



# The Horserace Totalisator Board (1968) Pension Scheme Implementation Report

2021

# 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 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)

The Scheme has updated its SIP 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 web address <https://iiconic-ptluk.s3.eu-west-2.amazonaws.com/s3fs-public/Tote-SIP-2020-updated-min.pdf>. Changes to the SIP are detailed on the following pages.

## Implementation Report

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

- actions the Trustee 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 Trustee 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 they invest

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

- Over 2020, the Scheme reviewed the investment strategy and cashflow expectations for the next 3 years to consider how the investment strategy should evolve as capital is returned from its illiquid investments (Direct Lending and Commercial Real Estate Debt Funds). The Trustee agreed, following a consultation with the Company, that the investment strategy would de-risk over the medium term. The de-risking of the strategy would involve three actions:
  - o An additional investment into the existing M&G Alpha Opportunities Fund (increasing the allocation to c.20% of the total portfolio). This took place in May 2020 and increased the Scheme's allocation to lower-risk contractual assets;
  - o An increase in the Scheme's allocation to the LDI portfolio. This was completed shortly following reporting end, in May 2021 resulting in a hedge ratio of 100% of uninsured liabilities on a self-sufficiency basis (an increase from 84% originally); and
  - o The implementation of a new Buy and Maintain Corporate Bond mandate (c.20% of the portfolio). The Trustee are set to consider the allocation of this mandate in conjunction with the latest Actuarial Valuation Results for the Scheme.

### Implementation Statement

This report demonstrates that The Horserace Totalisator Board (1968) Pension Scheme has adhered to its investment principles and its policies for managing financially material considerations including ESG factors and climate change.

**Signed:** Colin Richardson

**Position:** Trustee

**Date:** 1 October 2021

# Managing risks and policy actions DB

Risk / Policy	Definition	Policy	Actions
<b>Interest rates and inflation</b>	The risk of mismatch between the value of the Scheme assets and present value of liabilities from changes in interest rates and inflation expectations.	To target a hedge of c.84% on a self-sufficiency basis (liabilities not covered by the buy-in) of these risks on a self-sufficiency basis. This is expected to move to 100% hedged over time.	Shortly following the reporting period (May 2021), the Scheme increased the level of hedging provided by their LDI portfolio to c.100% of the uninsured liabilities on a self-sufficiency basis. The Trustee regularly reviews the overall level of hedging and, as part of a new strategy, is set to review this position over the next 12 months.
<b>Liquidity</b>	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 Scheme meets a large portion of the member benefits through the buy-in policy and Company contributions. However, the Scheme also holds assets in a daily dealt Absolute Return Bond Fund with LGIM to meet any unexpected cashflows and / or investment commitments. The Trustee reviews this position on a quarterly basis through the Investment Performance Report.
<b>Market</b>	Experiencing losses due to factors that affect the overall performance of the financial markets.	To remain appropriately diversified and hedge away unrewarded risks, where affordable and practicable.	The Scheme reduces market risk by diversifying its assets across a range of asset classes and investment managers. The actual allocations are monitored on a quarterly basis relative to the Strategic Asset Allocation (set out in the SIP) in the Investment Performance Report.
<b>Credit</b>	Default on payments due as part of a financial security contract.	To diversify this risk by investing in a range of credit markets across different geographies and sectors.	The Scheme reduces credit risk by diversifying its assets across a range of investment managers which provide exposures to a range of sectors and geographies.

			These positions are monitored on a quarterly basis relative to the Strategic Asset Allocation in the Investment Performance Report.
<b>Environmental, Social and Governance</b>	Exposure to Environmental, Social and Governance factors, including but not limited to climate change, which can impact the performance of the Scheme's investments.	To appoint managers who satisfy the following criteria, unless there is a good reason why the manager does not satisfy each criteria:  1. Responsible Investment ('RI') Policy / Framework  2. Implemented via Investment Process  3. A track record of using engagement and any voting rights to manage ESG factors  4. ESG specific reporting  5. UN PRI Signatory  The Trustee monitor the managers on an ongoing basis.	ESG actions undertaken:  The Trustees received training shortly following quarter end on their investment managers ESG policies and how these are integrated in their investment decisions.  Managers will be required to update the Trustee on actions they have taken in respect of ESG factors and their engagement activity when they attend meetings with the Trustee.  More details of the ESG policy and how it was implemented are presented later in this report.
<b>Currency</b>	The potential for adverse currency movements to have an impact on the Scheme's investments.	The Trustee hedges the Scheme's currency exposure as much as is deemed possible.	
<b>Non-Financial</b>	Any factor that is not expected to have a financial impact on the Scheme's investments.	Non-financial matters are considered in the selection, retention or realisation of investments.	

