Northern LGPS Stewardship Report: Q3

Introduction:

A major driver of the public health crisis the excessive prevalence of unhealthy food and drink products. In 2021, only 29% of UK sales came from healthier products, whilst the big four supermarkets (Asda, Morrisons, Sainsbury's and Tesco) run more promotions on high fat, salt and sugar (HFSS) products than they do for healthier foods.

The health of a company and the health its consumers go hand in hand. It is an imperative for investors to leverage their holdings to push investee companies to drive healthier outcomes for their localities.

Whilst this is a national issue, there is a clear north-south divide in health outcomes, demonstrated by a multitude of statistics on the prevalence of obesity. According to statistics compiled for a House of Commons obesity report, Merseyside contains two of the seven local authorities with the highest percentage of overweight or obese reception age children (Knowsley in second and St Helens in seventh, with nearby Halton in third). In Manchester, 42% of Year 6 children are overweight or obese compared to 28.7% in Brighton and Hove. In three Greater Manchester districts – Wigan, Rochdale, and Tameside – that figure rises to over 70% of the adult population.

The costs of obesity on individuals and society are well known, from lower life expectancy to impacts on health services. The NHS spends £6.5 billion on obesity related diseases every year, whilst an independent study commissioned by Novo Nordisk estimated the current social cost of obesity for the UK stands at £58 billion, taking into account both direct and indirect costs (such as reduced productivity).

The costs of inaction and the benefits of pursuing healthier products from companies should be clear for investors. In terms of direct impact on local populations, pushing for a greater proportion of healthy products and a reduction to the high levels of fat, salt and sugar in existing products would reduce negative health outcomes and all the socio-economic consequences that follow.

It is essential that investors engage food and drink companies on this issue. Governments are becoming increasingly aware to the risks of high obesity rates within their populations and the strains it places on public services. As such, the regulatory risks facing companies whose profits derive from HFSS products is significant.

Over 50 jurisdictions have now implemented taxes on sugary products, England has already banned BOGOF deals for HFSS products and introduced regulation on where they can be located within stores at the end of the third quarter. Scotland is planning to restrict junk food promotions, the US federal government is developing a national strategy on health and nutrition, whilst Czechia and other places in Europe have banned the sale and advertising of soft drinks, mayonnaise-filled sandwiches and crisps within schools.

If companies fail to respond to these trends, it could jeopardise financial performance and shareholder returns. The 2021 National Food Strategy found that HFSS product consumption needs to be reduced by 25% by 2032, and responsible investors are impressing upon food and drink companies the need to shift.

Northern funds have been at the forefront of efforts to tackle this issue. NLGPS, PIRC and LAPFF, are signatories to ShareAction's Healthy Markets Initiative, (now Long-term Investors in People's Health

(LHIP)) the 45-investor, $7.5 trillion strong coalition that uses its holdings and engagement experience to press to companies the financial and health imperatives of change.

Coming into its third year, the initiative has grown significantly in that time, the clear links between obesity and worse outcomes from Covid-19 a key driver for the surge in investor interest. Asset managers and owners with $215 billion in assets under management co-filed a shareholder resolution at Unilever earlier this year, and the experience of that filing and subsequent discussions is invaluable in dealing with future company engagements.

The Importance of Health as a Stewardship Focus for LGPS

Louisa Hughes, Senior Engagement Manager and Hannah Picton, Senior Engagement Officer at ShareAction have answered some questions regarding the importance of health as a stewardship focus for the NLGPS and how investors can help drive good outcomes.

"When asked what you are grateful for or what you would wish for, a happy and fulfilling life – your own good health and that of your loved ones if often top of the list. It is often something we take for granted until we don't have it. Yet, health is a topic that is still not at the top of the agenda when it comes to ESG. Amongst other ESG topics, good health is vital for public, economic and social wellbeing.

At ShareAction, we have been working to ensure that health is understood and prioritised through our Healthy Markets Initiative and now our new Long-term Investors in People's Health (LIPH) programme." *Louisa Hughes, ShareAction*

Why is health so important?

