

# Implementation Statement – DB assets

26 January 2024



## 1. Background

In 2019, the government published regulations<sup>1</sup> which introduced new requirements for pension schemes like ZPen setting out the policies they need to explicitly include in their Statement of Investment Principles (SIP) (the document that sets out the investment principles and practices the Trustee follows when governing the Scheme's assets).

This expanded on legislation<sup>2</sup> which was introduced in 2018 for schemes with more than 100 members to disclose the risks of their investments, including the ones arising from environmental, social and governance (ESG) considerations. It also required the Trustee to disclose policies in relation to the stewardship of investments, including engagement with investee firms and the exercise of the voting rights associated with the investment.

Further to this, from 1 October 2020 the Trustee is required to produce an implementation statement setting out how it has acted on the principles it set out in the SIP, including how it takes account of the views which, in its opinion, members hold. This must cover policies on the exercise of voting rights related to its investments and engagement activities. This document is intended to meet those requirements and will be included in the Scheme's Report and Accounts and published on [www.zpen.info](http://www.zpen.info).

The DB SIP in force during the Scheme year ended 30 June 2023 was prepared in accordance with all relevant legislation in-force at the date of the approvals. The SIP outlines the principles and policies governing investment decisions made by, or on behalf of the Trustee for the management of the defined benefit (DB) assets and the Trustee's policy for complying with Sections 35 and 36 of the Pensions Act 1995 and subsequent legislation.

### Review of the DB SIP during the year

During the year ended 30 June 2023 the Trustee agreed to a net zero ambition of 2050, the DB SIP was therefore reviewed and amended to reflect the net zero ambition. The review took place in 2022 and the DB SIP was formally approved by the Trustee on 29 September 2022. Prior to formally approving the DB SIP on that date, the Trustee's investment advisers reviewed the DB SIP to ensure it continued to comply with all statutory requirements and to incorporate the Trustee's net zero ambition as a secondary objective subject to the Trustee's primary goal of paying benefits to members.

During the Scheme year, the Trustee also agreed its Stewardship priorities. These were discussed at the Funding Committee in February 2023 and approved by the Trustee in March 2023. Further information is included in the 'Policy and Response' section of this Statement.

This Statement covers the policies included in the DB SIP in effect on 30 June 2023.

## 2. How have the policies in the SIP been followed over the year?

In the opinion of the Trustee, the policies set out in the SIP have been adhered to throughout the year for the Scheme. The rest of this statement explains how and the extent to which these policies have been adhered to.

### ***Policies for choosing and realising investments, and the kinds of investments to be held***

The DB SIP outlines the Trustee's principles and policies for choosing investments and the kind of investments to be held. In selecting investments, the Trustee obtains and considers written advice from a regulated investment adviser.

- For the ZPen and ES Executives' Sections, the Trustee complies with these policies by identifying appropriate objectives which reflect the risk and return requirements and then constructing a portfolio of investments to meet these objectives. In the Scheme year, the Trustee made a number of changes to the investment strategy:
  - In July 2022, the Trustee had target hedging ratios for interest rates and inflation (on a gilts + 1.50% basis) at 90% and 80% respectively for the ZPen Section. The target hedging ratios were set on a glide path that were due to finish in June 2023, however due to market conditions, the rise in gilt yields meant a trigger was reached to accelerate the glide path. Following this, the Funding Committee agreed to further accelerate the hedging ratios to their agreed target as soon as reasonably practical. Interest rates and inflation represent a market risk for the Scheme on an economic basis, and hedging reduces these risks. The revised investment guidelines were signed on 5 July 2022.
  - In March 2023, the Trustee agreed to refinements of the investment strategy for the ZPen Section:
    - An allocation equal to 2.5% of the section's assets to a new asset class, infrastructure equity. The Trustee intends to subscribe to c.£120m of investments in line with the section's approved strategic asset allocation (SAA). The subscription is likely to be complete by Q1 2024.
    - Increase of the interest rate and inflation hedging ratios, due to the continued increase in gilt yields, the Trustee increased the hedging to 95% and 90% for interest rates and inflation (on a gilts+1.50% basis). The revised investment guidelines were signed in April 2023.

