



# Drax Power Group of the Electricity Supply Pension Scheme

Implementation Statement

June 2022

# Background and Implementation Statement

## Background

The Department for Work and Pensions ('DWP') is increasing regulation to improve disclosure of financially material risks. This regulatory change recognises Environmental, Social and Governance (ESG) factors as financially material and pension schemes need to consider how these factors are managed as part of their fiduciary duty. The regulatory changes require that schemes detail their policies in their statement of investment principles (SIP) and demonstrate adherence to these policies in an implementation report.

## Statement of Investment Principles (SIP)

In September 2020, the Group updated its SIP in to in response to the DWP regulation to cover:

- Policies for managing financially material considerations including ESG factors and climate change.
- Policies on the stewardship of the investments.

The SIP can be found online at the following web address:

<https://www.drax.com/wp-content/uploads/2020/09/001-Drax-SIP-Sep-2020-web-version.pdf>

Changes to the SIP (if any), covering the 12 months to 31 March 2022, are detailed on page 4.

## Implementation Report

This implementation report is to provide evidence that the Group continues to follow and act on the principles outlined in the SIP. This report details:

- Actions the Group has taken to manage financially material risks and implement the key policies in its SIP.
- The current policy and approach with regards to ESG and the actions taken with managers on managing ESG risks.
- The extent to which the Group has followed policies on engagement covering engagement actions with its fund managers and in turn the engagement activity of the fund managers with the companies in the investment mandate.
- Voting behaviour covering the reporting year up to 31 March 2022 for and on behalf of the Group including the most significant votes cast by the Group or on its behalf.

### Summary of key actions undertaken over the Group reporting year

- There were no major strategic changes over the 12 months to 31 March 2022. During the year, there were actions to rebalance the Group's assets towards their strategic benchmark weights and increase the expected return of the portfolio.
- For example, during Q3 2021, £23m was disinvested from the Group's holdings with Cardano which was overweight in comparison to its benchmark. £17m of this was used to meet transfer values and the further £6m was invested with the L&G Absolute Return Bond Fund (which is primarily used to meet ongoing cashflow requirements) to provide liquidity for the Group and move the mandate closer to its target weighting.

### Implementation Statement

This report demonstrates that Drax Power Group of the Electricity Supply Pension Scheme has adhered to its investment principles and its policies for managing financially material consideration including ESG factors and climate change.

Signed

Position

Date

# Changes to the SIP

There have been no significant changes to the SIP over the 12-month period to 31 March 2022 as there were no changes to the Group's strategic asset allocation. The most recent changes to the Group's SIP were made during September 2020 to comply with the DWP's ESG regulations.

# Managing risks and policy actions

Risk / Policy	Definition	Policy	Actions and details on changes to policy
Interest rates and inflation	The risk of mismatch between the value of the Group assets and present value of liabilities from changes in interest rates and inflation expectations.	To hedge c.75% of these risks on a gilts +0% basis.	<p>The Group's hedging arrangements are reviewed periodically to ensure they remain appropriate.</p> <p>During the year, the Group undertook an LDI retool to refine the hedge following changes to the Group's liabilities, as a result of significant transfer values.</p>
Liquidity	Difficulties in raising sufficient cash when required without adversely impacting the fair market value of the investment.	To maintain a sufficient allocation to liquid assets so that there is a prudent buffer to pay members benefits as they fall due (including transfer values), and to provide collateral to the LDI manager.	The Group holds an allocation to the L&G Absolute Return Bond Fund in order to maintain sufficient liquidity to meet ongoing cashflow requirements. During the period, the Fund was topped up to be more in line with its 3% target allocation.
Market	Experiencing losses due to factors that affect the overall performance of the financial markets.	To remain appropriately diversified and hedge away any unrewarded risks, where practicable.	During the year, there were actions to rebalance the Group's assets towards their strategic benchmark weights, maintaining a diversified portfolio.
Credit	Default on payments due as part of a financial security contract.	<p>To diversify this risk by investing in a range of credit markets across different geographies and sectors.</p> <p>To appoint investment managers who actively manage this risk by seeking to invest only in debt securities where the yield available sufficiently compensates the Group for the risk of default.</p>	No changes to policy during the period.

