LOTHIAN
PENSION FUND

Covering the period 1 April 2023 to 31 March 2024

THE STEWARDSHIP REPORT

LOTHIAN PENSION FUND

CONTENTS

A MESSAGE FROM OUR CEO

As a responsible investor, Lothian Pension Fund (LPF) has a long-established commitment to stewardship. This is our fourth report prepared in accordance with the standards of the Stewardship Code 2020. As a leader in responsible investment amongst Local Government Pension Scheme (LGPS) funds, we prepare and submit this report to demonstrate the nature of our commitment to stewardship, for the benefit of our stakeholders.

In the context of a complex and unpredictable world, we think hard about our approach to stewardship and regularly reassess how we should exert our influence as assets owners in an appropriate and consistent manner. First and foremost, we own assets to fund our members' income in retirement, an important social responsibility in its own right, but with ownership comes the opportunity to encourage positive corporate behaviour for the benefit of society. We see this as an additional responsibility, which we address through our voting and engagement activities that are explained in the following pages. This report confirms our adherence to the standards of the UK Stewardship Code. Our commitment is to amplify our influence as a £10.2bn pension fund in an industry measured in the trillions, by working with other asset owners to drive the long-term value of our investment portfolio and contribute to the long-term health of the financial system.

David Vallery
CEO, Lothian Pension Fund

A MESSAGE FROM OUR PENSIONS COMMITTEE

The role of the Pensions Committee is to ensure that the pension fund is run in a sound and sustainable manner that guarantees we deliver on our pensions promise to our beneficiaries. We do this by investing prudently and carefully. We also do this by striving to ensure that the companies and assets we invest in are well governed and well managed, that they minimise their negative impacts on society and the environment, and that they make a positive contribution to our societies and our communities.

We use our rights as an investor to challenge companies when they fall short of the standards that we expect, and we stand with them and support them when they're developing and implementing strategies that enhance their long- term sustainability and resilience.

Our work to support good governance and engagement is underpinned by our belief in the power of our voice, often alongside others, to lead to positive change that sustains and drives value for our stakeholders today and in the future.

The Pensions Committee has a critical role to play. We want Lothian Pension Fund (LPF) to take meaningful action on a range of issues, notably corporate governance and climate change. We've encouraged the fund to continue to develop its approach to climate change, incorporating climate scenario analysis to stress test the results of our 2023 valuation, while focusing engagement on real-world decarbonisation policies to limit global warming.

The Pensions Committee welcome this report as a record of LPF's past efforts, outcomes and future areas of focus for further improvement in our approach to responsible investment, within the wider financial system on which our current and future stakeholders rely. We continue to encourage, support and commend LPF's work in this critically important area for our members and employers, for a resilient financial system, and for a better world.

STEWARDSHIP IN PRACTICE: CREATING LONG-TERM INVESTMENT VALUE

Our Purpose, Vision and Duty

Our Purpose is to administer the LGPS in Edinburgh and the Lothians. By paying pensions and benefits to members, we contribute to the financial well-being of members and their families in retirement.

Our Vision is to deliver outstanding pension and investment services for the benefit of members and employers.

LPF is the second largest LGPS in Scotland. It's a funded, defined benefit, statutory occupational pension scheme.

LPF's stakeholders are the people and entities with an interest in the assets and activities of LPF. They include the members of the pension scheme (existing and future), their dependants and beneficiaries, as well as the participating employers who contribute to the assets of the fund and our governing bodies. We have a fiduciary duty to act in a financially prudent manner and to act in the best interests of the scheme employers and the scheme members.

It's this duty that defines our approach to stewardship. We need to manage our investments responsibly and sustainably so that we can pay pensions and benefits because they'll fall due over many decades to come.

We need to ensure that the risks to our investments are effectively managed and we know that Environmental, Social and Governance (ESG) factors are fundamental considerations in driving the long-term value of our investment portfolio. They matter to society, so they matter to us.

Stewardship as an investment function

So, what does this mean in practice? At its heart, it means that we see stewardship primarily as an investment function. Our core responsibility is to invest in a way that takes full account of the downside risks and the upside opportunities presented by ESG factors. We need to be properly compensated for risks, avoid over-paying for opportunities, and we need to manage and mitigate these risks in our investment portfolio.

This emphasis on the investment implications of ESG issues is reflected in our approach to stewardship. We're unusual among UK asset owners in that responsibility for stewardship sits with our investment teams. It's our portfolio managers and investment analysts who are responsible for engaging with companies and with investment managers. It's our portfolio managers who lead our work with collaborative initiatives, such as with Climate Action 100+.

Stewardship as a collaborative activity

As an asset owner acting alone, our potential for direct influence is relatively modest. While direct company engagement is important and can be influential in situations where we have a significant holding, our biggest impact comes through working with others.

STEWARDSHIP IN PRACTICE: CREATING LONG-TERM INVESTMENT VALUE

Our approach to stewardship therefore includes:

- Collaboration with our industry peers
- Engagement with our investment managers. We challenge our managers on their approach to responsible investment and ESG
- Supporting collaborative engagement and escalations through Federated Hermes EOS (EOS), which derives considerable influence from representing owners of assets worth approximately $1.4tn.

STEWARDSHIP IN PRACTICE: LOOKING FORWARD

Our aim, in all our stewardship efforts, is to ensure that the companies we invest in are sustainable and successful over the long-term and create enduring value for us as investors. We have a long track record of voting and engaging on what are often referred to as the traditional corporate governance issues, such as executive remuneration and board independence. These issues remain of central importance. Governance failures can lead to major financial losses for investors, to avoidable job losses or harm to employees or to unpaid suppliers and creditors.

However, the world is changing profoundly. Environmental and social issues have risen up the agenda that shapes our present and our future: the climate emergency; human rights; geopolitical instability; nature degradation; equality, diversity and inclusion; and economic volatility, for example. These issues and the global response to them will affect our ability to deliver retirement savings for our existing and future members. As asset owners with a long-term horizon, we take these global issues seriously, we exercise our ability to vote and engage and we encourage others to do the same. We believe the most effective stewardship approach to climate change is to: 'Engage Your Equity, Deny Your Debt'.

Engage your equity, deny your debt

As an organisation, we've outlined our ambition to avoid providing any new financing to companies which aren't aligned with the goals of the Paris Agreement on Climate Change, (which aims to keep the global temperature rise this century well below 2◦C above pre-industrial levels and to pursue efforts to limit the temperature increase to 1.5◦C). While the trading of equities (shares) may not in itself affect the capital position of a company, subscribing to new bonds and new equity does provide companies with funding. Within our equity portfolio we engage with our holdings, and that engagement includes using the tools and strategies we have at our disposal to influence companies to commit to align with the goals of the Paris Agreement. In our debt portfolios, we aim to deny funding to those non-aligned companies.

STEWARDSHIP IN PRACTICE: OUR PRIORITIES FOR 2024 AND 2025

Our main stewardship priority is to continue strengthening our stewardship approach on environmental and social issues, in particular climate change, while maintaining our focus on ensuring that companies are well governed and well managed. With the Taskforce for Nature-related Financial Disclosures having published its recommendations in September 2023, we'll also be looking for companies and investors to improve their understanding of the importance of addressing nature degradation/biodiversity loss alongside climate change. In June 2024, we created two new dedicated responsible investment roles within our investment team, illustrating our organisational commitment to appropriate resourcing and further development of our approach to responsible investment.

This is our fourth stewardship report, and it's set out to report against each of the 12 principles of the Financial Reporting Council's (FRC) Stewardship Code 2020 in the following sections. We were pleased to be early adopters to the updated Code in 2021 as it provides a context for and a description of our activities with a focus on outcomes. We'll continue to report on our stewardship efforts, and we invite and welcome feedback on our approach.

PRINCIPLE 1: PURPOSE, STRATEGY AND CULTURE

Signatories' purpose, investment beliefs, strategy, and culture enable stewardship that creates long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.

OUR PURPOSE

Our purpose is to administer the LGPS in Edinburgh and the Lothians. By paying pensions and benefits to members, we contribute to the financial well-being of members and their families in retirement. For that reason, our primary objective is to ensure that there are sufficient funds available to meet all pension and lump sum liabilities as they fall due for payment. This means we need to generate the necessary long term cash flow returns to pay promised pensions and to make the scheme affordable to participating employers, now and in the future, while minimising the risk of having to increase contribution rates in the future.

In this report, we set out our assessment of how our purpose, strategy and culture meet the needs of our stakeholders.

Our investment beliefs

With liabilities extending decades into the future, it's in our interests to take our responsibilities as institutional asset owners seriously. To this end, our approach to responsible investment centres on effective stewardship of all assets, with a particular focus on good corporate governance to deliver sustainable value.

As required by LGPS legislation, we maintain a Statement of Investment Principles (SIP) which articulates the investment principles which guide our strategies and decision-making. In terms of those principles, which enable stewardship and lead to sustainable benefits for the economy, the environment and society, we believe:

- Responsible investment supports our purpose and that through robust stewardship and an effective approach to ESG issues, we should reduce the risk associated with the invested assets that LPF owns to pay pensions when they become due
- As a provider of responsible capital, LPF should be an agent for positive change, engaging with companies to help them maintain or adopt best business practices and sustainable business models
- In being transparent about the methods we use to foster responsible investment as an organisation and being accountable for our responsible investment strategy and approach
- Successful engagement adds value to our investment process and that divestment has no effect on company finances in the long term and can produce perverse incentives in the short term
- As responsible owners we should engage with our investee companies and appointed managers, either directly or via collaborative partners. However, we also believe that this engagement must lead to action and where we feel progress is too slow, and the prospect of financial risk to us increases as a result, we're willing to withdraw our support and end our investment.

PRINCIPLE 1: PURPOSE, STRATEGY AND CULTURE

Finally, we believe that Climate Change is one of the defining issues of our time. We believe that asset owners are uniquely positioned to engage with global policy makers and industry regulators as well as with investee companies, to bring about an acceleration in the sustainable energy transition and a decarbonisation of the global economy.

We reiterated this by working with the Institutional Investors Group on Climate Change to engage with the Bank of England in its role as the Prudential Regulatory Authority (PRA), encouraging the PRA to ensure that capital adequacy is properly assessed across the banking system to provide confidence that there's system-wide resilience to realistic negative climate scenarios.

> "By engaging with the Bank of England in its role as the Prudential Regulatory Authority, we're promoting more effective climate risk management and system-wide resilience in the face of climate change. This collaborative engagement activity is aligned with our focus on real world decarbonisation as long-term investors."
>
> **David Vallery**, Chief Executive Officer

OUR STRATEGY

We have a clear strategic goal to earn an appropriate risk adjusted investment return as responsible investors. More details about our investment approach are provided in Principle 6.

Introducing our Statement of Responsible Investment Principles

To reflect our belief in the importance of responsible investment, we published a Statement of Responsible Investment Principles (SRIP). This describes our sustainable investing beliefs and commitments, and our strategy for integrating those with our investment activities.

Responsible investment remains a core part of the Statement of Investment Principles (SIP), which is required under LGPS legislation. However, in view of the growth in our responsible investment and stewardship activities across all asset classes, we released the first version of LPF's SRIP in June 2020 to inform members and employers more fully. This document is reviewed annually and updated to reflect how we evolve our responsible investment practices.

The SRIP explains how we incorporate ESG issues into investment analysis and decision-making processes, as well as how we seek appropriate disclosure on ESG issues from any entities in which we invest. It also publicly confirms our approach to climate change and the carbon transition.

The SRIP allows us to communicate with our stakeholders to explain our strategy in detail. It sets out how we implement responsible investment on an asset class by asset class basis, as well as detailing how we utilise all the tools at our disposal to achieve our stewardship aims.

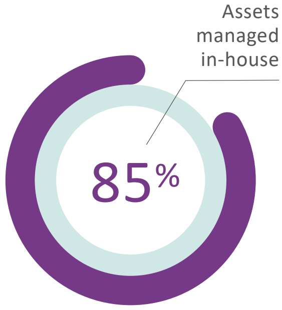
Our SRIP supports conversations with external managers and other institutional investors on evolving best practice in responsible investment as well as on implementation challenges and approaches to systemic issues. From oversight and monitoring, to affirming our position on climate change and the carbon transition, we'll provide examples of how we implement the SRIP throughout this report.

PRINCIPLE 1: PURPOSE, STRATEGY AND CULTURE

OUR CULTURE

Operating within the public sector means that we're subject to applicable public sector regulations and relevant public law duties. These require LPF to act fairly and transparently and brings us in-scope of the Freedom of Information regime. This promotes a strong degree of discipline and accountability across the organisation. We're always mindful of fulfilling our duties to stakeholders and serving their expectations regarding sustainable benefits for the economy, the environment and society.

We manage over 85% of assets in-house, through internal equity, bonds and certain real asset portfolios. This aligns our investment decision-makers with the fund's best interests.

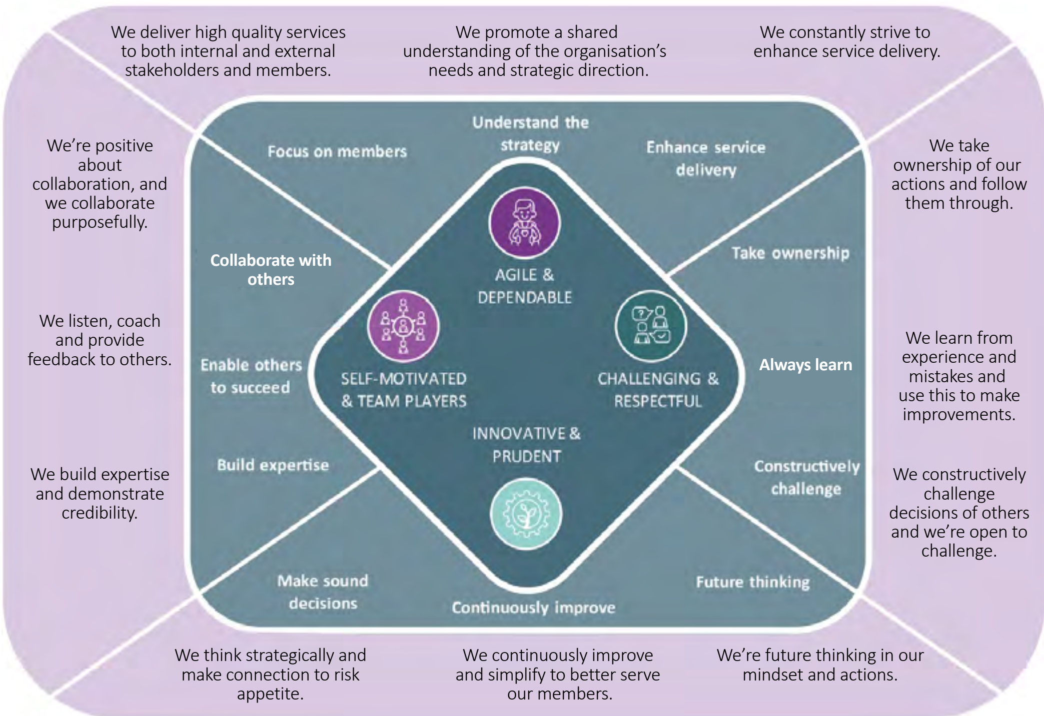


As explained in relation to Principle 2 (Governance), operating an FCA-authorised company within the group influences the culture throughout LPF. It allows LPF to build on the in-house investment expertise and promotes accountability and responsibility amongst individuals.

In September 2023, we were proud to be named "LGPS Fund of the Year (assets over £2.5bn)" at the LAPF Investment Awards. During that same year, we also retained the Pensions Administration Standards Association accreditation, along with the Customer Service Excellence Award which we've held for the last 15 years. Whilst these accreditations aren't directly relevant to stewardship, they reflect LPF's stakeholder orientated culture.

VALUES THAT SUPPORT OUR PURPOSE

We're passionate about enabling desirable and sustainable pensions, and our values are the enduring principles that inform, inspire and instruct the day-to-day behaviour of individuals working for LPF.



PRINCIPLE 1: PURPOSE, STRATEGY AND CULTURE

These values drive our active stance to stewardship and responsible investment and inform our approach to ESG. For example, our belief in the power of company engagement and the way in which we engage with companies and stakeholders, is relevant to our values of being 'Self Motivated and Team Players' and being 'Challenging and Respectful'.

Our value of being 'Innovative and Prudent' means that we focus on future thinking, which is critical in managing ESG risks today for positive outcomes for current and future beneficiaries.

INCLUSIVITY

We're one team, but we represent many ideas, experiences and backgrounds. We value everyone's contributions and believe that our colleagues should be their whole self at work. We want a diverse, inclusive and respectful workplace.

In 2019, we signed up to Disability Confident and more importantly, committed to review and improve everything we do with respect to recruitment and employment. Through Disability Confident, we work to ensure that disabled people and those with long term health conditions can fulfil their potential and realise their aspirations with us as an employer.

We continue our work with the Scotland chapter of the Diversity Project and the Asset Owner Diversity Charter (See Case Study on page 13-14), which aims to accelerate progress toward a more inclusive culture in the investment and savings sectors across all demographics, including gender, ethnicity, sexual orientation, age and disability.

We continue to work towards our goal of being fully gender balanced across the organisation by 2030:

- As of 31 March 2024, we have, in aggregate, 53% women in our top three leadership layers and across the whole company, 58% of our workforce are women
- Our mean gender pay gap is 21.9%
- Our positive action approach to gender, which is benchmarked externally, is helping to ensure that our people policies and processes are inclusive and accessible, from how we attract and recruit, to how we reward and engage our colleagues. This includes our inclusive gender-neutral parent policy covering maternity, paternity, surrogacy and adoption, which we launched in 2021
- In 2023/24 we recruited 12 colleagues, 58% of these were women.

We're proud to partner with both Future Asset and Girls Are Investors (GAIN):

- Future Asset is an organisation in Scotland that aims to raise aspirations and confidence in girls in the senior phase of high school, encouraging them to choose ambitious career paths, and informing them about rewarding opportunities in investment
- GAIN is a charity set up by investment professionals to improve gender diversity in investment management by building a talent pipeline of entry-level female and non-binary candidates.

Case study

SUPPORTING GENDER DIVERSITY IN THE INVESTMENT INDUSTRY

Context

Gender diversity is an area where the investment industry sadly falls short. Not only is the sector burdened with an outdated image of testosterone-fuelled trading floors, it hasn't done nearly enough to attract and develop female talent. As a result, women make up only 12% of fund managers in the UK.

How

At LPF, we're mindful of our responsibility to help bring about a more inclusive investment industry. We do this both through promoting a culture of diversity, equity and inclusion among our own colleagues, as well as supporting a variety of external initiatives focused on building a fairer and more representative future.

- **Asset Owner Diversity Charter (AODC)**

  As a signatory, we commit to including diversity as part of our ongoing manager monitoring and to take account of diversity and inclusion records from fund managers when choosing new partners. Fund managers are asked to disclose information and demonstrate how they're tackling diversity and inclusion within their workforce.

- **Future Asset**

  This is a charity based in Scotland that aims to inspire high-school-age girls to discover what the investment sector has to offer as a potential career choice. Future Asset runs many excellent events, including its flagship 'Growing Future Assets' investment competition where teams from across the country vie to present the best stock pitch. Our colleagues have volunteered as judges or team mentors for the Future Asset competition over the last three years and LPF has hosted successful teams to undertake work experience at our office.

- **Girls Are Investors Network (GAIN)**

  GAIN is a charity set up by investment professionals to improve gender diversity in investment management by building a talent pipeline of entry-level female and non-binary candidates. The GAIN Empower Investment Internship Programme provides university students the opportunity to learn about and gain experience in investment management during a summer internship. In summer 2023, LPF welcomed two interns to our investment team, including one recruited through the GAIN internship programme.

Industry statistics from GAIN Impact Report 2023

There's still much to do to achieve gender diversity in the industry, as these stats show:

SENIOR LEVEL
The 2023 Citywire Alpha Female report found that female fund managers make up just 12% of those managing funds in the UK.

MID-LEVEL
A 2023 industry report by Level 20 found that 22% of mid-level roles are held by women, dropping to 10% in senior roles.

ENTRY-LEVEL
Our 2022 GAIN survey of the industry found that of firms that had recruited graduates in the prior 12 months, the average number of female and non-binary applicants was 22% (with 82% of firms reporting 50% or less).

Case study

SUPPORTING GENDER DIVERSITY IN THE INVESTMENT INDUSTRY

Outcomes

- **AODC**

  Over the last year, AODC has increased its signatory base to 27 representing £1.8trn, responded to the FCA's diversity consultation, and undertaken a light touch review of its annual questionnaire. With two years of data from asset managers, data disclosure on diversity, equity and inclusion has improved by 61%, helping to highlight issues and target action.

- **Future Asset**

  As well as offering valuable insight into what investing careers are really like, the 'Growing Future Assets' investment competition has helped participating schoolgirls to build important skills that will serve them well regardless of the direction they choose. Participation in the competition has grown each year, reaching over 1,000 girls since 2020.

- **GAIN**

  In 2023, GAIN worked with 98 firms (representing a 51% increase in participating firms) to deliver internship placements and placed 119 interns. 63% of interns were offered an investment role or secured a subsequent internship (excluding those still at university and those who didn't respond to the follow up survey).

Assessment of effectiveness

It's important to remember that addressing the investment industry's gender diversity gap is a significant challenge. While there are signs that the industry is moving in the right direction, the rate of change is far too slow. One estimate suggests that parity in the numbers of UK male and female fund managers won't be achieved until 2215 at the current pace.

However, by directly acting to develop the next generation of female and non-binary investment professionals, there's cause for optimism that we can accelerate the process of breaking down barriers and building a more diverse workforce. Judging by the excellent efforts of the AODC, Future Asset participants and the GAIN interns, the future looks promising.

"This year, I had the privilege of mentoring two teams from Broxburn Academy, which was participating in the competition for the first time. Both teams impressed, with one earning a 'Highly Commended' award for their excellent research on US chocolate manufacturer Hershey, while the other group saw off dozens of rivals to make it to the live finals in Edinburgh where their exceptional stock pitch on Greggs earned them the runners-up prize."

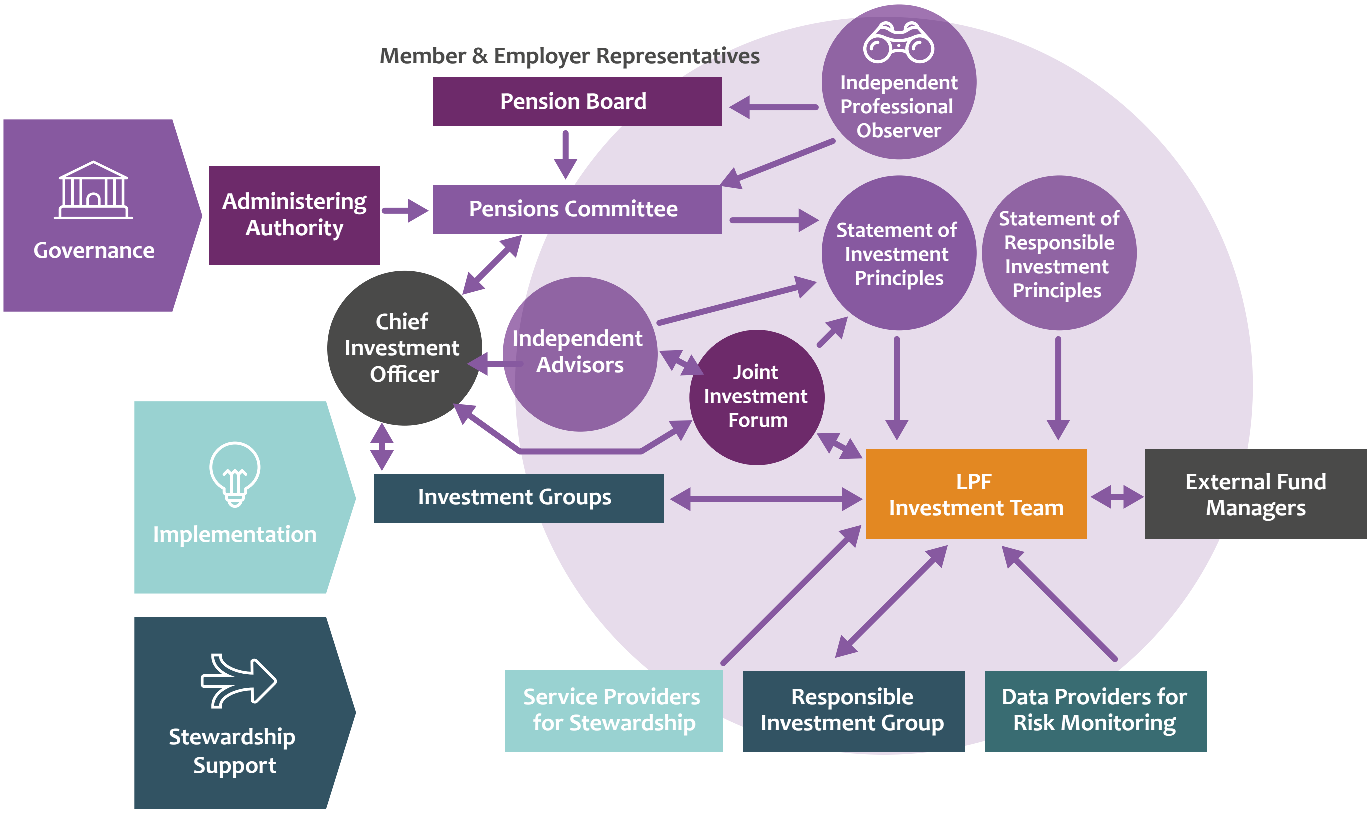
Mark Dobbie, Portfolio Manager

PRINCIPLE 2: GOVERNANCE, RESOURCES AND INCENTIVES

Signatories' governance, resources and incentives support stewardship.