<sup>1</sup> Occupational Pension Scheme (Investment and Disclosure) (Amendment) Regulations 2019

<sup>2</sup> The Occupational Pension Schemes (Investment and Disclosure) (Amendments) Regulations 2018 (now the Pension Protection Fund (Pensionable Service) and Occupational Pension Schemes (Investment and Disclosure) (Amendment and Modification) Regulations 2018)

- No changes to the SIP were required as a result of these investment strategy amendments. Formal advice was provided to the Trustee by regulated investment advisers prior to the SAA changes, confirming the suitability of the investments for the purposes of Section 36 of the Pensions Act 1995. The investment advisers were involved throughout the investment review processes to leverage market expertise in order to review the Trustee's investment analyst's proposals. The DB Investment Policy Implementation Document (IPID) will be updated to reflect the amendments to the SAA for ZPen Section.

Throughout the year, the Managers had discretion in the timing of realisation of investments.

The asset allocation is reviewed for all arrangements on a quarterly basis via the Funding Committee. The DB assets are referred to the Trustee board on a quarterly basis and are reviewed regularly by the ZPen team and the Trustee's investment analyst. In September 2022, following the announcement of the Government's growth plan ("mini-budget"), markets experienced heightened volatility. Long-dated gilts yields in particular moved with unprecedented scale and speed resulting in a number of collateral calls for liability driven investment (LDI) portfolios and funds. At one point during September, the value of the Scheme's LDI portfolio dropped by more than 60% since the beginning of the month – or £900m. Yield movements in late September meant the portfolio increased in size again, the overall monthly movement was a decrease of £300m. While these numbers are extraordinary on an asset-only basis, the funding position of the Scheme improved over the Scheme year with the increase in the gilts yields. As a result of the gilt yield volatility there were a number of transactions that took place to re-balance the assets back within the agreed SAA. Any re-balancing that takes place outside of the monthly outflows is reported to the Funding Committee and the Trustee board on a quarterly basis. The Trustee is comfortable that over the year the investments held were consistent with the policies set out in the DB SIP.

For more information on how the Scheme's investments are governed, please see the Report and Accounts at [www.zpen.info](http://www.zpen.info).

#### ***Policies on managing and measuring risk, and expected returns DB assets: ZPen & ES Executives' Sections***

The Trustee's objectives are to:

- invest in assets of appropriate quality and liquidity which meet, together with contributions from the employers, the benefits the Scheme provides as and when they fall due, as set out in the Trust Deed and Rules and
- to manage the investment risk relative to the agreed levels to which the Trustee is prepared to expose the Scheme.

The Trustee believes by fulfilling its objectives and by adhering to the policies in the DB SIP it ensures that assets are invested in the best interests of members and their beneficiaries.

During the year, the Trustee monitored the return on assets on a quarterly basis. The SAA changes on a quarterly basis in line with an agreed glidepath that was due to end in June 2023. Assets were monitored and re-balanced in line with the agreed policy. Where possible, re-balancing was done with monthly outflows (for example, pensioner payroll) to reduce unnecessary transaction costs. Transaction costs increased significantly over the Scheme year due to two separate investment strategy changes and the market volatility following the mini-budget.

The Trustee sets target hedging ratios for interest rates and inflation in order to manage interest rate and inflation risk. The target hedging ratios were set on a glide path that was due to finish in June 2023, however due to market conditions, the rise in gilt yields meant a trigger was reached to accelerate the glide path. Following this, the Funding Committee agreed to further accelerate the hedging ratios to their agreed target as soon as reasonably practical. Interest rates and inflation represent a market risk for the Scheme on an economic basis, and hedging reduces these risks. The revised investment guidelines were signed on 5 July 2022.

Due to the gilt yields remaining high throughout the Scheme year, the Trustee approved a further increase in interest rate and inflation hedging ratios to 95% and 90% respectively (on a gilts + 1.5% basis) in March 2023.

The Trustee has an Integrated Risk Management (IRM) policy that it adheres to. Risk monitoring has been reported to the Trustee board via the Funding Committee on a quarterly basis. Any investment strategy decisions are taken in the context of IRM, this includes the investment strategy refinements referred to in the previous section.