Environmental, Social and Governance	Exposure to Environmental, Social and Governance factors, including but not limited to climate change, which can impact the performance of the Group's investments.	To appoint managers who account for ESG factors as a part of their investment process.  The Group Trustees monitor the managers in this regard on an ongoing basis.	Further detail provided later in this report.
Currency	The potential for adverse currency movements to have an impact on the Group's investments.	Hedge the currency risk on direct lending assets as much as practically possible.	No changes to policy during the period.
Non-financial	Any factor that is not expected to have a financial impact on the Group's investments.	Non-financial matters are not taken into account in the selection, retention or realisation of investments.	No changes to policy during the period.

# Current ESG policy and approach

## ESG as a financially material risk

The SIP describes the Group's policy regarding ESG as a financially material risk. The Group has agreed a more detailed ESG policy which describes how it monitors and engages with the investment managers regarding the ESG policies. This page details the Group's ESG policy.

### Current Policy

Areas for engagement	Method for monitoring and engagement	Circumstances for additional monitoring and engagement
Environmental, Social, Corporate Governance factors and the exercising of rights	<ul style="list-style-type: none"><li>The Group Trustees' investment managers provide annual reports on how they have engaged with issuers regarding social, environmental and corporate governance issues.</li><li>The Group Trustees receive information from their investment advisers on the investment managers' approaches to engagement.</li></ul>	<ul style="list-style-type: none"><li>The manager has not acted in accordance with their policies and frameworks.</li><li>The manager's policies are not in line with the Group Trustees' policies in this area.</li></ul>

## Areas of assessment

The below table outlines the areas which the Group’s investment managers are assessed on when evaluating their ESG policies and engagements. The Group Trustees intend to review the Group’s ESG policies and engagements periodically to ensure they remain fit for purpose.

<b>Risk Management</b>	<ol style="list-style-type: none"> <li>1. Integrating ESG factors, including climate change risk, represents an opportunity to increase the effectiveness of the overall risk management of the Group.</li> <li>2. ESG factors can be financially material and managing these risks forms part of the fiduciary duty of the Group Trustees.</li> </ol>
<b>Approach / Framework</b>	<ol style="list-style-type: none"> <li>3. The Group Trustees should understand how asset managers make ESG decisions and will seek to understand how ESG is integrated by each asset manager.</li> <li>4. ESG factors are relevant to investment decisions in all asset classes.</li> <li>5. Managers investing in companies’ debt, as well as equity, have a responsibility to engage with management on ESG factors.</li> </ol>
<b>Reporting &amp; Monitoring</b>	<ol style="list-style-type: none"> <li>6. Ongoing monitoring and reporting of how asset managers manage ESG factors is important.</li> <li>7. ESG factors are dynamic and continually evolving; therefore the Group Trustees will receive training as required to develop their knowledge.</li> <li>8. The role of the Group’s asset managers is prevalent in integrating ESG factors; the Group Trustees will, alongside the investment advisor, monitor ESG in relation to the asset managers’ investment decisions.</li> </ol>
<b>Voting &amp; Engagement</b>	<ol style="list-style-type: none"> <li>9. The Group Trustees will seek to understand each asset managers’ approach to voting and engagement when reviewing the asset managers’ approach.</li> <li>10. Engaging is more effective in seeking to initiate change than disinvesting.</li> </ol>
<b>Collaboration</b>	<ol style="list-style-type: none"> <li>11. Asset managers should sign up and comply with common codes and practices such as the UNPRI &amp; Stewardship code. If they do not sign up, they should have a valid reason why.</li> <li>12. Asset managers should engage with other stakeholders and market participants to encourage best practice on various issues such as board structure, remuneration, sustainability, risk management and debtholder rights.</li> </ol>

# Engagement

Isio engaged with the Group's investment managers over the year on behalf of the Group Trustees to discuss their ESG policies and set actions and priorities.

As the Group invests in pooled vehicles accessed via fund managers the managers provided details on their engagement actions, including a summary of the engagements by category for the 12-month period to the end of March 2022.

