

**Agenda Item No.4 (c)**

**DERBYSHIRE COUNTY COUNCIL  
PENSIONS AND INVESTMENTS COMMITTEE**

**1 November 2017**

**Report of the Director of Finance & ICT**

**FRC STEWARDSHIP CODE**

**1 Purpose of the Report**

To obtain approval to publish a statement regarding the Authority's compliance with the Financial Reporting Council's UK Stewardship Code.

**2 Information and Analysis**

The FRC is the UK's independent regulator responsible for promoting high quality corporate governance and reporting. The FRC promotes high standards of corporate governance through the UK Corporate Governance Code which sets out standards of good practice in relation to board leadership and effectiveness, remuneration, accountability, and relations with Shareholders. The Pension Fund considers these best practice standards when exercising its voting rights.

The Government and regulators, such as the FRC, have put increasing pressure on companies to raise their standards of governance. As a consequence of the global financial crisis, the focus has moved to long term institutional investors, including pension funds, with a strong encouragement that they act as responsible and engaged corporate owners.

The UK Stewardship Code was first published in July 2010, revised in September 2012 and will be revised again in 2018 by the FRC and is designed to lay out the responsibilities of institutional investors as shareholders and provide guidance as to how these responsibilities might be met. Whilst it is aimed in the first instance at asset managers, particularly those regulated by the Financial Conduct Authority (FCA), pension fund trustees are strongly encouraged to report if, and how, they have complied with the Code.

The Code is a set of best practice principles that are intended to frame both shareholder engagement with companies, and the disclosure of such activity. It is intended that shareholders adhere to the principles with the same "comply or explain" approach used with the UK Corporate Governance Code for listed companies.

Institutional investors are encouraged to publish their Statement of Compliance with the Code on their website and also within their Annual Report and Accounts. In addition, notification of compliance should be provided to the FRC.

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 require an administering authority of an LGPS fund to include its policy on the exercise of the rights (including voting rights) attaching to investments in its Investment Strategy Statement ("ISS"). The Guidance on Preparing and Maintaining an Investment Strategy Statement from the Department for Communities and Local Government includes a requirement for administering authorities to explain their policy on stewardship with reference to the Stewardship Code. Administering authorities are expected to become signatories to the Code and state how they implement the seven principles and guidance of the Code, which apply on a "comply or explain" basis.

### **3 Considerations**

In preparing this report the relevance of the following factors has been considered: financial, legal, human rights, human resources, equality and diversity, health, environmental, transport, property, social value and prevention of crime and disorder considerations.

### **4 Officer's Recommendation**

The Committee is requested to approve the Pension Fund's Statement of Compliance with the UK Stewardship Code for Institutional Investors, which is attached at Appendix 1

PETER HANDFORD

Director of Finance & ICT

**APPENDIX 1****Derbyshire Pension Fund****Compliance with the UK Stewardship Code prepared by the Financial Reporting Council  
2017**

Derbyshire Pension Fund supports the FRC Stewardship Code and, seeks to apply the Principles in the Code to its investment activity. Although the Code is focused on the UK, the Fund seeks to apply the Principles of the Code to its non-UK investments subject to local practice and law.

The management of the Fund's assets is split between the internal investment manager and a number of external fund management groups. Some of these managers Statement of Compliance with the UK Stewardship Code can be viewed at [www.frc.org.uk](http://www.frc.org.uk)

**Principle 1 – Institutional investors should publically disclose their policy on how they will discharge their stewardship responsibilities**

The Fund takes its responsibilities as a shareholder seriously and seeks to adhere to the Principles of the Stewardship Code. The Committee believes that responsible investment covers both incorporating Environmental, Social & Governance (ESG) factors into the investment process and Fund stewardship and governance through considered voting and engagement with investee companies.

Effective management of financially material ESG risks should support the requirement to protect investment returns over the long term. The Fund's investment team seek to understand relevant ESG factors alongside conventional financial considerations within the investment process, and the Fund's external investment managers are expected to do the same. Non-financial factors may be considered to the extent that they are not detrimental to the investment return.

The Committee recognises the UK Stewardship Code as best practice and encourages the Investment Managers of our pooled investment holdings to comply with the UK Stewardship Code or explain where they do not adhere to this policy.

How the Authority discharges its responsibilities is set out in the Authorities Investment Strategy Statement which can be found at <http://www.derbyshire.gov.uk/pensions>

**Principle 2 – Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publically disclosed**

Derbyshire County Council, the administering authority of the Derbyshire Pension Fund requires each Member of its Pensions and Investments Committee to make declarations of interests prior to each committee meeting.

The Code of Conduct for Councillors and Employees can be found on the Council's constitution online.

[http://www.derbyshire.gov.uk/council/council\\_works/constitution/default.asp](http://www.derbyshire.gov.uk/council/council_works/constitution/default.asp)

Individual employees of the internal investment management team are required to gain permission from the Head of Investments or, in the Head of Investments case, the Director of Finance prior to investing in any applicable investments, as set out in the Fund's compliance manual, on a personal basis.