#### ***Responsible Investment (RI) Strategy***

As a long term investor, the Trustee has agreed that the Scheme should be an active responsible investor. The Trustee has agreed five responsible investment principles:

- We believe that incorporating ESG factors into investment decisions improves long term risk-adjusted returns
- We are an active owner – we vote proxies and engage, where appropriate
- We take a pragmatic approach to responsible investments – we focus on what matters most
- We note Zurich Group's strategy and will leverage its global resources where it makes sense
- We will evolve our responsible investment approach over time – and acknowledge that we will never be done

During the latest Scheme year the Trustee has continued its focus on climate change risks and opportunities as a result of the responsible investment (RI) strategy development as well as changing regulatory requirements. The additional climate change regulations under Section 175(2A) of the Pensions Act 1995 require pension schemes with assets exceeding £5bn to comply with the Task Force on Climate-Related Financial Disclosures (TCFD) recommendations, applicable from 1st October 2021. In order to comply with the regulations the Trustee has agreed and published a TCFD report, describing governance, strategy, metrics and targets, and risk management of climate change risks and opportunities. The TCFD report is included in the Responsible Investment section of the Scheme's website [www.zpen.info/Library/Responsible Investment](http://www.zpen.info/Library/Responsible%20Investment). The Trustee continues to monitor the progress on its 25% weighted average carbon intensity (WACI) reduction target over 5 years for its equity and corporate bond portfolios.

### ***Policies on the exercise of voting rights and undertaking engagement activities***

The Trustee's specific strategy on engagement is summarised below, together with its assessment of how, and the extent to which, this has been implemented over the Scheme year to 30 June 2023:

## **Policy & response**

### ***DB assets: ZPen & ES Executives' Sections***

#### *Selecting Managers*

During the Scheme year, the Trustee agreed to amend the strategic asset allocation to include a 2.5% investment in infrastructure equity. Zurich Investment Management conducted a thorough asset management selection process, this analysis was in accordance with its service agreement with the Trustee. The proposal was for the Trustee to invest in infrastructure equity via two funds, one managed by JPMorgan (JPM) and the other by Kohlberg Kravis Roberts (KKR). The Funding Committee agreed that the JPM and KKR funds were the most suitable Managers for the infrastructure equity allocation and were satisfied with their approach to responsible investment practices and consideration of ESG factors. The Funding Committee therefore approved both of the funds in order to invest in the infrastructure equity asset class.

#### *Financially material considerations*

During the Scheme year, the Trustee continued to operate its restriction list with regard to companies exposed to coal and oil for directly held equities and bonds. The restriction list is updated on a quarterly basis and has been shared with the equity and bond Managers. There were no exceptions noted to the restriction list during the Scheme year.

Following the Trustee setting a target for its equity and corporate bond portfolios to reduce its WACI by 25% over 5 years, the Trustee has also been working with its Managers to progress a net zero ambition. The Trustee recognises its duty to manage climate change and other sustainability risks, and therefore has set an ambition to actively tackle climate change as both a risk and an opportunity. On 29 September 2022, the Trustee set a net zero ambition for the Scheme to achieve net zero by 2050 or earlier. The net zero ambition covers the ZPen DB Section assets and the Trustee's operations, more information is included in the Responsible Investment section of the Scheme's website [www.zpen.info/Library/Responsible Investment](http://www.zpen.info/Library/Responsible%20Investment).

#### *Voting & Stewardship*

For the directly held securities, the Trustee delegated voting activities and decisions to CTI, the equities fund manager. All of the voting decisions are available on the CTI's website seven days after each company meeting. The Trustee reviewed quarterly updates on voting statistics from CTI during the Scheme year.

Taking into account the periodic reviews and the responses given to the questions raised during the annual responsible investment meeting, the Trustee is satisfied that CTI's voting policy is aligned with its own guiding principles. CTI votes actively at company meetings, applying principles on a pragmatic basis. CTI views this as one of the most effective ways of signalling approval (or otherwise) of a firm's governance, management and strategy. CTI's RI team makes the final voting decisions in collaboration with the firm's portfolio managers and analysts. CTI's proxy voting dashboard can be found on the following website [dashboard](#).

The Trustee agreed its stewardship priorities for the DB assets:

- Climate and energy transition, this includes climate policies, net zero targets, climate litigation, carbon capture storage technologies, global summits, green hydrogen and nuclear.
- Food and materials transition, this includes biodiversity, circular economy and sustainable food.
- Corporate governance, ensuring companies are well governed in order to manage the risks and challenges inherent in business.

