Smart Pension

Smart Pension Master Trust Responsible Investment Policy

June 2022

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We believe that to provide the best outcomes for our members we need to take into consideration the long term impact of their investments and the policies of the individual companies and countries to ensure sustainable outcomes, equality and fairness.

Our Responsible Investment Policy is embedded in our investment strategy and informs all the investment funds we provide for members, both within the default funds and the self-select investments. The policy is written and executed by the Trustee's Investment Sub-Committee which constantly monitors the application of the principles and investment guidelines. The policy is summarised and referred to in the Trustee's Statement of Investment Principles.

Guiding Principles

There are many ways to invest responsibly. In all our investments we take into account Environmental (E), Social (S) and Governance (G) considerations when investing members retirement savings.

- Environmental factors look at the conservation of the natural world, such as the levels of pollution and recycling.
- Social factors examine how a company treats people covering a range of issues including gender, diversity and labour standards.
- Governance factors consider how well a company is run from the executive pay and anti-corruption to the diversity of its board members.

We also look to invest sustainably and have a positive impact on people and the planet and investments in solutions for social and environmental issues.

The risks

We look to ensure effective and integrated management of ESG and climate risks, to support the Trustee's desire to protect and enhance value of its member assets over the long term. Governments around the world, particularly in Europe, are committed to try to limit global warming and bring in new environmental policies. Companies which do not reduce their pollution face greater penalties and costs and will be worth less. When these factors are taken into account and the risks are mitigated, we can also prevent negative outcomes for people and the planet.

The Trustee also looks to receive feedback from members (such as webinars and surveys) to understand any specific ESG and climate issues that they want to see reflected in the investment strategy.

The opportunities

We look to invest sustainably and have a positive impact on people and the planet. While the term 'sustainable investing' can often be used interchangeably with 'responsible investing', we define this as going beyond mitigating ESG risks. In particular we look at preventing negative outcomes by avoiding the worst offenders (i.e. being responsible), and investing in companies who are trying to generate positive outcomes for people and the planet, which will help "sustain" long-term financial performance.

We believe that a sustainable company is one which is actively trying to reduce their carbon emissions and use climate-aware responsible business practices. In addition, we believe investments in solutions for social and environmental issues are powerful, such as investing in wind farm projects, we call this 'impact investing'. We aim to identify sustainable companies and capture investment opportunities offering solutions to environmental and social challenges provided they are aligned with the investment objectives and strategy of our fund offerings. When assessing opportunities for new investments, we pay particular attention to the United Nations' Sustainable Development Goals. We do this by categorising opportunities through the Principles for Responsible Investment's Impact Investing Market Map which aims to bring more clarity to the process of identifying mainstream impact investing companies and thematic investments so that asset owners and fund managers can better assess opportunities in this market.

Investment Beliefs

We want to contribute to a better world whilst generating good investment returns for our members. Pension investments are for the long term. For younger members it will be decades before the benefits of the contributions they make today are enjoyed. How we invest now will shape how the world looks for many years. It impacts not just our own future but that of future generations.

The Trustee believes that investing responsibly and sustainably will not only improve societal and environmental outcomes but will also lead to improved returns for members' pension savings. The Trustee's responsible investment beliefs are summarised below:

- ESG and climate risks pose a real and material threat to members' retirement outcomes. Generating an appropriate and sustainable financial return for members while also addressing global challenges helps to mitigate these risks.
- Responsible investment factors influence long-term performance which presents opportunities and risks. Each stage of the investment decision making process needs to consider ESG and climate risks (investment strategy, investment selection, reporting etc).
- Being active owners of investments over the long term is critical for responsible stewardship of assets.

- Responsible investment is a discipline that is continuously evolving. Being open to new approaches and standards is critical to maximising what can be achieved. Remaining informed of appropriate investable innovations that address challenges (such as climate change) supports delivery of tangible impact.
- There are financial reasons for making impact investments part of the default arrangement, as they can contribute positively to returns and asset diversification, reducing risk, and future proof the strategy for long-term capital growth. Any impact investments adopted in the default arrangement should aim to have a positive impact for people or the planet, in addition to financial benefits.
- Impact investments which help the agenda of the UN's Sustainable Development Goals (SDGs), looking to contribute to solutions to world challenges, will be considered for investment. Recognising that not all the SDGs will be applicable to all companies, the Trustee will look to invest in investment vehicles which aim to have an impact across a broad range of SDGs, at a portfolio level.
- Illiquid investments (which may yield a direct positive social and environmental impact) may provide investment opportunities. There is an opportunity to enhance return through capture of the illiquidity premium while yielding measurable impact solutions that address global challenges.