A ROBUST GOVERNANCE FRAMEWORK

We've set out below an overview of LPF's governance framework. Upholding and maintaining sound corporate governance supports the long-term success of LPF, leading to better outcomes for our members, employers and partners. We're also committed to enhancing our governance.



PRINCIPLE 2: GOVERNANCE, RESOURCES AND INCENTIVES

Pension Board

Our Pension Board was established on 1 April 2015 in accordance with the Public Service Pensions Act 2013 and the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015. Its membership consists of equal numbers of representatives appointed from the employer bodies and trade unions for the membership of LPF. The Pension Board's role is to help ensure that the operation of LPF is in accordance with the applicable laws and regulations.

Pensions Committee

The City of Edinburgh Council (CEC) is the administering authority of LPF. Functions relating to pensions matters are delegated to CEC's Pensions Committee. The Pensions Committee oversees LPF's officers who carry out the operational activities of LPF. The members of the Pensions Committee act as 'quasi trustees' and normally hold four meetings a year. The Pensions Committee is made up of five elected CEC Councillor members and two external (non-councillor) members representing the employers and members of the fund.

The Pensions Committee is responsible for setting LPF's investment strategy. It formally reviews and agrees the SIP and the SRIP annually. The implementation of the strategy, through more granular investment decisions, and monitoring of investments, is delegated to suitably qualified and experienced individuals employed by LPF.

The Pensions Committee has also established a separate Pensions Audit Sub-Committee to review and scrutinise certain delegated matters, such as the control and assurance environment and framework of internal controls of the pension fund; agree internal audit plans; to ensure sound financial procedures are in place, and to promote the development of appropriate risk management strategies and procedures. The Audit Sub-Committee meets at least three times a year and reports to the Pensions Committee.

Group Companies

To support the distinction between LPF's purpose and the functions and responsibilities of City of Edinburgh Council as the administering authority for LPF, we have two Group companies, each with their own Board of Directors:

- LPFE Limited: an employment services company with the primary purpose to recruit, develop and retain LPF colleagues who support the specialist business and activities of LPF and LPFI Limited

- LPFI Limited: a regulated investment company, initially established to provide investment advice to our partner funds in Fife and Falkirk and now managing equity and bond mandates for those partners. LPFI is regulated by the Financial Conduct Authority.

PRINCIPLE 2: GOVERNANCE, RESOURCES AND INCENTIVES

Joint Investment Strategy Forum

During the year, the Joint Investment Strategy Panel (JISP) was replaced by the Joint Investment Forum (JIF). The external independent advisers previously on the JISP continue to sit on the JIF, providing strategic advice to Lothian, Falkirk and Fife pension funds. The purpose of the change was to define the roles and responsibilities of all stakeholders, distinguishing more clearly between the strategic advisory services provided to Falkirk and Fife pension funds by LPFI, and the advice provided to all three funds by the external advisers to support decisions in relation to investment strategy and supporting investment decision making governance processes.

Meetings of the JIF take place quarterly and are attended by external investment advisers and representatives from each participating Fund, who receive advice and discuss investment issues common to the three Funds. The JIF enables the Funds to share expertise and resources and to align investment approaches where appropriate, with the aim of implementing investment strategy in the most effective way.

The external advisers provide an independent, expert view to support decisions in relation to investment strategy, bringing external challenge and supporting a key area of governance in the investment decision-making process. Each pension fund retains responsibility for its own decisions and specifically, LPF's Chief Investment Officer has delegated responsibility for implementing LPF's investment strategy and for appointing, monitoring and reviewing managers and advisers.

Portfolio Managers and Policy Investment Groups

The day-to-day management of LPF's assets is performed by internal and external professional portfolio managers. Pension fund officers monitor the assets including mandate and policy group performance quarterly with the support and advice of the JIF and report to the Pensions Committee at its regular meetings. Portfolio manager activities are defined by investment management agreements detailing the portfolio objectives and constraints. Portfolio managers may have discretion to buy and sell investments within the terms of their mandates, or they may require approval from the relevant equity, debt, or real asset investment group.

PRINCIPLE 2: GOVERNANCE, RESOURCES AND INCENTIVES

Fiduciary responsibilities

LPF's activities are guided by the legal principle of fiduciary duty. A legal opinion on the nature and extent of LPF's fiduciary responsibilities was obtained by the Scheme Advisory Board for the Scottish LGPS in 2016. LPF regularly reviews this analysis and monitors legal and regulatory developments as they relate to responsible investment.

Staff resourcing

We've built out a staff structure to best resource our activities and allow us to enhance the exercise of our stewardship. Our headcount of 99 (as at 31 March 2024) includes dedicated teams which support our communication with stakeholders, good governance, stable ICT systems, effective management of risk, people and finances, and the delivery of legal services.

During the year we recruited 12 new colleagues across a variety of roles. This included Emmanuel Bocquet joining as Chief Investment Officer and Alan Sievewright as Chief Finance Officer, succeeding Bruce Miller and John Burns respectively. These hires will not only ensure that we remain adequately resourced to deliver what we need today but will enable us to continue to improve our capabilities and the services we deliver to our members and employers.

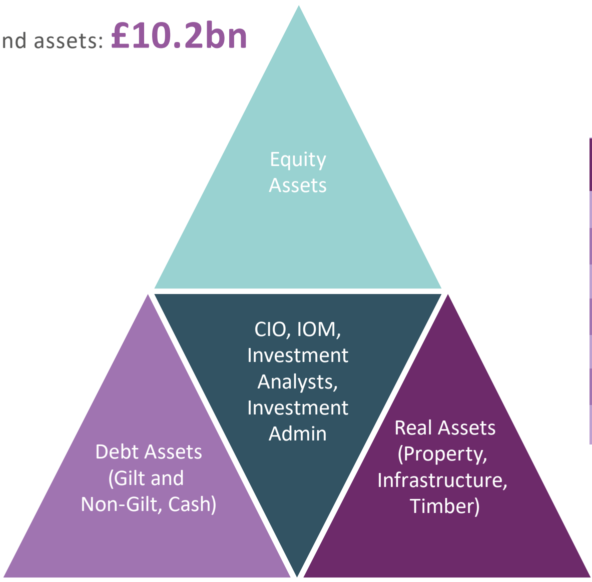
PRINCIPLE 2: GOVERNANCE, RESOURCES AND INCENTIVES

STAFF STRUCTURE

Senior Leadership Team (SLT) as at March 2024

Internal Investment Team as at March 2024

Fund assets: **£10.2bn**



Internal Investment Team of 20	
Chief Investment Officer (CIO):	1
Investment Operations Manager (IOM):	1
Portfolio Manager:	10
Deputy Portfolio Manager:	2
Property Asset Manager:	1
Investment Analyst:	3
Investment Administrator:	2

All Portfolio Managers are subject to annual fit and proper assessments and all LPF staff are subject to a Code of Conduct, which sets the minimum expected standards of individual behaviour. A range of relevant professional qualifications are held across the team, including from CFA Institute, MRICS and CISI. At least eight of the internal investment team have over 20 years of experience in investing, which supports a long-term, through market-cycle perspective. We encourage and support members of the team to gain experience, both through professional development and professional qualifications: three of our analysts were part-way through the CFA program as of 31 March 2024. We monitor the experience and qualifications of external managers as part of our due diligence process.

Furthermore, senior managers have a duty of responsibility to take reasonable care to avoid and/or stop a breach from occurring in the business area that they're responsible for, and such duty is formalised by regulation. All SLT appointments at LPF are subject to the FCA's Senior Managers and Certification Regime such that LPF benefits from implementing the standards of the FCA more widely than just for LPFI activities.

PRINCIPLE 2: GOVERNANCE, RESOURCES AND INCENTIVES

Internal stewardship resource and Responsible Investment Group

At LPF we primarily see stewardship as an integrated element of the investment function. Our core aim is to exercise our rights and responsibilities as investors; our entitlement to vote provides an opportunity to engage to enhance both corporate governance and investee company prospects. Analysis of ESG factors supports investment decision-making, shedding light on downside risks and upside opportunities.

In June 2024, in recognition of increasing stakeholder interest in responsible investment topics, continual advances in best practice and expanding reporting expectations, two new dedicated responsible investment roles were created within our investment team:

- The Head of Responsible Investment (HoRI) supports the CIO in fulfilling responsibility for implementing our responsible investment strategy with oversight of responsible investment service providers, managing our participation in collaborative initiatives, driving the evolution of our approach as best practice evolves and leading our reporting to stakeholders

- The Responsible Investment Analyst provides additional capacity to support the HoRI and Portfolio Managers with implementation of our responsible investment strategy and processes.

Our internal portfolio managers also participate actively in collaborative initiatives, such as Climate Action 100+ for which we're a co-lead engager, and it's our portfolio managers and analysts who are responsible for engagement and escalation activities with investee companies. These activities are undertaken directly or through our external managers or through our engagement and voting provider (see External stewardship resource on page 22).

We also utilise stewardship knowledge from LPF's other functional teams. The Responsible Investment Group (RIG) was established in 2021 to bring together members of the different functional teams formally and regularly to share diverse perspectives sourced from experience in: ESG investment analysis and research, public policy and advocacy, thematic investment, investment management, investment consultancy, law, actuarial advice and pension trusteeship.

The SLT oversees the RIG, which is comprised of:

- Chief Investment Officer
- Head of Responsible Investment (from June 2024)
- Portfolio Managers/Heads of investment policy groups as Responsible Investment Leads for all the major asset classes
- Representatives from the Legal, Risk & Compliance, Finance and Communications teams

PRINCIPLE 2: GOVERNANCE, RESOURCES AND INCENTIVES

The inter-disciplinary group enables the sharing of knowledge, experience and insight relevant to other areas, while improving the governance and oversight of stewardship activities. By providing stewardship advice to LPF officers and the Pensions Committee, the RIG aims to mitigate risk and identify opportunity, for example by supporting internal and external managers in navigating regulatory changes and shareholder actions.

Members of the RIG have extensive experience in responsible investment roles and have relevant qualifications, undertaking continuing professional development and participating in industry Responsible Investment groups to maintain and build best practice knowledge. Over the 12 months to 31 March 2024, the RIG logged over 90 hours of continuing professional development across a range of themes including climate risk, fossil fuel stranded asset risk, narrative climate scenario analysis, biodiversity and nature risks, greenwashing, executive remuneration, diversity, human rights in conflict-affected and high risk areas, responsible mining, aligning expectations between asset owners and asset managers on voting, and UK corporate governance/stock market listing rules. The HoRI (previously in their role as a Portfolio Manager and Responsible Investment Lead) also led training sessions for the internal investment team and the Pensions Committee on responsible investment topics. The combination of skill sets, backgrounds and practical experience of team members is well suited to the development and execution of our responsible investment policy and integration into LPF's wider investment approach.

Our HoRI's expertise as an investor with specialist knowledge across the asset classes in which we invest is essential to delivering effective stewardship. The HoRI manages the relationships with our voting and engagement supplier and ESG data providers and works with our other internal portfolio managers to ensure material ESG risks are identified, monitored and managed throughout the investment process. They support the oversight and monitoring of external managers, and champion LPF's responsible investment beliefs and stewardship activity in the wider investment industry.

LPF also allocates a budget for the procurement of ESG data to support our integration of these factors into our investment process, including the analysis of climate-related risks and opportunities.

PRINCIPLE 2: GOVERNANCE, RESOURCES AND INCENTIVES

External stewardship resource

To adequately resource our stewardship activities, LPF utilises a range of ESG providers, tools and technologies (see table below). We contract an external voting and engagement provider, Federated Hermes EOS (EOS), to undertake much of LPF's voting and engagement activities. Engagement focuses on company strategy covering many ESG issues, such as climate change, plastic usage, diversity and labour practices. LPF engages with companies on these issues because they can create significant risks which, if not appropriately addressed, threaten investments with material and permanent capital impairment.

Our investment team interacts with EOS to contribute to the work plan and access the body of knowledge that resides with their engagement professionals. EOS represents owners of assets with a total worth of more than $1.4tn, which creates more influence than LPF would have engaging on its own. In addition, EOS is structured to undertake multi-year engagements, often leveraging its access to engage across multiple themes.

ESG Providers, Tools and Technology
ESG research providers: MSCI ESG research
Proxy voting analysis: ISS, Federated Hermes EOS
Business involvement research: MSCI ESG research
Trade Associations: PLSA, Investment Association, GRESB*
Investor Initiatives: IIGCC, CA100+, LGPS X-Pool RI Group, Asset Owner Council, PRI*
Technology Enablers: Bloomberg, Factset, MSCI One

** Further details are provided in Principle 10 on Collaboration*

The EOS team draws on a wide range of skills and backgrounds: senior engagers come from a range of backgrounds including banking, academia, law, corporate governance, sciences, corporate strategy and climate change. The engagement team consists of 31 people (supported by four voting specialists, three senior advisers and ten client service professionals). EOS undertakes a skills gap analysis of the wider team with reference to the thematic and sectoral issues covered, to ensure EOS has the right mix of professionals who can represent EOS and its clients' views in engagements with companies. Furthermore, it delivers training to share knowledge across different sectors and themes to facilitate cross-pollination of expertise. EOS has intentionally built a diverse team (53% female/47% male for permanent staff as at 31 December 2023) of experienced and international professionals who have the expertise, language skills (fluency in 16 different languages) and cultural knowledge to access and maintain constructive relationships with company boards across the globe to deliver real beneficial change at companies.

EOS reports on voting and engagement activity across LPF's assets every quarter, as well as annually. Through this regular reporting and dialogue, we're able to ensure that the service is being delivered as expected and in alignment with our responsible investment policies. EOS also engages with regulators, industry bodies and other standard setters to shape capital markets and the environment in which companies and investors operate. We present voting and engagement case studies in relation to Principle 9 (Engagement) and Principle 12 (Exercising rights and responsibilities), later in this report.

PRINCIPLE 2: GOVERNANCE, RESOURCES AND INCENTIVES

External managers

We expect our external managers to engage investee companies on our behalf on material issues including ESG issues and opportunities. We encourage our external managers to enhance stewardship by participating in collaborative engagements (see Principles 9 and 10) and to support best practice disclosure. We receive quarterly updates from our external fund managers, which include updates on company engagements and stewardship initiatives.

Learning and development to support our responsible investment beliefs

Members of the Pensions Committee are required to undertake a minimum of 21 hours training per year. This supports them in fulfilling their role and managing the lobbying they may receive, as elected officers, on a wide range of issues (including aspects of LPF's investment activities).

During the year to 31 March 2024, the Pensions Committee received training on a number of stewardship topics including: climate change related risks (including exposure to fossil fuels) and opportunities, exposure to the Israel/Gaza conflict, and a review of the voting and engagement activities undertaken by EOS on our behalf.

The fund's officers also access a range of resources to support learning and development across responsible investment themes through our membership of collaborative initiatives such as CA100+, IIGCC, PRI, EOS and the Global Investor Commission on Mining 2030. More details on these are provided in Principle 10 (Collaboration), later in this report.

Performance and reward

We recognise the importance of our people in achieving our responsible investment commitments and stewardship aims, and the need to develop, reward and support them in their roles, within their teams and as individuals.

In terms of staff performance, the role profile for each member of our investment team includes explicit reference to LPF's responsible investment and ESG aims. This makes each person involved in LPF's investment decision-making individually accountable for furthering LPF's responsible investment aims.

The annual performance review for portfolio managers and deputy portfolio managers looks at how they "ensure compliance with the Fund's policies and procedures, including its commitment to responsible investment, which involves company engagement and voting and integration of ESG analysis into investment decision-making."

LPF's remuneration scheme is deliberately structured to align staff with LPF's long-term aims and to avoid incentivising inappropriate risk-taking.

PRINCIPLE 3: MANAGING CONFLICTS OF INTEREST

Signatories manage conflicts of interest to put the best interests of clients and beneficiaries first.

Our commitment to managing conflicts of interest

In all its activities, LPF acts honestly, fairly and professionally. This approach is aligned to our values of being 'Agile and Dependable', and 'Innovative and Prudent'. As described in relation to Principle 2 (Governance), LPF has adopted the FCA standards across its investment operations, and this includes standards in relation to conflict identification and management. This response focuses on LPF's own investment operations (distinct from any client services delivered by LPFI).

We're aware of the duties owed to our various stakeholders and the range of actual or potential conflicts of interest that may arise while carrying out investment activities. We recognise that effective management of conflicts of interest is fundamental to the effective stewardship of our assets. It also protects the best interests of LPF, our staff and our stakeholders. Identifying and managing conflicts of interest is a vital part of ensuring these duties are upheld.

LPF has a Conflicts of Interest policy that is reviewed on a regular basis, most recently in December 2023 (see Principle 5). This review led to improvements to our conflicts record keeping approach, to enable LPF to better demonstrate that we take reasonable steps to identify and manage all potential and perceived conflicts. Our Conflicts of Interest Policy sets out how we implement and maintain effective arrangements. The policy specifies the required standards and procedural controls for identifying, recording, monitoring and preventing conflicts of interest, and is supported by training for all new and existing staff. LPF takes steps to identify and manage conflicts to ensure fair treatment for our scheme members and employers as well as our clients and it’s incumbent on all staff to be alert to potential conflicts of interest and act accordingly.

Actual or potential conflicts are raised directly through individuals, governance forums, or indirectly through oversight and assurance work. A conflicts of interest register is maintained which records details of each conflict including how it was identified and what actions are in place to manage it. Any instances where the Conflict of Interest policy hasn’t been followed would be recorded as an incident and managed through the standard incident management policy which is part of LPF's Risk Management Framework. All staff are requested to complete an annual attestation that they understand their obligations under this policy. A conflicts of interest thematic review undertaken during the reporting period found no evidence of any actual conflicts that resulted in the failure to act in the best interest of beneficiaries.

Conflicts of interest can arise at LPF in a number of ways, but most likely in the form of an employee’s financial or external interest or through a connected person to them. Conflicts could also arise where LPF benefits at the expense of a client, or through a conflict from holding an interest in the outcome of a service or transaction at odds with clients or other beneficiaries.

PRINCIPLE 3: MANAGING CONFLICTS OF INTEREST

Whilst no actual conflicts resulting in the failure to act in the best interest of beneficiaries have been identified, those actual or potential conflicts considered most likely to arise in LPF, are noted below, together with our approach to addressing these:

- **Director conflicts.** A conflict could arise where executive or non-executive directors of LPFE or LPFI have personal or professional interests that conflict with the interests of LPF or its stakeholders

  LPF approach: All LPFE and LPFI directors are required to disclose conflicts of interest upon appointment and on an ongoing basis through a standing agenda item at Board meetings

- **Outside Business Activities (OBAs).** A conflict could arise where a LPF employee has an outside business interest, employment, or role or connection that conflicts with their role at LPF

  LPF approach: All employees must disclose external roles and apply for permission before taking up new external appointments

- **Fiduciary duty for Pensions Committee and Pension Board members.** A conflict could arise where the personal, professional, or political interests of Pensions Committee or Pension Board members differs from their fiduciary duty owed to LPF's pension stakeholders

  LPF approach: All Pension Board and Pensions Committee members are subject to a Code of Conduct which sets out their responsibilities. An Independent Professional Observer provides impartial observations on the operation of the Pensions Committee and Pension Board, to support them in fulfilling their duties

- **Gifts and Entertainment.** A conflict could arise where LPF provides or receives gifts or entertainment that may influence decisions

  LPF approach: All employees follow standards set out in a Gifts & Entertainment policy on when such offers may be accepted or declined. Records are kept of all such offers, accepted or declined and periodic monitoring is undertaken by the R&C Team to provide assurance regarding compliance with this policy

- **Personal Account Dealing.** A conflict could arise when an LPF employee or close friend or family member owns or trades in a personal capacity in securities which LPF or LPFI also has an interest in

  LPF approach: All employees are required to declare ownership of personal securities on commencing employment and on an annual basis thereafter. A Personal Dealing policy sets out required standards which includes preapproval before trading and record keeping obligations. Periodic monitoring is undertaken by the R&C Team to provide assurance regarding compliance with this policy

PRINCIPLE 3: MANAGING CONFLICTS OF INTEREST

- **Stewardship.** A conflict may occur in relation to Environmental, Social and Governance (ESG) matters between LPF as an asset owner with duties owned to its pension stakeholders and LPF's administering authority, the City of Edinburgh Council.

LPF approach: LPF adheres to a Statement of Responsible Investment Principles, which is reviewed by the Pensions Committee at least annually

- **Third-party providers.** A conflict may arise due to the need to achieve best value for money, and the best interest of pension stakeholders or clients

LPF approach: LPF appoints and manages suppliers through a detailed procurement process and supplier management framework.

Case study

MISALIGNMENT OF STEWARDSHIP EXPECTATIONS BETWEEN ASSET OWNERS AND ASSET MANAGERS

Context

LPF is one of many asset owners that publicly recognise that climate change presents material investment risks with the potential to disrupt economic systems and affect long-term beneficiary interest. We highlighted in our 2023 Stewardship Report Case Study on Collaborative Engagement: Climate Action 100+, the world's biggest greenhouse gas emitters still have significant work to do to align their businesses with a net zero world.

While LPF manages most of its listed equity investments internally, many asset owners invest through funds where the external asset managers undertake voting in accordance with their own voting policies. The 2023 proxy voting season indicated that the majority of investors failed to challenge oil and gas companies that were inadequately progressing or even backtracking on their climate commitments (see Case Study on "Say on Climate Votes" in Principle 12 for more details). This indicated a need for the industry to address the perceived misalignment or conflicts of interests in this area of stewardship.

Action

In October 2023, LPF attended a roundtable convened by the UK Pension Fund Roundtable (now called the Asset Owner Council) to discuss this perceived misalignment of interests between asset owners and asset managers in relation to stewardship expectations on climate change. The roundtable provided an opportunity for discussion of practical steps to address the misalignment and to identify how fund managers could be better supported in delivering asset owners' climate stewardship strategies.

Research undertaken by Professor Andreas Hoepner evaluated the 2023 voting records of select fund managers for oil and gas companies and provided evidence of varying degrees of misalignment between the stewardship activities some of these asset managers and the expectations of large UK asset owners. The full research was published in November 2023, providing insights on misalignment trends. It proposed the following rationales for the observed discrepancies in stewardship approaches, highlighting the need for further research to explore these issues in further detail:

Case study

MISALIGNMENT OF STEWARDSHIP EXPECTATIONS BETWEEN ASSET OWNERS AND ASSET MANAGERS (CONTINUED)

- **Cultural Misalignment:** differences between UK based asset owners and non-UK based asset managers may contribute to misalignment
- **Resource Allocation Misunderstanding:** a fundamental misunderstanding of the importance of stewardship and voting, leading to insufficient resource allocation
- **Fiduciary Duty Conceptualisation:** misunderstanding fiduciary duty, particularly in terms of risk management related to climate change
- **Stewardship Process Differences:** differing views over the treatment of voting and engagement as mutually exclusive or complementary activities, impacting on extent of misalignment toleration and what is considered an engagement success
- **Financial Conflicts of Interest:** potential misalignment due to commercial relationships between asset managers (especially those owned by banks) and issuers.