### *Engagement*

The Trustee continues to meet with its Managers on a regular basis and RI remains a standing item for the majority of Managers. RI is discussed less regularly with the Liability Driven Investment (LDI) manager, Insight, due to the limited scope of its investments (mainly Gilts). For more information about the meetings with Managers, including examples of meetings which have taken place and matters that the Trustee has raised with Managers, please see the below section entitled 'Engagement with Managers'.

### *Non-financial matters*

The restriction list to exclude the investment in the debt and equity of companies involved in the manufacture of UN-sanctioned weapons is updated on a quarterly basis and has been shared with the equity and bond Managers quarterly. There were no exceptions noted to the restriction list during the Scheme year.

### *Member engagement*

The Trustee maintained its position on soliciting member views on non-financial matters in their investment decision making between the effective date of the SIP and the Scheme year end.

### *The realisation of investments*

The Trustee operates an investment re-balancing process which is set out in the DB IPID. The management of the re-balancing process is delegated to the ZPen Finance and Investment team. During the Scheme year there was an increase in the re-balancing activity due to the rise in gilt yields, there were a number of large sales of equities in order to maintain sufficient collateral in the LDI portfolio. Aside the equity sales, a number of transactions took place for the less liquid asset classes, including the CTI Property fund and the M&G European Loan fund. The CTI Property fund withdrawal request was made in September 2022, however it subsequently gated withdrawal requests during September and October 2022, the request was honoured on 15 November 2022. Any active re-balancing transactions were communicated with the Funding Committee within the standing investment management agenda item.

### *The expected return from investment and performance measurements*

The Trustee continues to monitor the performance of the DB assets on a quarterly basis. The Funding Committee considers the performance of the assets and takes additional actions if necessary. During the Scheme year the performance of the equity mandate led to the Funding Committee requesting the Investment Analyst to provide further analysis on equity performance. Work continued on the equity review throughout the Scheme year and is likely to be finalised in the Scheme year ending 30 June 2024.

### *Turnover*

The Trustee maintained its position of not setting specific targets on transaction costs. The Trustee commissioned a report from an external provider to provide analysis on the DB asset's transaction costs and turnover for the Scheme year. During the Scheme year, the transaction cost report for the Scheme year ended 30 June 2022 was reviewed by the Funding Committee. There were a number of follow up actions that were raised by the report, the Pension Investment Manager and Finance and Investment Manager discussed these with the relevant asset managers to their satisfaction and shared the outcome with the Funding Committee. The Trustee has commissioned a transaction cost report for the latest Scheme year end and will consider this once it has been received.

### *Duration*

None of the agreements with the Managers ceased during the Scheme year.

### *Incentives*

There were no changes to the current fee arrangements during the Scheme year. In the Trustee's opinion all of the Managers are incentivised to act in accordance with the Trustee's policies and in the best interest of the Scheme and its beneficiaries.

## 3. Engagement with Managers

The Trustee engages with the Managers regularly. This includes engagements through the Funding Committee and meetings with Trustee and ZPen team representatives. The Trustee has found direct meetings with Managers is the most effective ways to engage on responsible investment and voting records.

### **Annual Responsible Investment meetings – 29 June 2023 – 30 June 2023**

The annual Responsible Investment meetings consisted of 3 attendees representing the Trustee. This included the nominated Trustee for responsible investment, the ZPen Finance and Investment Manager and the Trustee's Investment Analyst. The attendees were briefed ahead of each Manager meeting with key information on each mandate in order to facilitate discussions.

The meetings all followed a similar format and were structured to discuss four main topics, these were:

- Responsible investment updates through 2022/2023 (including policy changes/personnel)
- TCFD reporting
- Stewardship priorities
- An update of the Scheme's net zero ambition

The Scheme's requirements were discussed in respect of different asset classes and ways of measuring the Scheme's climate change risks and opportunities. All Managers provided an update on any net zero targets, both for investments and operations, this information was especially helpful as the Trustee set its ambition to become net zero by 2050 in September 2022. Specific engagement examples and voting activities were also challenged with the respective Managers. From each meeting conclusions were drawn and next steps determined to follow up on. The Trustee's stewardship priorities were also shared with the Managers in order to set expectations of future engagements with investee companies.