We aim to mitigate the risks from ESG factors including climate change and unsustainable business practices, while addressing opportunities to contribute to help people and our climate crisis. This is an important matter to the Trustee and requires detailed considerations in our investment processes. Our investment policies are aligned with the 'best efforts' target of the Paris Agreement and recommendations by the Intergovernmental Panel on Climate Change (IPCC), to limit global warming to 1.5°C above pre-industrial levels. To achieve this we aim to reach net zero carbon emissions in our default by 2040, halving emissions before 2025 from our baseline year of 2019. We provide further details on our approach to climate-related risks and opportunities in our Climate Policy, here.

Smart Pension's Responsible Investment Policy is based on the broader investment principles set out in the Trustee's Statement of Investment Principles which can be found here. This policy covers all the investments we make on behalf of our members, across different asset classes, and determines our overarching approach to the selection of external asset managers and individual funds.

Investment Strategy

Smart Pension's investment process is built upon the integration of responsible investment factors into the investment strategy and the selection of appropriate investment funds which incorporate ESG factors. In addition, the investment strategy is structured to help meet the net zero goals, outlined above.

The Trustee's Investment Sub-Committee of the Smart Pension Master Trust sets the investment strategy for the funds and the selection of external managers and funds. The execution of the investment strategy and the profiles of the funds are regularly reviewed to ensure it is in line with the stated principles and the strategy continually evolves to improve the sustainability outcomes, including the net zero goals outlined above.

Asset Allocation

We have framed portfolio decisions in two approaches; 'reduce negative impact' and 'increase positive impact'. In particular, we can reduce negative impact by removing the worst offending companies, and increase positive impact by investing in climate solutions, for example. We also look to steward our assets which are 'in-between', i.e. they are on their way to creating a positive impact in areas such as climate change and social projects. We detail our approach to stewardship and engagement in the next section.

In terms of removing the worst offending companies, the Trustee seeks to minimise financially material risks to protect long-term returns by excluding companies that:

- are involved in the manufacturing of controversial weapons (chemical weapons, biological weapons, nuclear weapons, anti-personnel mines and cluster munitions) as defined by the United Nations;
- derive the majority of their revenues from coal mining. Not only does coal put out the most carbon dioxide per unit of energy vs other fossil fuels, it also has dangerous working conditions, it causes mercury pollution, acid rain and can pollute nearby water with sediments and chemicals. Therefore we do not see the stewardship benefits, as seen in other fossil fuel companies;
- violate the United Nations Global Compact standards on human rights, labour, the environment and corruption.

Some companies operate in industries which have inherently negative environmental or social outcomes and so the funds have selective exclusions on top of these. However, the funds we invest in focus on engagement as a first priority, in order to have the greatest long term impact.

Engagement and Active Ownership

Our Responsible Investment policy is built on the principle that engagement and encouraging behavioural change will lead to better long term sustainability outcomes than simply exclusion. Numerous automatic exclusions may lead organisations to move outside public asset markets where their actions are less easily monitored and assessed and to continue to pursue damaging environmental, social and governance policies. Therefore, only companies which consistently refuse to engage or consider change in behaviour will be subject to exclusion.

Smart Pension does not manage investment funds directly and so our members' voting rights are exercised through our external asset managers. We require all managers to have an active and transparent engagement policy and for their activities to be in line with our Responsible Investment principles. We regularly review their engagement history to track performance.

Investment managers

Our members' contributions are invested by external asset managers. When we select a new fund for the default investment funds or self-select options, we analyse each fund to ensure their practices align with the following:

- Fund manager’s responsible investment policies are integrated into their investment process including the management of ESG and climate risk and identification of opportunities (in particular for active managers);
- Ensuring that fund managers are, or are working towards becoming, signatories of the UN Principles for Responsible Investment and the UK Stewardship Code;
- Using investment managers with net zero ambitions that are aligned, or will be aligned, with the net zero ambitions of the Scheme; and
- Certifying that fund managers’ engagement strategies are aligned as far as is possible with the stewardship and engagement priorities for the Scheme, including the Red Line Voting Initiative. This means engaging with companies to reduce the negative environmental and social impact of their activities and enhance the positive.

We require external asset managers to be active stewards of our investments which means voting on all company resolutions in the best interests of our members and driving sustainable best practice.

