareholder interest.

The People's Pension expects UK investee companies to consider the following criteria for director independence:

- participation in related-party transactions and other business relations with the company
- employment history with company
- excessive tenure and a preponderance of long-tenured directors
- relations with controlling shareholders
- family ties with any of the company's advisers, directors or senior employees
- if the company classifies the director as non-independent.

Audit-related issues

Companies should have robust internal audit and control systems to manage potential and emerging risks to company operations and strategy. The responsibility for setting out an internal audit function lies with the audit committee, which should include independent non-executive directors, where possible.

Appointment of external auditors

We believe that a company's auditor is an essential feature of an effective and transparent system of external supervision. We also believe that shareholders should be given the opportunity to vote on their appointment or re-appointment at annual meetings.

Managers should consider voting against members of the audit committee if they have concerns with audit-related issues or if the level of non-audit fees to audit fees is significant. In certain circumstances, managers should consider auditor tenure when evaluating the audit process.

Shareholder rights and capital related issues

Issuing new shares

The ability to raise capital is critical for companies to carry out their strategy, grow and achieve returns above their cost of capital. The approval of capital raising activities is fundamental to shareholders' ability to monitor the amount of proceeds and to ensure capital is deployed efficiently. We support capital increases that have sound business reasons and that are not excessive relative to a company's existing capital base.

Share repurchase programmes

We generally support a company's proposal to repurchase shares. We would make exceptions when the issuer does not clearly state:

- the business purpose for the programme
- a definitive number of shares to be repurchased
- the range of premium/discount to market price at which a company can repurchase shares
- the timeframe for the repurchase.

Managers should consider voting against share re-purchase if any of these criteria are not adequately satisfied or for requests that allow share repurchases during a takeover period.

Dividends

We generally support dividend payouts that constitute 30% or more of net income. Managers may vote against dividend payouts if the dividend payout ratio has been consistently below 30%

without adequate explanation or if the payout is excessive given the company's financial position. Payments that are significantly out of line with previous dividend payments will be reviewed on a case-by-case basis. Attention will be paid to cases where the payment may damage the company's long-term financial health.

Mergers and acquisitions

Company mergers or reorganisations often involve proposals relating to reincorporation, restructures, mergers, liquidations and other major changes to the corporation. We would generally expect managers to support proposals that are in the best interests of the shareholders, demonstrated through enhanced share value or by improving the effectiveness of company operations. In general, we wouldn't expect managers to support provisions that are economically unsound or considered destructive to shareholders rights.

We would generally expect managers to support transactions that enhance shareholder value. Some relevant considerations include, but are not limited to:

- whether premiums are offered
- strategic rationale
- board oversight of the process for the recommended transaction, including director and/or management conflicts of interest
- offers made at a premium and if there are any higher bidders
- offers in which the secondary market price is substantially lower than the net asset value.

Anti-takeover measures

We oppose anti-takeover defences such as authorities for the board, when subject to a hostile takeover, to issue existing shareholders with warrants that can be converted into shares.

Remuneration

Executive pay

The People's Pension has a simple underlying philosophy: There should be a direct relationship between remuneration and company performance over the long term.

Shareholders should have the opportunity to assess whether pay structures and levels are aligned with business performance, including profit growth, balance sheet strength and risk management, and sustainable long-term shareholder value growth.

When assessing remuneration policies and reports, we generally expect managers to consider factors, including the following:

- Adequate disclosure of different remuneration elements.
- Absolute and relative pay levels.
- Peer selection and benchmarking.
- The mix of long-term and short-term incentives.
- Aligning pay structures with shareholder interest, as well as with corporate strategy and performance.

Equity incentive plans

We may not support proposals on equity-based incentive plans if insufficient information is provided on matters such as grant limits, performance metrics, performance and vesting periods and overall dilution. We don't generally support options under such plans being issued at a discount to market price or plans that allow for re-testing of performance metrics.

Non-executive director pay

Authorities seeking shareholder approval for non-executive director fees are generally not controversial. So, as a rule, we support resolutions on director fees – unless disclosure is poor and we're unable to determine whether they're excessive in relation to fees paid by other companies in the same country or industry.