Outcome & assessment

The roundtable was a starting point for dialogue on this issue, enabling commitment towards better communication and transparency (including bilateral conversations between asset owners and their asset managers on the research findings). The next phase will consider how asset owners can better articulate their views on climate stewardship. We also note that the FCA launched a consultation in June 2023 on a standardised ‘vote reporting template’ to improve communication by asset managers on their voting activity. There have also been calls from UK asset owners for more asset managers to adopt “pass-through” or “client-directed” voting with new technologies, enabling asset owners to preset voting instructions to align with their stewardship policies in both segregated and pooled mandates.

While LPF manages most of its listed equity investments internally and only 4% of our equity assets are in funds where voting is undertaken by our external managers, it’s still relevant for us to work with the industry to address concerns of climate stewardship misalignment as LPF is a small asset owner in the global context. We recognise that corporate managers are unlikely to respond meaningfully to shareholder proposals calling for more ambitious approaches to transform their business to align with the aims of the Paris Agreement if these shareholder proposals are only supported by a minority of votes. It’s therefore in the interest of our scheme members and employers that like-minded investors’ climate concerns are better communicated to investee companies either through client-directed voting or improved alignment of asset managers’ stewardship activities.

PRINCIPLE 4: PROMOTING WELL-FUNCTIONING MARKETS

Signatories identify and respond to market-wide and systemic risks to promote a well-functioning financial system.

IDENTIFYING AND ADDRESSING MARKET AND SYSTEMIC RISKS

As a long-term investor, sustainable, well-functioning markets are essential to our purpose of delivering a valued retirement savings product for our members. They'll enable us to pay pensions and benefits when they fall due over the next several decades.

We ensure that the risks to our investments are effectively managed as we know that Environmental, Social and Governance (ESG) factors are fundamental considerations in driving the long-term value of our investment portfolio.

We're very aware that investment markets can go down as well as up and market conditions can change rapidly. Uncertainties that affect the behaviour of markets within the macroeconomic environment can affect the value of the assets held within a portfolio. When considering or reviewing investments we look at factors such international political developments, market sentiment, economic conditions, circumstances where markets aren't allowed to freely move (due to government controls), changes in government policies, restrictions on foreign investment and currency repatriation, currency fluctuations and other developments in the laws and regulations of countries in which investment may be made.

Given the potential impact on our investment returns, we closely monitor market-wide and systemic risks. We collect information from many sources.

PRINCIPLE 4: PROMOTING WELL-FUNCTIONING MARKETS

External advisers

- LPF uses the JIF to gain insights on market trends and conditions
- LPF's external managers include market commentary within their periodic investment reports, which LPF reviews in detail
- LPF's actuary may comment on general investment issues as part of the valuation work they do for LPF
- LPF's investment consultant provides an Economic Scenario Service to support our Investment Strategy Review.

External providers

- EOS supports us in identifying systemic and emerging risks as well as mitigating these risks through engagement. Our Internal Equities team work closely with EOS in our collective approach to engagement, reflecting the areas of stakeholders' interest and concern. We undertake to utilise our voting rights, including those exercised through proxy, to engage with the management of companies in whom we invest, to promote appropriate standards of corporate governance that safeguard shareholder interests and respect stakeholder interests
- The organisations which support LPF's portfolio monitoring for shareholder litigation share insights on market-wide issues relevant to risk.

Reviews

- LPF monitors its counterparties and suppliers to ensure they remain creditworthy and suitably authorised to provide services
- Our investment team monitors the creation of debt within the financial system to identify systemic and non-systemic vulnerabilities.

Collaboration

- Collaborative initiatives are a valuable source of intelligence on emerging risks and ways to mitigate these risks. We have a long track record of collaborating with other investors, asset owners and organisations
- By participating actively in in the Climate Action 100+ initiative, our officers and service providers have influenced real change, including an accelerated timetable for methane emissions reduction
- We also continued as an active participant in both the Occupational Pensions Stewardship Council (OPSC) and the UK Asset Owner Responsible Investment Roundtable, supporting the initiative to merge these two initiatives to form the Asset Owner Council in 2024, which we expect to be a more efficient means of sharing stewardship best-practice across the industry
- In November 2023, LPF became an investor-supporter of the Global Investor Commission on Mining 2030, which is a multi-stakeholder commission including representatives from communities, intergovernmental organisations, civil society, academia, law, unions, the mining industry, banking, insurance and investors, who recognise the need for the industry to manage systemic risks which can threaten its social license to operate.

PRINCIPLE 4: PROMOTING WELL-FUNCTIONING MARKETS

UNDERSTANDING MARKET AND SYSTEMIC RISKS

We discuss the materiality of each potential risk and agree an action plan for addressing it, including:

- Responding to consultations: engaging with government and industry bodies, for example:
  - In May 2023 the FCA launched a consultation on Primary Markets Effectiveness and proposed equity listing rule reforms. We explicitly supported a detailed response through our voting and engagement service provider, Federated Hermes EOS. We believe that public markets exist to provide an environment in which companies, guided by beneficial corporate governance requirements and robust protection of shareholder rights, gain access to capital which allows them to grow and deliver long-term, sustainable wealth creation. Balancing capital access with a strong focus on protecting shareholder rights will thus attract the right combination of companies and investors to create a deep pool of liquid capital. The response sets out our view that standards for governance and minority shareholder protection rights shouldn't be lowered within listing requirements as this could promote a 'race to the bottom' ideology, devaluing the benefits to investors of companies listing and trading publicly.

- Direct dialogue:
  - Engaging directly with policymakers: through the Scottish Scheme Advisory Board, we provided feedback on the draft Economic Activity of Public Bodies (Overseas Matters) Bill which was progressing through parliament in 2023/24
  - Engaging with regulators: working with the IIGCC to engage with the Bank of England in its role as the Prudential Regulatory Authority, to promote more effective climate risk management and system-wide resilience in the face of climate change (see Case Study on page 32)
  - Engaging directly with companies as part of Climate Action 100+ (CA100+)

- Collaborative initiatives: this includes our membership of IIGCC, CA100+, PRI, OPSC and LAPFF [more details provided in Principle 10]

- Participation in a workshop organised through the UK Asset Owner Responsible Investment Roundtable (see Case Study on page 27) to showcase research assessing voting activities of asset owners and managers (using oil and gas as a critical example) and enabling a constructive dialogue around the pace and scale of climate action needed to achieve net zero alignment, the extent to which stewardship strategies have reinforced climate ambitions, and future expectations around pathways for voting escalation

- Advocating for better standards through engagement with our external managers: in 2023, we communicated with our external fixed income managers to outline our commitments to responsible investment, introduce enhanced monitoring of primary investments, request updates on their net zero commitments and plans for product-level TCFD reporting, and request completion of the Diversity and Inclusion Questionnaire.

Case study

ENGAGING WITH REGULATORS TO PROMOTE EFFECTIVE CLIMATE RISK MANAGEMENT

Background

Through our collaboration with other investors, LPF aim to have a more significant impact on the companies who need to transition their current operations and future investment spending to climate-friendly adaptions, but that's not the limit of where we can help drive positive change. Governments and regulators are also important stakeholders, with vital interests in addressing the risks and opportunities presented by climate change.

We collaborate through Climate Action 100+ (CA100+), which aims to get companies to disclose vital information, allowing shareholders and other stakeholders to hold them to account, and its benchmark is a key tool for assessing whether companies across sectors and industries with the highest emissions are meeting best practices. CA100+ is coordinated by five regional investor-led networks. LPF is a member of the Institutional Investors Group on Climate Change (IIGCC), which is the network for investors across Europe.

Through our relationship with IIGCC, we have access to their working groups which provide an opportunity for participants to share knowledge and respond to areas of interest using an array of perspectives from different asset owners, managers and stakeholders. Topics cover specific sectors of the economy, public policy, asset classes and more. LPF participate in the utilities working group as this links well with our participation as co-lead engager with a utility company through CA100+. We also became aware of the accounting working group, with its focus on climate accounting and the evolving array of tools available to investors to assess climate risk.

In late 2023, the accounting working group started to assess the viability of influencing the key UK banking regulator, the Bank of England, in its role as the Prudential Regulatory Authority (PRA), whose purpose is to ensure sufficient capital and risk controls are in place across the banking, insurance and investment sectors. Banking regulation covers many aspects of how banking institutions are governed – from how they protect customers through to how they ensure there's the capacity to absorb shocks from global and local macroeconomic volatility.

In 2022 the PRA itself was in contact with key bank leaders, CEOs and CFOs, underlining that climate risk needs to be incorporated effectively into valuations for the assessments banks must make of their exposures and available capital to absorb losses.

LPF Action

We spent time working with other members of the IIGCC accounting working group to adapt a proposed letter encouraging the PRA to take this valuable work further forwards, making it clear that we entirely support the efforts being made, but underlining the importance of turning these insights into concrete action. In particular, we asked to see proactive enforcement of existing rules to ensure that capital adequacy is properly being assessed with realistic negative outcomes on the values of the assets that banks lend against. We asked for the regulator to also consider disclosure of climate stress-testing exercises.

Assessment of the effectiveness of our approach

Our letter, co-signed with 20 other investors, was well received by the Bank of England, and we intend to continue taking this issue forwards with other banking regulators, through collaboration and open discussion with our peers and all current and future stakeholders.

Capital adequacy

The availability of sufficient capital is referred to as 'Capital Adequacy', and lack of transparency on this was one of the key reasons why the Great Financial Crisis spread so rapidly, as banks were unsure whether there was enough money within the system to absorb losses, as the assets they lent against plunged in value.

Over the following 15 years, regulators have worked globally to tighten and raise standards over the quality and amount of safe assets banks must hold to be able to cope with economic volatility.

To ensure this, regulators – and investors – must have sufficient detail on the types of assets, and how their values are assessed to be able to have confidence that there's enough resilience system-wide and with individual banks

PRINCIPLE 4: PROMOTING WELL-FUNCTIONING MARKETS

OUR APPROACH TO CLIMATE CHANGE RISK

In Principle 7 we identify Climate Change as our Top Priority for integration within our stewardship and investment processes, as a key systemic risk, and stated (in Principle 1) that asset owners are uniquely positioned to engage with global policy makers and industry regulators as well as with investee companies, to bring about an acceleration in the sustainable energy transition and a decarbonisation of the global economy. The case study on page 32 (Principle 4) describes how we seek to engage with regulators on this systemic risk.

Principle 7 provides further details on how we integrate climate change risks (and other ESG risks) into our investment processes. In Principle 10, we highlight collaborative engagement activities through Climate Action 100+. In Principle 12, we provide details on our voting policies and how we voted, with a case study on “Say on Climate” votes.

Assessment of effectiveness

Our ability to influence investee companies through voting and engagement is limited as a minority investor. However, by collaborating with like-minded investors on engagement and being transparent about our voting actions, we can amplify our influence to drive the long-term value of our investment portfolio and contribute to the long-term health of the financial system.

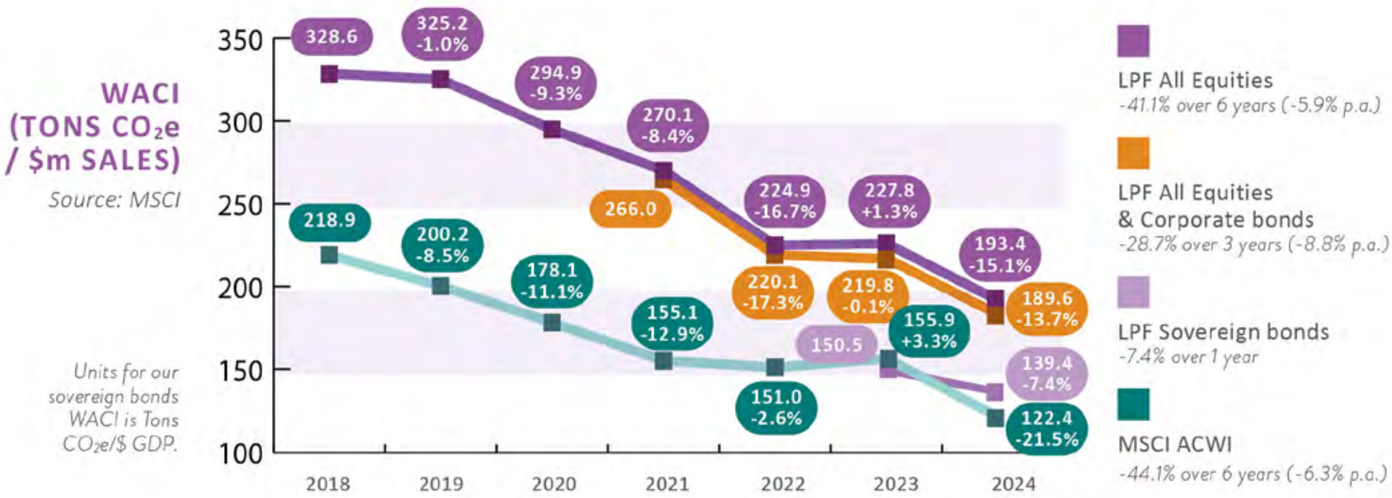
The companies in which we invest need a clear legal and regulatory framework in which to operate. We'll continue to call on governments to deliver consistent policies to support a well-functioning market and an energy transition that mitigates risk. These policies need to adequately discourage the production and consumption of fossil fuels. We'll continue to engage with and encourage our investee companies to develop and implement credible plans consistent with the Paris Agreement. And, as part of our diversified portfolio, we'll continue to make investments where we believe they'll generate both a sufficient return and support the energy transition. We’ve committed to continue to develop our approach to increasingly avoid financing non-Paris aligned investments as the real-world transition progresses.

PRINCIPLE 4: PROMOTING WELL-FUNCTIONING MARKETS

MEASURING CLIMATE RISK IN OUR PORTFOLIOS

We believe that accurate measurement of emissions is an important element in assessing the climate risk of an investment portfolio. Supported by a research budget specifically allocated to data services targeting ESG and climate-related risks and opportunities, we published our first annual carbon footprint (weighted average carbon intensity - WACI) for listed equities in 2018 and expanded the scope to include our corporate bond investments in 2020/21 and sovereign bonds in 2022/2023. Our most recent carbon footprint covered 72.5% of our total fund (up from 67.3% prior year).

In 2021 the UK Government announced that emissions reporting will be mandatory for occupational pensions schemes by 2025 using specific Department of Work and Pensions (DWP) guidelines based on the TCFD framework. Although this doesn't apply to the Local Government Pension Scheme (LGPS), the UK Government launched a consultation proposing to apply broadly the same requirements to the LGPS. The timing for introduction of mandatory Climate Risk Reporting for the LGPS is uncertain, but we continue to prepare for this.



While there are currently challenges with the cost and availability of emissions data, particularly where we're dependent on the level of information provided by external managers, this is a priority for us, and we support industry-wide efforts to improve the provision and quality of data. During 2022 and 2023, we proactively wrote to our external managers informing them of our future regulatory reporting requirements and requested information from them on emissions reporting, noting that our in-scope investment managers regulated by the Financial Conduct Authority (FCA) were expected to meet the FCA's TCFD reporting requirements by mid-2024.

Our view on divestment from companies involved in the extraction of fossil fuels

LPF is often challenged about its approach to responsible investment, including requests to promote a policy of divesting from companies involved in the extraction of fossil fuels. We don't reduce our position size or sell existing holdings for purely non-financial reasons. Nor do we exclude companies from our investment universe for purely non-financial reasons. We do, however, believe that environmental, social and governance issues can affect the financial performance of the companies in which we invest. We take these issues seriously and integrate them into our decision-making processes.

We have a policy of engagement with companies and policymakers rather than a policy of exclusion or divestment. By engaging with the companies in which we own shares, we strive to improve the sustainability of corporate strategy to the benefit of shareholders, and to the benefit of wider society. We believe that a policy of divestment potentially passes shares to less responsible or less active share owners, who are less likely to hold the company's managers to account on planning for and managing significant transitions in their businesses over the next decades. In our view, this achieves nothing in terms of real-world sustainability.

We recognise the outsized impact that some specific sectors and industrial activities have on climate change by virtue of the magnitude of their greenhouse gas emissions. While some prefer to label companies in carbon-intensive industries as 'bad' and those in low-carbon and alternative energy businesses as 'good', history shows that firms need to reinvent themselves to survive. We therefore strive to influence and support positive changes by corporate leaders to achieve sustainability for their firms and for society.

Our policy of engagement allows us to exert influence on companies to improve their business practices, align with the Paris goals, and disclose their climate-related risks and transition plans as well as their investments in solutions, with TCFD compliant reporting.

Where material risks remain following engagement activity, we retain the ability to reduce our position size or selectively sell to mitigate our risk exposure on a case by case basis.

PRINCIPLE 4: PROMOTING WELL-FUNCTIONING MARKETS

HOLDING COMPANIES TO ACCOUNT

In addition to our engagement activities supported by EOS, we recognise shareholder action as another way that we, as an institutional investor, can promote good corporate governance and therefore contribute to well-functioning markets.

Where it's economical to do so, our fiduciary duty may require us to take action to recover funds lost through investments in companies as the result of corporate mismanagement, but we wish to highlight how this can also reduce some systemic risk where corporate reforms can be secured alongside financial recovery. This may be important where there's a void in the role of industry regulators, (due to constrained resources for example) or where changes in political administration can impact the willingness of regulators to take enforcement actions.

We use third party providers to support our portfolio monitoring, to collect information and to undertake legal analysis necessary to make informed decisions about the best options for asset recovery and the wider benefits of participating in potential claims. We have an internal policy to guide our actions, and this considers the significance of a company's wrongdoing, and the wider context of our stakeholder expectations.

Confidentiality restrictions limit how much detail we can provide about specific actions, but LPF continues to actively monitor its loss exposure in relation to class actions, and has previously taken 'lead plaintiff' status for US-based actions.

PRINCIPLE 5: REVIEW AND ASSURANCE

Signatories review their policies, assure their processes and assess the effectiveness of their activities.

We have a range of internal and external review and assurance processes which support good stewardship. We run our review and assurance in conjunction with other underlying business and compliance processes, such as external manager monitoring programmes, which includes responsible investment governance and stewardship, to assess and ensure responsible investment policies are being implemented (see Principle 8).

REVIEW

We take a formal approach to reviewing our policies and their effectiveness. For example, our Conflicts of Interest policy (see Principle 3) is reviewed on a regular basis, most recently in December 2023. This review led to improvements to our conflicts record keeping approach, to enable LPF to better demonstrate that it takes reasonable steps to identify and manage all potential and perceived conflicts.

ANNUAL REVIEW OF OUR SRIP

Our SRIP is reviewed annually. Potential improvements to our responsible investment approach are suggested by LPF staff, reviewed by our Responsible Investment Group (RIG), and proposed for inclusion in the SRIP.

Our JIF advisers appraise any changes. The updated SRIP then becomes official policy when it's approved by the Pensions Committee. The training standards described earlier in this report support the ability of our various governing bodies to provide a meaningful review of our policies. In addition, their fiduciary duty requires them to take proper advice to discharge their function. This means they may need to consider using suitably qualified advisers before revising policies and procedures.

PRINCIPLE 5: REVIEW AND ASSURANCE

ASSURANCE

We care about and respect our members and employers and are committed to being a responsible business. We have comprehensive policies and procedures in place, and collectively, our Governance, Legal, Risk & Compliance functions ensure that LPF and its group companies meet all corporate governance, legal and regulatory obligations and expectations that impact our work. This requires a continued focus on how to improve the effectiveness of everything we do.

During 2023/24 we enhanced our existing risk management arrangements by creating a fully integrated framework based on the following principles:

- Focus on managing risk across the business in a proportionate and pragmatic way
- Ensure arrangements are scalable with an emphasis on investing for the future and building resiliency
- Reduce complexity by standardising processes wherever possible and appropriate
- Extend the annual internal audit programme to include the LPFE and LPFI entities

We continue to develop and embed enhanced risk management arrangements, supported by improved processes and methodology.

RISK MANAGEMENT FRAMEWORK

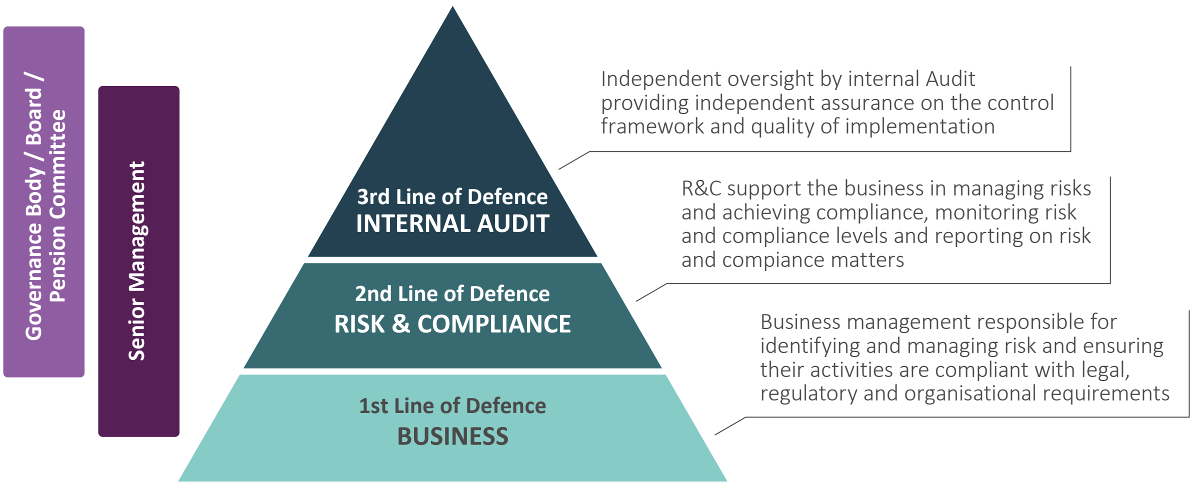
LPF has a risk management framework (RMF) in place across its business functions and group entities, including a toolkit and methodology for identifying, assessing, evaluating, monitoring and reporting risks and controls. This helps to ensure that we're able to operate and demonstrate an appropriate and effective control environment which continues to facilitate and support LPF's forward looking business strategy and objectives.

During 2023 a comprehensive review of the LPF group risk register was undertaken, which has resulted in an improved articulation and evaluation of current risks which the group is exposed to and how these are being managed. Our risk register is formally considered by our Risk Management Group quarterly, but it's also updated on an ad hoc basis where required. The Risk Management Group oversees the implementation and ongoing effectiveness of LPF's risk management framework.

PRINCIPLE 5: REVIEW AND ASSURANCE

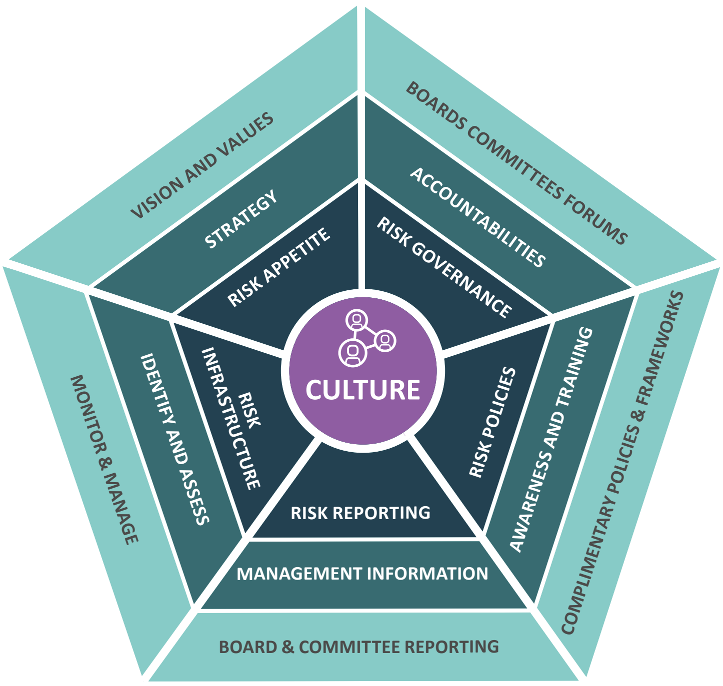
An overview of monitoring and assurance activities undertaken within LPF is provided to the Pensions Audit Sub-Committee on a quarterly basis, with a summary also provided to the Pensions Committee. In addition, an outline of the key risks that LPF is exposed to is reported to the Audit Sub-Committee each quarter, with a summary of the LPF risk register included in papers for both the Pensions Committee and Audit Sub-Committee.