The Fund encourages external fund management groups where it has investments to have effective policies addressing potential conflicts of interest.

**Principle 3 – Institutional Investors should monitor their investee companies**

The Pensions and Investment Committee delegates responsibility for managing the Fund's assets to the Director of Finance & ICT and the Internal Fund Management Team, who are expected to monitor the investment holdings and intervene where necessary, reporting back at committee meetings if action is taken

The Committee has appointed Institutional Shareholder Services, a third party voting agency to provide voting services for its directly held UK equity investments. Voting is carried out in line with recommendations from ISS, whose voting principles cover four key principles on accountability, stewardship, independence and transparency. The Fund also periodically receives voting alerts from the Local Authority Pension Fund forum (LAPFF) on certain resolutions. If the voting alert from the LAPFF conflicts with the ISS recommendation, due consideration is given to all the arguments before the vote is cast. A report to review the Fund's voting activity is taken to the Committee on a quarterly basis.

Membership of the Local Authority Pension Fund Forum (LAPFF) helps Derbyshire Pension Fund to engage with companies to understand the issues and to promote best practice. Collective pressure from investors via organisations such as the LAPFF has helped to encourage listed companies to enhance their corporate governance and to improve their environmental and social impacts. The Fund attaches great importance to the exercise of

voting rights and currently casts votes in respect of its directly held equity investments in the United Kingdom and North America.

The Internal Fund Management Team actively engages with Investee company management or representatives, as appropriate, along with monitoring a vast range of information from financial analysis of publicly available information, market intelligence, broker research, fundamental analysis and meetings with companies.

The fund holds its external fund managers to account in other geographical locations for their engagement approach as part of its monitoring activities. All external managers of Derbyshire Pension Fund assets are prepared to provide information on engagement and voting by request

**Principle 4 – Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.**

As highlighted above, responsibility for day-to-day interaction with companies is delegated to the Fund's Internal Fund Management Team, including the escalation of engagement when necessary.

The Fund Managers will try to engage with the company before it embarks on a programme of action whenever possible; this dialogue could be over an extended period. Escalation of any engagement activities, if the company proves to be unreceptive to engagement, will depend on individual circumstance and resources.

Where special situations arise which are not covered by the Fund's corporate governance strategy or where the policy is unclear, the Fund Managers will consult with the Head of Investments on action that may be taken; this includes, but is not limit to, communications through the company's brokers, direct engagement with Chairman or non-executive directors or joint intervention with other shareholders.

Although willing to act alone, as the Fund typically holds a very small percentage of equity in Individual companies, there are strong reasons to collaborate with other asset owners in order to present a stronger case. The Fund utilises its membership of the LAPFF, which co-ordinates collaborative engagement with companies, regulators and policymakers to protect and enhance shareholder value, in order to maximise its influence.

If deemed appropriate, the Fund will participate in shareholder litigation. Any such actions and subsequent outcomes would be reported to the Pensions Committee in order to monitor activity and assess effectiveness.

**Principle 5 – Institutional investors should be willing to act collectively with other investors where appropriate.**

Collaborative engagement is a key part of the Fund's Investment Strategy Statement. A strategy of engagement with companies, rather than negative screening to exclude stocks from the portfolio on ESG/ethical grounds, is more compatible with the administering authority's fiduciary duties and supports responsible investment.

The Fund seeks to achieve this through membership of the LAPFF, which engages with companies over environmental, social, and governance issues on behalf of its members, and also its relationships with its external fund managers. The Fund will also consider collaborating with other investors if it is considered to be appropriate.

**Principle 6 – Institutional investors should have a clear policy on voting and disclosure of voting activity.**

The Fund regards the exercise of voting rights attached to its investments as having great importance. The Fund exercises its voting rights on its own behalf at meetings of all UK Listed companies in which there is a holding.

Voting is carried out in line recommendations from ISS, whose voting principles cover four key principles on accountability, stewardship, independence and transparency. A report to review the Fund's voting activity is taken to the Committee on a quarterly basis.

The fund also votes on directly held equity investments in North America via a discretionary agreement with an external fund manager. This manager is expected to have policies and procedures to ensure that they collect and analyse all relevant information for each meeting, applying their proxy voting guidelines accurately and executing votes in a timely manner in line with local practise.

The Committee recognises the UK Stewardship Code as best practice and encourages the Investment Managers of the Fund's pooled investment holdings to comply with the UK Stewardship Code or explain where they do not adhere to this policy. The Committee also encourages our external managers to provide voting records when request.

Whilst Derbyshire Pension Fund has the ability to loan out its directly held equity positions it does not currently engage in this practice.

**Principle 7 – Institutional investors should report periodically on their stewardship and voting activities.**

The Pensions and Investments Committee reviews a detailed voting report on the voting activity of the internal fund managers, on a quarterly basis. The fund proxy voting system logs all fund voting and uses the funds voting policy to indicate suggested voting intentions that best represents the Pensions and Investment Committee's approved policy. A copy of these quarterly reports can be found on the Derbyshire County Council website under the Pension and Investment Committee meeting minutes.

All voting activity of our external managers can be obtained upon request.