Erskine Hospital Limited Retirement Benefits Scheme Implementation Report

October 2022

isio.

Document classification: Public

Background and Implementation Statement

Background

The Department for Work and Pensions ('DWP') has increased regulation to improve disclosure of financially material risks. This regulatory change recognised Environmental, Social and Governance (ESG) factors as financially material and schemes need to consider how these factors are managed as part of their fiduciary duty. The regulatory changes require that schemes detail their policies in their Statement of Investment Principles (SIP) and demonstrate adherence to these policies in an implementation report.

Statement of Investment Principles (SIP)

The Scheme has updated its SIP in response to the DWP regulation to cover:

- policies for managing financially material considerations including ESG factors and climate change
- policies on the stewardship of the investments

The SIP can be found online at the following link.

There were no changes to the SIP over the 2021/22 reporting year.

Implementation Report

This Implementation Report is to provide evidence that the Scheme continues to follow and act on the principles outlined in the SIP. This report details:

- actions the Trustees have taken to manage financially material risks and implement the key policies in its SIP
- the current policy and approach with regards to ESG and the actions taken with managers on managing ESG risks
- the extent to which the Trustees have followed policies on engagement, covering engagement actions with its fund managers and in turn the engagement activity of the fund managers with the companies they invest
- voting behaviour covering the reporting year up to 5 April 2022 for and on behalf of the Scheme including the most significant votes cast by the Scheme or on its behalf

Summary of key actions undertaken over the Scheme reporting year

- There were no changes to the Scheme's investment strategy over the year. The Scheme's strategic asset allocation remains in line with the benchmark stated in the SIP.
- However, the Trustees have agreed to a review the suitability of the Scheme's investment strategy. Post reporting year end Isio produced a 'Journey Planning' paper which will help in the evaluation of the Scheme's short and medium term objectives, as well as the suitability of the current strategic benchmark.
- The Trustees also agreed to a 'health check' of the Scheme's LDI hedge solution, using revised cashflows from the 2021 Valuation. This will enable

the Trustees to gain comfort that the current solution remains fit for purpose, relative to the Scheme's latest data.

Both will be implemented in the 2022/2023 reporting year.

Implementation Statement

This report demonstrates that the Erskine Hospital Limited Retirement Benefits Scheme has adhered to its investment principles and its policies for managing financially material considerations including ESG factors and climate change.

Signed

Position

Date

Managing risks and policy actions DB

Risk / Policy	Definition	Policy	Actions
Interest rates and inflation	The risk of mismatch between the value of the Scheme assets and present value of liabilities from changes in interest rates and inflation expectations.	To hedge 45% of the impact of interest rate and inflation risk on the value of the Scheme's uninsured liabilities (on a gilts basis).	The Trustees have monitored and maintained the Scheme's hedging through semi-annual reporting. **The Trustees have agreed to formally review the hedging portfolio in the 2022/23 reporting period.**
Liquidity	Difficulties in raising sufficient cash when required without adversely impacting the fair market value of the investment.	To maintain a sufficient allocation to liquid assets so that there is a prudent buffer to pay members benefits as they fall due (including transfer values), and to provide collateral to the LDI manager.	The Trustees monitor the Scheme's liquidity position as part of semi-annual reporting. The Trustees have also agreed to conduct a cashflow forecast and review and draft a formal policy in order to manage the Scheme's cash requirements going forward.
Market	Experiencing losses due to factors that affect the overall performance of the financial markets.	To remain appropriately diversified and hedge away unrewarded risks, where affordable and practicable.	
Credit	Default on payments due as part of a financial security contract.	To diversify this risk by investing in a range of credit markets across different geographies and sectors. To appoint investment managers who actively manage this risk by seeking to invest only in debt securities where the yield available sufficiently compensates the Scheme for the risk of default.	

