WIRRAL COUNCIL

PENSIONS COMMITTEE

27 SEPTEMBER 2010

REPORT OF THE DIRECTOR OF FINANCE

THE STEWARDSHIP CODE FOR INSTITUTIONAL INVESTORS

1. EXECUTIVE SUMMARY

1.1 This paper provides an outline of the contents of the U.K. Stewardship Code, the background to its formation and its relevance to the Statement of Investment Principles. A statement of compliance with the Stewardship Code is included as an appendix to this report, and Members are requested to approve its publication.

2. BACKGROUND

2.1 In the aftermath of the financial crisis, the previous Government set up the Walker Review to examine the role of U.K. banks and other financial institutions. One strand of reform recommended by Walker was to improve the extent and effectiveness of shareholder engagement with companies. The Walker Review recommended that the Financial Reporting Council (FRC) should have responsibility for a new Stewardship Code, setting out best practice in respect of shareholder engagement.

2.2 At the start of July 2010 the FRC published its version of the Stewardship Code, which adopted wholesale the principles laid down by the Institutional Shareholders Committee (ISC) in its 2009 document 'Code on the Responsibilities of Institutional Shareholders and Agents'. The Statement of Investment Principles (approved by Pensions Committee on 23 March 2010) endorses the ISC Code, *"The ISC Code sets out best practice for institutional investors that choose to engage with the companies in which they invest. The Fund considers that its responsible ownership policy already complies with, and may even exceed, the principles in the ISC Code. However, the Fund believes it has direct relevance for managing its relationships with external investment managers, and will require its managers to state their approach to the ISC Code on a 'comply or explain' basis…"*

2.3 The LGPS Regulations (Investment & Management of Funds) 2009 contain a requirement to abide by guidance from the Secretary of State when producing a Statement of Investment Principles (SIP). This guidance has taken the form of the CIPFA paper on adapting the revised Myners Principles to the LGPS, which was used in the preparation of the SIP and which makes explicit reference to adopting the ISC Code. Therefore, it can be inferred that adherence to the Stewardship Code is a requirement of the Scheme Regulations.

2.4 MPF has contributed to the development of the Stewardship Code through its participation in the Local Authority Pension Fund Forum (LAPFF). The Forum submitted detailed responses to both the FRC consultation exercise on the Stewardship Code, and to the earlier consultation preceding the Walker Review.

3. THE STEWARDSHIP CODE

3.1 The Stewardship Code is a set of best practice principles that are intended to frame both shareholder engagement with companies and the disclosure of such activity. It is intended that shareholders adhere to the principles with the same ‘comply or explain’ approach used by U.K. companies in respect of the FRC Corporate Governance Code.

3.2 The principles are as follows –

Institutional investors should:

1. Publicly disclose their policy on how they will discharge their stewardship responsibilities
2. Have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed
3. Monitor their investee companies
4. Establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value
5. Be willing to act collectively with other investors where appropriate
6. Have a clear policy on voting and disclosure of voting activity
7. Report periodically on their stewardship and voting activities.

3.3 The FRC has stated that, while the Stewardship Code is principally aimed at asset managers, other institutional investors (and especially pension funds as a significant client group for asset managers) are strongly encouraged to report under it. The FRC has asked that institutional investors publish by the end of September 2010 a statement on their website of the extent to which they have complied with the Code, and to inform the FRC when they have done so.

3.4 The FRC has asked that such a statement consists of a description of how the principles of the Code have been applied. In many respects, the SIP already fulfils this brief. The Local Authority Pension Fund Forum (LAPFF) has issued guidance to member pension funds on reporting under the Code. The guidance included a ‘model’ statement, which has been adapted to suit MPF arrangements and practices (as outlined in the SIP), and is included as an appendix to this report.

3.5 Those institutions who publish their statements on the Code by the end of September 2010 will be recognized by the FRC as early adopters and will be included in a ‘roll of honour’ on the FRC website. The FRC has stated that it will undertake annual monitoring of the take-up and application of the Code, as well as regular reviews of its content and impact. This is due to commence in the second half of 2011.

3.6 Issues likely to be considered for future inclusion in the Code will include policy recommendations on stock-lending, voting rights for beneficial owners in pooled funds and the form of voting disclosure. There also remain wider questions as to whether the scope of the Code should be widened to consider ownership responsibilities beyond listed equities; and whether there should be a review mechanism, independent of the FRC, to monitor investors’ adherence to the Code.

4. FINANCIAL AND STAFFING IMPLICATIONS

4.1 There are none arising from this report.

5. EQUAL OPPORTUNITY IMPLICATIONS

5.1. There are none arising from this report.

6. COMMUNITY SAFETY IMPLICATIONS

6.1. There are none arising from this report.

7. LOCAL MEMBER SUPPORT IMPLICATIONS

7.1. This report has no particular implications for any Members or wards.

8. LOCAL AGENDA 21 IMPLICATIONS

8.1. There are none arising from this report.

9. PLANNING IMPLICATIONS

9.1. There are none arising from this report.

10. BACKGROUND PAPERS

10.1 LAPFF member briefing, 'Reporting under the Stewardship Code' September 2010.

11. RECOMMENDATION

11.1 That Members approve the submission to the FRC of the appended statement of compliance with the Stewardship Code, and its publication on the MPF website.

