

# Xylem UK Pension Plan Implementation Statement 31 December 2020

## Introduction

This implementation statement is a reporting obligation required by new pensions regulations. The Trustee of the Xylem UK Pension Plan (the 'Plan') has prepared this statement to provide members with a review of how it has acted in line with the policies set out in the Statement of Investment Principles during the reporting year.

This statement includes details of:

- A description of any review of the Statement of Investment Principles ("SIP") during the reporting period, including an explanation of any changes;
- Details of how and the extent to which, in the opinion of the Trustee, the SIP has been followed during the year; and
- Specifically, how the investment managers have acted on behalf of the Trustee and how it has engaged with those managers.

This statement has been prepared by the Trustee to cover the period 1 January 2020 to 31 December 2020. The statement is publicly available at <https://www.xylem.com/en-uk/about-xylem/defined-benefit-pension-schemes/>.

To the best of its knowledge, the Trustee has followed all of the policies as outlined in the relevant SIP during the reporting period.

## Plan Overview

### ***Defined Benefit (DB) Section***

At the start of the reporting year, the Plan was solely invested in cash and liability matching assets, in preparation for securing the members' benefits with an insurer.

As of January 2020, the Trustee had entered into a buy-in policy with Rothesay Life plc (the 'Insurance Provider'). This policy, when finalised on buy-out, is designed to meet all members' benefit payments as they fall due. It is expected that the buy-in policy will be converted into a buy-out policy over the course of 2021, or early 2022. As a consequence, the DB section invested assets in their entirety have been transferred to the Insurance Provider, with a small cash reserve to cover expenses and minor benefits that will be insured on buy-out.

Given this change took place towards the start of the reporting year and no assets such as equities were held in the reporting year, we do not include any voting or engagement activity for the DB section in this statement.

### ***Defined Contribution (DC) Section (also known as the 'Money Purchase Section')***

We note that the Trustee will be including the DC Section assets as part of the prospective Plan buy-out exercise, but these arrangements are still in the process of being finalised.

During the reporting year, the DC arrangements consisted of:

- Original Xylem Plan assets, consisting of market-linked funds held with Legal & General Investment Management
  - Including a Default Fund (also known as the 'Standard Investment Programme')
- Ex - C&K Switches Ltd Pension Plan assets (which merged with the Xylem Plan during 2017), including:
  - Clerical Medical Market-linked funds managed by Aberdeen Standard; and
  - With-profits funds managed by Aviva and Phoenix Life

## **Section 1 – Our investment policies**

### **Statement of Investment Principles Review**

During the reporting year, the Trustee undertook two reviews of the Plan's SIP, which came into effect in February and September 2020. In February the main change was to reflect the buy-in of the DB Section assets. The main change addressed during the September review was to update the Trustee's Responsible Investment and Corporate Governance policy. This section was updated to set out in more detail our requirements for our investment manager arrangements. The extended policy improves accountability and aligns with broader legislative initiatives.

We consider the implementation of the investment policies and the extent to which the Trustee has followed the SIP in the following sections.

### **INVESTMENT OBJECTIVES – DC Section**

#### **What is our investment objective?**

The Trustee's key investment objective is to provide a range of investments that are suitable for meeting members' long and short-term investment objectives allowing for members' differing individual circumstances. In particular, the range of members' attitudes to risk and term to retirement are considered.

#### **How have we implemented our investment objectives?**

The Trustee's policy is to provide suitable information to members so that they can make appropriate investment decisions. The Trustee is currently reviewing their DC provision as part of a wholesale Plan review. In choosing investment options, it is the Trustee's policy to consider:

- A full range of asset classes
- The suitability of the possible styles of investment management and the need for manager diversification
- The suitability of each asset class
- The need for appropriate diversification of asset classes

Where a member does not wish to make a decision, the Trustee offers a Standard Investment Programme (the 'Default Fund').

The assets of the Default Fund are invested in a range of different funds at different points in time. Members also have the option to select from a range of funds, where the return achieved will depend on their selection. These funds include a balanced fund (investing across a range of asset classes), a global equity fund, a bond fund, and a cash fund.

The Default Fund aims to provide exposure to a range of asset classes in order to deliver investment growth over time, gradually de-risking to protect the value of members' account against stock market fluctuations as members approach retirement.

Highest growth is targeted, with a corresponding level of potential volatility of the capital value, in the period up to 15 years before a member's expected retirement age. As a member gets closer to retirement, assets are gradually switched into less volatile holdings, which are also expected to provide lower investment returns.

Details of the mix of assets within the Default Fund as a member approaches their expected retirement date is shown in the table below.

