

# ESG: how is LGIM helping you?

Five pointers to help you understand what we at LGIM are doing to support your pension governance strategy



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**Recent months have highlighted how regulators, scheme managers and employees alike are increasingly alive to the need to incorporate ESG considerations into pension governance.**

In 2018, the Department of Work and Pensions (DWP) flagged the importance of environmental, social and governance (ESG) issues in a consultation on strengthening pension funds' investment duties. Stewardship obligations, which include voting on and engaging with investee companies, including consulting indirectly via asset managers or with fellow shareholders on ESG issues, must now be incorporated in a policy by all trust-based schemes. As a matter of good practice in due diligence, the Financial Conduct Authority (FCA) will expect providers of contract-based schemes to follow suit, as a baseline to develop an understanding of how their asset manager approaches these issues.

For our part, we are improving our corporate governance and active ownership policies to stay in lockstep with increasing member demand for responsible approaches.

The following five pointers cover what Legal & General Investment Management (LGIM) is doing for our clients, to give you an informed starting point to consider your scheme's governance stance.

## 1. EMBEDDING ESG CONSIDERATIONS AND REPORTING ON ENGAGEMENT SUCCESS

There is a lot of confusion in the industry about what 'ESG' considerations are, how to integrate them, and how to show these issues are being considered. ESG factors – from climate change to the quality of management – pose potential risks and opportunities, which can have a material impact on the performance of investments.

There are many different ways to integrate ESG considerations, including through corporate governance and 'responsible investing'. Put simply, responsible investing is about identifying and supporting good management: companies aware of their impact on wider stakeholders are less likely to face political or regulatory pressure. Importantly, unlike other approaches, such as ethical investing, at LGIM we define responsible investing as seeking to deliver desired financial outcomes, rather than being subject to moral or values-based considerations.

In practice, corporate governance and responsible investment means exercising shareholder's voting rights, engaging in dialogue with companies to promote best practice and continuing to monitor companies where it can lead to the safeguarding and enhancement of shareholder value.

Below are some examples of high-level ESG themes and how LGIM engaged and reported on them during 2018:

- **Sustainability** – It is in the interest of all stakeholders that companies build a sustainable business model that is beneficial to society as a whole. We reported the leaders and laggards under our Climate Impact Pledge, a targeted engagement process to support the transition to a low-carbon economy, for the first time
- **Working with clients** – We evolved our reporting for clients in areas such as carbon footprinting and engagement
- **Executive pay** – We strengthened voting policies on pay, especially on pension provisions
- **Diversity** – We launched a fund aimed at promoting gender diversity, run according to a proprietary company scoring process

Other areas we focused on:

- **Audit** – improving the quality of corporate reporting
- **Listening** to stakeholders – responding to the priorities of our clients and other stakeholders
- **Lobbying to support market resilience and long-termism** – as a long-term investor, we push for transparency on corporate efforts to sway policy
- **Board effectiveness and accountability** – engaging on board composition to strengthen corporate governance
- **Shareholder rights** – fighting to protect our clients' rights
- **Mergers and acquisitions** – safeguarding our clients' interests amid corporate deal-making
- **Public policy** – promoting the highest standards of corporate governance worldwide

## 2. VOTING ON COMPANY MANAGEMENT AND PUBLISHING OUR RECORD

The number of votes against management and abstentions on company resolutions at shareholder annual general and/or quarterly or half-yearly meetings is a useful **indicator**<sup>1</sup> of the degree to which asset managers seek to use their influence.

At LGIM, we vote and do not abstain from resolutions to fulfil our objective of being a truly “active owner”. We expect companies to acknowledge and respect the rights of investors through adhering to the highest market standards. This includes providing high-quality disclosures and treating shareholders equally. LGIM supports the ‘one share one vote’ philosophy and does not support the issue of shares with enhanced or impaired voting rights. We publish our voting reports on a quarterly basis and our latest reports, split by global region, are available **here**.<sup>2</sup>

Voting highlights during 2018:

- LGIM voted on 3332 companies in 2018\*
- In the US, we supported more key shareholder resolutions on climate than any of the world's 10 largest asset managers
- In 2018, LGIM voted against the largest number of UK chairs – over 100 – to date on the issue of gender diversity
- At key votes in the US, LGIM's level of opposition to management on executive pay last year was higher than that of any of the world's 10 largest asset managers

\* in main FTSE pooled index funds.