LPF's risk management framework is underpinned by the 3 Lines of Defence model:



PRINCIPLE 5: REVIEW AND ASSURANCE

LPF's RMF brings together various component parts of individual risk arrangements, governance and operations:



The scope of the RMF covers both financial and non-financial risks, and is built around a 'top down' and 'bottom up' approach. Accountabilities for risk management are clearly communicated and reinforced to all employees through:

- A framework of delegations of authority
- Mandatory training and ongoing training
- Position descriptions and formal staff performance target setting and reviews
- Regular written and verbal communications from senior management
- Various assurance reviews and reports.

LPF is supported by numerous systems and tools available to assist with identification, measurement, management and monitoring its risk exposures.

The R&C team is responsible for managing and facilitating the risk management framework, monitoring risk and compliance levels across the business, and reporting on risk and compliance matters to management and governance forums. Monitoring includes themed reviews and spot checks. The R&C team is also responsible for oversight of incident management and issues management.

The internal control environment is subject to reviews throughout the year by both internal and external audit as defined in their respective audit plans. The results of all audit activity are independently communicated to management and the various governance forums. Findings arising from audit activity are assessed and remedial action monitored through the issue management process.

PRINCIPLE 5: REVIEW AND ASSURANCE

ASSESSMENT OF EFFECTIVENESS

PRI assessment

As a signatory to the Principles for Responsible Investment (PRI), a United Nations supported network of investors which works to promote sustainable investment through the incorporation of ESG, we agree to submit a comprehensive survey of our approach to responsible investment annually to the PRI. As part of this process, LPF is able to undertake a gap analysis on areas of best practice highlighted by PRI, alongside our evolving responsible investment experience, supported by our internal assurance of our PRI survey response.

The PRI did not conduct signatory surveys in 2022 due to changes in the PRI reporting tool and didn't undertake an assessment of the survey responses of asset owners such as LPF in 2023. On our website, however, we provide our PRI transparency report which details our responses to the 2023 signatory survey. We use the process of undertaking the survey to conduct a gap analysis, to assess progress and highlight areas for further improvement towards industry best practice. Further significant changes to the PRI Reporting Framework are planned for 2025.

UK Stewardship Code (2020)

As part of the process of producing our third Stewardship Code report in 2023, we addressed feedback on our successful previous submissions from 2021 and 2022 and internally assessed our stewardship policies, processes and reporting. We continue to develop better practice, such as pre-declaring our voting intentions for high-profile votes that we anticipate will be of interest to our stakeholders (see Continuous Improvement section on page 44).

Retaining our status as a signatory to the UK Stewardship Code (2020) in February 2024 with our latest submission (which was submitted in October 2023) itself provides external assurance that we're meeting the standard expected of an institutional investor of our scale.

PRINCIPLE 5: REVIEW AND ASSURANCE

Award Success

In 2023, we were delighted to have a run of award successes.

We were awarded a further two Green Apple Awards for environmental and biodiversity initiatives in our direct property portfolio (see case study on page 43).

In September 2023, we were named "LGPS Fund of the Year (Assets over £2.5bn)" at the LAPF Investments Awards 2023. The LGPS Fund of the Year award looks at best practices in pension fund operations, investment performance and thought leadership within the LGPS and is acknowledged throughout the industry as a mark of excellence in the field of pension fund investment.

Shortly after, we were recognised by the Sustainable Finance Disclosure Rewards for Asset Owners (SFDR4AO) as a leading pension fund for our approach and disclosure on gender. Our commitment and the actions we're taking to drive gender diversity and equality was highlighted, both in regard to our own organisation and how we steward (through voting and engagement) the companies in which the fund is invested. The awards celebrate best practice based on reports published last year. Our positive action approach to gender balance, which is benchmarked externally, is helping to ensure that our HR policies and processes are inclusive and accessible, from how we attract and recruit, to how we reward and engage our colleagues.

In October, Bruce Miller, LPF's former Chief Investment Officer (retired January 2024), received the Lifetime Achievement Award at the LGC Investment Seminar. Bruce joined LPF in 2006 and back then, we had less than £3bn in assets with a small inhouse team and assets predominantly managed externally. Today, LPF has a 20-strong internal investment team with around £10bn in assets and an FCA-registered entity, LPFI. Most of LPF's assets are now managed in-house. Under Bruce's tenure as CIO, we've evolved into one of the leading LGPS in the UK, generating peer-leading risk adjusted returns at industry-leading costs for our employers and members.

At LPF, our primary objective is to pay the pensions for our members, whilst aiming to reduce the costs to employers and investing in a responsible manner. Being recognised by peers and external specialists helps affirm we're on the right path.

Case study



GREEN APPLE AWARDS UPDATE

Context and objectives

LPF has a direct property portfolio of approximately £400m, which we actively asset manage. This means we work closely with our consultants, facilities managers and tenants on a wide array of matters including environmental initiatives. Following the achievement of being awarded two Green Apple Awards in 2022, in 2023 we submitted additional direct property assets for assessment by The Green Organisation, which is an independent, international, non-political, non-profit environment group dedicated to recognising, rewarding and promoting environmental best practice around the world.

The aim of the Green Apple Awards is to improve environmental performance, encourage the efficient use of resources, enhance the competitiveness of organisations, support the wider goals of sustainable development including social benefits through community and staff involvement, and help Green Apple Award winners to benefit from their environmental endeavours.

The Green Apple Environment Award can be awarded to any company, organisation or individual that has helped the environment. There are several categories of awards: Green Champions, Gold, Silver and Bronze. Winners are presented with a Green Apple Award Trophy.

Outcome

LPF was Green Apple Environment Award winners for the following direct property assets:

- Office in St Johns Street, London – Bronze Award
- Leisure Park in Walsall – Bronze Award.

The awards were granted for installing a water management system within the London office building, resulting in significant water savings, and biodiversity improvements at Walsall, including installations of bird boxes and insect hotels.

We also received a commendation for further biodiversity improvements at one of our retail parks in Exeter for the supply and installation of bird boxes, insect hotels and hedgehog boxes.

Assessment and future plans

Independent assessment and award success provides assurance that our environmental endeavours are positively impactful and supports the continuation of these asset management activities across our direct property portfolio.

During 2024, we're looking to put forward submissions for two further property assets.

PRINCIPLE 5: REVIEW AND ASSURANCE

TRANSPARENCY AND REPORTING

LPF welcomes external scrutiny of its activities to support its assurance and review processes. In line with the expectations of a public sector organisation, many of our policies and procedures are available on our website. We also publish our PRI assessment results, our PRI transparency report, our Stewardship Report and our voting records on our website.

We recognise the importance of external reporting, which facilitates independent assessment of our practices. Internally, LPF commits senior resources to supporting the quality of such reporting. For example, related to responsible investment:

- Our HoRI (previously the Responsible investment Lead) has day-to-day ownership of our reporting commitments such as the PRI and the FRC Stewardship Code, with oversight from the Responsible Investment Group
- Our Risk and Compliance and Communications teams ensure accuracy, regulatory compliance, clarity of message and public communication of reporting, as necessary
- Our Senior Leadership Team, specifically our CEO and CIO, are chief sponsors and have responsibility for approving Responsible Investment communications and reporting.

Within our annual report we include information on our approach to climate-related risks and opportunities, following the guidelines produced by the Taskforce for Climate related disclosures. In addition, we submit an annual UK Stewardship Code Report to the FRC.

As reflected in our governance structure, we have multiple layers of regulation and oversight. We prepare extensive internal reporting across all aspects of the organisation. Together, this reporting brings strong discipline in ensuring we review our policies, assure our processes and assess the effectiveness of our activities.

CONTINUOUS IMPROVEMENT

Having improved the availability of our responsible investment policy and guidance documents in 2020 with the publication of our SRIP, which is reviewed and updated annually, and the creation of our responsible investment e-zine, ENGAGE, we further improved the governance of our responsible investment activities by creating our Responsible Investment Group in 2021. We set up our Climate Disclosure and Strategy Project, which progressed through 2022-23 and concluded in 2024 with ongoing responsibility for review and development of our climate strategy and reporting practices transferred to the Responsible Investment Group. In June 2024, two new dedicated responsible investment roles were created within our investment team, demonstrating organisational commitment and support from the SLT to further developing our resources and approach to responsible investment (as described in Principle 2).

While we reinstated full disclosure of our quarterly voting records on our website in 2022/23, publication of company-level voting data is hard to consume (with details on specific companies lost amongst the scale of disclosure). In recognition of growing stakeholder interest in specific votes, such as “Say on Climate” votes and shareholder resolutions (see "Say on Climate" Case Study in Principle 12), we provided more details about how and why we voted on specific companies’ climate plans or emission reduction targets in our Winter 23/24 Engage publication. In May 2024 we further improved the timeliness of the communication of our stewardship activities to stakeholders by pre-declaring our voting intentions for certain high-profile votes.

PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

Signatories take account of client and beneficiary needs and communicate the activities and outcomes of their stewardship and investment to them.

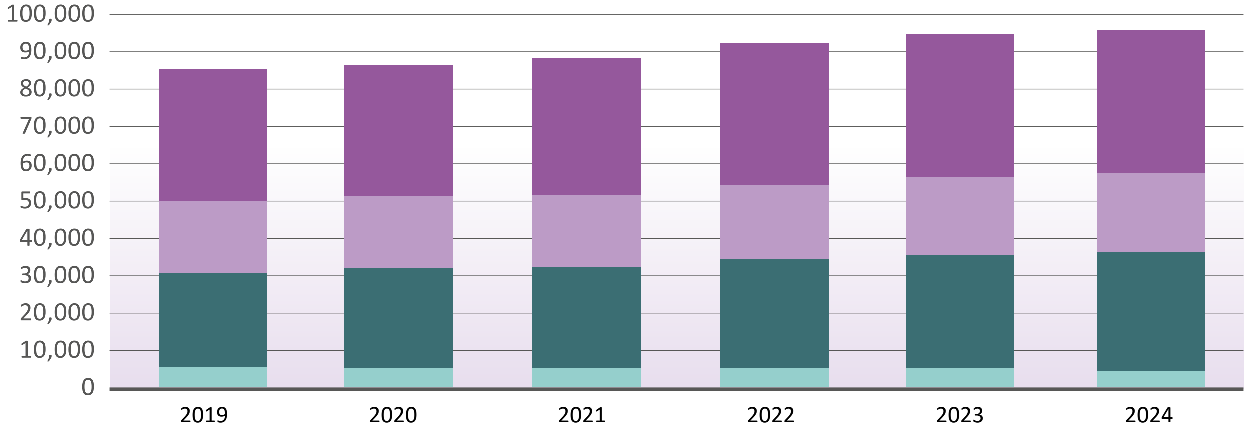
As mentioned earlier in this report, LPF is the second largest Local Government Pension Scheme (LGPS) in Scotland, which is a funded, defined benefit, statutory occupational pension scheme. We refer to our stakeholders, rather than clients and beneficiaries. LPF's stakeholders are the people and entities with an interest in the assets and activities of LPF.

Our stakeholders include the members of the pension scheme (existing and future), their dependants and beneficiaries, as well as the participating employers who contribute to the assets of the fund, and our governing bodies.

OUR MEMBERSHIP

The table and bar chart below shows a breakdown of the membership of our defined benefit scheme. As at 31 March 2024, the number of members in the scheme was 93,612. As at 31 March 2024, the average age of our members is 55 years old.

LOTHIAN PENSION FUND MEMBERSHIP DATA



	2019	2020	2021	2022	2023	2024
Active	35,014	35,874	36,149	37,207	37,614	37,590
Deferred	19,094	19,098	19,049	19,832	20,427	20,721
Pensioner	25,627	27,091	27,843	28,870	29,800	31,112
Dependant	4,199	4,229	4,173	4,161	4,155	4,189
Total	83,894	86,292	87,214	90,070	91,996	93,612

PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

Investment time horizon

The Pensions Committee considers the duration of LPF's liabilities when it sets the investment strategy to ensure that there's sufficient cash flow to pay pensions when they fall due. The Fund is open to new members and contributions which means that we'll be paying pension benefits to today's youngest members in several decades time. However, the Fund is a multi-employer fund, so we consider the different needs of those employers and offer different investment strategies to reflect their investment time horizons and cash flow needs, which vary significantly based on the maturity profile of their pension liabilities. These investment time horizons range from a few years to several decades. The different employer strategies are described on the following page.

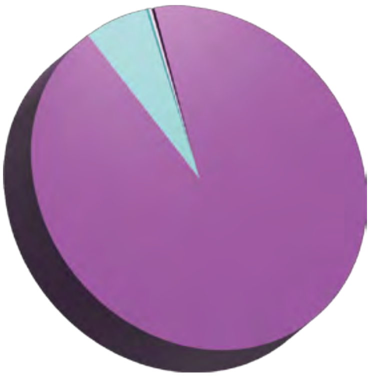
PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

AN OVERVIEW OF OUR INVESTMENT APPROACH

Employer strategies

LPF is a multi-employer pension scheme and not all employers are alike. To address their differing funding requirements the fund operates four distinct investment strategies. The assets in each strategy are shown in the table below.

EMPLOYER GROUP STRATEGIES 31 MARCH 2024



Main Strategy **94.5%** (£9,622m)

Buses Strategy **5.0%** (£505m)

50/50 Strategy **0.4%** (£37m)

Mature Employer Strategy **0.1%** (£13m)

TOTAL WEIGHT 100%
TOTAL ASSETS £10.2bn

Employers fund their liabilities with the strategy that reflects their ability to tolerate risk within an appropriate time horizon, considering the maturity of their liabilities.

Most employer liabilities are funded under the Main Strategy, which adopts a long-term investment strategy, aiming to generate an investment return that will minimise the cost to the employer within reasonable and considered risk parameters. The Main Strategy maintains significant exposure to real investments, such as Equities and Infrastructure, which have a history of protecting and growing purchasing power.

A small number of employers are funded in the Mature Employer Strategy, which invests in a portfolio of UK index- linked gilts to reduce funding level and contribution rate risk as they approach exit from the fund. The liabilities funded by the Mature Employer Strategy represent approximately 0.1% of total liabilities.

The 50/50 Strategy enables another small group of less mature employers to fund liabilities with a 50/50 mix of the Main Strategy and the Mature Employer Strategy. The liabilities funded by the 50/50 strategy represent a further 0.4% of total liabilities.

The Buses Strategy, which was created when the assets and liabilities of Lothian Buses Pension Fund were consolidated into the Lothian Pension Fund on 31 January 2019, is a 55/45 mix of the Main Strategy and the Mature Employer Strategy. As part of the recently completed investment strategy review, the Buses Strategy will move to a 50/50 mix with effect from 1 April 2024. At 31 March 2024, the Buses strategy represented approximately 5.0% of total assets.

> "I really enjoy being part of a team focused on generating positive investment outcomes for the fund, its members and employers. Working with like-minded partners on shared issues and challenges are also a really satisfying part of my role."
>
> **Albert Chen**, Portfolio Manager

PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

Policy groups

The investment strategies are described in terms of allocations to broad asset classes, or policy groups, which are the key determinants of risk and return. These policy groups are Equities, Real Assets, Non-Gilt Debt, LDI (Gilts) and Cash. Although individual investments within each group will have different risk and return characteristics, each policy group has a long-term return target, which provides perspective on the expected risk of each group in relation to Fund liabilities.

The table below presents the policy group target allocations of the four investment strategies at end March 2024 along with the total Fund strategy, which is the weighted average of the four employer strategies.

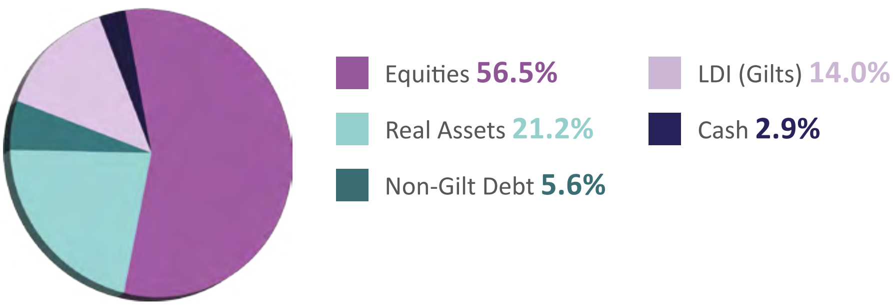
LOTHIAN PENSION FUND 31 March 2024	Main strategy	Mature Employer Strategy	50/50 strategy	Buses strategy	Total Fund Strategy
Equities	60.0%	0.0%	30.0%	33.0%	58.5%
Real Assets	20.0%	0.0%	10.0%	11.0%	19.5%
Non-Gilt Debt	10.0%	0.0%	5.0%	5.5%	9.7%
LDI (Gilts)	10.0%	100.0%	55.0%	50.5%	12.3%
Cash	0.0%	0.0%	0.0%	0.0%	0.0%
Total	**100%**	**100%**	**100%**	**100%**	**100%**

Note: In March 2024, the Pensions Committee reviewed and agreed a new Strategic Asset Allocation for the Main Strategy - to be implemented from 1 April 2024. It modestly reduces overall investment risk, via a 5% reduction in our equity investments and a 5% increase in our sovereign debt investments.

The LDI (Gilts) policy group comprises index-linked and nominal gilts (UK sovereign debt). It doesn't use financial leverage, which caused some pension funds to become forced sellers of assets in the autumn of 2022. This is the lowest risk, lowest expected return policy group as it's possible to match the cash flows of gilts with the pension payments that the Fund expects to pay in the future. The purpose of the other policy groups is to generate a return in excess of the gilt return to make the Fund affordable to employers. The other policy groups, therefore, are expected to generate higher returns over the long term - the actuary models 20 years into the future. These higher returns come at the cost of higher risk or volatility.

The Pensions Committee delegates implementation of investment strategy to the fund's officers, who are tasked with investing each policy group within specified ranges. These are laid out in the Statement of Investment Principles. The actual allocation at end March 2024 is presented in the pie chart below. The largest deviation from strategy is the underweight position in Non-Gilt Debt (-4.1%) as credit spreads are deemed broadly unattractive at current levels. The fund's exposure to Equity (-2%) and Real Assets (+1.7%), which should help protect against inflation, is broadly in line with target. Exposure to both Cash and LDI (Gilts) is above target at +2.9% and +1.7% respectively. The fund has operated comfortably within the prescribed ranges over the year.

ACTUAL ASSET ALLOCATION TOTAL FUND 31 MARCH 2024

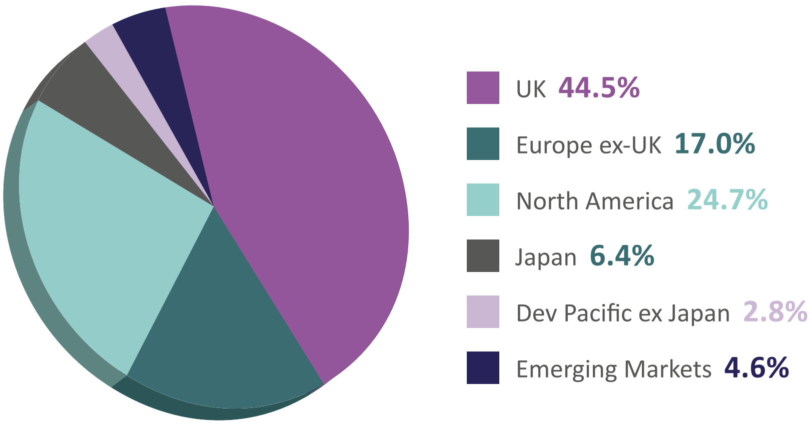


PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

OUR GEOGRAPHICAL EXPOSURE

The pie charts below show an estimated breakdown of the investments of the total fund by geography and asset class at 31 March 2024.

PORTFOLIO ANALYSIS LPF 31 MARCH 2024



PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

STAKEHOLDER VIEWS

Due to the complexity and breadth of responsible investment topics, we don't seek to directly survey our members' views on these topics. However, we benefit from deep integration of member representatives within our Pension Board and Pensions Committee, who provide the important insight that we require about our stakeholders' needs with constructive two-way dialogue.

The Pension Board's role is to provide oversight of the Pensions Committee to ensure that the pension scheme is meeting its legal and administrative requirements and is being operated in the best interest of its stakeholders. Our Pension Board consists of five member representatives and four employer representatives (as at 31 March 2024). The member representatives are union representatives from different unions (who bring insight from their constituent members in different industries but represent all pension members when they sit on the board). We ensure both large and smaller employers are represented on the Pension Board.

We also have an employer representative and a member representative on our Pensions Committee, alongside the five elected members of City of Edinburgh Council (CEC). Pensions Committee members are quasi trustees. Committee papers and minutes are publicly available for all our stakeholders to read, with a link to the relevant CEC website page provided on the LPF website. Contact details for the Pensions Committee are also provided there. The Pensions Committee therefore acts as a conduit for stakeholder views.

Our Senior Leadership Team (SLT) engages with stakeholders (including employers, elected members, Scottish Scheme Advisory Board and The Pension Regulator) in listening exercises to understand their expectations.

Stakeholder needs

Through this stakeholder engagement, we believe our stakeholders' primary needs to be:

- The provision of a secure pension entitlement for members
- Affordable and stable contribution rates for employers
- Recognition of LPF as a Responsible Investor.

Our investment approach and operating plan is driven by what is required to meet these needs. Our strategic goal to “Earn an appropriate risk adjusted investment return as responsible investors” reflects our belief that Responsible Investment and stewardship should reduce the risk associated with the invested assets that the Fund owns to pay pensions when they are due.

LPF has been a signatory to the Principles of Responsible Investment (PRI) since 2008 and demonstrates good stewardship through maintaining our status as a signatory of the UK Stewardship Code (2020), most recently confirmed in February 2024.

As explained above, we have four different employer strategies to meet the needs of our different employers, reflecting their maturity profile and hence the needs of the underlying beneficiaries. This ensures investment is aligned with an appropriate investment time horizon.

Case study

FUNDING STRATEGY AND EMPLOYER CONTRIBUTIONS

Context

Every three years LPF is required to instruct its Actuary to undertake a formal assessment of its funding position. The resulting valuation is used to review the Funding Strategy Statement (FSS) and propose amendments to employer contribution rates for the following three-year period.

Our October 2023 funding level of **157%**, up from **106%** in 2020.

FUNDING PENSION BENEFITS

Valuation Result

LPF's funding level increased from 106% at 31 March 2020 to 157% at 31 March 2023, with assets exceeding liabilities (accrued pension benefits) by £3.5bn. This was a great result, driven by both an increase in the value of assets (due to higher achieved investment returns) and a reduction in the value of liabilities (due to higher interest rates which increased the discount rate used to calculate the value of the liabilities).

Action

A draft revised FSS was presented to the Pensions Committee in December 2023, considering the indicative results of the 2023 valuation and proposed changes to the funding policy as a result. Following Committee approval of this draft revised FSS, an employer consultation exercise was carried out. The revised FSS was then approved by the Pensions Committee in March 2024.

Assessment

The positive valuation results allowed LPF to build in additional prudence when setting employer contributions, including a minor change to investment strategy (reducing exposure to equities), building in allowance for investment market volatility and increasing the target likelihood of success of achieving full funding over the time horizon relevant to employers. Even after taking these additional prudent measures, LPF was able to reduce or freeze employer contribution rates for the three-year period from 1 April 2024. Through delivery on our goal of delivering an appropriate risk-adjusted return as responsible investors, LPF is meeting our stakeholders' needs for provision of a secure pension entitlement for members as well as affordable and stable employer contribution rates.

PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

COMMUNICATION

We believe that transparency in terms of investments, communication, access to information and cross-industry collaboration are key components in protecting our stakeholders' interests and ensuring we continuously improve.

At LPF, we support our stakeholders on both a proactive and a reactive basis. Considerable time and effort is spent on proactive engagement designed to support our stakeholders. It means that we can provide clear, carefully constructed responses to frequently asked questions, demonstrating understanding of the issues, and provide insights into the work that we do and the work that's done on our behalf by third parties and collaborative partners.

Specifically on the subject of proactive responsible investment communications, we've created a library of publicly available resources on our website, including:

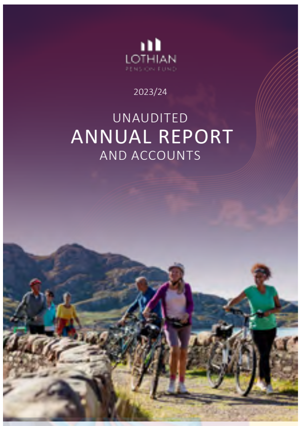
Statutory reporting:

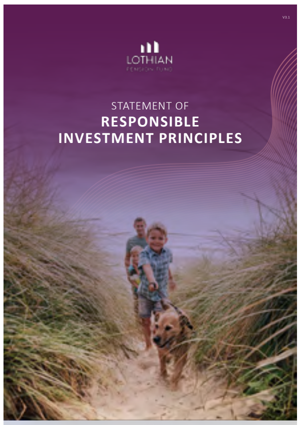
- The Annual Report and Accounts (which voluntarily includes reporting aligned with Taskforce for Climate-related Financial Disclosures)
- The Statement of Investment Principles (SIP)

Voluntary reporting:

- The Statement of Responsible investment Principles (SRIP)
- PRI Transparency report
- Stewardship Report
- Voting data
- Engagement case studies
- Internal equity approach to responsible investment
- The *ENGAGE* responsible investment newsletter

We encourage members to read, listen and understand these resources to be well informed about the nature of investing and LPF's approach to responsible investing.





PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

THOUGHT LEADERSHIP

LPF is both responsive to, and proactive in its approach to media engagement and external communications. Our Responsible Investment Lead takes an active role in contributing thought leadership through media articles and industry events.

This included involvement in the following:

- Participating in a Universal Ownership and Systemic Risks Summit at Cambridge University
- Participating in an industry roundtable on aligning expectations between asset owners and asset managers around pathways for voting escalation regarding the energy transition
- Participating in the PRI working group on reporting equivalency
- Providing training to the internal investment team as well as the Pensions Committee and Pension Board on our approach to responsible investment
- Presenting on our stewardship activities at a seminar for scheme employers
- Participating in the GAIN (Girls Are Investors Network) Empower Investment Internship Programme
- Participating in the Growing Future Assets Competition run by Future Asset through provision of judges/mentors and hosting teams of schoolchildren at the LPF office for work experience.

We also undertake reactive engagement in three broad categories:

- Freedom of information requests
- General and stewardship enquiries
- Indirect general enquiries through Councillors/MSPs/MPs.

PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

Enquiries

Both the direct and indirect general enquiries typically follow a similar format. They're enquiries either generated by a website form or downloaded from a website, suggesting that it should be directed to a local political representative. Often these enquiries are from individuals unrelated to the pension fund.

In these instances, we support busy councillors by providing standardised responses. This ensures consistent responses, speed, and greater efficiency and time savings for councillors, committee members and officers alike, as well as upholding the levels of service our stakeholders expect.

We make a pledge to our members that, when they contact us, we'll:

- Deal with the query promptly, efficiently, fairly and in an easy-to-understand way
- Communicate our service standards
- Reply as quickly as possible with information if we can't answer the query on the spot
- Treat all queries with respect
- Treat our members as individuals.

EVALUATION OF EFFECTIVENESS

Through our proactive and responsive communication strategy combined with the make-up and role of the Pension Board and Pensions Committee in our governance structure we aim to engage with stakeholder representatives from all our key constituencies. This supports our understanding of stakeholders' needs.

Based on the enquiries from Councillors and the Pensions Committee about LPF, we also believe that our public communication channels are working effectively. While we recognise that some of these enquiries may be from individuals who aren't members of LPF, we note that this engagement can be useful in reflecting broader views on emerging issues.

Over the year to March 2024, we made great progress towards our vision of delivering outstanding pension and investment services. We retained the Pension Association Standards Award (PASA) accreditation, maintained our Customer Service Excellence award with increased scores, and reported 94.7% overall customer satisfaction in our annual surveys.

Our progress towards our vision of delivering outstanding pension and investment services was confirmed by CEM, an independent benchmarking service:

- CEM's pension administration analysis shows that LPF delivers a high level of above benchmark service at below benchmark cost
- CEM's investment benchmarking reports that LPF's investment costs are significantly lower than its global peer group and their UK Local Government Pension Scheme (LGPS) universe. Over the long-term, LPF has delivered investment returns above its peer group with a lower level of risk and at lower cost.

PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

Customer Service Excellence (CSE)

We're proud to have held the Customer Service Excellence (CSE) Award (previously known as Charter Mark) since 2008.

The CSE Awards were established to provide a practical tool for service providers to drive customer-focussed change within their organisation. It's helped us to become even more efficient and effective and provide an excellent service to our members and employers.

Yearly formal assessments are carried out by a licenced certification body and we're delighted to have received successful inspections for the last 17 years.

PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

LOOKING FORWARD

LPF follows a two-year strategic planning cycle, and our planning process begins and ends with a focus on our members through an ongoing feedback loop of listening to our members when we engage with them on administration matters, and in asking for feedback through our complaints and compliments process. The process to develop our 2024-2025 Strategy and Business Plan included consulting with the Convenor of the Pensions Committee prior to its formal consideration and approval by our Pensions Committee in March 2024 on behalf of our members and employers.

The plan centres around four broadly defined strategic goals, each with more detailed objectives and accompanying targets and measures to allow us to monitor our progress.

STRATEGIC GOALS 2024-2025

How we aim to achieve the sustainability that our multi-generational obligations require

OPERATING PLAN GOALS

Develop and deliver a member and employer proposition for service excellence

- Continue to target external validation including the Pensions Administration Standards Association (PASA) accreditation, the Customer Service Excellence (CSE) award and CEM Benchmarking
- Delivery of our digital strategy to further improve our service proposition for both members and employers
- Implementation of the requirements of the McCloud judgement and the Pensions Dashboard.

Earn an appropriate risk adjusted investment return as responsible investors

- Deliver sufficient investment returns over the long term to meet funding targets
- Seek to have a positive impact on the economy and society by continuing to integrate ESG into our investment processes and demonstrating good stewardship of our assets
- Implement the revised strategic asset allocation.

Extend collaboration and services to existing partners and deepen where possible

- Continue to collaborate through successful investment partnerships
- Offer reliable and impartial advice to policy makers including the Scheme Advisory Board.

Foster a great team and a great work environment

- Empower a broad range of talents to meet organisation priorities
- Cultivate leadership competencies and develop succession plans across the team
- Give our people capacity and encouragement to contribute to our communities
- Re-locate to our new office which is better suited to the needs of our colleagues.

PRINCIPLE 6: CLIENT AND BENEFICIARY NEEDS

Through engagement with stakeholders, we recognised the need for LPF to be recognised as a responsible investor and to demonstrate good stewardship meeting the requirements of the UK Stewardship Code (2020). We published our first Stewardship Report in Q4 2021. This document is our fourth Stewardship Report.

We have also recognised the views of our stakeholders by taking on board their need for information on climate risk. This led to the creation of Responsible Investment Group (RIG) in 2021 and the initiation of the Climate Disclosure and Strategy project, which progressed through 2022-23 and concluded in 2024. This encompassed a review of evolving best practice and regulation as well as implementation challenges. One of the outcomes of reviewing evolving best practice was the reinstatement of full disclosure of our voting records on our website with further details on our voting actions provided through our *ENGAGE* publication.

Implementation

Implementation of our investment strategy is achieved using both internal and external managers. We assess all our investments with a view to meeting a required level of financial return in the context of achieving an appropriate level of risk diversification. ESG issues are an integral part of that assessment. The benefit of having an experienced portfolio manager as our in-house Responsible Investment Lead (now Head of Responsible Investment) is that we're able to integrate our stewardship and our investment decisions across the fund, according to asset type (see Principle 7).

Debt denial

We recognise that our ambition (as described in our SRIP) to avoid providing new financing to companies or projects that are incompatible with the aims of the Paris Agreement is a leadership position for asset owner climate policy. Substantial research is taking place across the investment industry on how to determine whether certain companies or specific projects are aligned (or aligning) with the aims of the Paris Agreement. Some frameworks and tools exist (such as the Transition Pathway Initiative and the Science Based Targets Initiative), but their coverage is incomplete.

For externally managed assets, such as corporate bonds, we're dependent on our external managers to implement this policy on our behalf. In 2023 we proactively wrote to all our fixed income managers outlining our responsible investment policies and commitments, requesting an update on their policies and commitments (particularly regarding net zero alignment), enhanced reporting on new (primary) financing investments, and their timelines for including product level emissions data in standard reporting. In addition, we also sent our managers the Asset Owner Diversity Project diversity and inclusion questionnaire in accordance with our commitments to this initiative. Monitoring our external managers' responses and provision of enhanced reporting is being progressed through 2024 along with a review of alternative strategies/benchmarks for corporate bond strategies.

PRINCIPLE 7: STEWARDSHIP, INVESTMENT AND ESG INTEGRATION

Signatories systematically integrate stewardship and investment, including material environmental, social and governance issues, and climate change, to fulfil their responsibilities.

The purpose of our pension fund is to pay pensions to members as they fall due over a multi-decade timeframe. As an early signatory to the PRI, we've incorporated environmental, social and governance issues into our investment decision-making since 2008. We see stewardship as an essential and integral part of our investment process.

- Our stewardship activities inform us about how companies are performing on specific ESG issues, about how proactively these issues are being managed, and about companies' wider approach to strategy and risk management
- Our stewardship activities often encourage better disclosures to support our investment research and decision-making on ESG issues
- Our investment process identifies risks and opportunities both at a stock and sector level, providing us with a prioritised list of issues to focus on in our engagement
- Our dialogue with companies often generates wider insights about trends, drivers, best practices, and relative company performance, informing ESG analysis.

"There is no such thing as a risk-free investment. ESG issues are central drivers of investment risk and return. Our job is to be aware of the relevant risks, to ensure that we're being paid for the risks we're taking, and to manage and mitigate these risks."

Gillian de Candole
Head of Responsible Investment, Lothian Pension Fund

PRINCIPLE 7: STEWARDSHIP, INVESTMENT AND ESG INTEGRATION

As discussed in Principle 2, our stewardship efforts are purposely managed within our investment team, so that they're embedded in the investment process systematically. We don't treat this as a separate activity. We encourage company management teams to improve their practices and give them time to do so. This support is not open-ended or unquestioning; if we feel progress is too slow, and the prospect of financial risk to us is increasing, we'll withdraw our support and reduce or exit an investment.

We integrate stewardship and ESG issues into our investment analysis and decision-making process.

ESG and stewardship integration

Implementation of our investment strategy is achieved using both internal and external managers. We assess all our investments with a view to meeting a required level of financial return in the context of achieving an appropriate level of risk diversification. ESG issues are an integral part of that assessment. The benefit of having a portfolio manager as our in-house responsible investment lead is that we're able to integrate our stewardship and our investment decisions across the fund, according to asset type. How ESG issues are incorporated into investment analysis and decision-making processes varies according to the asset category (but not geography) and whether the mandate is internally or externally managed. The following table explains our approach by asset category and mandate type:

Internal Equity Investment	Our portfolio managers analyse ESG data as part of the stock selection process and, on an ongoing basis, monitor ESG developments at underlying investee companies. Data and rating changes from independent providers trigger stock reviews. We aim not to provide new financing to companies or projects that are incompatible with the aims of the Paris Agreement because of the investment risks we believe it presents. We engage with existing portfolio companies to ensure climate risk is accounted for and to encourage the development of realistic transition plans. Our internal managers invest directly in listed markets and private market funds, and they monitor public and private markets with the benefit of having integrated ESG analysis into investment decision-making for many years. Our internal managers are ideally looking for investments where ESG- related improvements are in evidence with long term benefits likely to accrue to shareholders. For example, our internal managers assess and monitor the capital spending on green energy noting that much of it is undertaken by the incumbent energy providers (the diversification of carbon-extractive companies and carbon burning utilities). Through our engagement activity, we encourage positive outcomes for asset owners through good capital allocation decisions.
Internal Sovereign Bond Investment	Our portfolio managers analyse ESG reports and respond to government and market consultations, either directly or with our collaborative partners.

PRINCIPLE 7: STEWARDSHIP, INVESTMENT AND ESG INTEGRATION

External Managers	During the appointment process, we assess the managers' approaches to integration of ESG issues into their investment analysis and decision-making processes. We monitor the managers' implementation of their approach on a quarterly basis alongside all other investment matters, with ESG a standing agenda item. We engage regularly and review the PRI transparency reports of external managers, where available. Managers are encouraged to join PRI as signatories where they're not already members and also to become signatories to the UK Stewardship Code, where appropriate.
External Equity	We assess how our managers incorporate ESG into their investment process and stewardship activities. Our ambition is to appoint managers who won't provide new financing to companies or projects that are incompatible with the aims of the Paris Agreement because of the investment risks we believe it presents. We engage regularly to discuss and review holdings.
External Corporate Debt	We assess how our managers incorporate ESG into their investment process and stewardship activities. Our ambition is to appoint managers who won't provide new financing to companies or projects that are incompatible with the aims of the Paris Agreement because of the investment risks we believe it presents. We engage regularly to discuss and review holdings.
Internal Direct Property Investment	During the selection and monitoring process, we assess the environmental efficiency and sustainability credentials of properties, including physical climate risks and transition risks (investment needed to meet tightening energy performance standards). In conjunction with an appointed property manager, we ensure that ESG initiatives to mitigate risk and maximise opportunities are implemented at every stage of the ownership cycle. ESG improvement targets and performance will be incorporated into strategy through asset management plans for owned assets and all new investment acquisition appraisals. As part of our monitoring and review of direct property assets, we engage directly with tenants and build long-term relationships with them.
Real Asset (Infrastructure, Property and Timber) Investment	During the appointment process, we assess the approach of managers to incorporating ESG issues into their investment analysis and decision-making processes. We monitor the managers' implementation of the approach on a quarterly basis alongside all other investment matters, and review PRI transparency and GRESB reports of external managers, where available. Where appropriate, we seek improvement to both the management and implementation of that approach. Managers are encouraged to join PRI as signatories where they're not already members.

Case study

ESG INTEGRATION IN DIRECT PROPERTY

Background

One example of the financial materiality of ESG issues is provided by a series of legislation affecting the UK property sector, such as the Minimum Energy Efficiency Standards (MEES) for UK commercial property and the requirement for an Energy Performance Certificate (EPC).

The MEES restricts commercial landlords from letting (and hence generating an income or financial return from) energy inefficient buildings. The EPC rating is a measure of the notional energy efficiency of a building, based on its CO_2 emissions. These legislative initiatives support the drive to net zero as commercial buildings are estimated to contribute 20% of the UK's carbon footprint.

Initially introduced in 2015 in England and Wales, the MEES has the following implications for commercial property:

- 1 April 2018 – Unlawful to grant new leases of commercial property with an EPC rating of below E (the minimum standard)
- 1 April 2023 – Unlawful to "continue to let" commercial property with an EPC rating of below E (the minimum standard)
- 1 April 2025 – Requirement to register a valid EPC for let, commercial property (proposed regulation)
- 1 April 2028 (previously 2027) – The minimum standard raised to EPC rating C (proposed regulation)
- 1 April 2030 – The minimum standard raised to EPC rating B (proposed regulation)

In late 2023, the UK Government pushed back the interim deadline for commercial property to achieve a minimum EPC rating of C from April 2027 to April 2028. However, the ultimate deadline of an EPC rating of B or higher remains steadfast for 2030. With that in mind, continuing to improve the EPCs throughout our direct property portfolio is a key focus and a fundamental consideration in all our asset management and transactional decisions.

The Scottish Government plans to introduce regulations in 2025 to reduce greenhouse gas emissions from heat in non-domestic buildings.

Actions taken

Across England & Wales, all our direct property assets are fully compliant with the 2023 MEES Regulations, with no F or G rated properties. In terms of the overall portfolio, just under half of our portfolio is either A or B rated with a further 31% rated C. Improvements continue to be made via direct liaison with the occupational tenants and on lease events and vacant properties.

Case study

ESG INTEGRATION IN DIRECT PROPERTY (CONTINUED)

Fareham Trade Park, Gosport

Following the launch of the Better Building Partnership's new Green Lease Toolkit in January 2024, we conducted a review of our property leases with our external solicitors to consider how best to adopt elements of the toolkit and incorporate them within the LPF portfolio. Following this review, adjustments to the fund's adopted standard form of lease were made to expand the green lease clauses where appropriate. We also agreed to incorporate green lease clauses within Heads of Terms for all new lease transactions, to ensure that these clauses are agreed early in negotiations and incorporated into the lease. This promotes greater alignment between the fund, as landlord, and the tenant, as occupier. The overall objective is to identify areas of mutual value where co-operation between the stakeholders will improve the sustainability of commercial buildings.

A good example of this engagement and EPC improvement is at Fareham Trade Park, Gosport where, as part of the lease renewal negotiations, the tenant committed to replace gas-powered radiant heating with a more efficient air conditioning system, improving the EPC from a D rating to a B rating.

Market demand also drives improvement with new tenants seeking the most efficient and ESG focussed buildings. During vacant unit refurbishments, changes from gas to electric and improvements to L.E.D. lighting has delivered some positive improvements to EPC ratings.

Case study

ESG INTEGRATION IN DIRECT PROPERTY (CONTINUED)

Outcome

The fund was fully compliant with the MEES regulations ahead of the 1 April 2023 deadline, with the improvements made since December 2021 and more recently shown in the table below:

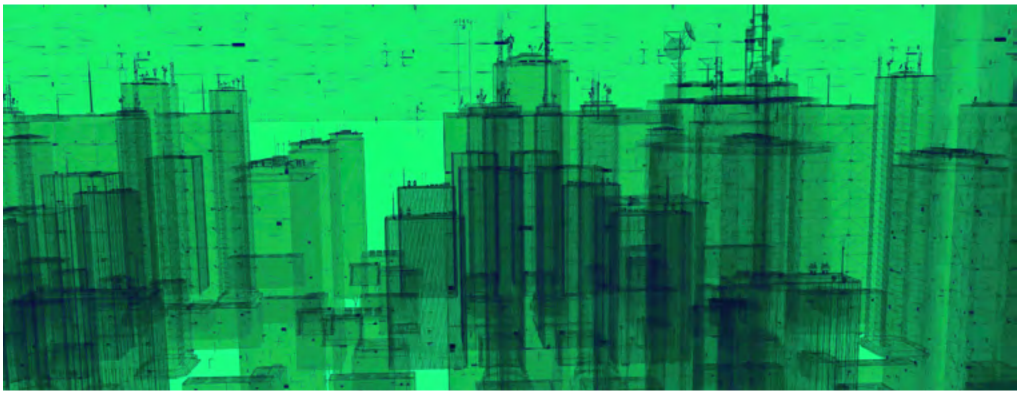
		Dec 2021	Dec 2022	May 2024
EPC Risk Rating	Red	24	0	0
EPC Risk Rating	Amber	76	93	68
EPC Risk Rating	Green	19	26	46

(Numbers reflect sales and acquisitions over this period)

Assessment and Outlook:

Our proactive approach enabled us to meet the 2023 standards ahead of the deadline. However, we continue to improve the EPC ratings of the assets within our direct property portfolio, both through refurbishment and through engagement with tenants to improve how efficiently the buildings are used, to ensure compliance with proposed regulations anticipated to come into force in future.

We're also expanding our ESG initiatives in direct property to address social issues. In conjunction with our dedicated property management team at JLL, we've conducted a review of the asset management contracts. Actions have been taken to ensure that all suppliers' employees are paid the Real Living Wage. We intend to repeat this ESG initiative regularly in line with annual changes to the Real Living Wage. The Living Wage Foundation asserts that earning the Real Living Wage, as opposed to the minimum wage, makes a huge difference to workers' productivity, mental health and family relationships.



PRINCIPLE 7: STEWARDSHIP, INVESTMENT AND ESG INTEGRATION

PRIORITY ESG ISSUES

We've identified 12 financially material ESG issues or themes that represent our engagement priorities for 2023-25. These guide our voting and engagement activity both internally and through our external engagement provider, EOS (for more information, see Principle 9). We believe they're important issues that will impact shareholder value and so deserve focus in any investment analysis.

- Climate change action
- Circular economy and zero pollution
- Natural resource stewardship
- Human and labour rights
- Human capital
- Wider societal impacts

- Board effectiveness
- Executive remuneration
- Investor protection and rights
- Business purpose, strategy and policies
- Risk management
- Corporate reporting

Within this, we prioritise what we assess to be the most material drivers of long-term value: climate change action, human and labour rights, human capital, and board effectiveness. We also identify increasing materiality to issues related to biodiversity (within natural resource stewardship), digital rights (within human and labour rights), and tax (within wider societal impacts).

OUR TOP PRIORITY: CLIMATE CHANGE

Complex, global systemic risk.

We identify climate change as our top priority for integration within our stewardship and investment processes, as this is a key systemic risk with potentially far-reaching consequences across all sectors and regions. The need for an energy transition is creating change that represents both risks to, and opportunities for, LPF. We aim to address climate change risks in two ways – through our investment selection process and through our engagement and voting activities. As part of the stock selection process for the fundamentally managed portfolios, any material climate- related risks and opportunities (such as carbon pricing and the low carbon transition) are individually assessed by the managers before acquisition and monitored once they're portfolio holdings. Both the fundamental and quantitatively managed equity funds utilise engagement with investee companies to improve practices.

In our meetings with company management, we routinely discuss how they'll align their businesses with the aims of the Paris Agreement. We encourage our external managers to do likewise and to report on their engagement activity. We believe that accurate measurement and disclosure of corporate emissions and clarity of strategic direction are key to accurately assessing the climate risk and return potential of company shares. Encouraging better disclosure remains a standard part of our dialogue with companies. Data quality remains variable depending on geography and publicly listed companies are generally more transparent than private companies.

We align our stewardship activities to achieve shared outcomes

Carbon intensity numbers are currently treated as outputs of our investment process rather than targeted inputs into the investment process. This is because these numbers are backwards-looking and fundamentally easy to "game". For investors, reported portfolio carbon intensity metrics could easily be lowered simply by selling the most carbon intensive stocks and replacing those investments with lower emission stocks. This may be optically attractive, but companies will continue to emit carbon in the same manner whether our, or any other, fund sells or retains the shares.

Strengthening corporate reporting on climate change has therefore been a key focus of our engagement efforts. We work with Climate Action 100+ to encourage better, more meaningful corporate carbon reporting from companies.

We escalate engagement with climate laggards through our voting

Through EOS we've had a formal climate change voting policy in place since 2019 targeting climate change laggards. This policy was strengthened in 2021 with the emergence of formal shareholder votes on companies' responses to the climate crisis: we support proposals that demonstrate robust target-setting, and that are aligned with external frameworks and accreditations such as the Science-Based Targets initiative; we also want to see a clear and credible strategy in place to achieve the stated targets. In 2022 and 2023, further specificity was introduced as to how Transition Pathway Initiative (TPI) assessments are used to identify climate laggards in key sectors such as Oil & Gas, Electricity Utilities, Oil & Gas Distribution and Autos, and we consider voting against the reappointment of relevant directors (see Case Study in Principle 12 for examples of the implementation of this policy).

PRINCIPLE 7: STEWARDSHIP, INVESTMENT AND ESG INTEGRATION

We need good data to build a clear roadmap of risks, opportunities and implications of climate change, so we can make informed decisions in the long-term interests of our stakeholders.

While we assess and manage climate-related risks and opportunities for all our assets, our approach differs by asset class. Above, we highlight how we use available data and tools to assess climate change risks and engage, often in collaboration with like-minded investors, to address this systemic risk. Below we provide a spotlight on how we integrate ESG considerations, including climate risk, in infrastructure investment.

We recognise the contribution that some specific sectors and industrial activities make to climate change. While there's a tendency to label companies in carbon-intensive industries as 'bad' and those in low-carbon and alternative energy businesses as 'good', investment is more nuanced than this.

We differentiate between:

- Secondary investment activity (the trading of shares) - this rarely affects the capital position of a company

    - We have a policy of engagement rather than exclusion and divestment. This enables engagement to exert influence on companies to improve their business practices, align with the Paris goals, and disclose internal management of climate-related risks and opportunities through TCFD compliant reporting. Finance theory indicates that exclusions may result in lower risk-adjusted returns while the body of empirical research reaches different conclusions depending on the time period chosen. Our inference is that divestment is a sub-optimal strategy as it provides no incentives for management to change. On climate change specifically, divestment may be having the unintended effect of shifting ownership to less climate-aware investors and directing finance-streams into "pollution-havens"
    - LPF's approach is to consider investments on a case-by case basis: in the energy sector, we consider the risk and returns available for companies with the capability to direct capital into renewables or back to shareholders, as well as to fossil fuels, and engage to encourage robust transition planning. We use TPI assessments to identify climate laggards
    - Where analysis of climate risk (or any other risk) points to poor financial outcomes we would expect to escalate engagement (including through our voting) and retain the ability to selectively divest (see Principle 11 for more details of our approach to escalation)

PRINCIPLE 7: STEWARDSHIP, INVESTMENT AND ESG INTEGRATION

- Primary investment activity (subscribing to new bonds or new equity issuance) - this provides companies with funding
  - We aim not to provide new financing to companies or projects that are incompatible with the aims of the Paris Agreement
  - We apply extra scrutiny to assessing whether to participate in initial public offerings or rights issues for our internally managed equity portfolios (see Case Study on National Grid in Principle 11) and we've communicated our expectations of our external equity managers to do likewise
  - We are engaging with our external corporate bond managers and reviewing alternative strategies/benchmarks to support the implementation of our debt denial policy.