IAN COLEMAN
DIRECTOR OF FINANCE

FNCE/186/10

MERSEYSIDE PENSION FUND

Statement of compliance with the U.K. Stewardship Code for Institutional Investors

Merseyside Pension Fund has a long-standing commitment to the values of stewardship, in relation to its conduct as an asset owner. It considers the responsibilities of stewardship to be part of its fiduciary duty to its stakeholders. In 2007, the Fund became a signatory to the United Nations Principles for Responsible Investment: stewardship is one of the cornerstones of the Fund's responsible investment policy.

Principle 1 – Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.

Merseyside Pension Fund takes its responsibilities as a shareholder seriously. It seeks to adhere to the Stewardship Code and encourages its appointed asset managers to do so too.

In practice the Fund's policy is to apply the Code both through its arrangements with its asset managers and other agents and through membership of the Local Authority Pension Fund Forum (LAPFF) and other collaborative groups. The Fund makes this explicit in its Statement of Investment Principles and will, in time, directly refer to the Stewardship Code in Section 5 of the SIP, 'Responsible Ownership'.[1]

The Fund has previously required its asset managers to state their approach to the ISC Code on the Responsibilities of Institutional Investors on a comply or explain basis. The Fund has also promoted adoption of the UNPRI as representing the highest standard of best practice of responsible ownership. The Fund's investment strategy seeks long-term returns from investing in equities and appoints asset managers who best reflect this long-termism in their investment philosophy and process.

The Fund does not delegate all responsibility for stewardship to its asset managers. It retains control of its voting policy, including where possible, over its underlying beneficial interests in pooled funds. The Fund retains a corporate governance and voting advisory and execution service (PIRC Ltd) to ensure that the maximum of its voting rights are exercised in support of high corporate governance standards.

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[1] http://mpfmembers.org.uk/content/statement-investment-principles

Principle 2 – Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.

The Fund encourages the asset managers it employs to have effective policies addressing potential conflicts of interest, when it comes to matters of stewardship.

The Fund requires all those who are directly involved in its management and governance to disclose any interest in any company, or other entity, in which the Fund has an ownership interest.

Principle 3 – Institutional investors should monitor their investee companies.

Day-to-day responsibility for managing our equity holdings is delegated to our appointed asset managers. The Fund expects them to monitor companies, and intervene where necessary, and to report back regularly on activity undertaken. Quarterly review meetings with our asset managers are used to raise particular issues of note or concern.

In addition, the Fund receives an ‘Alerts’ service from LAPFF, which highlights corporate governance issues of concern at investee companies.

Principle 4 – Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.

As highlighted above, responsibility for day-to-day interaction with companies is delegated to the Fund’s asset managers, including the escalation of engagement when necessary. Their guidelines for such activities are expected to be disclosed in their own statement of adherence to the Stewardship Code.

However, on occasion the Fund may itself choose to escalate activity, principally through engagement activity with LAPFF. When it believes it is warranted by the egregious conduct of a company board causing a loss of shareholder value, the Fund will seek redress by pursuing shareholder litigation, of whatever form and in whatever jurisdiction deemed suitable. The Fund considers this an appropriate tool for use by long-term shareholders to send a powerful message of reproach to a company’s directors and to the wider industry.

Principle 5 – Institutional investors should be willing to act collectively with other investors where appropriate.

The Fund seeks to work collaboratively with other institutional shareholders in order to maximize the influence that it can have on individual companies. The Fund seeks to achieve this through membership of the LAPFF, which engages with companies over environmental, social and governance issues on behalf of its members.

On environmental issues in particular, the Fund also pursues engagement with companies through membership of the Institutional Investors Group on Climate Change (IIGCC). One of the core objectives of the IIGCC is to engage in dialogues with companies to standardize and improve disclosure on climate change and improve performance.

Principle 6 – Institutional investors should have a clear policy on voting and disclosure of voting activity.

The Fund has adopted as its voting policy the Global Shareholder Voting Guidelines of its voting agent, PIRC Ltd. The Fund commissions PIRC to provide detailed voting recommendations and to exercise all votes attaching to its UK equity holdings in accordance with these. PIRC's analysis includes consideration of company explanations of compliance with the Corporate Governance Code. Where practical, the Fund seeks to exercise its voting rights attaching to its non-UK equity holdings.

The Fund discloses summary level information on voting activity on its website, on a semi-annual basis. The Fund intends to disclose voting activity by company on its website in the near future.

Principle 7 – Institutional investors should report periodically on their stewardship and voting activities.

The Fund maintains a Responsible Investment section on its website. Annual reporting on stewardship activity, including voting and engagement work, has formed part of the report and accounts. In future, it is envisaged that the Fund will report through a Responsible Investment Review, which will also report on the stewardship activities of the Fund's asset managers.

About Merseyside Pension Fund:

Merseyside Pension Fund is the 5th largest fund in the Local Government Pension Scheme. It has assets under management of £4.6 billion, managed by a combination of an in-house team and external investment managers.