Fund name	Engagement summary	Commentary
Cardano Solution Fund 12	Total direct engagements: 0	<p>Given the fund of funds structure of the Group's mandate with Cardano, there were no direct engagements between Cardano and the underlying portfolio companies over the reporting period. Instead, Cardano have provided engagement data for their external investment managers. Cardano engage with all investment managers regularly through their manager research team, operational due diligence team and as part of the delivery of Implementation Statements for their clients.</p> <p>Examples of significant engagements from the external investment managers include:</p> <p><b>Egerton</b> – Egerton engaged with a car manufacturing company to improve their governance, with the intention of increasing shareholder returns and the treatment of minority shareholders. Egerton had frequent one-on-one discussions with the Chairman about governance where they conveyed a strong preference that minority shareholders should be better represented and receive a vote. Egerton proposed that the company equalise or harmonise its dual share class structure of non-voting preference shares and voting ordinary shares into one share class of voting shares. This has provided shareholders with better representation and improved the treatment for a variety of stakeholders, particularly minority shareholders.</p> <p><b>CC Japan</b> – CC Japan engaged with a construction company following concerns over an insufficient number of female directors on the board. The management of the company has since made a step forward to improve gender diversity on the board, driven by Cardano's engagement, by appointing a female director as an independent audit director in June 2021.</p>

Permira Credit Solutions II	<p><b>Total engagements: 4</b></p>	<p>Permira's position as lenders means that they often rely on the equity sponsor to report ESG-related concerns and lead ESG improvements. However, Permira maintain ongoing contact with the management teams of their portfolio companies and are able to leverage their influence when applicable.</p> <p>Examples of significant engagements include:</p> <p><b>Soho House</b> – Permira engaged with Soho House by encouraging the development of their sustainability strategy focusing on: climate, environment, diversity and inclusion, social and economic. This led to a new sustainability section on their website which showcased their strategy and progress. Permira also developed a sustainability linked loan ("SLL") with Soho House, engaging with external advisers to develop and identify suitable ESG Key Performance Indicators ("KPIs") for the SLL.</p> <p><b>Paperchase</b> – Permira engaged with Paperchase to expand and develop their existing 'Paperchase Promise', focusing on sustainable sourcing and plastic reduction. Although Permira believe the company recognises sustainability as a key pillar of their new strategy, Permira also introduced an external adviser to support on sustainability. This has increased the number of board level discussions on ESG factors.</p>
Permira Credit Solutions IV	<p><b>Total engagements: 4</b></p>	<p>Permira's position as lenders also limits their engagement power with respect to the PCS IV Fund.</p> <p>The engagement with Soho House above also applies to the PCS IV Fund as the investment was held across both Funds. Permira could not provide any other examples of significant engagement for the PCS IV Fund.</p> <p>Permira have also requested ESG-related KPI data for PCS IV as part of a pilot process. Likewise, Permira issued its second ESG questionnaire with expanded questions to align with industry standards agreed in the ESG Data Convergence Project in December 2021. The questionnaire was sent to all companies within PCS IV. Additionally, Permira engaged with an external company to undertake a climate risk assessment of their portfolio.</p>
L&G Absolute Return Bond Fund	<p><b>Total engagements: 125</b></p> <p>Environmental: 80</p> <p>Social: 34</p> <p>Governance: 62</p> <p>Other: 26</p> <p>Please note some engagements cover more than one area.</p>	<p>L&amp;G's Investment Stewardship team are responsible for engagement activities across all funds. L&amp;G share their finalised ESG scorecards with portfolio companies and the metrics on which they are based. L&amp;G regularly monitor companies and where engagements are unsuccessful, the team will assess where problems arose and new approaches to be employed. L&amp;G engage with regulators, governments, and other industry participants to address long-term structural issues. L&amp;G has firm wide stewardship priorities with a current priority focus on inequality, ethnic diversity and tax transparency.</p> <p>L&amp;G do not consider engagement on a fund-by-fund basis but do actively approach ESG at a firm level. As such, L&amp;G do not employ a formal framework for measuring the success of an engagement, as they believe success is difficult to measure, and is best reflected in the overall market value of an asset. L&amp;G could not provide specific examples of significant engagements.</p>