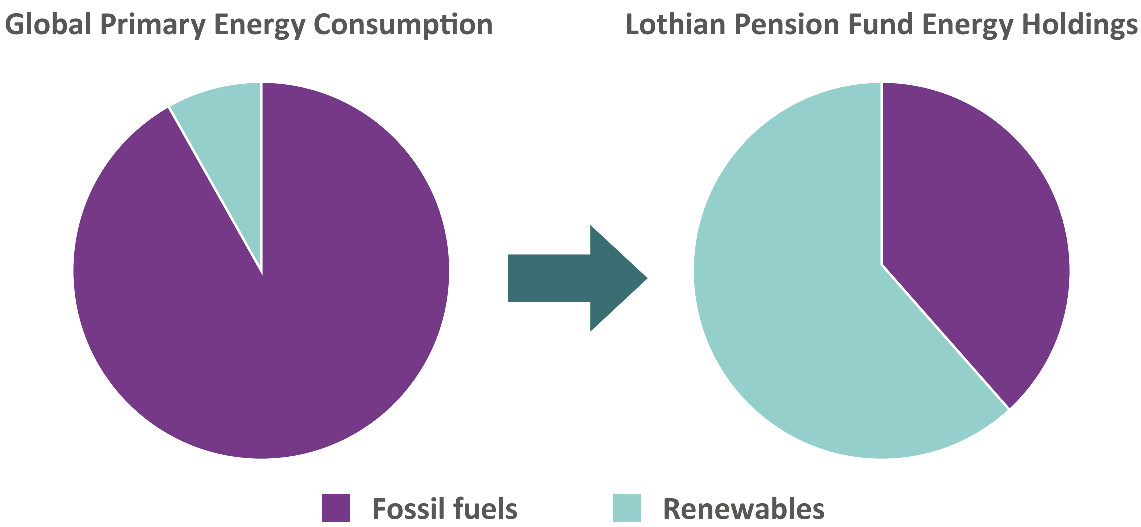
DENY DEBT, ENGAGE EQUITY

"Within our equity portfolio we engage with our holdings, and that engagement includes using the tools we have at our disposal to influence companies to commit to align with the goals of the Paris Agreement. In our debt portfolios, we aim to deny funding to those non-aligned companies."

Gillian de Candole
Head of Responsible Investment, Lothian Pension Fund

PRINCIPLE 7: STEWARDSHIP, INVESTMENT AND ESG INTEGRATION

We also invest in renewable energy projects, mainly through our infrastructure portfolio, which can be a more efficient route to access renewables exposure than through listed equities. While our exposure to fossil fuel stocks was c.2% of the total fund at 31 March 2024, our exposure to renewables exceeded this at >3% of the total Fund, illustrating that the transition of our investments away from fossil fuels is already underway, and ahead of the real economy (where 80% of global primary energy demand is still met from fossil fuels).



Sources: Global primary energy data from Reuters; LPF energy holdings data (listed equities and infrastructure investments) as at 31 March 2024

While we expect the transition of our portfolio away from fossil fuels to continue over the coming decades as the real-world energy transition progresses, we don't have a short- or medium-term target for allocation to renewables or climate solutions as we recognise that opportunities for investment returns exist across all segments and the Just Transition requires encouraging companies across all sectors and regions to transition their business models. This is why we also engage with governments and policymakers to support systemic change (see Case Study in Principle 4).

PRINCIPLE 7: STEWARDSHIP, INVESTMENT AND ESG INTEGRATION

SPOTLIGHT ON RESPONSIBLE INVESTMENT IN INFRASTRUCTURE

Our infrastructure investments have the potential to generate attractive risk-adjusted returns, with cash flows often linked to inflation.

Infrastructure investments represented 15% of the value of Lothian Pension Fund assets at 31 March 2024, comprising one of the largest and most diversified allocations among UK LGPS funds. Of the total infrastructure investment of £1.5bn (31 Mar 2023 £1.3bn), the majority is invested in the UK.

Integrating ESG in infrastructure investment

In addition to being a PRI signatory, we also subscribe to GRESB (an investor-led, sustainability benchmarking provider for real assets, covering real estate and infrastructure assets) to further enhance our analysis of ESG issues. We use the PRI and GRESB annual surveys of managers' ESG policies and activities to support our engagement with our managers, which drives improvements and implementation of best practice.

At 31 March 2024, 88% of the infrastructure portfolio value was invested in assets/funds which were also signatories of the PRI and 19% of funds participated in the 2023 GRESB Infrastructure Assessment. Most of our infrastructure funds also publish an internal ESG policy, outlining the consideration given to ESG issues within the decision-making and ongoing investment monitoring process, and this has become a standard consideration for manager selection.

Within the GRESB Infrastructure Assessments, participating funds and assets report annually to GRESB on their internal controls and policies. GRESB validates the submitted data and assesses the fund or asset with reference to a series of performance indicators, including the sustainability of its investment strategy, stakeholder relations and level of gender/diversity reporting. We use the GRESB scores to benchmark performance of these funds and assets against their peer groups.

Funds and assets across all infrastructure sub-sectors can participate in the GRESB Infrastructure assessments, but Transport and Renewable Power assets currently have the greatest participation rate within our portfolio.

We consider environmental and social factors

We recognise the role of infrastructure investment in providing facilities for a range of civic purposes as well as to address environmental challenges related to climate change. Approximately 16% of the infrastructure portfolio is invested in renewable energy. However, renewables aren’t the only way we invest in the transition to a low carbon economy. We’ve also found attractive investment opportunities in electricity transmission links (utilities), new electric or hybrid/electric train sets (transport) and energy from waste projects (environmental services). During the year, the fund allocated more than £200m to investments in social infrastructure, transport, renewables, utilities, environmental services and data infrastructure. New opportunities continue to be appraised.

PRINCIPLE 8: MONITORING MANAGERS AND SERVICE PROVIDERS

Signatories monitor and hold to account managers and/or service providers.

LPF's Supplier Management Framework sets out our consistent approach to the management and oversight of third-party suppliers in a manner which is proportionate to the contract value and importance of the service.

Before engaging with a supplier, contractual protections which allow us to exercise effective oversight are incorporated into the legal terms. For example, LPF secures:

- Clear performance and quality standards applicable to specified services, and measurement of these using 'key performance indicators' where appropriate
- Regular review meetings/calls
- Documented escalation procedures applicable where standards aren't met, with specified supplier personnel dedicated to our client relationship
- Continuous improvement initiatives to improve the efficiency and effectiveness of the service.

Key suppliers relevant to our stewardship of assets include our JIF, our global custodian, the provider of our order management system software, our engagement and voting service providers, and the providers of data and research services, including ESG information.

PRINCIPLE 8: MONITORING MANAGERS AND SERVICE PROVIDERS

MONITORING OUR ENGAGEMENT AND VOTING SERVICE PROVIDERS

We use EOS for the provision of engagement work and as our proxy voting advisor across the bulk of our listed investments. We frequently discuss voting-related issues with EOS, especially during voting season when there's a concentration of activity. We also review global developments in governance standards with them each year so we can be sure our engagement and voting policies are updated and aligned as appropriate.

EOS provides regular updates on its voting recommendations and progress on engagement activity with companies, regulators and public policy makers:

- Confidential alerts and reports provide timely updates for use by our internal portfolio managers
- Quarterly reports and an Annual Review of our voting and engagement activities are provided which we publish to our website to enable us to keep our stakeholders informed
- We participate in EOS' biannual client advisory meetings, which are an effective means of reviewing current practices, monitoring performance and providing meaningful input into engagement priorities
- We undertake regular update meetings with our client team at EOS to ensure services have been delivered to meet our needs and strive for further improvements. Key Performance Indicators include:
    - On demand access to EOSi portal
    - Timely and proactive provision of voting alerts, thematic ESG alerts, engagement progress updates and individual company case study reports
    - Execution of voting rights in line with our policy to vote 100% of our shares. We monitor voting reports on a monthly basis to verify that votes have been cast as expected
    - Scale of engagement programme coverage: details enable us to prioritise our direct and other collaborative engagements (e.g. through CA100+) on holdings not covered by EOS
- In 2023 EOS engaged with 194 companies in our portfolio on 1,085 environmental, social, governance, strategy, risk and communication issues and objectives – see Principle 9
- In 2023 EOS provided LPF with voting recommendations for 513 company meetings (7,789 resolutions) – see Principle 12.

100% of LPF's ballots were voted in 2023/24 vs 99% in the prior period. This improvement was supported by amendments that EOS made to its instructions and procedures for votes that require an administrative declaration.

Following a review and streamlining of our internal processes in 2021/22, we didn't miss any votes due to share-blocking the last two years: in certain markets investors can't trade shares in the period between registering a vote and the shareholder meeting taking place. This can create liquidity issues for investors if the voting process becomes protracted.

In addition, a small proportion of our equity investments are managed by Baillie Gifford, who carry out their own voting and engagement. As well as providing information in a quarterly questionnaire, Baillie Gifford include voting, governance and engagement information within their quarterly reporting. We meet with Baillie Gifford on a quarterly basis where we discuss in more detail various elements of their voting and engagement – in particular, areas which at first glance appear to be deviating from their stated policy. Notes of these meetings are written up for the investment team to view and any areas of interest are discussed at a formal quarterly meeting and followed up if required.

PRINCIPLE 8: MONITORING MANAGERS AND SERVICE PROVIDERS

INTERNAL MANAGER MONITORING

Portfolios managed by the in-house investment team are monitored at different levels and at different intervals. Daily reconciliations of assets between custodial and front office systems confirm that portfolios are being managed within the relevant constraints. Systems are coded to prevent managers from breaching those parameters and to alert the Risk & Compliance function of potential or actual breaches, which could occur. The Chief Investment Officer attends monthly meetings of our investment groups, which are arranged by policy group, providing oversight and scrutiny of portfolio construction and transactions. The Chief Executive Officer and the Chief Investment Officer review all mandates and reports on a quarterly basis.

All quarterly reports include detail on portfolio risk and return, portfolio construction, transactional activity, ESG analysis and engagements. The external independent advisers on the JIF review all reports every quarter and meet with each of the portfolio managers annually to provide assurance that the mandates are being managed in-line with expectations. At the annual review meeting the external independent advisers on the JIF expressed satisfaction with the internal management over 2023, including ESG integration.

The benefit of managing a substantial proportion of assets internally is that we have full transparency and that our internal managers are fully cognisant of and aligned with our policies.

EXTERNAL MANAGER MONITORING

We monitor all our external managers to ensure they continuously maintain their own responsible investment and stewardship commitments.

Equities and debt

- During the appointment process, we assess the approach of managers to incorporating ESG issues into their investment analysis and decision-making processes and in their active ownership activities
- We monitor our managers' implementation of their approach, in addition to their performance against the mandate and related investment matters (with any subsequent amendments) on a quarterly basis. Some of the content which our managers must include in their quarterly reports is specified by regulations, but we agree the extent of additional content we require to be included in such reports upon appointment. In addition to the quarterly reports that managers provide, we issue a quarterly questionnaire to address other material points, including ESG issues
- Members of our internal investment team also meet with external managers quarterly to understand any changes that might affect the management of the mandates. Both the Chief Executive Officer and the Chief Investment Officer review all external mandates with the internal investment team after these meetings.

PRINCIPLE 8: MONITORING MANAGERS AND SERVICE PROVIDERS

Private markets fund managers

- To monitor our diversified portfolio of private market funds, the largest portion being infrastructure assets, we review each manager's quarterly updates of activity, performance and portfolio construction to demonstrate adherence to the fund's agreed strategy. Monitoring includes performance, risk, ESG issues and portfolio construction relative to diversification constraints
- Our portfolio managers are in regular contact with our fund managers, attending annual investor meetings and reviewing the periodic reporting and updates received. In some cases, an LPF representative sits on the advisory board of the fund to review matters such as management of conflicts of interest which require investors' consent. This can provide greater transparency and a forum for challenge.

General

- Where available, we review external managers' PRI transparency reports, GRESB reports and/or TCFD reports
- Internal reports on our external managers are submitted for senior oversight, with any issues and escalation actions discussed at the quarterly JIF meetings.

We don't always expect external fund managers to be the “finished article”. In some instances, we'll consider selecting fund managers with less-developed approaches to responsible investment if we can be assured that there's a present and demonstrable road map towards improvement and development. One example where this may be the case is in relation to infrastructure and real estate investments, where ESG and responsible investment reporting may not be as established as in other asset classes. We believe we can add value in working with managers at this level if we're confident in the investment case and their overall philosophy.

PRINCIPLE 8: MONITORING MANAGERS AND SERVICE PROVIDERS

HOLDING MANAGERS AND SERVICE PROVIDERS TO ACCOUNT

In the past year, all of our contracts with our managers and service providers were fulfilled to our expectations, but we continue to engage with our providers on how their service provision can further improve. For example, during Q4 2023 and Q1 2024 we worked with two of our investment systems suppliers to plan and provide bespoke training for the investment team. This was to improve understanding of system capabilities to provide greater confidence and identify where processes could be made more efficient. This was well received by our investment team and it increased understanding and identified areas for continual improvement to the information displayed to aide more efficient decision making.

We also engaged with an investment system supplier to improve their customer service. They were often unresponsive, with issues taking some time to be dealt with, so we elevated the issue with the supplier who made changes internally. This has transformed the relationship and resulted in the level of outstanding issues being at an all-time low, a long-awaited upgrade being completed and more efficient access to problem resolution and implementation of improvements.

Evolving expectations on climate reporting

Following the announcement of our ambition to avoid funding companies whose business models aren't aligned with the goals of the Paris agreement, we began engaging with our managers on steps that they could take to align their practices with our aims and objectives. This is a complex area and work is currently being progressed through 2024 with a review of alternative strategies/benchmarks for corporate bond strategies.

Our monitoring (and selection) processes for external managers incorporate ESG assessments, which continue to be refined as industry practices evolve. Our policies and expectations change over time, and this is no more evident than in the climate-related commitments that we've made in our SRIP. Our approach is to work with managers, requesting change where required, and we've found a willingness to evolve alongside us, through reporting on ESG analysis and engagements, followed by discussions to gain a better understanding to ensure we're aligned. Where we're not aligned, we would ultimately terminate the mandate. One external equities mandate was terminated in the period under review, however, this was due to a reallocation of capital from equities to debt assets, while at the same time, providing a meaningful saving to LPF's costs.

In 2022 we reviewed our manager monitoring process and devised additional questions for our quarterly manager questionnaire to support alignment/assessment of alignment with our ambition. This was implemented for our external equity managers through 2022/23 and for our external debt managers through 2023/24.

Extract from our updated quarterly manager questionnaire:

"Please list all stocks or bonds purchased during the quarter that raised new equity or new debt for the company (eg. rights issues, IPOs, new bond issuance or bond conversions)."

"Please state whether your organisation or this product has made a net zero commitment."

PRINCIPLE 8: MONITORING MANAGERS AND SERVICE PROVIDERS

We monitor private market funds in a similar way, engaging to promote higher standards of reporting and identifying managers with whom we won't invest in the future due to concerns over their approach to managing climate risk.

Monitoring our managers' diversity performance

Another area we seek to address relates to the severe lack of diversity within the fund management industry. This is an ESG issue that we as asset owners and responsible investors feel strongly about, both in terms of our values and our role as a manager of managers. It also links to our commitment to promoting well-functioning markets, with a better investment industry. This is why we worked with other asset owners to establish the Asset Owners Diversity Charter (see Principle 1). As a signatory to this initiative, we've recognised that diversity for asset managers is at a critical tipping point and asset owners have a crucial role in holding them to account. We've committed to:

- Incorporate diversity questions into manager selection
- Incorporate diversity into ongoing manager monitoring
- Lead and collaborate with others in the investment industry to identify diversity and inclusion best practice.

Charter signatories will increase the pressure on fund management firms to share information about diversity, so that industry progress can be benchmarked.

"Diversity, Equity and Inclusion is increasingly being considered a business imperative in the investment and savings industry to better reflect society at large, create better financial outcomes through diversity of thought; and build a pipeline of diverse talent for the future."

Gillian de Candole

Head of Responsible Investment, Lothian Pension Fund

PRINCIPLE 9: ENGAGEMENT

Signatories engage with issuers to maintain or enhance the value of assets.

As discussed in Principle 7, we believe that a proactive combination of collaboration, engagement and voting supports our mission to pay pensions over the long term. We believe that successful engagement adds value to the investment process by promoting best practice governance and by highlighting and promoting best practice in dealing with environmental, climate change and social issues.

Also discussed in Principle 7 are the 12 key ESG issues or themes which we focus on in our engagement and in our investment research. We've chosen these because of their actual or potential financial significance to our portfolios.

Where material risks remain following engagement activity, we retain the ability to reduce our position size or sell to mitigate our exposure to these risks on a case-by-case basis.

PRINCIPLE 9: ENGAGEMENT

OUR APPROACH TO ENGAGEMENT

We commit significant resources to engagement activity, which we divide into four distinct elements as shown in the table, below.

We use a variety of engagement approaches, including written correspondence, face-to-face meetings, voting and public communications. Our preference is for direct engagement as it allows us to set out our expectations and to fully explain our interests and motivations. Irrespective of the engagement approach, the goal is always to achieve good financial outcomes for our stakeholders and to encourage positive corporate behaviour.

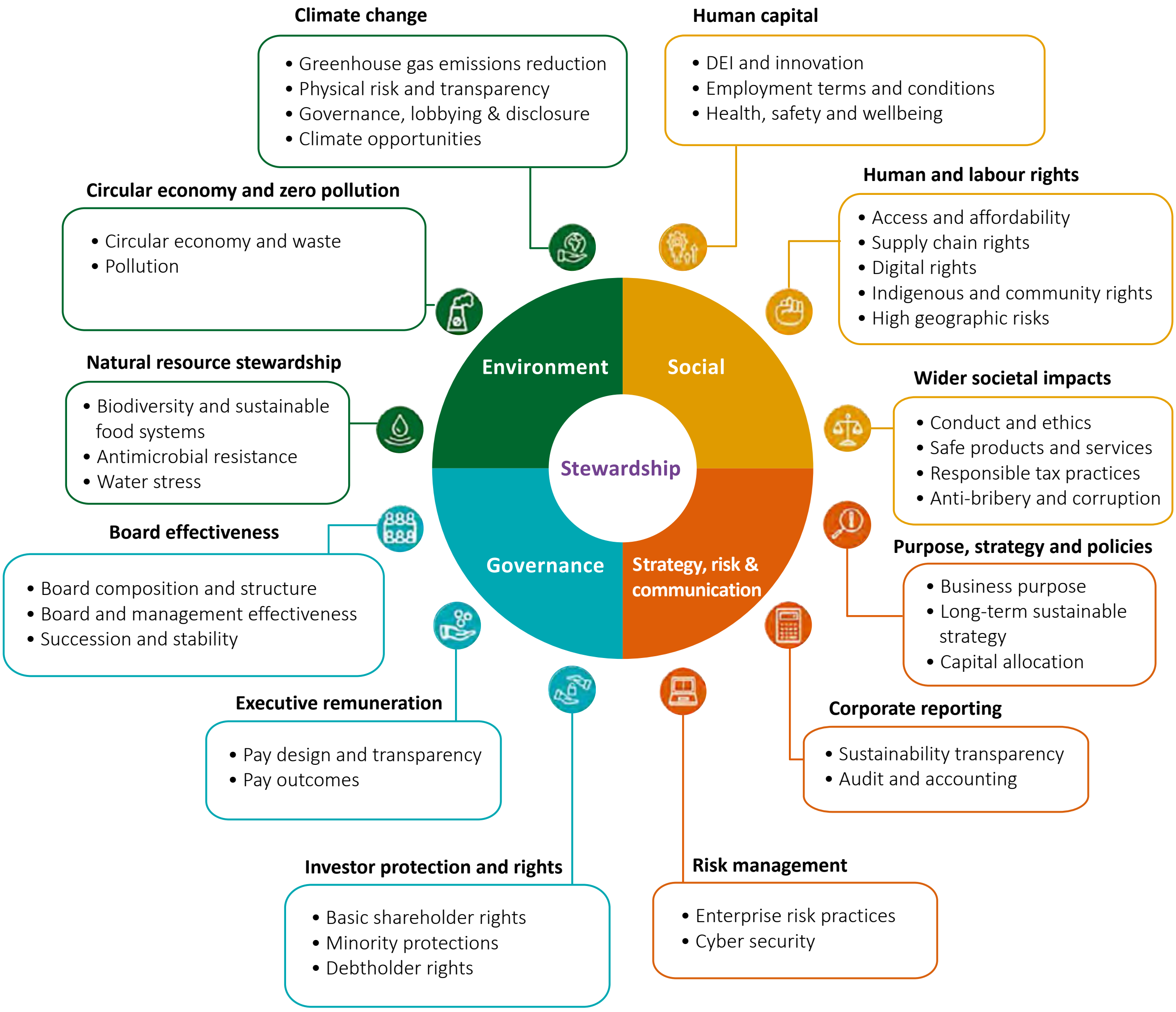
Direct engagement with companies and issuers	In situations where we have significant holdings or where companies have financially significant ESG issues, we'll look to engage directly with these companies to understand their approach. In Principle 12 we discuss how we vote our shareholdings, including how we engage with companies on proposals relevant to ESG issues that have been the subject of either direct or collaborative engagement.
Indirect engagement with companies and issuers through our investment managers	We encourage our external investment managers to engage with the companies and other entities in which they invest. As we discuss in Principle 7, we assess external managers' approaches to engagement and stewardship as part of the manager selection process. We then review each manager's approach on a quarterly basis alongside all other investment matters, and we also review the PRI transparency reports and Stewardship Reports of these external managers, where available. We regularly challenge our managers on their approach, to understand the goals and effectiveness of their engagement activities. We routinely ask our managers to sign up to the same efforts that we sign up to. This includes PRI (as required in PRI Principle 4), and Climate Action 100+.
Collaborative engagement with other investors	We recognise that there are limits to the influence that we can achieve as a single investor and the resources that we can reasonably commit. We therefore collaborate with other investors to raise awareness of and to encourage systemic change on a range of ESG issues. We provide more detail in Principle 10.
Indirect engagement with companies through an engagement service provider	We recognise that engagement can bring important benefits to our investment portfolio and the wider market. We also recognise that we, our investment managers, and the collaborations that we support, cannot cover every ESG issue at every company, with the detail and care that's needed to ensure that engagement is effective in driving improvements in company practice and performance. Working with EOS provides us with a breadth and depth of coverage that we couldn't achieve alone. In 2023, EOS engaged with 194 of the companies in which we're invested, on 1,085 environmental, social, governance, strategy, risk and communication issues and objectives. We present some data and examples of the EOS engagement below, including the outcomes that have resulted from this engagement.

PRINCIPLE 9: ENGAGEMENT

WE HAVE AN AGREED ENGAGEMENT PLAN WITH EOS

Each year, we consult with EOS to develop an engagement plan that aligns our priority issues and supports the wider goal of driving higher standards of corporate behaviour. EOS engagement themes for 2024-2026 expand on the 12 main priority themes set out in Principle 7 and are illustrated below, with 36 related sub-themes. We agreed that we would support EOS's public policy engagement (explained later in this section), as we recognise that many ESG and sustainability issues require policy interventions.

ENGAGEMENT THEMES



Case study

EOS ENGAGEMENT REPORT
META PLATFORMS

Meta is a multinational technology conglomerate based in California, USA. The company owns and operates Facebook, Instagram, Threads and WhatsApp, among other products and services.

Objective

Our engagement began in 2018 on a range of issues: how the platform works (including issues concerning manipulation of the news, lack of control over illegal content, privacy concerns and how it manages to obey the law) and its social licence to operate. These are governance and business model issues. We're engaging with the company to strengthen its policies and protections for children and young people, to better communicate progress on these issues and to demonstrate a convincing plan to address the business model flaws. We're also engaging to improve the board's effectiveness, given excessive executive compensation and its dual-class share structure, which enables CEO Zuckerberg to control the company with 61% of the voting rights while owning only 14% of its equity.

"We continue to advocate for the company to strengthen its policies and protections for children and young people, to prevent abuse and exploitation."