Environmental, Social and Governance	Exposure to Environmental, Social and Governance factors, including but not limited to climate change, which can impact the performance of the Scheme's investments.	To appoint managers who satisfy the following criteria, unless there is a good reason why the manager does not satisfy each criteria: 1. Responsible Investment ('RI') Policy / Framework 2. Implemented via Investment Process 3. A track record of using engagement and any voting rights to manage ESG factors 4. ESG specific reporting 5. UN PRI Signatory (or equivalent) The Trustees monitor the managers on an ongoing basis.	The ESG policy was reviewed by the Trustees as part of the SIP update in September 2019 and 2020. The Trustees still deem this policy to be appropriate. The Trustees received summaries of the ESG integration within each investment mandate as part of the H2 2021 investment report.
Currency	The potential for adverse currency movements to have an impact on the Scheme's investments.	Hedge all currency risk on all assets that deliver a return through contractual income.	
Non-financial	Any factor that is not expected to have a financial impact on the Scheme's investments.	Non-financial matters are not taken into account in the selection, retention or realisation of investments.	

Changes to the SIP

Policies added to the SIP
There were no changes to the SIP during the reporting period. Date last updated: 23 September 2020

Implementing the current ESG policy and approach

ESG as a financially material risk

The SIP describes the Scheme's policy with regard to ESG as a financially material risk. This page details how the Scheme's ESG policy is implemented, the rest of this statement details our view of the managers, our actions for engagement and an evaluation of the stewardship activity.

The below table outlines the areas which the Scheme's investment managers are assessed on when evaluating their ESG policies and engagements. The Trustees intend to review the Scheme's ESG policies and engagements periodically to ensure they remain fit for purpose.

Implementing the Current ESG Policy

Areas for engagement	Method for monitoring and engagement	Circumstances for additional monitoring and engagement
Environmental, Social, Corporate Governance factors and the exercising of rights and engagement activity	• The Trustees will obtain regular training on ESG considerations in order to understand fully how ESG factors including climate change could impact the Scheme and its investments; • As part of ongoing monitoring, the Trustees will use any ESG ratings information provided by their investment consultant to assess how the Scheme's investment managers	• The manager has not acted in accordance with their policies and frameworks. • The manager has received a 'red' ESG rating from the Investment Consultant, signifying that ESG considerations are below satisfactory.

	take accounts of ESG issues; • Through their investment consultant, the Trustees will request that all of the Scheme's investment managers provide information about their ESG policies, and details of how they integrate ESG into their investment processes on an annual basis. • As part of any manager selection exercise, ESG considerations are included as part of the evaluation criteria.	

ESG summary and engagement with the investment managers

Manager and Fund	ESG Summary	Actions identified	Engagement details
LGIM Passive Equity	LGIM have shown a strong commitment to highlighting, identifying and managing ESG risks across their entire fund range, including their passive equity funds. LGIM are a market leader in their approach to ESG. They have developed a clear and comprehensive framework for scoring portfolio companies on ESG factors. They actively communicate these scores to the companies and engage with them directly to help mitigate ESG risks moving forwards.	Isio proposed LGIM consolidate the ESG score of underlying portfolio companies to generate an overall score as well as broken down by E, S and G, that allows investors to digest the ESG impact of the funds. Isio also suggested that LGIM should incorporate ESG reporting into their standard quarterly reports.	Isio engaged with the manager on behalf of the Trustees over the period. Following engagement, LGM aim to include social and governance metrics in future versions of the ESG quarterly reporting and have developed an LGIM ESG score which has split the E, S, and G components into 29 metrics. LGIM's ESG quarterly reports provide data on carbon, voting and engagement and are looking to streamline their ESG reporting output with the aim of integrating reporting with standard client quarterly reports. However, this is dependent on upgrading internal systems before they can incorporate the ESG information into the quarterly investment reports. Fund level data extracts are due to be available in H1 2022 to provide more granular detail on specific engagements. LGIM have employed EcoAct, an external consultancy to help in the development of
LGIM Corporate Bonds	LGIM is aware of ESG issues and the effect on long-term returns within its Fund offering. They have also taken steps to integrate these issues within their investment process at a business level. LGIM made a number of key improvements and have appointed a dedicated Head of Responsible Investment, refined their investment process to better reflect ESG factors and improved their stewardship approach to leverage off a wide range of assets across the firm.	LGIM should provide more detail on how they have engaged with the companies found in the Corporate Bond Funds including information on the ESG issues that have been raised/addressed, and the outcome of LGIM intervention. LGIM should provide standard and regular reporting (not only available on request), in relation to the Corporate Bond Fund outlining: 1) the exposure to ESG	