1 <https://5050climate.org/news/2018-key-climate-vote-survey/>

2 [https://documentlibrary.lgim.com/documentlibrary/library\\_55458.html](https://documentlibrary.lgim.com/documentlibrary/library_55458.html)

### 3. IMPROVING GOVERNANCE STANDARDS

Action in these areas can [help to raise](#)<sup>3</sup> overall standards in the market. To this end, we have signed up to a number of [codes and standards](#)<sup>4</sup>:

- **Signatory to the UNPRI:** The UN Principles for Responsible Investment are six voluntary principles regarding the incorporation of ESG factors in investment analysis and decision-making, “active ownership” (the use of the rights and position of ownership to influence the activities or behaviour of investee companies, also defined as “stewardship”), appropriate disclosure, reporting and co-operation between asset owners. LGIM’s 2018 Responsible Investing Transparency Report is available [here](#).<sup>5</sup>
- **The Financial Stability Board Task Force on Climate-related Financial Disclosures (TCFD)** works to develop voluntary, consistent climate-related financial risk disclosures for use by companies in providing information to investors, lenders, insurers, and other stakeholders;<sup>6</sup> LGIM’s report for the group, covering governance, strategy, risk management, metrics and targets can be found [here](#).<sup>7</sup>
- **The Local Government Pension Scheme (LGPS) Advisory Board – Code of Transparency**
- The standards published by the **FICC Markets Standards Board**
- **UK Money Market Code**
- **FX Global Code**

### 4. INVESTMENT SOLUTIONS TO SUPPORT ESG INTEGRATION

We believe asset managers should enable clients to express a conviction on ESG themes via investment solutions.

Our FutureWorld index range ‘tilts’ towards higher-scoring companies and away from lower-scoring companies. According to our analysis, these ESG-tilted indices should provide a similar risk/ return profile to comparative non-tilted indices while performing significantly better against ESG metrics, such as exposure to carbon risk. In 2018, LGIM launched 14 funds with ESG-related objectives as part of the Future World range. We also run a number of segregated funds along client-specific ESG guidelines, available on request.

During 2018:

- We created a list of companies that fail to meet the minimum standards of business practices, in which the FutureWorld funds will refrain from investing, for example, manufacturers of controversial weapons
- LGIM developed more investment solutions to support the low-carbon economy

<sup>3</sup> <http://www.lgim.com/uk/en/capabilities/corporate-governance/influencing-the-debate/>

<sup>4</sup> <http://www.lgim.com/uk/en/about-us/codes-and-standards/>

<sup>5</sup> [www.lgim.com/files/\\_document-library/capabilities/pri-transparency.pdf](http://www.lgim.com/files/_document-library/capabilities/pri-transparency.pdf)

<sup>6</sup> Text sourced and adapted from: <https://www.fsb-tcdf.org/about/>

<sup>7</sup> [http://www.lgim.com/files/\\_document-library/capabilities/lgim\\_tcdf\\_report.pdf](http://www.lgim.com/files/_document-library/capabilities/lgim_tcdf_report.pdf)

## 5. CHAMPIONING MEMBER ENGAGEMENT

We expect DC members to be increasingly engaged with efforts to integrate ESG considerations into their default and self-select options. If they knew their pension was having a positive social impact, 53% of respondents to an LGIM member survey said they would engage more with their pension. 27% of respondents said they would even pay more into it.<sup>8</sup> This demonstrates a clear increased awareness and appetite for ESG integration on the ground. LGIM provides an array of communications to keep members informed; most recently an animated video on our [Corporate Governance initiatives](#)<sup>9</sup> and our [Active Ownership SHORT REPORT](#)<sup>10</sup>.

## ESG INTEGRATION – IN SPIRIT AS WELL AS LETTER

As uniquely long-term investors, pension schemes have an important role to play in encouraging companies to create sustainable value. We recognise the importance of our stewardship of assets on behalf of your members.

We hope that in addition to helping schemes prepare for the new regulatory duties, this guide shows how embracing the spirit of the regulation can have a positive impact on investment portfolios. The new landscape may also bring significant engagement opportunities for members, as public awareness and demand for responsibly managed investments increases.

<sup>8</sup> Source: LGIM survey of 1,000 respondents, made up of contract-based members, mastertrust members and L&G staff members, 2019.

<sup>9</sup> <https://www.youtube.com/watch?v=BN6u9GaQjBc>

<sup>10</sup> <https://www.legalandgeneral.com/investments/learn-about-investing/why-invest-with-us/corporate-governance-2019-short-digital.pdf>

## CONTACT US

If you are interested in finding out how we can help increase the levels of member engagement for your scheme, please get in touch with Simon Chinnery to find out more:

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