- Nick Pelosi, EOS, Sector Co-Lead: Technology Software

Discussion

In 2022, Meta published its first standalone human rights report. This provided some helpful information on policies and procedures, including on governing content on its platforms. It enhanced its bullying and harassment policy and expanded its policies that prohibited veiled and implicit threats. However, we remained concerned that the business model – which correlates higher revenue with higher quantities of clicks, likes, posts and shares – contributed to the spread of problematic content on its platforms. In our view, the report fell short of the highest standard for user privacy rights, which is a commitment to obtaining user consent for collection, inference, sharing and retention of their data.

In October 2022, we signed a joint letter from institutional investors to the CEO reiterating this feedback, with additional recommendations related to human rights governance, impacts of the business model and artificial intelligence. We met with the company ahead of its annual meeting in May 2023 to discuss the proxy statement. We informed the company of our voting policies with recommendations to vote against directors due to concerns about shareholder rights, executive remuneration and human rights, as well as supporting the shareholder proposal for a switch to "one share, one vote."

Outcome and Next Steps

While the company shows no intent to change its dual-class share structure or executive compensation practices, it has increased disclosure on content moderation, political advertising, data privacy and other human rights topics. Meta points to the role of its separate oversight board as a strong challenge to its own governance on these topics. However, we remain concerned about the wider societal impacts of the company's business model and our policy is to continue to support shareholder proposals calling for a switch to a "one share, one vote" structure.

Case study

BAILLIE GIFFORD ENGAGEMENT REPORT OLYMPUS

Olympus is a Japanese medical technology company that operates globally and mainly manufactures medical and surgical endoscopes. It provides a comprehensive line-up of solutions for early diagnosis and minimally invasive therapy, suitable for a range of diseases. Olympus is the market leader in gastrointestinal endoscopic equipment with approximately 70% market share.

Objective

We met with the CEO of Olympus, Stefan Kaufmann, to understand its status in the remediation of issues raised in recent warning letters from the Food and Drug Administration (FDA) relating to the manufacturing process of their endoscope products. The meeting sought to cover the underlying drivers of the FDA complaints and establish a starting point for future monitoring and engagement.

Discussion

The underlying drivers which led to the FDA letter were discussed and the CEO shared that part of the cause was a clash between Japanese manufacturing practices and American regulation and disjointed internal systems that led to longer feedback loops. Mr Kauffman also acknowledged that strengthening internal information flows between teams could have facilitated more effective issue escalation.

The CEO commented that Olympus is currently working on improving the capacity of its quality assurance and product safety team, that he now believes to be industry leading. To fix the issue, Olympus is implementing new IT tools to create faster feedback loops while also promoting a culture of openness to better enable the escalation of issues. Part of the incentives to enable this change include the introduction of product quality-related targets in its employee bonus scheme.

Outcome

We came away from the meeting positive about the directionality of remediation and with a greater understanding of Mr Kaufmann’s efforts to improve patient outcomes. The meeting provided insight into Olympus’ ongoing efforts to address the FDA’s concerns. The engagement also provided us with some data points for future monitoring.

Case study

LAPFF ENGAGEMENT REPORT
COMPANY PRODUCT USE IN CONFLICT ZONES

The Local Authority Pension Fund Forum (LAPFF) has noted an increasing scale and intensity of armed conflict globally in the last few years and is concerned both about its social and environmental impacts and, consequently, its financial impacts. Through its participation in the Investor Alliance for Human Rights pilot project on conflict-affected and high-risk areas, LAPFF has learned that companies operating in conflict zones need to be undertaking heightened human rights due diligence in line with UN Guiding Principles on Business and Human Rights.

Objective

LAPFF sought engagement with several defence and manufacturing companies regarding humanitarian and human rights impacts in high-risk and conflict-affected areas such as Gaza. It's important for companies operating in or providing products and services involved in conflicts, to recognise their heightened risks and responsibilities when it comes to upholding human rights standards.

LAPFF aims to ensure companies are implementing robust human rights due diligence practices and are adhering to international standards. Failure to do so could leave a company open to reputational damage, erosion of public trust and legal liabilities.

"LAPFF has learned that companies operating in conflict zones need to be undertaking heightened human rights due diligence."

Discussion

In Q1 2024, LAPFF sent letters to several companies in the defence and industrials sectors, including Lockheed Martin and Caterpillar. LAPFF sought to better understand how these companies manage human rights risks associated with use of their products, particularly in the context of conflict zones.

Outcome and Next Steps

LAPFF received replies to these letters from Lockheed Martin and Caterpillar, who provided links to their respective human rights policies, but didn't provide substantive responses on the issues. LAPFF has arranged a meeting to discuss these issues with one of the other defence companies to which it sent a letter and is still awaiting a response from another (at the time of writing).

PRINCIPLE 9: ENGAGEMENT

LPF ENGAGEMENT WITH MANAGERS

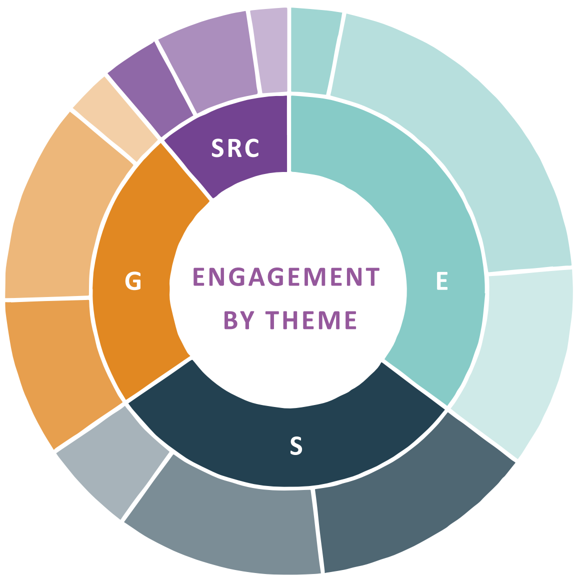
As mentioned in Principles 7 and 8, over recent years we've been engaging with our managers on steps that they could take to align their practices with our Responsible Investment aims and objectives, in particular, our ambition to avoid funding companies whose business models aren't aligned with the goals of the Paris agreement. This is a complex area and work is currently being progressed through 2024 with a review of alternative strategies/benchmarks for corporate bond strategies.

PRINCIPLE 9: ENGAGEMENT

2023: AN OVERVIEW

In 2023, EOS engaged with 194 of our portfolio companies on 1,085 environmental, social, governance, and strategy, risk and communication issues and objectives. The charts below show the breakdown of companies engaged by region and the spilt of engagement by theme.

- Developed Asia 11.9%
- Emerging & Developing Markets 2.1%
- Europe 24.2%
- North America 46.4%
- United Kingdom 13.9%
- Australia & New Zealand 1.5%



ENVIRONMENTAL 35.2%
- Circular Economy & Zero Pollution 8.9%
- Climate Change 58.4%
- Natural Resource Stewardship 32.7%

SOCIAL 30.2%
- Human & Labour Rights 42.7%
- Human Capital 39.3%
- Wider Societal Impacts 18.0%

GOVERNANCE 23.2%
- Board Effectiveness 38.6%
- Executive Remuneration 49.6%
- Investor Protection & Rights 11.8%

STRATEGY, RISK & COMMUNICATION 11.2%
- Corporate Reporting 30.6%
- Purpose, Strategy & Policies 48.8%
- Risk Management 20.7%

PRINCIPLE 9: ENGAGEMENT

Milestone status of engagement

To measure progress and achievement of engagement objectives, EOS use a four-stage milestone strategy.

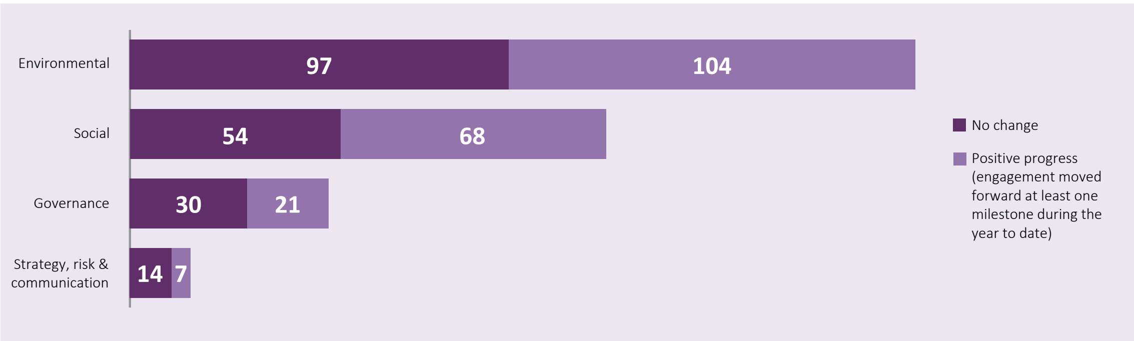
MILESTONE 1: Concern raised with the company at the appropriate level

MILESTONE 2: The company acknowledges the issue as a serious investor concern

MILESTONE 3: Development of a credible strategy/stretching targets set to address the concern

MILESTONE 4: Implementation of a strategy or measures to address the concern.

EOS made solid progress in delivering engagement objectives across regions and themes. At least one milestone was moved forward for about 51% of its objectives during the year. The following chart describes how much progress has been made in achieving the milestones set for each engagement.



PRINCIPLE 9: ENGAGEMENT

ENGAGEMENT WITH REGULATORS AND POLICYMAKERS

EOS engages with policymakers for a more sustainable financial system. This is achieved through engagements and meetings with government officials, financial regulators, stock exchanges, industry associations and other key parties. It also participates in public consultations. In 2023 EOS undertook several public policy engagements, including responding to the UK's Financial Conduct Authority's Consultation on Listing Rules and the Financial Reporting Council's Consultation on the UK Corporate Governance Code.

LPF supports EOS's public policy engagement, recognising that many ESG and sustainability issues require policy interventions. As mentioned in Principle 4, we explicitly supported EOS' response to proposed changes to the UK listing rules reiterating our view that standards for governance and minority shareholder protection rights should not be lowered.

EOS participates in sign-on letters on ESG policy topics which it supports. For example, in July 2023 EOS signed an open letter to the UK Secretary of State for Energy Security and Net Zero welcoming an amendment to the Energy Bill, which included a specific net zero and carbon budget objective as part of the mandate for Ofgem, the UK's electricity and downstream natural gas regulator.

LPF also participated directly in advocating for regulators to ensure system-wide resilience to climate change. (More detail on how we worked with the Institutional Investors Group on Climate Change to engage with the Bank of England in its role as the Prudential Regulatory Authority, is provided in Principle 4.)

PRINCIPLE 10: COLLABORATION

Signatories, where necessary, participate in collaborative engagement to influence issuers.

LPF is committed to working collaboratively to increase the reach, efficiency and effectiveness of our Responsible Investment activities. We work with a host of like-minded partner funds, service providers and related organisations striving to attain best practice in the industry and to improve industry standards. A list of our collaborative partners and their roles is publicly available on our website.

We work with others towards common goals

There are limits to the influence that we can achieve as a single investor and the resources we can reasonably commit. We recognise that progress can be best achieved on ESG issues through collaboration with other investors and organisations and we take a very active role in several of the Responsible Investment initiatives below.

Collaborative Initiatives and Industry Bodies

We've been a signatory of the UN-backed PRI since 2008 and align our practices and processes to their six principles and definition of Responsible Investment. Our SRIP formally acknowledges the role and integration of the PRI's six principles within our investment process.

PRI Principle 5:
“We will work together to enhance our effectiveness in implementing the Principles."

Advance was launched in December 2022 aiming to protect and enhance risk-adjusted returns by advancing progress on human rights through investor stewardship. LPF is an endorser of this PRI-led collaborative initiative.

CA100+ is an international collaborative initiative by institutional investors representing over $50 trillion in assets. Signatories to Climate Action 100+ engage with the boards and senior management of companies to take necessary action on climate change [See case study on page 90 for more details].

The Institutional Investor Group on Climate Change (IIGCC) is the leading European-focused investor membership organisation for collaboration on climate change with a network of over 400 European investors, representing over $65 trillion in assets. LPF joined IIGCC in 2020 to further the work we do alongside other like-minded asset owners. The workstreams at IIGCC include: the Policy Programme; the Corporate Programme; the Investor Strategies Programme.

PLSA is a trade association for those involved in designing, operating, advising and investing in all aspects of workplace pensions.

The Investment Association (IA) is the trade and industry body for UK Investment Managers. LPF became a member in November 2023, providing access to a range of resources to support us in our day-to-day roles, including Sustainability & Responsible Investment.

TPI is a global initiative led by asset owners and supported by asset managers. It assesses companies' preparation for the transition to a low-carbon economy, supporting efforts to address climate change. In our SRIP, we've committed to benchmarking holdings against TPI's management quality assessment as a measure of financial risk.

GRESB is an investor-led, sustainability benchmarking provider for real assets, covering real estate and infrastructure assets. It's a key driver of transparency regarding energy consumption data, particularly for standing real estate. We support this collaborative initiative as an investor member.

We've been clients of EOS since 2008 and they manage most of our voting and engagement activity. Our Internal Equities team work closely with EOS in our collective approach to engagement, reflecting the areas of stakeholder interest and concern. Through working collaboratively with EOS, and alongside EOS's international client base, we're able to have a stronger voice when engaging with our investee companies. We provide more detail in our text on Principle 9.

LOTHIAN
PENSION FUND

LAPFF is a collaborative shareholder engagement group, comprising over 80 UK local authority pension funds and six of the LGPS pension fund pools in England and Wales. A member of LPF's Pensions Committee is on the executive board of LAPFF, representing LAPFF and its member funds in high level engagement with company management.

Global Investor Commission on Mining 2030 - in 2023 we became an investor supporter of this initiative, which seeks to develop a socially and environmentally responsible mining sector by 2030, recognising that the sector poses a range of ESG issues, while also providing critical minerals for society and the low carbon transition.

Asset Owner COuncil

Formed in early 2024 by the merger of the UK Asset Owner Responsible Investment Roundtable (also known as the UK Asset Owner Roundtable) and the Occupational Pensions Stewardship Council, it aims to be a forum for sharing best practice on investor stewardship and responsible investment implementation and to support engagement with regulators in a coordinated way. LPF is an active participant and a member of the steering committee.

The Asset Owner Diversity Charter was formed with an objective to formalise a set of actions that asset owners can commit to in order to improve diversity, in all forms, across the investment industry. Signatories collaborate to build an investment industry which embodies a more balanced representation of diverse societies. It's now part of the Diversity Project, which aims to accelerate progress toward a more inclusive culture in the investment and savings sectors across all demographics, including gender, ethnicity, sexual orientation, age and disability.

And supporting charities:

Working with high school girls throughout Scotland to promote careers in investment management, Future Asset strives to open up the industry to poorly represented pools of talent. The investment industry has a well-known gender diversity problem, and LPF's investment professionals support Future Asset events acting as presenters and mentors for the girls, as well as providing work experience.

Girls Are INvestors (GAIN) is a charity set up by investment professionals to improve gender diversity in investment management by building a talent pipeline of entry- level female and non-binary candidates. In 2023 LPF recruited a summer intern through GAIN.

Case study

COLLABORATIVE ENGAGEMENT: CLIMATE ACTION 100+

Six years in, Climate Action 100+ (CA100+), the collaborative engagement initiative that targets the world's biggest emitters, has now launched phase two of its programme, set to run until 2030.

The UN's first global stocktake on climate change served as a stark reminder of the significant physical climate risks in an economy misaligned with the goals of the Paris Agreement. The UN's technical report, published in September 2023 ahead of COP28, concluded that the world wasn't on track to limit global warming to 1.5°C above preindustrial levels and urged the raising of ambitions to accelerate the energy transition with transformation needed on all fronts.

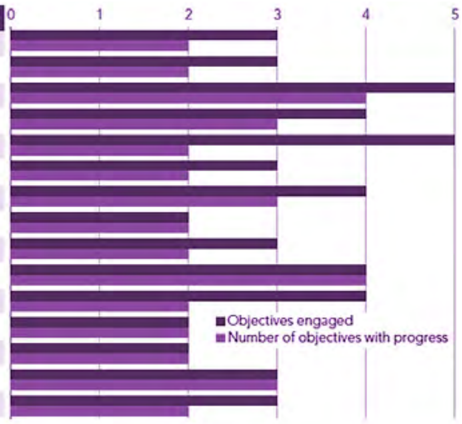
CA100+ is responding to this need for urgent action by increasing its emphasis on the implementation of robust transition plans – disclosure and pledges are no longer enough.

Encouragingly, in the run up to COP28, policymakers started to raise the bar on climate action, with a methane charge on oil and gas producers in the US and carbon border adjustment mechanisms planned in Europe. In tandem, the Science Based Targets initiative (SBTi) published more sector pathways, providing glide paths for companies in hard-to-abate sectors. The challenge for companies is to develop and implement transition plans and decarbonisation strategies in line with these pathways.

Investor engagement on climate change remains vital to help steward companies through the major transformation required to adequately manage climate risks. Phase two of CA100+ recognises this with an updated Net Zero Company Benchmark, to drive greater company ambition, plus new sector and thematic engagements. This new phase should support more intensive engagement on companies' decarbonisation strategies, capital allocation alignment, climate governance and emissions performance.

Progress of environmental objectives for selected CA100+ companies engaged by EOS, 2023

Company Name	EOS Sector	Participation
Air Liquide	Chemicals	Co-lead
Dow	Chemicals	Co-lead
LyondellBasell Industries	Chemicals	Co-lead
Lockheed Martin	Industrials	Co-lead
Exxon Mobil	Oil & Gas	Support
Shell	Oil & Gas	Support
Suncor Energy	Oil & Gas	Support
Glencore	Mining & Materials	Support
thyssenkrupp	Mining & Materials	Support
Hon Hai Precision Industry	Tech Hardware & Equip	Co-lead
Caterpillar	Transportation	Support
Bayerische Motoren Werke (BMW)	Transportation	Co-lead
Mercedes-Benz Group	Transportation	Co-lead
Volkswagen	Transportation	Co-lead
Power Assets Holdings	Utilities	Co-lead



Source: EOS data

LPF committed internal engagement resource to CA100+ by becoming a participant member of CA100+ in 2020 and co-leading engagements with a focus company. In addition to direct engagement as part of CA100+, we encourage our external managers to support the initiative.

Our engagement provider EOS, also a significant supporter of CA100+, is leading or co-leading engagement on 21 of the CA100+ focus companies across Europe, North America, and Asia.

Case study

COLLABORATIVE ENGAGEMENT: CLIMATE ACTION 100+ (CONTINUED)

For example, in March 2023 EOS met with ConocoPhillips to scrutinise the scenario analysis underpinning its capital allocation decisions. The company stated that it uses four scenarios, all of which are consistent with 1.5°C, but didn't plan to adopt the International Energy Agency's "NZE by 2050" scenario. Following a request from EOS for the company to disclose the differences in assumptions between its internal scenarios and the "NZE by 2050" scenario, ConocoPhillips has since explained that its internal scenarios assume an earlier use of direct air capture, nature-based offsets, carbon capture and sequestration technologies. The credibility of these assumptions will be a focus of ongoing engagement.

In the case of ConocoPhillips, engagement identified significant improvement to its climate strategy compared to laggard companies, not least its target of near-zero methane intensity by 2030. EOS therefore recommended support for the company's directors at the annual meeting in May, while encouraging further progress, including on Scope 3 (value-chain) emissions.

Outcomes

By participating actively in the CA100+ initiative, our officers and service providers have influenced real change, including an accelerated timetable for methane emissions reductions and a change to the corporate lobbying practices of companies with significant carbon emissions.

In October 2023, the CA100+ Net Zero Benchmark tracked further progress with 77% of focus companies committed to net zero by 2050 across at least Scope 1 and 2 emissions (up from 75% last year). Also, 87% of focus companies had set medium-term emissions reduction targets (up from 81% last year).

Assessment

We believe that such collaborative engagement actions have assisted the target companies in becoming better prepared for a net-zero world. Equally, we recognise that CA100+ focus companies still have significant work to do to align their businesses to achieve a net zero world.

However, in many sectors, companies are reliant on the policy environment to guide how decarbonisation will look in different regions. For example, transitioning gas utility companies could opt for decarbonisation strategies based on district heating, electrification via heat pumps or hydrogen heating. Companies are understandably unwilling to commit significant capital expenditure to one solution over another where policy has yet to guide investment. In these cases, we're asking companies to outline a roadmap for decision-making on technology, so that delayed policy guidance doesn't perpetuate planning for business-as-usual.

We continue to engage to encourage companies to assess and disclose the financial consequences of the risks and opportunities that arise from their own climate-related actions and the systemic economic impacts of the energy transition and climate change. We're increasingly scrutinising and engaging companies to ensure that their lobbying of policymakers helps rather than hinders the development of responsible climate policy.

PRINCIPLE 11: ESCALATION

Signatories, where necessary, escalate stewardship activities to influence issuers.

We aim to engage proactively and constructively in public and private markets, with companies directly or via external managers. As we illustrate in this report, our stewardship activities include:

- Direct engagement with investee companies and issuers
- Collaborative engagement with companies, including with CA100+
- Abstaining or voting against management (including against specific directors and against the annual report and accounts)
- Requiring our external managers and/or engagement service provider to undertake engagement with investee companies and issuers
- Engaging with policymakers and regulators to support companies’ long-term planning
- Using the media and other forums to challenge companies
- Using the insights from engagement to inform our investment research and decision-making.

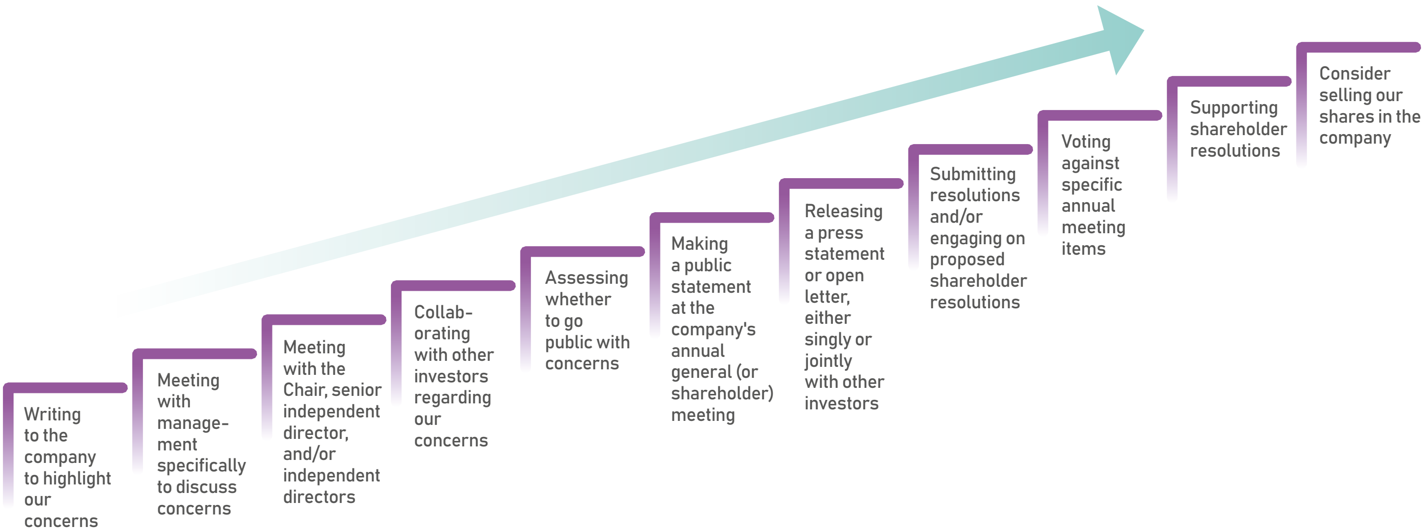
Given the range of assets in which we invest, we don't have a universal escalation policy. Instead, we tailor our approach to the investment type and the scale of the issues identified. We prefer to engage through dialogue for improvement, but we'll escalate our concerns if necessary improvements aren't forthcoming.

PRINCIPLE 11: ESCALATION

Escalating concerns with companies in which we invest

We expect companies to advise us when there are material changes and issues which impact long term shareholders. Our initial position is to support the board and management to improve their corporate strategy to the benefit of shareholders.

When appropriate and where we have concerns, we'll begin a dialogue (either directly or through EOS, our engagement and voting service provider, or other collaborative initiatives) and put forward proposals for the board's consideration. If our concerns aren't adequately addressed, we may consider a range of escalation options as part of the escalation process illustrated below:



As no two engagement escalations are the same, different steps may be taken at a different order for different cases. However, selling our shares isn't among the first steps. It's often the last step on the long escalation ladder, as engaging and addressing an issue in an undervalued firm, can create financial returns for long-term investors.