### **Insight meeting – 15 February 2023**

Representatives from Insight presented at the Funding Committee, Insight were asked to present on the following topics:

- Update on LDI markets and the gilts 'crisis'
- Resilience of ZPen's LDI portfolio throughout the crisis
- Lessons learned – strategy considerations
- LDI portfolio update

The Funding Committee were satisfied with Insight's presentation and their responses to the questions it asked. The Funding Committee noted that the ZPen portfolio was less affected than the average pension scheme during the LDI crisis as it had strong collateral levels at the start, and was able to top-up the portfolio using equity proceeds when collateral levels dropped.

### **Exercise of voting rights**

#### **Voting policy**

The Trustee operates a proxy voting policy, the policy operates with the following principles:

- The Trustee is ultimately responsible for exercising voting rights efficiently and in line with its mandate to generate superior risk-adjusted economic returns on the investments for the benefit of the Scheme's members. No consideration shall be given to an investee company's potential business relationships to Zurich outside of the Scheme.
- The safety of the underlying investment and obtaining the sustained generation of long-term economic return generated by the shares are the primary objectives in determining how votes are exercised. In the process, due attention shall be paid to the assessment of ESG issues.
- As a long-term investor, the Scheme does apply a longer-term focus, and expects Managers to vote in order to support the investee companies' strong and sustainable governance, as well as a long-term oriented strategy and its implementation. Long-term value creation is preferred over short-term gains.
- Voting rights for financial investments shall be exercised actively following clearly defined voting guidelines.
- However, where economic costs of exercising voting rights are not commensurate with expected benefits, voting may be refrained from.

As all of the Scheme's assets are externally managed, the Trustee reviews the Manager's applicable proxy voting policies every three years or more frequently if there are any material changes. If these are in alignment with the guiding principles described above, the Trustee will delegate the authority to exercise voting rights to the Managers.

As discussed in the 'Policy and Response' section, the Trustee met with all of its Managers during the Scheme year, with RI as a key topic for the majority of meetings.

The Scheme has two types of equity structures within the ZPen & ES Executives' sections.

- Segregated mandates in segregated custody accounts (DB).
- Pooled mandates in segregated custody accounts (DB).

The table on the next page sets out the portfolios that contain equities.

Across ZPen DB & the ES Executives' Section all equity assets are held by CTI. There are approximately £1.3bn of equities held in total, the majority of these equities at the Scheme year end were held through segregated mandates, and small holding of equities were held via pooled funds. The statistics for the DB assets will reflect the fact that CTI would have voted on behalf of the Trustee (through the segregated custody accounts) and as fund managers (through the pooled funds).

The Trustee reviewed quarterly updates on voting statistics from CTI during the Scheme year. During the annual responsible investment meetings, key individual company voting records were challenged. All of the voting decisions are available on the CTI's website seven days after each company meeting.

As discussed in the 'Policy and response' section, the Trustee is satisfied that CTI's voting policy is aligned with its own guiding principles. CTI votes actively at company meetings, applying principles on a pragmatic basis. CTI views this as one of the most effective ways of signalling approval (or otherwise) of a firm's governance, management and strategy. CTI's RI team makes the final voting decisions in collaboration with the firm's portfolio managers and analysts.

The key statistics and significant votes for CTI are shown on in the **significant votes section**.

DB assets	% of Scheme equity assets
Fund 1 (ZPen)	99.4 %
Fund 5.1 (ES Executives')	0.6%

#### Fund 1

CTI's statistics showed the following:

- Number of meetings eligible to vote: 528
- Number of resolutions eligible to vote 7,457
- % of resolutions vote: 99.2
- Of the resolutions on which voted, % voted with management: 90.2
- Of the resolutions on which voted, % voted against management: 7.8
- Of the resolutions on which voted, % abstained from voting: 2.0
- Of the meetings in which voted, % with at least one vote against management: 51.9

#### Fund 5.1

CTI's statistics showed the following:

- Number of meetings eligible to vote: 400
- Number of resolutions eligible to vote: 5,238
- % of resolutions vote: 99.6
- Of the resolutions on which voted, % voted with management: 87.7
- Of the resolutions on which voted, % voted against management: 11.1
- Of the resolutions on which voted, % abstained from voting: 1.2
- Of the meetings in which voted, % with at least one vote against management: 58.5