# Changes to the SIP

## Policies added to the SIP

Date updated: August 2020

**How the investment managers are incentivised to align their investment strategy and decisions with the Trustee's policies.**

- As the Scheme is invested in pooled funds, there is not scope for these funds to tailor their strategy and decisions in line with the Trustee's policies. However, the Trustee invests in a portfolio of pooled funds that are aligned to the strategic objective.

**How the investment managers are incentivised to make decisions based on assessments of medium to long-term financial and non-financial performance of an issuer of debt or equity and to engage with them to improve performance in the medium to long-term.**

- The Trustee reviews the investment managers' performance relative to medium and long-term objectives as documented in the investment management agreements.
- The Trustee does not incentivise the investment managers to make decisions based on non-financial performance.

**How the method (and time horizon) of the evaluation of investment managers' performance and the remuneration for their services are in line with the Trustee's policies.**

- The Trustee reviews the performance of all of the Scheme's investments on a net of cost basis to ensure a true measurement of performance versus investment objectives.
- The Trustee evaluates performance over the time period stated in the investment managers' performance objective, which is typically 3 to 5 years.
- Investment manager fees are reviewed periodically to make sure the correct amounts have been charged and that they remain competitive.

**The method for monitoring portfolio turnover costs incurred by investment managers and how they define and monitor targeted portfolio turnover or turnover range.**

- The Trustee does not directly monitor turnover costs. However, the investment managers are incentivised to minimise costs as they are measured on a net of cost basis.



**The duration of the Scheme's arrangements with the investment managers**

- The duration of the arrangements is considered in the context of the type of fund the Scheme invests in.
  - For closed-ended funds or funds with a lock-in period, the Trustee ensures the timeframe of the investment or lock-in is in line with the Trustee objectives and Scheme's liquidity requirements.
  - For open-ended funds, the holding periods are flexible, and the Trustee will from time-to-time consider the appropriateness of these investments and whether they should continue to be held.
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# Implementing the current ESG policy and approach

## ESG as a financially material risk

The SIP describes the Scheme's policy with regarding to ESG as a financially material risk. This page details how the Scheme's ESG policy is implemented, while the following page outlines Isio's assessment criteria as well as the ESG beliefs used in evaluating the Scheme's managers' ESG policies and procedures. The rest of this statement details our view of the managers, our actions for engagement and an evaluation of the stewardship activity.

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

### Implementing the Current ESG 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 and engagement activity	<ul style="list-style-type: none"><li>• Through the manager selection process ESG considerations will form part of the evaluation criteria</li><li>• The Scheme's investment advisor Isio will monitor managers' ESG policies on an ongoing basis.</li></ul>	<ul style="list-style-type: none"><li>• The manager has not acted in accordance with their policies and frameworks.</li></ul>



## Areas of assessment and ESG beliefs

<b>Risk Management</b>	<ol style="list-style-type: none"> <li>1. ESG factors are important for risk management and can be financially material. Managing these risks forms part of the fiduciary duty of the Trustee.</li> <li>2. The Trustee believe that ESG integration leads to better risk adjusted outcomes and want a positive ESG tilt to the investment strategy.</li> </ol>
<b>Approach / Framework</b>	<ol style="list-style-type: none"> <li>3. The Trustee want to understand how asset managers integrate ESG within their investment process and in their stewardship activities.</li> <li>4. The Trustee believe that sectors aiming for positive social and environmental impacts may outperform as countries transition to more sustainable economies. Where possible the investment strategy will allocate to these sectors.</li> <li>5. The Trustee will consider the ESG values and priority areas of the stakeholders and sponsor and use these to set ESG targets.</li> </ol>
<b>Voting &amp; Engagement</b>	<ol style="list-style-type: none"> <li>6. ESG factors are relevant to all asset classes and, whether equity or debt investments, managers have a responsibility to engage with companies on ESG factors.</li> <li>7. The Trustee believe that engaging with managers is more effective to initiate change than divesting and so will seek to communicate key ESG actions to the managers in the first instance.</li> <li>8. The Trustee want to understand the impact of voting &amp; engagement activity within their investment mandates.</li> </ol>
<b>Reporting &amp; Monitoring</b>	<ol style="list-style-type: none"> <li>9. ESG factors are dynamic and continually evolving, therefore the Trustee will receive training as required to develop their knowledge.</li> <li>10. The Trustee will seek to monitor key ESG metrics within their investment portfolio to understand the impact of their investments.</li> </ol>
<b>Collaboration</b>	<ol style="list-style-type: none"> <li>11. Asset managers should be actively engaging and collaborating with other market participants to raise ESG investment standards and facilitate best practices as well as sign up and comply with common codes such as UNPRI and TCFD.</li> <li>12. The Trustee should seek to sign up to a recognised ESG framework to collaborate with other investors on key issues.</li> </ol>