		risks; 2) carbon emissions exposure; 3) a fund-specific summary of voting and engagement activity.	science-based targets in line with their net zero carbon aims by 2030. In relation to LGIM real assets, they are currently working on producing a fund level report which will include ESG metrics and engagement progress across their portfolios.
LGIM Long Lease Property	LGIM have a strong and integrated ESG approach which follows a robust framework. At a firm level, LGIM have a strong history of active engagement and collaboration on ESG related topics. LGIM believe that sustainable investments are crucial to provide resilient, long-term investment returns. The use of third parties, such as Evora, to advise on ESG policies, shows strong commitment to ESG at both firm and portfolio level. LGIM are also pioneering on social value creation and have achieved their carbon emissions target two years early.	LGIM have identified key areas they must implement to become net zero carbon across their real estate portfolios by 2050, including: the introduction of a new property management model and technologies – It would be useful to have more evidence of LGIM's progress in implementing these actions Isio proposed that LGIM could provide more granular information/data on the diversity metrics in place at portfolio level, including ethnicity, gender and social mobility stats.	
LGIM LDI	LGIM have a team dedicated to understanding and assessing the impact of ESG factors for the wider business. LGIM have evidenced their ability to integrate ESG factors in their LDI fund range through counterparty review and engagement and use	LGIM should include the ESG scoring of counterparties in regular client reporting of LDI Funds.	Following Isio's engagement, LGIM are working on enhanced ESG counterparty reporting for delivery to clients, and are having internal discussions around how best to present this information in a meaningful way. LGIM provided an example of current thinking

	proprietary tools to quantify and monitor ESG risk. LGIM believe engaging with regulators, governments and other industry participants will help mitigate ESG risk.		around this, with this detailing the LGIM ESG score for the counterparty, and engagement highlights.
M&G Alpha Opportunities Fund	M&G have evidenced their ability to consider the significance of ESG factors in this Fund. M&G should consider measurable ESG aims for the Fund and increase the number of ESG risk metrics that are being monitored. Although M&G are actively developing their integrated ESG approach in investment decisions, M&G should consider more in-depth reporting for clients and progress reports on aims for the Fund.	M&G currently have a qualitative approach and are working towards a more quantitative scorecard approach. M&G should seek to roll this out for all analysts and to develop an integrated ESG scoring system that captures not only the issuer level but also the sector and country levels. M&G should clearly publicise engagements throughout the quarter as part of their quarterly reporting, and on their website. In addition, M&G should provide updates on past engagements. M&G should increase the number of risk metrics they monitor, such as climate change and portfolio's sensitivity to these metrics.	Isio engaged with the manager on behalf of the Trustees over the period. Following this engagement M&G are developing climate scenario capabilities and temperature pathway analysis and developed an ESG scorecard which is used for all potential issuers. M&G have also improved reporting of ESG metrics and engagements within quarterly reporting.

Engagement

As the Scheme invests via fund managers the managers provided details on their engagement actions including a summary of the engagements by category for the 12 months to 31 March 2022