## Significant votes

Company name	Amazon.com Inc.
Date of vote	24 May 2023
Summary of the resolution	Report on impact of climate change strategy consistent with Just Transition guidelines
How you voted	For
Rationale for the voting decision	Shareholders would benefit from more disclosure on whether and how the company considers human capital management and community relations issues related to the transition to a low-carbon economy as part of its climate strategy. CTI are supportive of requests to enhance disclosure and transparency concerning climate risk so long as the resolution does not directly circumvent management discretion or seek to entirely redefine the company's existing business strategy. To meet the ambition of the Paris Agreement and avoid massive risk to shareholder value, corporations should demonstrate the nexus between their climate aspirations and business strategy via disclosure of credible Paris- or 1.5 degree-aligned emissions reduction targets. Current disclosure does not sufficiently provide investors such information.
Outcome of the vote	Fail
Implications of the outcome e.g., were there any lessons learned and what likely future steps will you take in response to the outcome?	Active stewardship (engagement and voting) continues to form an integral part of CTI's research and investment process.
On which criteria have you assessed this vote to be "significant"?	Vote against management on certain environmental or social proposals; Deemed significant.

Company name	Shell Plc
Date of vote	23 May 2023
Summary of the resolution	Request Shell to Align its Existing 2030 Reduction Target Covering the Greenhouse Gas (GHG) Emissions of the Use of its Energy Products (Scope 3) with the Goal of the Paris Climate Agreement
How you voted	Abstain
Rationale for the voting decision	Whilst CTI appreciate the progress made by the company and engagement to date, CTI felt abstaining was the best option to recognise this progress whilst retaining CTI's position that it would prefer to see greater movement towards full Paris alignment in the coming years.
Outcome of the vote	Fail
Implications of the outcome e.g., were there any lessons learned and what likely future steps will you take in response to the outcome?	Active stewardship (engagement and voting) continues to form an integral part of CTI's research and investment process.
On which criteria have you assessed this vote to be "significant"?	Vote against management on certain environmental or social proposals; Deemed significant.



Company name	Apple Inc.
Date of vote	10 March 2023
Summary of the resolution	Report on Median Gender/Racial Pay Gap
How you voted	For
Rationale for the voting decision	The proposed enhanced disclosure would help the board and shareholders better assess existing and potential future risks related to human capital management.
Outcome of the vote	Fail
Implications of the outcome e.g., were there any lessons learned and what likely future steps will you take in response to the outcome?	Active stewardship (engagement and voting) continues to form an integral part of CTI's research and investment process.
On which criteria have you assessed this vote to be "significant"?	Vote against management on certain environmental or social proposals; Deemed significant.

Company name	The TJX Companies, Inc.
Date of vote	6 June 2023
Summary of the resolution	Report on third-party assessment of human rights due diligence in supply chain
How you voted	For
Rationale for the voting decision	The company faces risks related to human rights in its global operations. Good practice includes developing a clear human rights policy or code of practice, along with a narrative on how impacts are monitored and effectively mitigated. Shareholders would benefit from an independent analysis and report on the effectiveness of the company's supply chain management practices. Particularly, as it relates to vendor shipments being withheld from the US and other jurisdictions.
Outcome of the vote	Fail
Implications of the outcome e.g., were there any lessons learned and what likely future steps will you take in response to the outcome?	Active stewardship (engagement and voting) continues to form an integral part of CTI's research and investment process.
On which criteria have you assessed this vote to be "significant"?	Vote against management on certain environmental or social proposals; Deemed significant.

<b>Company name</b>	<b>The Walt Disney Company</b>
Date of vote	3 April 2023
Summary of the resolution	Report on political expenditures
How you voted	Abstain
Rationale for the voting decision	While CTI generally agree with the sentiment of this proposal, it appears the company provides reasonable disclosure of its political donations and CTI are encouraged by the recent efforts to increase transparency on this issue.
Outcome of the vote	Fail
Implications of the outcome e.g., were there any lessons learned and what likely future steps will you take in response to the outcome?	Active stewardship (engagement and voting) continues to form an integral part of CTI's research and investment process.
On which criteria have you assessed this vote to be "significant"?	Vote against management on certain environmental or social proposals; Deemed significant.