Where possible, managers should evaluate on a company-by-company basis any non-cash or performance-related pay to non-executive directors.

Risk management

We believe that risk management is a key function for boards of investee companies that are responsible for setting the overall risk appetite of that company and for providing oversight on the risk management process established by senior executives at the company.

Where possible, we expect companies to disclose how the board provides oversight on its risk management system and to identify key risks facing the company. Boards should also review existing and emerging risks that can grow or evolve with a changing political and economic landscape, or as companies diversify or expand their operations into new areas.

Environmental and social issues

We consider the financial and economic implications of environmental and social issues. In their public reporting, we expect companies to disclose information on relevant management tools, environmental and social performance metrics. We support the efforts made by companies to demonstrate how sustainability fits into their overall strategy, operations and business activities.

As far as possible, managers should evaluate risks and the shareholder proposal relating to them on an case-by-case basis. It's important they understand that environmental and social risks can vary widely depending on a company's industry, operation and where it's located.

Managers should also consider opposing the re-election of board members if they have serious concerns over ESG practices and the company has not been responsive to shareholder concerns.

Appendix 3: Draft policy wording

Taking account of ESG factors is an intrinsic part of our investment and engagement processes, as reflected in our investment belief.

Investment decisions should reflect environmental, social and governance considerations

Incorporating ESG factors in our investment not only has the potential to influence change in corporate behaviour, it also has the potential to generate positive returns over the long-term.

Pension scheme investments are long-term in nature and factors such as poor corporate governance or unsustainable business practices, together with other long-term risk factors such as climate change, can have a significant detrimental impact on returns. We believe it's our responsibility to manage our investments to deliver a positive contribution to society and future generations where this does not negatively affect returns.

We believe that:

- a company's **environmental actions** can signal:
  - operational efficiency: higher or lower costs
  - environmental liability: reduced or enhanced
  - revenue sources: opportunities or threats
- a company's **social behaviours** can signal:
  - human capital: effective or ineffective management of people
  - product/service safety: reduced or enhanced financial and reputational risks
  - customer base: expanding or declining
- a company's **governance practices** can signal:
  - decision-making: shareholder value enhanced or reduced
  - controls: reduced risk from impaired reputation or weak financial controls
  - management: better or worse performance from reaction to and implementation of change.

The ESG issues we're addressing

We're serious about ensuring our portfolios reflect beliefs held by us and our members.

We talked about prioritisation earlier on in this policy. The first order of priorities for our work are issues relating to climate change and also items identified in the UN Global Compact.

Issue	Description	Rationale	Activity
Climate change	Carbon footprint and reserves; exposure to climate change effects; exposure to the transition to a low-carbon economy.	Seeking compelling evidence that specific investment approaches offer material performance improvements.	Working with research agencies to assess how to incorporate carbon reduction metrics into portfolio construction.
Controversial weapons	Securities issued by companies that manufacture controversial weapons, as defined by the UN Global Compact.	Material reputational issue. Immaterial financial impact – a small number of investments excluded.	Exploring how best to introduce exclusions into the portfolio, and the effect this has on the resulting portfolio.
Asbestos mining	Companies extracting and processing asbestos.	Material reputational issue. Immaterial financial impact – a small number of investments excluded.	Researching how to define and monitor exclusions of companies involved in any form of asbestos processing.

Once this research have been completed, we have highlighted the following issues for further research.

Issue	Description	Rationale	Activity
Gender diversity	Balance of genders by level of seniority.	Seeking compelling evidence that specific investment approaches offer material performance improvements.	Researching the impact of gender diversity on company performance. Engaging with companies.
Pay inequality	Distribution of pay by level of seniority.	Seeking compelling evidence that specific investment approaches offer material performance improvements.	Researching the impact of gender diversity on company performance. Engaging with companies.
Board diversity	Composition of board appointments and decision-making.	Seeking compelling evidence that specific investment approaches offer material performance improvements.	Researching the impact of gender diversity on company performance. Engaging with companies.

Version	Document name	Nature of change	Implemented
Version 1	Initial creation		01/02/2018
Version 2	Update	Reflecting changes policy and strategy	01/10/2018

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The information in this document is correct as at November 2018 and may be subject to change.

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PS TPP 0003.1118