

Preface to questions

In its recent review of trustees' fiduciary duties with regard to responsible investment, the Law Commission made clear that if members of an institutional investment scheme wish the scheme's trustees to take "ethical" (that is, environmental, social, or governance) factors into account when managing the scheme's investments, and if doing so would not risk "significant financial detriment" to the scheme, then the scheme's trustees may do so.

We, the undersigned members of the CPS, are concerned that the Trustee should indeed do this. Specifically, we wish the Trustee to adopt responsible investment practices.

By "responsible investment practices", we mean investment practices that avoid risking significant financial detriment to the scheme, and that also include deliberate and transparent efforts by the investor (in this case, the Trustee on behalf of CPS members) to eliminate any risk that the investor's or investees' actions will result in environmental, social or financial harm, regardless of whether such harm would affect the beneficiaries directly.

There are two broad approaches available to investors acting to minimise the risk of harm resulting from their investees' actions. The first approach is for the investor to suitably exercise its voting rights, where those exist in relation to an investment. The second approach is for the investor to transfer money out of investee sectors or companies of concern, and into less contentious investments. The two approaches are not mutually exclusive: it is perfectly possible, in principle, for an investor to adopt both approaches. Questions 1 and 3, below, for example, relate to the first approach. Question 4 relates to the second approach.

Response: This section is uncontroversial except that the Trustee does not accept that it is necessary for it "to adopt responsible investment practices". It believes that it has always adopted investment practices responsible by the standards of the time. Consistent with this, the Trustee's triennial review of the Statement of Investment Principles, sequentially follow-on work to the 2015 Actuarial Valuation, will be amending the relevant section to reflect current best practice.

However there are, inevitably, differences of view as to what responsible investment practices comprise and how they are best advanced. For example, your definition of responsible investment practices refers to the elimination of "any risk that the investor's or investees' action will result in environmental, social or financial harm...". In the Trustee's view that is an unrealistically high standard.

Question 1

As members, we are concerned that the votes attaching to the investments made on our behalf should be exercised in a manner that promotes responsible investee behaviour and thereby safeguards those investments and our future, consequently maximising the benefits of our pensions to us.

We are also concerned that the votes attaching to the investments made on our behalf should be exercised in a manner that is consistent. That is, we wish to avoid the possibility that any two of the Trustee's fund managers might vote in opposite ways on the same ballot, thereby failing to adequately advance our interests as beneficiaries.

We have searched extensively for a means by which the Trustee may address these concerns.

We are mindful that such a means must be as easy and inexpensive as possible for the Trustee, and as beneficial as possible for members.

The Red Line voting initiative satisfies these requirements better than any other means we have found. It is at the forefront of responsible investment practice.

The Red Lines voting initiative is applicable to investments in companies listed in the London Stock Exchange. We note that as of the latest Annual Report, the CPS apparently held investments in such companies (via fund managers if not directly).

We therefore attach three related documents: a Red Lines Q&A document; the Red Lines themselves; and a document showing the 10 easy steps we wish the Trustee to take in order to adopt the Red Lines. We especially wish to draw the Trustee's attention to Q12 and Q13 on the Q&A document.

We understand that a number of other pension schemes are in the process of adopting the Red Lines. We also understand that Institutional Shareholder Services (ISS), a proxy advisory and voting company used by some (perhaps all) of the CPS's fund managers, is already capable of providing a Red Lines compliant service. In short, the infrastructure for adopting the Red Lines appears to be in place.

In view of these points, and also in view of the conclusions of the Law Commission's review of trustees' fiduciary duties with regard to responsible investment, will the Trustee commit to adopting the Red Lines (i.e. to completing the 10 steps outlined) by the end of 2017?

If not, why not, and what alternative steps will the Trustee take to ensure that the Trustee's voting rights attaching to direct or indirect investments in companies listed in the London Stock Exchange, are exercised in a responsible and consistent manner?

