

Rolls-Royce UK Pension Fund

Trustee's annual report and financial
statements for the year ended
31 March 2023

Pension Scheme Registration Number: 12001014

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Trustee and advisors

Trustee:	Rolls-Royce UK Pension Fund Trustees Limited
Trustee directors:	<p>Company appointed directors Liz Airey – Chairman Jo Durkan Iain Foster Steve Jones Will Mansfield Mark McIntosh (resigned on 8 June 2022) Jane Stockwell (appointed 7 December 2022)</p> <p>Member nominated directors Paul Butler Mark Barron (appointed 7 December 2022) Stuart Hedley (resigned 1 November 2022) Colin High Mark Porter</p>
Secretary:	Caroline Veitch, Rolls-Royce Pensions Department
Sponsoring employer:	Rolls-Royce plc, Kings Place, 90 York Way, London N1 9FX
Administrator:	Rolls-Royce Pensions Department, Trent Hall (A90), Victory Road, Derby, DE24 8EJ
Banker:	National Westminster Bank
Investment managers:	Capital Dynamics Limited Hg Capital LLP The Rohatyn Group Asian Infrastructure & Related Resources Opportunity Fund UK LP Insight Investment Management (Global) Limited Legal & General Assurance (Pensions Management) Limited M&G Investment Management Limited Pantheon Ventures (UK) LLP Royal London Asset Management Limited
Custodian and performance measurement:	State Street Bank and Trust Company
Investment consultant:	Mercer Limited, Tower Place, London, EC3R 5BU
Scheme Actuary:	<p>Alastair McIntosh FIA, Aon Solutions UK Limited, The Aon Centre, The Leadenhall Building, 122 Leadenhall Street, London, EC3V 4AN until 21 July 2022</p> <p>Leanne Johnston FIA, Mercer Limited, 2 Clarence Street, Manchester, M2 4DW from 22 July 2022</p>
Legal advisor:	Linklaters LLP, One Silk Street, London, EC2Y 8HQ
Auditor:	Deloitte LLP, Four Brindleyplace, Birmingham, B1 2HZ
Covenant advisor:	Penfida Limited, One Carey Lane, London, EC2V 8AE

Annual report

Establishment

The Rolls-Royce UK Pension Fund (the “Fund”) provides retirement and life assurance benefits for employees of Rolls-Royce plc and related, participating companies (the “Company”). The Fund was originally established on 23 December 2008 but was significantly revised on 31 October 2016 when four of the Company’s other defined benefit pension schemes were consolidated into the Fund. The Fund closed to future accrual of benefits on 31 December 2020. The Fund is governed by a Trust Deed and Rules as amended by supplementary deeds. The Trustee is a UK limited company, Rolls-Royce UK Pension Fund Trustees Limited (the “Trustee”).

The Fund’s assets are held in the name of the Trustee and are entirely separate from the assets of the Company. The Fund is registered with Her Majesty’s Revenue & Customs for tax purposes. Consequently, the majority of the Fund’s income and investment gains are free of taxation. However, the Fund cannot reclaim certain amounts of withholding taxes relating to overseas investment income.

The Fund was contracted-out of the State Second Pension until 5 April 2016.

Management of the Fund

The Trustee Board

The directors of the Trustee are appointed and removed in line with the provisions of the Trustee’s Articles of Association. There are usually ten directors comprising six directors appointed by the Company (including a Chairman and a director nominated by the Company’s Central Negotiating Committee) and four directors nominated by members.

All directors have the same function except that the Chairman (or, if they are not present at any meeting the director appointed as Chairman of the meeting) has a casting vote. Mr Mark Porter was appointed to act as Deputy Chairman for a period of two years to 31 December 2022 and was succeeded by Mr Will Mansfield in that role from 1 January 2023.

During the year the Trustee Board held eight regular meetings and two strategy events. Attendance at the regular Trustee meetings during the year is shown in the table below:

Director	Meetings attended	Meetings applicable
Liz Airey – Chairman	8	8
Mark Barron (appointed 7 December 2022)	3	3
Paul Butler	8	8
Jo Durkan	7	8
Iain Foster	8	8
Stuart Hedley (resigned on 1 November 2022)	3	4
Colin High	8	8
Steve Jones	8	8
Will Mansfield	8	8
Mark McIntosh (resigned on 8 June 2022)	2	2
Mark Porter	8	8
Jane Stockwell (appointed 7 December 2022)	3	3

During the Fund year there were also additional meetings, for example Trustee training sessions, and sub-committee meetings to address various issues.