Good health is what enables us to thrive and live independent and fulfilling lives. It also allows us to contribute productively as workers, consumers and as active participants in society and the economy. Millions of people are limited by ill-health due to avoidable risk factors such as unhealthy diets and excessive alcohol consumption, and poor quality jobs and housing. Good health is determined by the context in which we live and is influenced by 'social and commercial determinants' such as access to education, adequate housing and decent work. As much as 60-80 per cent of health outcomes are driven by these environmental factors.

What sectors influence our health?

Companies significantly influence health through their roles as employers, as providers of consumer products and services, and as active participants in the wider communities and regulatory structures in which they operate. Therefore, companies have a responsibility to take steps to ensure that they, and their operations and supply chains, protect the health and wellbeing of their employees, the health of the consumers of their products and services, and the health of communities impacted by their operations more broadly.

What is the role of investors?

Investors have a critical role to play in upholding the human right to health. However, this is not just about investors' responsibilities as the providers of capital to companies. There are also compelling arguments – across company (or asset) level, portfolio level and the wider economic level – for investors to act on health.

People's health is strongly associated with the productivity and resilience of individuals, companies and portfolios. There are also increasing financial, legal, and reputational risks that companies may face if they fail to manage risks related to health – such as increasing regulation.

Investors also have a duty to properly and effectively recognise and act on longer-term risks such as those presented by sub-optimal population health. Investors therefore need to ensure population health considerations are fully integrated into their investment research and decision-making, engagement with the companies they invest in, public advocacy, and engagement with policy makers.

Although increasingly recognised by investors as a key investment issue, health is still an underdeveloped topic with no formally recognised definition or framing in the investor community.

Why is health of particular interest to Local Authority Pension Funds?

Poor population health places additional demand on local health and social care services, and with local councils in England being responsible for public health, this places increased strain on already stretched services and increasingly limited budgets.

Alongside innovative approaches to improve local environments – such as programmes to improve food environments, housing and education; local authorities have a powerful and underutilised tool at their disposal – their investments.

What is LIPH and how does it work?

Long-term Investors in People's Health is a programme that aims to raise health up the ESG agenda, bring investors together to gain the insight they need to work on this topic, and engage with companies and sectors to push for better practice and improved public health outcomes. The programme builds on ShareAction's Healthy Markets Initiative which has been running since 2019.

LIPH is built of three pillars of work: Consumer Health, Community Health and Worker Health, and is supported by a growing global alliance of (currently) 36 investors and $5.7 trillion assets under management.

The investor alliance is supported by ShareAction who provide relevant research and briefings, facilitate engagement with priority sectors, coordinate coalition letters to companies, ask AGM questions, and where needed, facilitate shareholder resolutions.

Members have the opportunity to help shape the programme as it grows and develops.

How has NLGPS/PIRC been involved to date?

NLGPS and PIRC have been members of the Healthy Markets Initiative since 2020. They have been actively involved in our engagement and have been instrumental in ensuring that company targets understand the importance of prioritising health and take meaningful steps to act on this. The Greater Manchester Pension Fund was also a co-filer on the resolution at Unilever earlier this year.

How can we get involved?

As outlined above, investors can have a huge impact on company practice, and therefore, public health. By becoming aware of the importance of health in investment decisions, they can start to incorporate this into their strategies. By joining the LIPH programme, investors can gain access to the information and support they need to ensure they are mitigating against health-related risk and can maximise impact through collaborative engagement opportunities.

You can contact health@shareaction.org for more information - we would be pleased to hear from you!

Healthy Products Company Engagements

Danone

All three, 627,719 shares worth 0.098%

Overview: Danone SA is a French multinational food-products corporation. NLGPS funds hold 627,719 shares worth 0.098%. Danone specialises in dairy products, diary alternatives, water and coffee, and sells brands in the UK including Activia, Alpro, Actimel, and Silk. It's Nutricia brand has a manufacturing, development and supply plant in Liverpool.

Issues arising: As explained earlier, there are material risks to companies that manufacture and market HFSS consumables. Regulatory and consumer trends towards healthier diets to combat public health crises have accelerated, and it is increasingly clear that the food and drink environment, flooded with less healthy products with high calorie counts, has been a significant driver of broader diet-related public health issues.

Food companies responsible for shaping this environment, like Danone, have a responsibility to ensure they are contributing positively toward public health.