PRINCIPLE 11: ESCALATION

Escalating ESG concerns with external managers

We also set clear expectations of stewardship in our mandates with external investment managers. We challenge them if we feel that they're not delivering on the stewardship commitments they've made to us. If we're concerned about an investment manager's performance (which we'll capture in our monitoring reports), and if the investment manager hasn't improved following feedback from us, we have a range of escalation options available to us, as outlined below.

Typical escalation options:

- Notifying the external manager about their placement on a watch list
- Engaging the external manager's board or investment committee
- Reducing our exposure to the external manager until any non-conformances have been rectified
- Terminating the contract with the external manager (or not reappointing them) if failings persist over a period of time.

Escalating concerns through our engagement and voting provider

As we discuss in Principles 9 and 12, EOS provides us with an engagement and voting service which involves engaging with the publicly listed companies in our portfolios and providing us with voting recommendations for these holdings. Generally, EOS' preference is to engage with companies. This is generally only escalated into voting against management in situations where engagement is proving to be ineffective. However, in 2021 EOS introduced a more proactive approach to use voting to target laggards on climate change and in 2022, they introduced another policy to consider voting against relevant directors where there are significant concerns about a company's actions relating to human rights. We strongly support this approach. We generally support EOS' voting recommendations, but we scrutinise their recommendations and do, infrequently, vote in a different way (e.g. if we think it's premature to escalate or if we think that it's time to escalate and EOS hasn't recommended it). In 2023 there were no occasions where we voted differently from EOS' recommendations (see Principle 12).

Escalating concerns in private markets

While the options available to us in terms of escalation of stewardship activities to influence issuers in closed ended investment funds (private equity, private debt, infrastructure and indirect property asset classes) are more limited, we do make it clear that concerns or a lack of transparency will feed into the assessment of subsequent investment opportunities presented by that manager.

Case study

ESCALATION WITH NATIONAL GRID - UPDATE

Background

National Grid plc is a multinational electricity and gas utility company with operations in the UK and the US. Its principal activities are operating electricity and natural gas networks as well as distribution and supply of electricity and gas. We consider National Grid to have a critical role in decarbonising UK electricity, while also recognising the risk that grid capacity issues and new connection delays could slow the deployment of clean energy.

While National Grid's management of climate risks was scored highly by the Transition Pathway Initiative, its decarbonisation strategy was still trailing what we considered necessary for a utility company operating within the UK, given the UK has committed to decarbonisation of its electricity power market by 2035. This highlighted the need for National Grid to devise a more ambitious plan.

Engagement and Escalation

As we reported in our 2023 Stewardship Report, in Q4 2022 we supported an escalation of engagement with National Grid by co-signing a letter (coordinated through LAPFF and CA100+) to the Chair, Paula Reynolds, calling on the company to enhance its commitment and collaborative efforts to accelerate the transition to a cleaner and more secure energy future. The letter appealed for urgent, ambitious and proactive action to be taken in regard to decarbonisation, including setting out its plans to invest in necessary electrical infrastructure and distribution systems.

Progress

In April 2023, National Grid revealed the creation of its Strategic Infrastructure business unit dedicated to delivering major strategic UK transmission projects and in May 2024 National Grid announced a rights issue, seeking to raise over £6bn of new equity to help fund its £60bn capital expenditure plan over the next five years. This investment opportunity was reviewed by our Head of Responsible Investment as well as the relevant Portfolio Manager. As the rights issue would provide the company with new financing, we needed to be confident that subscribing would be in line with our stated ambition to only provide new financing to companies or projects that are compatible with the aims of the Paris Agreement (see Principle 7 for more details about how our approach to climate change differentiates between primary and secondary investment activity).

Outcome

As funding investment in energy transition infrastructure was the main purpose of the capital raise, with 85% of the company's new investment plan directed to green investment (as defined by the EU Taxonomy), we were comfortable subscribing to the rights issue from a responsible investment perspective, as we believe it's compatible with the aims of the Paris Agreement.

National Grid successfully raised c.£7bn of new financing with the new shares commencing trading on 12 June 2024.

Assessment

While our role in the 2022 escalation was fairly minor, by co-signing the letter we signalled our support for real-world action on decarbonisation. We're therefore pleased to see the company respond with a significant increase in its investment in necessary electrical infrastructure and distribution systems, alongside an update to its financing strategy to create an interesting investment opportunity.

The integration of our responsible investment expertise within our investment team allowed for timely analysis of the rights issue, integrating ESG issues within our investment process, in line with our responsible investment policy.

PRINCIPLE 12: EXERCISING RIGHTS AND RESPONSIBILITIES

Signatories actively exercise their rights and responsibilities

We believe that responsible investment involves exercising our rights and responsibilities as an active owner. We consider voting to be an integral part of our engagement with companies.

We aim to vote on all resolutions tabled at the General Meetings of our investee companies (listed equity) and also on all LPF consent matters within the funds we've invested in (across private market asset classes). We also hold our managers to account on how they exercise rights and responsibilities on our behalf, for example, how our debt managers exercise their responsibilities to integrate ESG in credit investment through the negotiation of ESG-linked ratchets into loan documentation.

In Principle 8 we explain how the practice of share-blocking in certain geographies (e.g. Norway) can impact our ability to fully exercise our rights and responsibilities in these markets due to potential liquidity constraints. However, following a review and streamlining of our internal process for approving votes in share-blocking markets in 2021/22, we didn't miss any votes due to share-blocking in 2022 or 2023.

In Principle 4 we provide examples of exercising our rights and responsibilities by engaging with policymakers and responding to industry consultations. In Principle 7 we provide a case study on ESG integration in direct property which includes exercising of our rights and responsibilities to meet increasingly stringent minimum energy efficiency standards as a commercial landlord.

Our voting policy for listed equity investments

Voting, in combination with engagement, can reinforce the message we send to company management about how they're running their businesses. While much focus tends to be on controversial votes and votes against management, we think it's equally important to signal our support for management in situations where they're doing a good job of navigating risks, challenges and complexities. As can be seen from our voting data below, we recognise that, in most cases, boards are managing these issues effectively and we continue to support them in their endeavours.

We subscribe to a specialist third party service (EOS) to provide engagement (see Principle 9) and to provide proxy voting recommendations to us which covers approximately 96% of our listed equity investments (the remainder of our equity assets are in funds where our external managers undertake voting in accordance with their voting policies, which we monitor quarterly). Through EOS we monitor what shares and voting rights we have and apply an ESG lens informed by active engagement over the top of proxy voting recommendations provided by Institutional Shareholder Services Inc. (ISS), a proxy voting service provider whose primary research and proxy voting infrastructure is utilised by EOS.

PRINCIPLE 12: EXERCISING RIGHTS AND RESPONSIBILITIES

EOS' Global Voting Guidelines act as a policy to inform EOS' voting recommendations. EOS applies local market conventions in 20 markets around the world as a final overlay in the voting decision-making process, where EOS has developed region-specific principles due to different governance conventions across global market. These set out the fundamental expectations of companies, including on business strategy, communications, financial structure, governance and the management of social and environmental risks in each region. Generally, we follow EOS's voting policy and voting recommendations which are informed by their engagement with companies.

Generally, we follow EOS's voting policy and voting recommendations which are informed by their engagement with companies. However, we reserve the right to override EOS voting recommendations. In recognition of the value of active engagement, EOS works with our internal and external fund managers to co-ordinate and execute voting instructions. We require EOS to provide our portfolio managers with notice of voting instructions and allow them to override any EOS recommendation.

Whenever there's a controversial vote (e.g. a recommendation to vote against management) or when there's an issue that we're concerned about (e.g. a governance risk identified through our own investment research and direct engagement activities), we'll communicate with EOS about the resolution, to understand the context and their reasons for the recommendation being made. In practice the number of voting recommendations that we override each year is minimal. In 2023 we didn't override any, but significant consideration is given to each issue, with EOS voting alerts reviewed by the equity team and escalated to our Responsible Investment Group (RIG) where necessary.

Case study

2023 "SAY ON CLIMATE" VOTES

Background

Launched in 2020, the Say-on-Climate initiative encourages companies to consult shareholders about their climate strategies and net zero action plans at their annual general meetings. The number of companies providing these ballots doubled during the first two years of the initiative, however the number of management-proposed Say-on-Climate proposals dropped in 2023.

There were also several climate-related shareholder resolutions, including some filed by Follow This (a Dutch non-governmental organisation of activist shareholders), requesting that companies set comprehensive greenhouse gas emissions targets that are consistent with the goals of the Paris Agreement.

When exercising our equity voting rights, we're guided by EOS's proxy vote recommendations which consider both global best practice and regional governance requirements. EOS applies a rigorous case-by-case approach to assessment of transition plans and progress reports, only recommending support of plans that demonstrate robust targets and a clear and credible strategy to achieve the stated targets.

Voting activity and outcomes

Examples of how we voted in 2023 on climate plans or emission reduction targets are presented in the table with an explanation and assessment below .

	Management Proposed Say-on-Climate Vote	LPF Vote	Vote Result	Follow-This Shareholder Resolution	LPF Vote	Vote Result
Energy Companies						
Shell	Shell Energy Transition Progress Update	Against	80% support	Yes - Aligning emissions targets to Paris Agreement	For	20% support
Total Energies	Sustainable Development and Energy Transition Plan	Against	89% support	Yes - Aligning emissions targets to Paris Agreement	For	30% support
Exxon Mobil	n.a.	n.a.	n.a.	Yes - Adopt a medium term Scope 3 target	For	11% support
Chevron	n.a.	n.a.	n.a.	Yes - Adopt a medium term Scope 3 target	For	10% support
BP	n.a.	n.a.	n.a.	Yes - Aligning emissions targets to Paris Agreement	Against	17% support

Case study

2023 "SAY ON CLIMATE" VOTES *(CONTINUED)*

Assessment

Management proposed Say-on-Climate votes continued to garner strong support from shareholders, while resolutions filed by climate activist groups such as Follow This received support from only a minority of shareholders. This indicates that a majority of shareholders in these companies continue to be willing to support incremental progress on climate plans in the context of ongoing concerns about energy security and affordability.

Our voting record shows we continued to exercise our voting rights in alignment with our identification of climate change as a key systemic risk, while being willing to recognise leadership:

- **Shell:** we voted against Shell's energy transition progress update as we consider its strategy to be materially misaligned to a 1.5°C scenario, in addition to poor disclosure of metrics allowing tracking of overall decarbonisation progress. Shell also reduced disclosure relating to future capital expenditure, introducing further uncertainty about the company's future direction. We voted in favour of the Follow This shareholder resolution to align the 2030 reduction target for Scope 3 emissions to 1.5°C, as we assessed that it could prompt a review of the metrics used to demonstrate Shell's alignment with a 1.5°C scenario, and we don't believe that the company's current targets are aligned with this
- **TotalEnergies:** We voted against TotalEnergies energy transition plan as the strategy still relies on maintaining and growing fossil fuels (Liquified Natural Gas production forecast to grow 40% by 2030). We consider the companies' targets as lacking ambition as they're designed to be reached largely by an increase in low carbon energies rather than a decline in fossil fuels. This lack of ambition and alignment led us to vote in favour of the Follow This shareholder resolution for TotalEnergies to align its Scope 3 targets with the Paris-aligned 1.5°C scenario by 2030
- **Exxon:** we voted in favour of the Follow This shareholder resolution to adopt a medium-term scope 3 target, consistent with the Paris Agreement, as we believe this would increase the transparency of Exxon's climate change strategy. We also voted in favour of several additional shareholder proposals relating to emissions, plastics, and tax transparency, which would all improve the management and transparency of environmental, social, and governance impacts
- **Chevron:** we voted in favour of the Follow This shareholder resolution to adopt a medium-term scope 3 emissions reduction target as we believe this would increase the transparency of Chevron's climate change strategy and improve management of climate-related risks. We also voted in favour of several shareholder resolutions which would enhance transparency and governance practices
- **BP:** we voted against the Follow This shareholder resolution, as the additional benefit of this resolution was unclear given that BP have already had a shareholder resolution successfully passed (in 2019) requiring the company to disclose its strategy consistent with the Paris goals. BP responded to this in 2020 by launching its strategy to become a net zero company by 2050, including targets for emissions reductions in the short and medium term. This climate strategy was supported by a majority of shareholders (including LPF) in BP's 2022 Say-on-Climate proposal. In February 2023, BP disappointingly reduced the ambition of some of these targets, however we recognise that BP's disclosure and climate strategy (with 50% of its spending budget committed to low-carbon business by 2030) remain ahead of their sector peers. We continue to engage with BP through EOS and Climate Action 100+, reiterating the need to see clear progress on reducing both absolute emissions and the carbon intensity of its business.

PRINCIPLE 12: EXERCISING RIGHTS AND RESPONSIBILITIES

Stock lending

Our stock lending programme uses our existing asset base to generate an additional source of income. The programme is managed in accordance with our responsible investment policies. During 2020 we updated our policy for securities lending. We now automatically recall all securities on loan for voting purposes. This enables us to vote 100% of our holdings for our entire holding at 100% of the relevant meetings, which adds significant weight to the influence we exercise as shareholders.

Co-filing activity

We're prepared to file or co-file shareholder resolutions on important topics at our investee companies. While our activities didn't lead to any shareholder resolutions being filed in 2023/24, we were involved in some preparatory activity, and note that this stimulated meaningful engagement and progress. For example, in Q4 2023, alongside LAPFF and other like-minded investors, we explored co-filing a shareholder resolution at Rio Tinto, requesting that the company undertake independent water impact assessments at its mine sites. Although this activity didn't result in a shareholder resolution being filed at the April 2024 general meeting, Rio Tinto was open to engagement on this topic and published a water impact assessment in relation to its operation in Madagascar. LAPFF is pursuing further dialogue with the company on this topic and the resolution filing process could be resumed ahead of the company's next annual general meeting if there's a lack of further progress.

Voting transparency

In line with best practice voting disclosure in the UK, we report quarterly on our voting activities via our website: www.lpf.org.uk. This consists of details on the votes cast by stock name and includes rationale for votes against management, abstentions and shareholder resolutions. We also provide quarterly summary statistics on the voting recommendations provided by our service provider, EOS, by region. Alongside this we publish quarterly information on the engagement activities undertaken by EOS on our behalf because we believe that the two activities work together, not as discrete stand-alone activities. We also provide quarterly voting and engagement reports from one of our external managers, as a small percentage of our equities allocation is invested through a pooled fund where the manager retains voting rights.

We recognised and responded to growing stakeholder interest in specific votes and feedback that stock-level voting reports were hard to consume (with details on specific companies lost amongst the scale of disclosure) by publishing more detailed information on how and why we voted on high-profile "Say on Climate" votes within our ENGAGE publication (see Case Study on page 98). In May 2024 we further improved the timeliness of the communication of our stewardship activities to stakeholders by pre-declaring our voting intentions for certain high-profile votes.

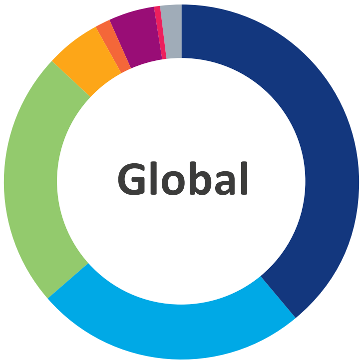
We also supported industry efforts to address misalignment between asset owners and asset managers on voting (see Case Study in Principle 3).

PRINCIPLE 12: EXERCISING RIGHTS AND RESPONSIBILITIES

DATA AND STATISTICS: EOS ADVISED FUNDS

100% of LPF's ballots were voted in 2023. This meant we voted on 7,789 resolutions at 513 meetings. At 329 of those meetings, we opposed one or more resolution. We abstained from voting on one meeting due to concerns related to the non-independent nature of the chair of the audit committee and the overly long tenure of the external auditors.

The issues on which we voted against management (in-line with EOS recommendations) are presented below.



We recommended voting against or abstaining on 890 resolutions over the last year.

- Board structure **39.0%**
- Remuneration **24.7%**
- Shareholder resolution **23.3%**
- Capital structure and dividends **5.2%**
- Amend articles **1.2%**
- Audit and accounts **4.3%**
- Poison pill/Anti-takeover device **0.4%**
- Other **1.9%**

PRINCIPLE 12: EXERCISING RIGHTS AND RESPONSIBILITIES

Reflections on the 2023 voting season

The 2023 shareholder meeting season was characterised by a continued focus on the need to accelerate the energy transition, particularly in Europe where growing physical climate risk was demonstrated by summer heatwaves and wildfires ravaging tourist destinations. However, after a busy year of Say-on-Climate votes in 2022, some companies chose not to put their climate strategies to the vote in 2023. This was especially the case for oil and gas companies, which many investors suspected of stalling on climate strategy development.

In North America social issues remained in the spotlight, with a record number of shareholder proposals filed on a range of topics such as worker health and safety, paid sick leave, wages and equity, freedom of association, workplace sexual harassment and digital rights. In general, we consider proposals on a pragmatic basis, reviewing each in its company-specific context. In line with fiduciary duty, we seek to determine the extent to which the proposal promotes long-term shareholders' interests and progress through engagement with the company, where practicable.

We also maintained our voting attention on two more traditional areas: executive remuneration, and board diversity. We offer some reflections on these topics below.

Executive remuneration

For executive remuneration, we emphasised the need for better disclosure where this was lacking, while scrutinising pay quantum where there appeared to be a disconnect between pay and the broader stakeholder experience. This was against a background of persistently high inflation in developed markets which squeezed household budgets. We benefited from EOS' specialist skills and resource to analyse complex pay packages. 25% of our votes against management in 2023 were on remuneration concerns.

Across North America, remuneration practices remained materially misaligned with our principles, particularly on quantum, variable pay ratio, and severance. We voted against executive pay and the compensation committee chair at Alphabet and Meta. While most independent shareholders did likewise, these companies' dual-class share structures maintain control in the hands of the executives/founders.

In Europe, we emphasised our desire for greater shareholding by executives and for improved disclosure where it was insufficient, or companies didn't provide a compelling rationale for excessive pay levels. At Nestlé, we found the company more open to engagement on executive remuneration in 2023, having experienced notable (c. 20%) dissent on pay in 2022. We engaged on our expectations for more transparency on targets and performance for the bonus scheme and the company provided more disclosure in 2023. However, we were amongst the c.10% of shareholders who opposed the CEO's remuneration package in 2023, as we considered it as lacking sufficient stretch targets for full vesting, compounded by the large overall package and high variable pay opportunity.

PRINCIPLE 12: EXERCISING RIGHTS AND RESPONSIBILITIES

Board diversity

Our diversity and inclusion voting policies encourage greater representation of women and ethnic minorities on boards and in leadership teams.

- In Europe, we support a goal of 50% overall board diversity, including gender (with at least 40% representation of the minority gender, including those who identify as non-binary). Where best practice or listing rule obligations exist in a country, we expect companies to adhere to these at a minimum
- In the US, we want to see companies strive for 50% overall board diversity including LGBTQ+ and disability. We're seeing this level of diverse representation in some US companies, but our minimum expectations are for at least 40% board diversity including gender, race and ethnicity
- Our expectations for gender diversity continued to tighten across Asia and global emerging markets. In Japan, it was encouraging to see some improvement following the government's new target for women to make up 30% of board directors at prime market companies by 2030 and we increased our minimum expectation for 2023 to 15%.

Where companies don't meet our minimum expectations for board diversity, we consider voting against the reappointment of the chair and/or the board member responsible for governance and nominations. Notable examples where we did this included Phillip Morris, Walmart and Softbank.

Case study

PARKER REVIEW ON IMPROVING THE ETHNIC DIVERSITY OF UK BUSINESSES

Background

In its first report, published in 2017, the Parker Review made a series of recommendations setting a "One by 2021" target for all FTSE 100 boards to have at least one director from an ethnic minority background by December 2021 and a similar "One by 2024" target for all FTSE 250 boards.

Outcome

The 2023 voluntary census (carried out jointly with the Department for Business and Trade and sponsored by Ernst & Young) revealed good progress on ethnic diversity for FTSE 250 companies in 2023:

- 96 FTSE 100 companies had ethnic minority representation on its company boards as of 31 December 2023. This is in line with the 2022 reported data. People with ethnic minority backgrounds now hold 19% of all director positions in the FTSE 100, a rise of one percent from last year
- 175 of the FTSE 250 companies (70%) met the "One by 2024" target. This is an increase from 149 (60%) in 2022, demonstrating significant progress during the year.

Assessment

While this year's Parker Review shows that progress is being made to increase the representation of ethnic minority talent, there's still more to do. We've already incorporated the Parker Review target as our minimum expectation for FTSE 100 companies (in 2022 we voted against the chair of a FTSE 100 company where this wasn't the case) and we'll continue to monitor progress through the evolution of market norms towards the targets set by the Parker Review. With c.15% of our equities allocation in UK listed stocks, we recognise the importance for UK businesses to secure the best talent – irrespective of ethnicity – into boardrooms and senior management teams, reflecting the diversity of our society.

PRINCIPLE 12: EXERCISING RIGHTS AND RESPONSIBILITIES

SHAREHOLDER ACTION

We describe our approach to shareholder action in relation to Principle 4: Promoting a well-functioning financial system. We consider participating in class actions to be another way that we exercise our responsibilities as asset owners. Taking action to recover assets lost through investments in companies as the result of corporate mismanagement or wrongdoing is an aspect of our duty to stakeholders.

Exercising rights and responsibilities in private markets

For our private market investments across private equity, private debt, infrastructure, forestry and property funds, we scrutinise corporate actions which require investor approval (such as fund term extensions) and vote in accordance with our fiduciary duty. We'll engage with our external managers to understand their rationale for such requests. Where we're able to obtain a position on the investors' advisory committee for a fund (e.g. through the size of our investment) we'll secure additional rights and responsibilities (such as being consulted on proposed changes to the fund's investment guidelines, approving certain matters such as changes to key executives, scrutinising potential or actual conflicts of interest and the related mitigating actions). We aim to use our rights and responsibilities to improve the value of the assets in our portfolio, in line with our fiduciary duty

Exercising rights and responsibilities in direct property

For our direct property portfolio, we aim to improve the value of the assets in our portfolio in line with our fiduciary duty. This includes consideration of health and safety issues and other regulations to ensure we're a good landlord. As detailed in the case study in Principle 7, we took a proactive approach to meeting the 2023 Minimum Energy Efficiency Standards and we continue to improve the energy performance of our assets to ensure future compliance with proposed regulations.

GLOSSARY

CA100+	Climate Action 100+ is a collaborative initiative by institutional investors to engage with companies identified as the largest (or systemically important) emitters to take necessary action on climate change
CEC	City of Edinburgh Council - administering authority for LPF
COP	Climate Change Conference of Parties - 'the parties' refers to the 197 nations that agreed to a new environmental pact, the United Nations Framework Convention on Climate Change, at a meeting in 1992
DEI	Diversity, Equity and Inclusion - Just Transition - A vision-led principle encompassing a range of social interventions to secure workers' rights and livelihoods when economies are shifting to sustainable production to combat climate change and protect biodiversity
DWP	Department of Work and Pensions
EOS	Federated Hermes EOS - engagement and voting provider for LPF
ESG	Environmental, Social and Governance
FCA	Financial Conduct Authority
FRC	Financial Reporting Council - an independent regulator responsible for setting the UK's Corporate Governance and Stewardship Codes
GRESB	An investor-led, sustainability benchmarking provider for real assets, covering real estate and infrastructure assets
IIGCC	Institutional Investors Group on Climate Change - a leading global investor membership body and the largest one focusing specifically on climate change
ISS	Institutional Shareholder Services - a proxy voting service provider
JIF	Joint Investment Forum (of advisers to the Fund)
LAPFF	Local Authority Pension Fund Forum - a collaborative shareholder engagement group, comprising UK local authority pension funds and most of the LGPS pension fund pools
LGBTQ+	An acronym for lesbian, gay, bisexual, transgender, queer/questioning and other terms (such as asexual, non-binary and pansexual)
LGPS	Local Government Pension Scheme
LPF	Lothian Pension Fund
OPSC	Occupational Pension Stewardship Council - UK initiative to promote and facilitate high standards of stewardship of pension assets
PLSA	Pensions and Lifetime Savings Association
PRI	Principles for Responsible Investment - an international network of investors, supported by the United Nations, working to promote sustainable investment through the incorporation of ESG
R&C	Risk and Compliance
SIP	Statement of Investment Principles
SRIP	Statement of Responsible Investment Principles

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