

Universities Superannuation Scheme/ USS Investment Management **Statement on the UK Stewardship Code** ***September 2013 Update***

Universities Superannuation Scheme (USS) is the principal final salary pension scheme provided for academic and senior administrative staff in UK universities and other higher education and research institutions. The fund is the second largest pension scheme in the UK, with assets of over £38bn. The majority of assets are managed in-house by USS Investment Management (USSIM), a wholly owned subsidiary of USS, authorised and regulated by the FCA.

USS has long practised the principles of stewardship espoused by the Code and was a founder signatory in 2010. The fund participated in the development of the Stewardship Code through written submissions and meetings with regulators including the Financial Reporting Council.

The fund first articulated its engagement approach to responsible investment (RI) in 1999 and has employed an in-house responsible investment team (based within USSIM) to engage with companies on environmental, social and governance (ESG) matters for over a decade.

In line with best practice, the fund regularly posts information on RI activities on its website, through periodic RI activity reports, voting disclosures and the fund's annual reports. The website discloses USS' RI objectives and strategy, rationale and resourcing, voting policies and outlines the fund's approach to investee company engagement and broader market wide collaborations. Representatives of the fund (including its trustee directors, portfolio managers, heads of RI and CIO) regularly present, write and comment publicly on the fund's stewardship activities and approach to RI.

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

The fund's website includes a section devoted to responsible investment policy and activities. The fund explains how it will discharge its stewardship responsibilities and work with companies to address poor corporate management of extra-financial factors through active engagement. The pages include links to the Statement of Investment Principles and RI strategy documents alongside explanations describing how the fund resources its work in this area, including sections on voting and engagement.

USS' Statement of Investment Principles embeds stewardship responsibilities into the fund's asset management, stating that:

"The Trustee Company aims to be an active and responsible long-term investor and steward of the assets and markets in which it invests. The Trustee Company expects this approach to both protect and enhance the value of the Scheme's investments in the long-term."

The Trustee Company therefore requires its investment managers to integrate material extra-financial factors, including corporate, environmental, social, governance and ethical considerations, into the selection, retention and realisation of all fund investments. The Trustee Company expects this to be done in a manner which is consistent with the Trustee Company's investment objectives, legal duties and other relevant commitments e.g. the UN backed Principles for Responsible Investment and the UK Stewardship Code.

Specifically, the Trustee Company has instructed USSIM and called on its external investment managers to follow good practice themselves and to use their influence as major institutional investors to promote good practice in the investee companies and markets to which the fund is exposed.

The Trustee Company also expects all the Scheme's investment managers to undertake appropriate monitoring of current and potential investments with regard to their policies and practices on material corporate, governance, social, ethical and environmental issues. These extra-financial factors should, where material, be taken into account when making investment decisions. Early identification can enable engagement with boards and management of investee companies to seek appropriate resolution of such problems. The Trustee Company tasks USSIM to provide oversight of external managers in this respect. [...]

The investment committee monitors this activity on an ongoing basis with the aim of maximising its impact and effectiveness. The Trustee Company's governance, social, ethical and environmental policies are also reviewed regularly by the board and updated as appropriate to ensure that they are in line with good practice."

Where fund management activities are outsourced, USSIM is tasked with reviewing external fund managers' approach to stewardship and responsible investment (RI), with oversight from the USS investment committee.

Further details on investment policy and the fund's approach to stewardship is outlined further on the fund's website and included in the USS Statement of 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.

As a beneficial owner with in-house fund management and RI capabilities serving only one client, USS does not face the potential conflicts of interest that commercial fund managers may need to address. However, we monitor for potential conflicts of interest on an on-going basis.

Principle 3: Institutional investors should monitor their investee companies.

Monitoring of investee companies is undertaken in-house by USSIM's portfolio managers and RI team through meetings with company executives and non-executive directors, analysts' briefings and through the voting process for shareholder meetings. Additional information is received through daily news feeds, discussions with peers or analysts, conferences, internally developed analytical tools, ESG ratings, and via proxy research.

Portfolio managers will flag ESG matters and concerns to the RI team, particularly where further advice or research or engagement is required. Similarly, the RI team will flag ESG areas of interest or concern on individual stocks, sectors and countries where investments are held to the relevant portfolio managers.

With regard to the receipt of material non-public information and being made insiders, the fund has established protocols which are overseen by an in-house compliance team.

Where fund management has been outsourced, USSIM will periodically review the external fund manager's approach to monitoring and engagement with a view to encouraging the adoption of best practice stewardship where appropriate.