In light of the above, we continuously monitor our external managers by:

- Regularly reviewing existing managers climate and ESG policies and actions to ensure these are in line with our responsible investment principles, including via an annual meeting with the Investment Sub-Committee;
- Requesting reports on their sustainable investment, including impact, activities, to disclose available metrics so we can assess the outcomes of our investments, and to explain how their own policies are evolving;
- Reviewing their engagement and voting activity where appropriate to ensure they are acting as responsible stewards of our members’ pension savings; and
- As we move towards monitoring and reporting the climate performance of our funds, we will ensure that external managers measure and disclose the carbon footprint of their funds, using consistent methodology.

Market engagement and reporting

We actively engage in policies and market initiatives, to promote and advance the assessment, data and consistency of net zero targets. For each engagement opportunity, we consider whether it is an important issue relating to our investment strategy, Trustee policies and Net Zero Plan, and how likely we are to have an influence in the matter. We have joined the Institutional Investors Group on Climate Change, the Impact Investing Institute and the Occupational Pensions Stewardship Council. We are also signatories to the UN PRI and are working towards becoming a signatory of the UK Stewardship Code.

We aim to be as transparent as possible with all our investments so that members have a complete understanding of how their pensions are performing, both in the investment returns and the environmental impact of the portfolios. Our Statement of how we implemented our policies and practices during the scheme year ending is here.

The Trustee supports the recommendations from the Taskforce for Climate-related Financial Disclosures (TCFD) and in future will report annually the climate profile of the default funds and the carbon footprint of members’ investments. As noted above, the Smart Pension Master Trust has committed to a target of halving carbon emissions by 2025 and reaching net zero carbon emissions by 2040.

As a signatory of the UN Principles for Responsible Investment, and targeted signatory of the UK Stewardship Code, the Trustee will report annually on responsible investment and stewardship activities. These reports will summarise and monitor our activities.

Glossary

UN Sustainable Development Goals (or Global Goals)
Set up in 2015 by the United Nations General Assembly they are a collection of 17 interlinked global goals designed to be a "blueprint to achieve a better and more sustainable future for all". Examples of the goals are to achieve gender equality, ensuring availability of water and sanitation for all, and protecting biodiversity.

Principles for Responsible Investment (PRI)
A United Nations-supported international network of investors working together to use responsible investment to enhance returns and better manage risks.

PRI Impact Market Map
The PRI designed a market map from the United Nations' Sustainable Development Goals and their own reporting framework to categorise mainstream impact investments into themes, of which the PRI identified 10. The themes include; energy efficiency, green buildings, renewable energy, sustainable agriculture, sustainable forestry, water, affordable housing, education, health and inclusive finance.

Climate solutions
Investments which look to help the conservation, restoration and improved land, water and waste management actions that increase carbon storage or avoid greenhouse gas emissions.

Net Zero
The balance between the amount of greenhouse gases produced and the amount removed from the atmosphere. We reach net zero when the amount we add is no more than the amount taken away. It will help limit global warming.

Greenhouse gases
There are four greenhouse gases linked to global warming: carbon dioxide (the majority), methane, nitrous oxide and fluorinated gases. "Carbon dioxide equivalent" or "CO2e" is a term for describing different greenhouse gases in a common unit. For any quantity and type of greenhouse gas, CO2e signifies the amount of CO2 which would have the equivalent global warming impact.

Paris Agreement
A legally binding international treaty on climate change to limit global warming to well below 2, preferably to 1.5 degrees Celsius, compared to pre-industrial levels. Countries communicate actions they will take to reduce their Greenhouse Gas emissions and they will take to build resilience to adapt to the impacts of rising temperatures.

Intergovernmental Panel on Climate Change (IPCC)
The United Nations body for assessing the science of climate change and to report on its

implications and potential future risks, as well as to put forward adaptation and mitigation options.

Institutional Investors Group on Climate Change (IIGCC)

The European membership body for institutional investor collaboration on climate change. Its work supports and helps to define the public policies, investment practices and corporate behaviours that address the long-term risks and opportunities associated with climate change.

Impact Investing Institute
Launched in 2019 with a simple mission: to accelerate the growth and improve the effectiveness of the impact investing market in the UK and internationally – as set out in the United Nations' Sustainable Development Goals.

Occupational Pensions Stewardship Council
The council provides schemes with a forum for sharing experience, best practice and research, and providing practical support on stewardship activities such as shareholder resolutions, climate change, corporate governance and other topics.

UK Stewardship Code
High stewardship standards for those investing money with the aim for responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.

Task Force on Climate-related Financial Disclosures (TCFD)
A Task Force which has developed consistent climate-related financial risk disclosures for use by companies, banks, and investors in providing information.

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