L&G Active Corporate Bond All Stocks Index Fund	<p><b>Total engagements: 147</b></p> <p>Environmental: 82</p> <p>Social: 48</p> <p>Governance: 80</p> <p>Other: 28</p> <p>Please note that the data above applies to the 12 months to 31 December 2021 and some engagements cover more than one area.</p>	The above wording on L&G's Investment Stewardship team and engagement on a fund-by-fund basis applies to all the L&G funds. Likewise, L&G could not provide specific examples of significant engagements.
L&G LDI Funds	L&G were unable to provide details of engagement during this period for these funds. Isio are working with	The above wording on L&G's Investment Stewardship team and engagement on a fund-by-fund basis applies to all the L&G funds. Likewise, L&G could not provide specific examples of significant engagements.
L&G Long Lease Property Fund	L&G to find ways of improving their engagement reporting and expect L&G to start sharing engagement data from Q2 2022.	

# Voting (for equity/multi asset funds only)

As the Group invests via fund managers the managers provided details on their voting actions including a summary of the activity covering the reporting year up to 31 March 2022. The managers also provided examples of any significant votes.

Fund name	Voting summary	Examples of significant votes																																										
Cardano Solution Fund 12	<p>Proposals voted: 0</p> <p>As Cardano holds no direct equity investments, they do not have voting rights for the underlying portfolio companies. Instead, Cardano provided voting data and examples of significant votes cast for the external investment managers they deem as being 'high focus' in relation to ESG (meaning ESG factors could materially impact the risk and return profile of the underlying manager's strategy).</p>	<p>Examples of significant votes cast by the external investment managers include:</p> <p><b>Egerton</b> – voted in favour of a shareholder proposal for the Canadian Pacific's board of directors to produce a greenhouse gas emission levels reduction plan, and to report annually on the progress made towards the plan. Egerton believed the vote in favour was the correct decision based on ESG considerations.</p> <p><b>Sunriver</b> – Sunriver voted for a dissident proxy against Box Inc, lead by an activist shareholder who proposed resolutions to nominate three of their own directors to the ten-member board, citing slow growth and a lack of company profitability. The analyst at Sunriver recommended this vote as they believed this would be in the best interests of the company and their shareholders.</p>																																										
	Full voting data for external managers Cardano have identified as 'high focus' is as follows:																																											
	<table border="1"> <thead> <tr> <th>Manager</th> <th>Potential votes</th> <th>Proportion of votes cast</th> <th>Proportion of votes cast for</th> <th>Proportion of votes cast against</th> <th>Proportion of votes abstained</th> </tr> </thead> <tbody> <tr> <td>Amia</td> <td>109</td> <td>95%</td> <td>100%</td> <td>-</td> <td>-</td> </tr> <tr> <td>CC Japan</td> <td>337</td> <td>100%</td> <td>100%</td> <td>-</td> <td>-</td> </tr> <tr> <td>Egerton</td> <td>513</td> <td>94%</td> <td>97%</td> <td>0%</td> <td>3%</td> </tr> <tr> <td>Polar Capital</td> <td>538</td> <td>99%</td> <td>95%</td> <td>5%</td> <td>0%</td> </tr> <tr> <td>Sands Capital</td> <td>524</td> <td>96%</td> <td>90%</td> <td>5%</td> <td>5%</td> </tr> <tr> <td>Sunriver</td> <td>155</td> <td>92%</td> <td>90%</td> <td>5%</td> <td>5%</td> </tr> </tbody> </table>		Manager	Potential votes	Proportion of votes cast	Proportion of votes cast for	Proportion of votes cast against	Proportion of votes abstained	Amia	109	95%	100%	-	-	CC Japan	337	100%	100%	-	-	Egerton	513	94%	97%	0%	3%	Polar Capital	538	99%	95%	5%	0%	Sands Capital	524	96%	90%	5%	5%	Sunriver	155	92%	90%	5%	5%
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