Principle 4: Institutional Investors should establish clear guidelines on when and how they will escalate their stewardship activities

The fund's escalation strategy is disclosed under the Engagement section of the website. If boards do not respond constructively to our engagement, then the fund will consider whether to escalate its action, for example, by:

- Writing to the company to highlight our concerns
- Voting against appropriate proposals at shareholder meetings
- Meeting with management specifically to discuss concerns
- Meeting with the Chairman, senior independent director, or independent directors
- Expressing concern through the company's advisers
- Collaborating with other investors regarding our concerns, subject to applicable regulations
- Speaking to the market regulators regarding our concerns
- Making a public statement at the company's meeting
- Releasing a press statement, either singly or jointly with other investors relating to the issue
- Submitting resolutions at a shareholder meeting
- Requisitioning a General Meeting
- In extremis, selling our shares in the company

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

USS recognises the power of investor collaboration to add weight to individual company engagements and to address market wide systemic failures. The fund's commitment to collaboration is acknowledged within USS's Statement of Investment Principles:

“Where collaboration is likely to be the most effective mechanism for encouraging issues to be addressed, the Trustee Company expects its investment managers to participate in joint action with other institutional investors as permitted by relevant legal and regulatory codes.”

The fund was an early leader in collaborative engagement and involved in the establishment of several collaborative initiatives which support stewardship activities and collective engagement in the UK and other markets. Collaborative engagement is articulated in the fund’s RI Strategy:

*“Principle 3: Work in alliances
USS will continue to work in collaboration with other institutional investors, particularly pension funds, in seeking to implement its RI strategy. The additional influence, the shared learning, and the greater efficiency associated with collaboration, means that this forms a central plank of [our] approach to RI.”*

The fund places significant emphasis on fostering good working relationships with peer funds in the UK and internationally and continues to hold key roles in many collaborative initiatives. These include:

ACGA (Asian Corporate Governance Association)
CGF (Corporate Governance Forum)
CII (Council of Institutional Investors)
Eumedion
GIGN (Global Investors Governance Network)
ICGN (International Corporate Governance Network)
ICPM (International Centre for Pension Management)

IIGCC (Institutional Investors Group on Climate Change)
JEC (Japan Engagement Consortium)
NAPF (National Association of Pension Funds)
Pharma Futures
Tomorrow’s Company
UN Principles for Responsible Investment

The RI Team often leads and participates in joint investor meetings with UK and global companies, particularly on matters relating to remuneration, board structure and independence, disclosure and environmental performance. On occasion, USS has been represented by another investor in an engagement where the fund has been unable to participate e.g. due to language or geographical constraints.

The fund’s collaborative engagement activities are reported within RI Activity Reports and the market wide initiatives sections on our website.

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

The fund considers the voting of shares to be one of the responsibilities of company ownership and an essential tool for engagement. USS’s Statement of Investment Principles highlights *“the trustee company aims to use its voting rights as part of its engagement work, in a prioritised, value-adding and informed manner”*.

The fund’s voting policy has been developed in-house and outlines the fund’s expectations from investee companies, reflecting international best practice - including the UK Corporate Governance Code. The policy is periodically reviewed and published on the USS website.

Individual vote decisions are reviewed and confirmed by the in-house RI team, working closely with USSIM's portfolio managers. The fund casts its votes on a case by case basis, taking account of the individual company circumstances, including the results of any past engagement, in-house analysis, proxy research and local market standards.

USSIM uses a number of proxy advisory firms (including Manifest, PIRC, Glass Lewis, ECGS, Japanese Engagement Consortium) to provide a summary of the proxy information released to the market. We use this information alongside a number of other sources to reach a final voting decision.

Where we have not supported management recommendations we advise companies of our vote and rationale in advance of the meeting where practicable. Our voting records are disclosed retrospectively on our website and include a brief comment to explain why we have not supported management.

USS has an active securities lending programme. To ensure that the fund is able to vote all its shares at important meetings or where USS is a significant shareholder, USS has worked with service providers to establish procedures to restrict lending for certain stocks and recall shares in advance of shareholder votes. Where we hold 3% or more of the issued share capital of a company, stock is recalled systematically. In other circumstances we monitor the meetings and proportion of stock on loan, and will restrict and/or recall lent stock on a case by case basis, e.g. in the event of a contentious vote or in relation to engagement activities, further to discussion with the portfolio manager.

Principle 7: Report periodically on their stewardship and voting activities

RI activities are subject to scrutiny by the fund's internal auditors and progress updates are regularly provided to the fund's Investment Committee and Board of Directors.

USS reports to members and publically on responsible investment activities through the fund's Annual Report and Members' Annual Report and RI Activity Reports. Public disclosure is balanced with the need to build confidence with the companies with whom we are engaging. Thus, the fund will rarely publicise current engagements, except where it forms part of an engagement strategy as outlined above.

The fund's website also discloses USS's approach to stewardship and voting under RI objectives and strategy, Statement of Investment Principles, rationale behind the fund's approach to responsible investment (RI), voting policy, voting records, and outlines the fund's approach to investee company engagement and broader market wide collaborations.

Further, representatives of the fund (including its trustee directors, portfolio managers, heads of desk and CIO) regularly present, write and comment publicly on the fund's stewardship activities and approach to RI.