Years to Retirement	LGIM Global Equity 60:40 Fund (%)	LGIM Multi-Asset Fund (%)	LGIM Over 15 year Gilts Index Fund (%)	Cash (%)
15+	100%	-	-	-
5-15	-	100%	-	-
4	-	80%	15%	5%
3	-	60%	30%	10%
2	-	40%	45%	15%
1	-	20%	60%	20%
0	-	-	75%	25%

There were no changes to the Trustee's investment objectives over the period or to how they are implemented.

### **INVESTMENT OBJECTIVES – DB Section**

#### **What is our investment objective?**

The Trustee's aim is to provide sufficient assets to pay benefits as they fall due. To this end, the Trustee, in consultation with the Plan's sponsoring employer, Xylem Water Solutions UK Limited, has selected Rothesay Life plc (the 'Insurance Provider') to provide a buy-in policy for the Plan. This policy is designed to meet all members' benefit payments as they fall due.

It is expected that the buy-in policy will be converted into a buy-out policy within the next two years (the 'Buy-out Objective'). At that point, the responsibility for meeting members' benefits will be transferred from the Trustee to the Insurance Provider.

In the meantime, the Trustee retains overall responsibility for reviewing the ongoing operation of and risks associated with the buy-in policy. This includes, but is not limited to, the Insurance Provider's ongoing credit quality and the timeliness and accuracy of payments made to the Plan.

### **RESPONSIBLE INVESTMENT – DB & DC Sections**

#### **What is our responsible investment policy?**

The Trustee considers responsible investment to be the integration of environmental, social and governance considerations into investment decisions in respect of the Plan's investment portfolio where financial risk and / or return is or could be materially affected ("Responsible Investment"). The Trustee acknowledges the importance of being a responsible investor, however, as the Trustee is aiming to buy out the Plan's liabilities with an insurer in the short term they do not expect Responsible Investment considerations to have a significant impact on the Plan's assets over this timeframe.

#### **How have we implemented our responsible investment policy?**

The Plan Defined Benefit assets are now substantially invested in an insurance policy. The Defined Contribution assets are held in pooled arrangements and the Trustee expects investment managers to take into account environmental, social and governance considerations (including but not limited to climate change) when making investment decisions where financial risk and / or return is, or could be, materially affected.

The Trustee recognises that their influence over some of the Defined Contribution investment managers is extremely limited, in the case of With Profits and legacy Clerical Medical investments. It is satisfied with this situation on the basis that a full buy out exercise is planned for the near future.

In the case of LGIM, the manager of the vast majority of the Defined Contribution assets, our Investment Adviser has engaged with them on their responsible investment activities over the reporting year.

### **Compliance with our Corporate Governance Policy**

As part of its responsibilities, where applicable, the Trustee expects the Plan's investment managers to:

- Engage with investee companies with the aim to protect and enhance the value of assets; and
- Exercise the Trustee's voting rights in relation to the Plan's assets

The following sections provide more detail on voting and engagement activity within the DC section, where we have been able to source the relevant data.

To the best of our knowledge we have complied with our Corporate Governance Policy.

### **Section 2 – How our shares were voted**

Please note, this only applies to the DC section of the Plan.

<b>Manager</b>	<b>Number of potential votes</b>	<b>Proportion of votes cast</b>	<b>For</b>	<b>Against</b>	<b>Abstain</b>
LGIM	155,133	99.66%	127,495	26,463	654

Source: LGIM, for year ending 31 December 2020. We have also requested data for the Clerical Medical managed funds however these were not received in time to be included. Going forward, the Trustee will continue to request this data for future reporting.

### **Use of proxy voting services**

Proxy voting services are specialist firms that provide an outsourced voting service. Some investment managers choose to use these services (rather than vote themselves). The reasons for using a proxy voting services could include:

- The investment manager lacks the resource to research each vote and submit votes
- The managers want to follow a recognised code of practice and the proxy voting service is an easy way to implement this

Many professional proxy voting services are able to devote significant resource to researching AGM motions and are able to follow best practice guides, like the FRC's Stewardship Code. However, the potential concern is that the manager who has chosen to invest in the company is arguably in the best position to vote and engage with the company, and by failing to do so directly, may be signalling indifference to the management.

The following table gives detail on LGIM's approach to proxy voting.

<b>Manager</b>	<b>Use of proxy voting service</b>	<b>Comment (in manager's own words)</b>
LGIM	Yes – ISS	LGIM's Investment Stewardship team uses ISS's 'ProxyExchange' electronic voting platform to electronically vote clients' shares. All voting decisions are made by LGIM and we do not outsource any part of the strategic decisions. To ensure our proxy provider votes in accordance with our position on ESG, we have put in place a custom voting policy with specific voting instructions.

