NAPF STEWARDSHIP POLICY

Securing the future of pensions

Introduction

Members of the National Association of Pension Funds (NAPF) have a clear interest in promoting the long term success of the companies in which they invest. For this reason we have since its launch in 2010 been a strong supporter of the UK Stewardship Code.

The informed use of votes, while not a legal duty, is a responsibility of owners and an implicit fiduciary duty of pension fund trustees and investment managers to whom they may delegate this function. Effective engagement with companies on issues ranging from strategy and performance to risk and corporate governance can a) protect funds against **reputational risk** and b) play a key role in **controlling investment risk;** helping guard the fund against potential destruction in shareholder value.

Despite the considerable efforts made by many pension funds, perceptions remain that funds are failing in overseeing the activities of their investment managers and other agents to whom most delegate the responsibility for engagement and voting.

In light of recent revisions to the Stewardship Code and increasing political focus on the issue the time is right for pension funds to review their approach to Stewardship, question whether it could be more effective and consider how they should adopt the Stewardship Code requirements.

Actions

The Stewardship Code states that the primary responsibility for stewardship – active monitoring of and engagement with companies - lies with the asset manager. However, there are **three simple actions** which can be expected of pension funds as the owners and providers of capital:

1. Include a section on ‘stewardship’ within the fund’s Statement of Investment Principles.
2. Include stewardship criteria in manager searches
3. Incorporate monitoring of stewardship activities into manager reviews

“Signing up”

“Signing up” to the Code demonstrates that a pension fund believes companies should adhere to the highest standards of governance and that their managers should integrate the Code’s Principles into their investment processes.

A growing number of asset owners have signed up to the Stewardship Code since its introduction and we encourage others to follow suit. A greater weight of pension fund signatories to the Code will further influence behavioural changes that lead to better stewardship by asset managers and companies.

There is good evidence that poor corporate governance practices are detrimental to the interests of long-term investors. Therefore part of the fiduciary duty of trustees is to take appropriate action if there are concerns about corporate governance or other non-financial risks within companies in which they are invested which may cause loss to shareholder value. As such **it is wholly in line with trustees’ legal duties to support active stewardship** of their funds either directly or indirectly via their manager and/or a third party.

To assist funds in ‘signing up’ to the Stewardship Code we have produced an **Implementation Questionnaire** which provides a framework which funds may wish to complete and submit to the FRC as a means of demonstrating their commitment to the Code.

In addition, we have provided a **short guidance document** which sets out the Code’s seven Principles, along with suggestions as to how funds may consider applying them. Funds may wish to utilise this when making their disclosures under the Code.

Regulatory Evolution

- **SRI Pensions Disclosure Regulation** (2000) - required trustees to disclose in their Statement of Investment Principles (SIPs) the extent (if at all) social, environmental or ethical (SEE) considerations are taken into account in investment decisions; and their policy in relation to the exercise of the voting rights.
- **Myners Review** (2001) **-** recommended that funds have a policy for shareholder activism and the subsequent Myners principles set out best practice for institutional shareholders.
- The updated **2008 Myners Principles** indicated that trustees should include a statement of the scheme's policy on responsible ownership within its SIP and adopt or ensure their investment manager adopts the ISC Code on the Responsibilities of Institutional Investors.
- **UK Stewardship Code** (2010) - replaced the ISC Statement of Principles and set out good practice on engagement with investee companies. The FRC made clear the responsibility for monitoring company performance does not rest with fund managers alone (this was clarified further in the 2012 Code revisions).
- **United Nations Principles for Responsible Investment** (UN PRI) - launched in 2006 and has become the benchmark for global best practices in responsible investing. It now has over 1,000 investment institutions, including 262 asset owners, as signatories, with assets under management of approximately US$ 30 trillion.
- **In 2012**, politicians have suggested pension funds should support **"responsible capitalism"** as engaged investors. Pending regulation in the UK and EU supports enhanced shareholder rights and responsibilities to improve oversight of companies.

NAPF PRINCIPLES FOR STEWARDSHIP BEST PRACTICE

PENSION FUND TRUSTEES SHOULD……

1. Act at all times in the best long-term interests of the fund's beneficiaries.

Funds should seek to act as responsible owners and ensure their policy for dealing with conflicts of interest also covers investment matters such as voting.

2. Develop an investment policy which includes an understanding of stewardship objectives and risks.

This policy should encourage the incorporation of material non-financial risks, including corporate governance factors, within investment decisions and the exercising of stewardship responsibilities such as engagement and voting – to be set out within the funds' Statement of Investment Principles (SIP).

3. Set mandates for asset managers which explicitly include Stewardship

Day to day responsibility for stewardship can be delegated, but investment managers' stewardship capabilities and policies should be a factor in manager selection and relevant criteria should be included within RFPs.

Mandates should encourage integration of corporate governance and other material non-financial risks into investment decision-making; align interests through fees and pay structure; ensure adherence to high standards of stewardship and provide for useful and transparent reporting to the fund.

4. Encourage and empower asset managers to engage with investee companies as a means of improving company performance to deliver investment returns

Funds should encourage collaboration between investment managers as a means of more effective engagement and voice. They should be clear about their managers' approach and should expect a report on such collaboration.

5. Review investment performance no more frequently than is necessary, and with reference to long-term absolute performance.

Within the regular manager reviews, funds should ensure that managers are adhering to the funds' stewardship policy. This may include questioning the effectiveness of managers' engagement activity and how they plan to engage with key holdings which have performed poorly over a period of time.

6. Provide information on Stewardship to beneficiaries, in a way which is clear and timely.

Trustees should endeavour to report annually to fund members on their stewardship policy and illustrate how it has been implemented in the past year and how its managers aim to address failings with investee companies in the coming year.