Engagement: As part of Share Action's Healthy Markets Initiative, engagement was undertaken with Danone to discuss the health of its products and receive an update on its commitments. The company was pressed to separately report its sales revenue from its healthier products; this would help investors gage whether the company was meeting its 2020 commitments to increase sales and consumption of healthy products. The investor group also called for long-term targets to be set on this basis. The company stopped short of committing to long-term targets increasing the share of healthy products by revenue, but did provide further detail on its overall strategy of driving better health outcomes for consumers.

Outcome and follow ups: The company has reported that almost 90% of the volume of products sold during 2021 were 'healthy', as defined by government-endorsed definitions. In this context it is confusing as to why Danone is uncomfortable with long-term targets.

In addition, NLGPS funds are also represented by LAPFF, an engagement partner to the Access to Nutrition Index (ATNI). It found that 65% of Danone's revenue derives from healthy products, making it one of the highest performing companies compared to other global manufacturers. The Healthy Markets Initiation will continue to push for Danone to adopt long-term targets and separately report sales.

Britvic

Overview: Britvic plc is a British soft drinks company; NLGPS funds hold 510,000 shares worth 0.191%. Its brands include Robinsons, J2O, Tango, and Fruit Shoot, amongst others, and has a partnership with PepsiCo to manufacture and sell a number of PepsiCo's products. It has a factory in Leeds.

Issues arising: Obesity rates continue to rise across the UK, particularly amongst children. Many of Britvic's brands are marketed especially at children, so it is imperative that companies exposed to the aforementioned risks should take both responsibility for shaping consumer health and take action to improve access to healthy soft drinks.

Engagement: On public health, the company outlined its newly introduced target to reduce the calorie content by 30 per 250ml serving by 2025. It has already achieved an average reduction of 25 calories through reformulation, based on initial calorie content of each product.

Outcome and follow ups: PIRC will continue to monitor changes to Britvic's products and the proportion of HFSS products sold.

Tax

Since the start of the year PIRC has been collaborating with the Centre for International Corporate Tax Accountability and Research (CICTAR) with the aim of engaging companies on their tax records and promoting greater transparency and reporting, in line with the GRI Tax Standard. Companies have been targeted based on their own reputation, that of the sectors in which they operate and the risk of government action from continued non-disclosure.

Following the successful filing and 21% vote of independent shareholders in favour of the PIRC coordinated tax transparency shareholder resolution at Amazon in May, there has been further success with the filing of similar proposals at tech firms Cisco and Microsoft. They were filed at the start of Q3 and by the end, with the rejection of Amazon's appeal against the vote setting a precedent, both were accepted.

PIRC is grateful for the support of the Greater Manchester Pension Fund and all co-filers as tax transparency becomes an issue of greater importance to investors. Northern funds know the damage that withdrawn or reduced government spending can have on localities, so it is in their own local interests, as well as long-term financial viability, to ensure that these companies are reporting their tax policies and figures.

Microsoft

Overview: Microsoft Corporation is an American multinational technology giant, incorporated in Ireland. NLGPS Funds hold 1,160,791 shares worth 0.015%.

Issues arising: Currently, Microsoft does not disclose revenues or profits in non-US markets, and foreign tax payments are not disaggregated. This makes it much more difficult for investors to evaluate Microsoft's risks from taxation reforms, or whether the company is engaged in responsible tax practices that ensure long term value creation for the company and the communities in which it operates.

Engagement: PIRC supported and coordinated the filing of a shareholder proposal calling on Microsoft to produce a tax transparency report in line with the GRI Tax Standard. The Greater Manchester Pension Fund was a co-filer, along with AkademikerPension, Nordea Asset

Management, PenSam, and OIP Trust. Their public support garnered significant media attention and shone a spotlight on Microsoft's dubious tax practices.

Outcome and follow ups: PIRC will be engaging Microsoft shareholders and proxy advisors to encourage them to vote in favour of the shareholder proposal. Microsoft subsequently wrote to PIRC confirming that it would not challenge the tax transparency shareholder proposal filed. The AGM takes place in November 2022, and PIRC will be liaising with GMPF and other co-filers on the best way forward.

<u>Engie</u>

Overview: Engie SA is a French multinational utility company; NLGPS funds hold 652,653 shares worth 0.027%.