Response: The Trustee will not have been able to consider your request in relation to the Red Line voting initiative before the meeting on 26 February, but it will be considered by the Trustee in due course. As noted above, that consideration will take as its starting point that, so far as reasonably practicable, the Trustee already exercises its voting rights in a responsible and consistent manner, so that the substantive question will be whether the Red Lines initiative is likely materially to improve the position.

Question 2

How much money does the CPS currently have ultimately invested, on behalf of its members, in companies listed on the London Stock Exchange?

Response: As at 31 December 2015 the amount, rounded, was £319 million.

Question 3

In view of the points made in Question 1, and again in view of the conclusions of the Law Commission's review of trustees' fiduciary duties with regard to responsible investment, which steps (if any) does the Trustee take, or intend to take, to ensure that the Trustee's voting rights, attaching to direct or indirect investments *other* than in companies listed in the London Stock Exchange, are exercised in a responsible and consistent manner? If the Trustee neither takes such steps already, nor plans to take such steps in future, what is the Trustee's justification for its inaction in this regard?

Response: Given the Trustee's belief that it already exercises voting rights in a responsible and consistent manner it is not clear what else it should do.

Question 4

At the previous members' meeting, CPS member Sam Kuper supplied the Trustee with data showing that at least £236m of the money entrusted to the Trustee was, as of the then-latest annual report, invested in pooled funds that were both:

- not classed as "ethical" funds by Trustnet, and
- being outperformed, even when fees and charges were taken into account, by pooled funds that were classed as "ethical" funds by Trustnet, and that had comparable risk profiles to the CPS's existing pooled fund investments.

The pooled funds classed as "ethical" funds by Trustnet primarily work by using "ethical exclusions", i.e. they screen out investees not meeting certain ethical criteria.

In response to Sam Kuper's submission, the CPS's investment advisor, Aon Hewitt, provided advice to the CPS acknowledging that there is no clear evidence that ethical exclusions can consistently detract from performance.

In view of Aon Hewitt's acknowledgement, and of the data showing the good performance of various "ethical" funds relative to the CPS's existing comparable investments, it appears that for the CPS to invest in such funds would not in itself risk "significant financial detriment" to the CPS, and would therefore be allowable under the guidance of the Law Commission mentioned in the prefatory note above.

That being so, if it has not already done so, then by when will the Trustee move some or all of the CPS money currently invested in relatively poorly-performing non-"ethical" pooled funds, into better-performing pooled funds with comparable or better risk profiles, that are classed as ethical funds by Trustnet? This action would be doubly in beneficiaries' interests: it would likely realise an equivalent or better pension, and a better world to use it in. If the Trustee does not intend to perform any such move, then what are the Trustee's justifications for this?

Response: There are two seemingly small, but in fact fundamental, errors in this question. First, CPS provides defined benefits and so investment performance is irrelevant to the level of pension paid: in effect the University underwrites the investment performance. Second, the job of the CPS Trustee is not to try to achieve "a better world", but to ensure that the promised level of benefits is delivered. That necessarily requires decisions about how to

invest the scheme's funds; responsible investment is "in the mix" of those decisions; if those decisions lead to a better world that is a happy by-product.

As to the substance of your question, it starts from the questionable premise that to adopt an investment policy of substituting "Trustnet ethical" for weak performers from time to time in the CPS portfolio is in and of itself appropriate whereas, as already noted, such a proposition can or certainly should only be part of a broader "in the mix" discussion. Add to this the practicalities - an initial substantial re-organisation of the portfolio coupled with a greater level of monitoring, with consequent increase in investment costs – and, , it is not obvious that this is sensible, given the Trustee's starting point that it already has responsible investment practices.

Furthermore, there is a fundamental flaw in your proposition that the CPS money currently invested in relatively poorly- performing non-ethical funds should be moved into better-performing ethical pooled funds. It is not at all clear that ethical funds would outperform the present CPS funds.