Fund name	Engagement summary	Commentary
LGIM World Equity Index Fund	Total engagements: 501 Environmental: 257 Social: 182 Governance: 237 Other: 82	LGIM's Investment Stewardship team are responsible for engagement activities across all funds. LGIM share their finalised ESG scorecards with portfolio companies and the metrics on which they are based. LGIM have not provided examples of Fund-specific significant engagements.
LGIM World Emerging Markets Equity Index Fund	Total engagements: 120 Environment: 82 Social: 40 Governance: 44 Other: 17	
LGIM Active Corporate Bond Fund	Total engagements: 165 Environmental: 102 Social: 52 Governance: 84 Other: 36	
LGIM LPI Income Property Fund	LGIM currently do not provide details of their engagement activities at Fund level for Property Funds. Isio remains in contact with LGIM surrounding the firm's engagement reporting.	Due to the nature of most of the leases within the LPI Fund, LGIM can only engage with the tenants of the assets which are held in the Fund, and their overall influence as a landlord is limited. They maintain dialogue with all occupiers, and as part of this ESG-related behaviours are encouraged.

LGIM LDI and Gilts	LGIM have engaged with a number of industry participants on long term strategic issues in relation to LDI, including: - The introduction of central clearing; - The LIBOR transition; - Recognising the pricing issues with bilateral RPI swaps.	LGIM leverage the wider capabilities of the global firm to engage with companies. The team also regularly engage with regulators, governments and other industry participants to address long term structural issues, aiming to stay ahead of regulatory changes and adopt best practice.
M&G Alpha Opportunities Fund	Total engagements: 22 Environmental: 18 Social: 1 Governance: 3	M&G have a systematic approach to engagements whereby specific objectives are outlined in advance and results measured based on the outcomes from the engagements. M&G Analysts are expected to have a more granular awareness of key ESG risks which impact the individual issues they monitor. Where engagement is deemed to be necessary, analysts engage with issuers supported by M&G's Corporate Finance & Stewardship ("CF&S") Team, allowing them to leverage their expertise and sustainability themes. Examples of significant engagements include: **Intesa San Paola** – M&G met the Italian banking group's Head of Investor Relations, Head of ESG Sustainable Investment and Climate, and Head of ESG assessment to discuss the company disclosing its interim carbon reduction targets and its loan book exposure to the fossil fuel sector. The company did not agree to disclose the targets requested by M&G, but agreed to consider them in the future, M&G will continue to monitor the progress of this engagement. **BASF** – M&G engaged with the German chemicals company to plan the next phase of their engagement, with the objective being to agree to Net Zero targets by 2050 for scope 1,2 and 3 emissions. Upon meeting with the company, an agreement to

		announce Net Zero targets for scope 1 and 2 emissions was made. M&G continues to engage with the company and provide support in their plans of extending this target to include scope 3 emissions.

Voting (for equity/multi asset funds only)

As the Scheme invests via fund managers the managers provided details on their voting actions including a summary of the activity. For ease of reporting, the following information covers the year up to 31 March 2022. The managers also provided examples of any significant votes.

Fund name	Voting summary	Examples of significant votes	Commentary
LGIM World Equity Index Fund	Meetings eligible to vote for: 3,079 Resolutions eligible to vote for: 36,675 Resolutions voted for: 99.80% Resolutions voted with management: 80.18%% Resolutions voted against management: 18.97% Resolutions abstained from: 0.85%	**Microsoft Corporation –** As part of their commitment to improving independence in the underlying companies in which they invest, LGIM voted against the election of Satya Nadella as Director. The rationale, to ensure the roles of CEO and Chair are kept separate as part of risk management and oversight.	LGIM's Investment Stewardship team are responsible for managing voting activities across all funds.
LGIM World Emerging Markets Equity Index Fund	Meetings eligible to vote for: 4,087 Resolutions eligible to vote for: 34,237 Resolutions voted for: 99.80% Resolutions voted with management: 81.11% Resolutions voted against management: 16.71%	**Housing Development Finance Corporation Limited** – LGIM voted against a resolution to approve the Company's Financial Statements and Statutory reports as part of LGIM's commitment to driving climate effort. LGIM deemed that the Company did not meet the minimum standards with regards to climate risk management and disclosures within the statements and reports. LGIM consider this vote to be significant as it is applied under the LGIM 'Climate Impact Pledge'.	LGIM's Investment Stewardship team are responsible for managing voting activities across all funds.

	Resolutions abstained from: 2.18%

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