Issues arising: The company has a Tax Policy Statement that briefly outlines its approach to tax governance issues and approach to legislation. This is in line with the GRI Tax Standard (the pinnacle for international corporate tax accreditation) 207-1. However, it does not fully comply with GRI Tax Standard as it does not publish an assessment of risks (207-2), nor country-by-country reporting (CbCR) (207-4).

Engagement: PIRC met with the Investor Relations team and the Global Head of Tax for the organisation. PIRC asked whether the company has discussed the implementation of the GRI Tax Standard, and specifically the publication of CbCR. This has been discussed at audit committee level, but there are currently no plans to publish CbCR; they believe that it wasn't set up as an instrument for the public, but rather as an instrument for tax authorities.

PIRC highlighted our support for public CbCR and peer uptake of the Standard. The GRI's disaggregated tax data demands provide for more robust reporting criteria than the OECD's tax policies. The company stated that ongoing litigation and investigations regarding older tax practices that they have since reformed, and that a more prudent approach to transfer pricing is taken than it was 10 years ago. This is due to pressure from its major shareholder, the French government. They confirmed that lobbying at EU and national level on tax issues does take place.

Outcome and follow ups: PIRC highlighted that, according to our tax brief regarding our expectations for companies regarding tax practices and disclosures, the publication of CbCR will be taken into account when deciding whether to recommend voting for or against a company's financial statement. NLGPS funds should look out for PIRC advise on this matter closer to the AGM.

<u>Roche AG</u>

All three, 737,250 shares worth 0.46%

Overview: Roche AG is a Swiss multinational healthcare company operating in pharmaceuticals and diagnostics. NLGPS Funds hold 737,250 shares worth 0.46%.

Issues arising: The company currently reports in line with GRI Tax standard 207-1 and 207-2, but not 207-4: the publication of CbCR. The company receives significant tax concessions for research and development from Swiss authorities.

Engagement: PIRC met with the Roche's Area Tax Director, its Head of International Trade Affairs & Customs Regulations, and the Investor Relations team to discuss the company's tax alignment with business and sustainability strategies, as well as approaches to tax risks and tax governance frameworks.

As with Engie, Roche argued that it does not view public CbCR provides useful for information for investors, as it was a tool designed by and for tax authorities. This is despite their confirmation that tax authorities have stepped up auditing of how company distributes profits between jurisdictions, a clear investor risk.

Outcome and follow ups: PIRC highlighted that, according to the tax brief regarding expectations for companies' tax practices and disclosures, the publication CbCR will be taken into account when deciding whether to recommend voting for or against a company's financial statement.

Workforce Engagement

The treatment of staff, from pay to working conditions, has increasingly become a salient issue for investors. In a world of labour shortages and demands for wage rises in line with inflation, how companies interact with their workforce is growing in financial materiality.

Starbucks Corporation and **Apple Inc** are both large, multinational, American companies, with hundreds of locations across the US and a multitude of locations in the north. NLGPS funds hold 249,211 shares and 2,403,006 shares respectively. But despite their well-honed reputations for supporting social justice and allyship, there have been accusations of mistreatment and anti-union activity.

PIRC has been engaging with a wide range of US-listed companies over issues relating to employment practices, including fundamental rights at work. PIRC mainly focused on Starbucks and Apple, with the former coming in for rebuke by the National Labor Relations Board for violating the National Labor Relations Act multiple times.

Both companies stand accused of sacking pro-union employees, and withholding pay and benefit improvements of union members. This has been in response to efforts by employees to seek independent trade union representation, with over 200 Starbucks stores voting to unionise in the US.

Apple and Starbucks both refer in their human rights policies to their support for ILO fundamental conventions on Freedom of Association and Collective Bargaining. According to the ILO, "Freedom of association refers to the right of workers . . . to create and join organisations of their choice freely and without fear of reprisal or interference". Nonetheless, such freedom is often denied to workers at these respective companies.

Meaningful engagement on freedom of association has not been successful. Therefore, engagement has been escalated through the filing of shareholder resolutions at both companies. The proposals ask that companies commission independent third-party reviews of the implementation of their commitments on freedom of association and collective bargaining. PIRC has supported the filing of these resolutions.

It was not clear whether either company will seek to exclude the proposals. PIRC will report in more detail in the next quarter, and NLGPS funds should look out for PIRC voting recommendations closer to next year's AGMs.