Question 5

Will the Trustee adopt a policy, in its Statement of Investment Principles, to the effect that if ever it is faced with a choice of two or more investments possessing effectively identical financial properties, it will always choose the investment that best satisfies the description of responsible investment given in the prefatory note?
If not, why not?

Response: Yes

Question 6

Can the Trustee, or the University's Head of Pensions Administration, confirm that members' meetings for the CPS will be held at least once per calendar year, for as long as the CPS (or its successor(s), if it is replaced) exists? If not, why not?

Response: The Trustee intends to maintain its practice of an annual meeting for CPS members.

Question 7

Can the Trustee, or the University's Head of Pensions Administration, confirm that members' meetings for the CPS will be open to deferred members (aka preserved members) and pensioners, as well as active members, for as long as the CPS (or its successor(s), if it is replaced) exists? If not, why not?

Response: The annual meeting will be open to actives, deferreds and pensioners: depending upon how this widened group of invitees works out in practice over the next couple of years – historically the meeting has involved only actives – it may prove necessary to introduce an overall limit on the number attending.

Question 8

The Principles for Responsible Investment (PRI or UNPRI) are six principles developed by an international group of institutional investors, convened by the United Nations Secretary-General, reflecting the increasing relevance of environmental, social and corporate governance issues to investment practices. The six principles, and further information about them, are to be found at <http://www.unpri.org/about-pri/the-six-principles/>. They are as follows:

- 1: We will incorporate ESG issues into investment analysis and decision-making processes.
- 2: We will be active owners and incorporate ESG issues into our ownership policies and practices.
- 3: We will seek appropriate disclosure on ESG issues by the entities in which we invest.
- 4: We will promote acceptance and implementation of the Principles within the investment industry.
- 5: We will work together to enhance our effectiveness in implementing the Principles.
- 6: We will each report on our activities and progress towards implementing the Principles.

We have been in contact with the PRI Association, which is responsible for supporting institutional investors wishing to adopt the PRI. Our understanding from them is that a number of institutional investors in the UK, of similar size to the CPS, have become signatories to all the above principles, and that this has helped those institutional investors to become more responsible investors, thereby helping to safeguard both their own legal beneficiaries and also our collective well-being as fellow citizens.

In view of this, and in order to address members' stated concerns that the CPS should adopt more responsible investment practices, will the CPS Trustee move to become a signatory to these laudable principles before the end of 2017? If not, why not?

Response: The Trustee will consider membership of PRI at the same time as it considers the Red Lines initiative, applying the same criteria.

Question 9

CDP is an international, not-for-profit organization providing the only global system for companies to measure, disclose, manage and share vital environmental information. For investors, it offers two tiers of membership: "Investor Signatory", and "Investor Member". The first tier is free of charge.

Membership of either tier would help the Trustee to better integrate environmental considerations into its investment process, by providing environmental data about listed companies in a standardised form that would not otherwise be available to the Trustee. An overview is given in the attached brochure.

Currently, there are 800+ investors who have membership in the scheme. Those investors, who are competing with the CPS in the market, currently have an advantage over the CPS due to their access to this information, which is not currently visible to the CPS. Membership of either tier would enhance the CPS's competitiveness by levelling the playing field in that regard.

Membership of either tier would also simplify the Trustee's PRI implementation, if the Trustee becomes a signatory to the PRI.

Finally, membership of either tier entitles the investor to free of charge membership of Carbon Action, a collective initiative in which 300+ investors with US\$22 trillion+ in assets under management ask 1300+ of the world's highest emitting companies to do the following:

- Make emissions reductions (year-on-year);
- Publicly disclose targets;
- Make ROI-positive investments in relevant projects.

As becoming an Investor Signatory of the CDP would incur no charge or commitment for the CPS Trustee, would assist it in adopting responsible investment practices, and would provide useful market insight with the potential to translate into better returns, will the Trustee commit to becoming an Investor Signatory by the end of 2017?
If not, why not?

Response: The Trustee will consider membership of CDP at the same time as it considers the Red Lines initiative, applying the same criteria.