# ESG summary and engagement with the investment managers

Manager and Fund	ESG Summary	Actions identified	Engagement details
<b>M&amp;G – Diversified Credit</b>	<p>M&amp;G have evidenced their ability to consider the significance of ESG factors in this Fund. M&amp;G should consider measurable ESG aims for the Fund and increase the number of ESG risk metrics that are being monitored. Although M&amp;G are actively developing their integrated ESG approach in investment decisions, M&amp;G should consider more in depth reporting for clients and progress reports on aims for the Fund.</p>	<p>M&amp;G currently have a qualitative approach and are working towards a more quantitative approach (scorecard). M&amp;G should seek to roll this out for all analysts, and they can develop an integrated ESG scoring system which scores both at an individual issuer level and also at a sector/country level.</p> <p>M&amp;G should clearly publicise engagements throughout the quarter on their website and provide updates on past engagements in their quarterly reports and on their website – with engagements focused on companies the Fund invests in.</p> <p>M&amp;G should increase the number of risk metrics they monitor such as, climate change and the sensitivity to these metrics to the portfolio.</p>	<p>Isio engaged with M&amp;G in Q2 2020 on the Trustee’s behalf to review their ESG policies and set actions and priorities. Isio reports back to the Trustee with updates on the M&amp;G engagements.</p>
<b>L&amp;G Liability Driven Investment</b>	<p>LGIM have a team dedicated to understanding and assessing the impact of ESG factors for the wider business.</p>	<p>LGIM should include the ESG scoring of counterparties in regular client reporting of LDI Funds.</p>	<p>LGIM noted a timeline for reporting ESG metrics and scoring, earmarking Q2 2021 for release of quarterly client ESG reports.</p>

	<p>LGIM use proprietary tools to quantify and monitor ESG risk, and believe engaging with regulators, governments and other industry participants will help to mitigate ESG risk.</p>		
<p><b>LGIM – Diversified Credit</b></p>	<p>LGIM is aware of ESG issues and the effect on long-term returns within its Fund offering. They have also taken steps to integrate these issues within their investment process at a business level. However, there was a lack of fund-specific information with respect to risk management and reporting and given the direction of travel we would expect these points to be addressed in the coming months.</p>	<p>LGIM should provide more information on their engagement with companies within the Fund.</p> <p>LGIM should provide standard and regular reporting on the Funds ESG risk exposure, carbon emissions exposure and fund-specific summary of voting and engagement activity.</p> <p>LGIM should be able to clearly evidence the materiality of ESG considerations in the investment process.</p>	<p>Isio engaged with LGIM in February 2021 where it was noted:</p> <ul style="list-style-type: none"> <li>- LGIM confirmed they are looking to update the reporting at fund level going forwards.</li> <li>- LGIM noted in following quarter they will begin providing Carbon data analysis.</li> <li>- ESG data is now directly incorporated into the credit assessments and an overall score following a redesign in their research, synchronisation and research across equity and credit.</li> </ul>
<p><b>LaSalle – Real Estate Debt Strategy III (“REDS III”)</b></p>	<p>LaSalle largely integrate ESG at the origination stage of their investment process, and have demonstrated commitment to ESG within the wider industry. However, LaSalle’s ESG influence is restricted by their position as a debt investor, meaning they have limited</p>	<p>LaSalle could look to implement a scoring system on the initial screening of the Fund’s loans in order to measure the effectiveness of their engagement overtime.</p> <p>LaSalle could provide commentary on their engagement activities on a more regular basis.</p>	<p>Isio engaged with LGIM in March 2021 where it was noted:</p> <ul style="list-style-type: none"> <li>- LaSalle incorporate environmental due diligence into their process, ESG considerations are viewed as part of the risk management. ESG scoring might be incorporated however LaSalle note that they are somewhat restricted in terms of varying data availability give the nature of the private debt asset class.</li> </ul>

control over the underlying real estate investments. Reporting of ESG monitoring on an ongoing basis is a key area requiring development.