## Examples of significant votes cast

LGIM cast votes in relation to a variety of different topics and issues throughout the year. Where possible, we have asked managers to provide more detailed examples of voting events that have occurred, highlighting some of the impacts these decisions will have on areas such as sustainability, social reform, and executive pay. The table below summarises some examples provided to us on notable events (as defined by the manager).

Manager	Significant votes cast	Rationale/ Comment (in manager's own words)
LGIM	<p><b>Whitehaven Coal</b></p> <p>LGIM voted for a proposal for the company to provide a report on the potential wind-down of the company's coal operations, with the potential to return increasing amounts of capital to shareholders.</p>	<p>The role of coal in the future energy mix is increasingly uncertain, due to the competitiveness of renewable energy, as well as increased regulation: in Q4 2020 alone three of Australia's main export markets for coal - Japan, South Korea and China - have announced targets for carbon neutrality around 2050. LGIM has publicly advocated for a 'managed decline' for fossil fuel companies, in line with global climate targets, with capital being returned to shareholders instead of spent on diversification and growth projects that risk becoming stranded assets. As the most polluting fossil fuel, the phase-out of coal will be key to reaching these global targets.</p>
LGIM	<p><b>ExxonMobil</b></p> <p>LGIM voted against a proposal to re-elect the combined chair and CEO of the company</p>	<p>In June 2019, under our annual 'Climate Impact Pledge' ranking of corporate climate leaders and laggards, we announced that we will be removing ExxonMobil from our Future World fund range and will be voting against the chair of the board. Ahead of the company's annual general meeting in May 2020, we also announced we will be supporting shareholder proposals for an independent chair and a report on the company's political lobbying. Due to recurring shareholder concerns, our voting policy also sanctioned the reappointment of the directors responsible for nominations and remuneration.</p>

## Section 3 – How our managers have engaged in respect of the investments held

Engagement is considered to be purposeful dialogue with a specific and targeted objective to achieve positive change in the interests of beneficiaries, thereby a key action required for delivering good stewardship.

We summarise examples provided by LGIM (in their own words) of notable engagement activity in the table below.

Manager	Engagement activity (in manager's own words)
LGIM	<p><b>Qantas Airways Limited</b></p> <p>The COVID crisis has had an impact on the Australian airline company's financials. In light of this, the company raised significant capital to be able to execute its recovery plan. It also cancelled dividends, terminated employees and accepted government assistance. The circumstances triggered extra scrutiny from LGIM as we wanted to ensure the impact of the COVID crisis on the company's stakeholders was appropriately reflected in the executive pay package. In collaboration with our Active Equities team, LGIM's Investment Stewardship team engaged with the Head of Investor Relations of the company to express our concerns and understand the company's views. The voting decision ultimately sat with the Investment Stewardship team. We supported the remuneration report (resolution 4) given the executive salary cuts, short-term incentive cancellations and the CEO's voluntary decision to defer the vesting of the long-term incentive plan (LTIP), in light of the pandemic. However, our concerns as to the quantum of the 2021 LTIP grant remained, especially given</p>

	<p>the share price at the date of the grant and the remuneration committee not being able to exercise discretion on LTIPs, which is against best practice. We voted against resolution 3 (Approve participation of Alan Joyce in the Long-Term Incentive Plan) to signal our concerns.</p>
<p>LGIM</p>	<p><b>Rank Group</b></p> <p>The company and its stakeholders have been impacted by the COVID crisis. As an active owner and responsible investor, LGIM wants to ensure this is reflected in the executive remuneration package paid for this year. In addition, in 2018 the company granted 'block awards' long-term incentives (LTI) to the executives and committed not to grant any LTI awards until financial year 2022. After review of the remuneration policy, the remuneration committee asked shareholders to adopt a new LTI structure with the first award under this plan to be made in the 2021 financial year. We decided to support the remuneration report, which looks back at the remuneration earned during the financial year. We noted the remuneration committee's decision to apply a 20% deduction and cancel the planned increase of salaries of the executives and fees of the board members. No annual bonus was granted, given the performance of the company. LGIM was comfortable that the impact of COVID-19 had been appropriately reflected in the remuneration of the executives and therefore decided to support the remuneration report. Regarding the remuneration policy, our direct engagement with the company allowed us to better understand the rationale for the proposed changes to the LTIP. We took into account their concerns around retention, and the fact that there would be a substantial gap in the vesting of any long-term incentives if this plan was not approved. Notably, that the structure of the proposed LTIP was in line with LGIM's remuneration principles.</p>