Merger and Acquisition

As part of work on corporate governance issues PIRC has been looking at stewardship in relation to merger and acquisition (M&A) activity. There has been a particular focus on the impact of funds undertaking merger arbitrage trades. Two limited companies subject that were subject to successful takeover bids in Q3 were **Meggitt plc** and **Go-Ahead Group plc**.

The widespread use of equity derivatives by such funds may be having a negative impact on voting turnout. With that comes less scrutiny of corporate decision making and less accountability for company decision-makers to shareholders. All mergers and takeovers will be of heightened interest to shareholding funds, but so too is the manner in which such acquisitions are completed.

Meggitt is a UK-based components and sub-systems provider for the aerospace and defence sectors. At the time of engagement, Meggitt was in the process of being acquired by American company Parker Hannifin, with ramifications for UK-wide defence, British workers and shareholders.

Go-Ahead is a public transport company providing contracted rail and bus services in the UK, Singapore and Europe. At the time of engagement, the company was in the process of being taken over by a consortium comprised of Australia's Kinetic Group (51% stake) and Spain's Globalvia (49%). NLGPS Funds held 150,000 shares worth 0.347%, and it ran Go North West bus operations in Greater Manchester since 2019.

In terms of company specifics, turnout at *Meggitt*'s AGM in 2022 was 25% compared to 81% in 2021. At *Go-Ahead* there was a 21% vote against the scheme of arrangement required to progress its takeover. Under the UK Corporate Governance Code companies are expected to respond to votes against of 20% or more.

A number of hedge funds had built up significant derivative positions prior to the Meggitt takeover. The company had been advised that, due to changes in its share register during the bid, it should expect turnout to drop. The reduction in voter turnout however was particularly sharp. There was also a significant vote against one of the directors due to concerns about over-boarding. The company stated in response to this result that the reduction in turnout may have been a factor in the result.

Go-Ahead refused to comment on the 21% vote against the scheme of arrangement. PIRC contacted the company for clarification on the factors behind the vote. To date however, the company has not responded.

PIRC's work on stewardship activity in relation to M&A has raised a number of concerns. In September, PIRC published an investor briefing on our findings. The main takeaway was that, with depressed turnout, those exercising their voting rights will wield greater power. This risks a vote being lost due to a low turnout. It also undermines ideas of stewardship when, for example, fewer than half of votes are cast.

To address these issues, the report sets out recommendations, including:

- A review of derivatives and voting by the Takeover Panel

- FRC/ARGA reviewing M&A activity and including guidance in the next Stewardship Code
- Requiring investors utilising derivatives to outline their approach to management of target companies and voting rights.

Climate

NLGPS funds have also had their interests represented through the Local Authority Pension Fund Forum's engagement on climate. Voting alerts and AGM attendance were used to press concerns about decarbonisation transition plans, pressing upon companies what precisely needs to be done to satisfy necessarily stringent criteria.

A voting alert was issued ahead of the *SSE* AGM, in which NLGPS member funds hold ,598,920 shares worth 0.243%. The recommendation was to vote in favour of the company's net zero transition report, with significant progress noted in alignment with targets to limit global warming with Science Based Targets and Scope 3 emissions targets. The recommendation demonstrates LAPFF's willingness to be a firm but fair engagement partner, showing other companies what is required to secure shareholder support.

LAPFF issued a voting alert against *National Grid*'s transition plan, and a discussion was held with the Head of Sustainability and Company secretary prior to the AGM. NLGPS members hold 7,600,854 shares worth 0.209% and have a clear interest in the sustainability of the UK's sole energy grid. At the AGM, LAPFF pressed the Company leadership on Scope 3 targets and alignment with the Science Based Targets initiative. Initial response to LAPFF's engagement suggests that the Company is accelerating measures to net zero infrastructure as well as a fair and just transition.

Q3 Data

Voting recommendations, by percentages:

Remuneration (advisory): 38.8% for, 58.7% oppose, 2.5% abstain

Remuneration (binding): 40.5% for, 50.6% oppose, 8.9% abstain

Auditor appointments: 79.5% for, 15.5% oppose, 5% abstain/withhold

Director elections: 23.9% for, 66.5% oppose, 9.6% abstain