- LaSalle note they are looking into including ESG data into their reports.

# Engagement

As the Scheme invests via fund managers the managers provided details on their engagement actions including a summary of the engagements by category for the 12 months to 31 March 2020.

Fund name	Engagement summary	Commentary
LGIM LDI Funds	<p>LGIM have engaged with a number of industry participants on long term strategic issues in relation to LDI, including:</p> <ul style="list-style-type: none"> <li>- The introduction of central clearing</li> <li>- The LIBOR transition</li> <li>- Recognising the pricing issues with bilateral RPI swaps</li> </ul>	<p>LGIM leverage the wider capabilities of the global firm to engage with companies. The team also regularly engage with regulators, governments and other industry participants to address long term structural issues, aiming to stay ahead of regulatory changes and adopt best practice.</p>
LGIM Absolute Return Bond Fund	<p>LGIM currently do not provide details of their engagement activities at Fund level, however, this is something they are looking to implement going forwards.</p>	<p>LGIM are aiming to improve their engagement reporting over 2023. Isio will continue to liaise with LGIM around the provision of this information.</p>
M&G Alpha Opportunities Fund	<p>Total Engagements: 14</p> <p>Environmental: 5</p> <p>Social: 2</p> <p>Governance: 7</p>	<p>Examples of significant engagements include:</p> <p><b>Quadient</b> – M&amp;G’s engagement with Quadient involved allowing the company to explain its full ESG strategy to the manager. This enabled M&amp;G to look in greater depth at its approach to supply chain management, especially relating to conflict minerals and human rights. Following their review M&amp;G asked the company to publish full public policy documents on human rights, supplier practices, business ethics and data privacy increasing the level of disclosure across the business.</p> <p>AB InBev – M&amp;G engaged with multi-national drinks company AB InBev, urging it to set</p>

		<p>medium-term scope 1-3 emissions reduction targets, post 2025, as well as a net zero target for 2050 or sooner. These primarily focused on the heat required in the brewing process - which is currently two-thirds of its energy requirements - and product packaging, which represents 40% of its scope 3 emissions. M&amp;G noted the company is aware of its challenges and is working on the solutions. The Manager is now giving the company time to work through these solutions, and will await its next ESG report, to be published in February 2021, to see if any new targets are published before deciding if further engagement is necessary.</p>
<p>Partners Group Private Market Credit Strategies 2015 Fund*</p>	<p>Total engagements: 4 Corporate: 4</p>	<p>Partners Group maintain ongoing contact with the management teams of their portfolio companies however, given their position as lenders they will typically rely on the equity sponsor to report ESG-related concerns and drive ESG improvements. Investing in private companies also reduces the transparency of the information available to assess ESG risks.</p> <p><b>MFG</b> – The CEO of MFG attended PG's Private Debt Academy to give a presentation on his business and field audience questions. This allowed Further insight into business / industry and current trends impacting it.</p>
<p>Partners Group Private Market Credit Strategies 2016 Fund</p>	<p>Total Engagements: 6 Corporate: 6</p>	<p>Partners Group maintain ongoing contact with the management teams of their portfolio companies however, given their position as lenders they will typically rely on the equity sponsor to report ESG-related concerns and drive ESG improvements. Investing in private companies also reduces the transparency of the information available to assess ESG risks.</p> <p>Examples of significant engagements include:</p> <p><b>DBI Services</b> - PG took an active Board and Ownership role following the comprehensive debt restructuring with the firm making significant progress following the board restructure.</p>
<p>LaSalle Commercial Real Estate Debt Fund</p>	<p>LaSalle currently do not provide details of their engagement activities at Fund level.</p>	<p>Isio will continue to liaise with LaSalle around the provision of this data.</p>