Each director has been provided with the relevant documentation required to perform their role as a pension scheme trustee and training is undertaken on a regular basis. These training

arrangements are designed to meet The Pensions Regulator’s pension scheme trustee training requirements, which were established by the *Pensions Act 2004*.

The audit committee

The Trustee has established an audit committee to oversee a range of activities, pursuant to ensuring the integrity of the Fund’s financial statements, identifying, monitoring and controlling risks, and monitoring the cost and performance of service providers. The audit committee was renamed the audit and risk committee with effect from 17 May 2023. The Trustee Board sets the terms of reference for the audit committee. The current terms of reference require a minimum of three directors appointed by the Trustee (with a quorum of two) and for the audit committee to meet at least twice a year and more frequently as required. The members of the audit committee and their attendance at meetings during the year are shown in the table below:

Director	Meetings attended	Meetings applicable
Will Mansfield – Chairman	5	5
Paul Butler	5	5
Mark Barron (appointed 7 December 2022)	1	1
Jo Durkan	5	5
Mark McIntosh (resigned on 8 June 2022)	1	1

The audit committee had oversight of the following significant business during the year:

- During the year, the Fund’s external auditor (Deloitte LLP) presented its audit plan, which set out its assessment of the key risks and the proposed scope of audit work. Following the year end, the audit committee reviewed the Trustee’s annual report and financial statements prepared by management and a report produced by Deloitte. The audit committee was satisfied that appropriate judgements and estimates had been made by management and that the disclosures were appropriate. The audit committee was also satisfied that there had been appropriate focus and challenge by Deloitte on the primary areas of the audit. The audit committee recommended approval of the annual report and financial statements, and the reappointment of Deloitte, to the Trustee Board.
- The audit committee oversaw a review of the Fund’s information security governance and wider governance framework by Ernst & Young.
- The audit committee also oversaw further development of the Fund’s risk management and mitigation processes with particular focus on information security and business resilience.

For the 2023/24 year, the audit and risk committee’s key areas for focus will be:

- Overseeing the audit of the Fund by Deloitte for the year to 31 March 2023.
- Ensuring the basis of the Fund’s financial statements are consistent with the financial position of the Company.
- Addressing the findings from the reviews by Ernst & Young and continuing to develop the Fund’s risk management and mitigation processes.

Changes to the Fund

Directors

Mr Mark McIntosh resigned as a company appointed director on 8 June 2022 and Mr Stuart Hedley resigned as a member-nominated director on 1 November 2022. The Trustee would like to place on record its thanks to Mr McIntosh and Mr Hedley for their service to the Fund. Mr

McIntosh and Mr Hedley were succeeded respectively by Ms Jane Stockwell and Mr Mark Barron on 7 December 2022.

Review of Scheme Actuary and investment consultant

During the year the Trustee undertook a formal review of its appointed Scheme Actuary (including ancillary actuarial services) and investment consultant. Following a comprehensive and detailed review, the Trustee decided to appoint Leanne Johnston of Mercer Limited as Scheme Actuary to replace Alastair McIntosh FIA of Aon Solutions UK Limited. Mr McIntosh resigned with effect from 21 July 2022 and Mrs Johnston was appointed with effect from 22 July 2022. As required by Regulations made under the Pensions Act 1995, Mr McIntosh confirmed in his notice of resignation that he knew of no circumstances connected with the resignation that significantly affected the interests of the members, prospective members or beneficiaries of the Fund. The Trustee would like to place on record its thanks to Mr McIntosh and his colleagues for many years of service to the Fund and its members. The Trustee decided to retain Mercer Limited as its appointed investment consultant.

Establishment of investment implementation and funding committee

Following a review of its governance arrangements, the Trustee established an investment implementation and funding committee (“IIFC”) with effect from 1 April 2023. The IIFC’s terms of reference include regular investment risk monitoring, the development of investment and funding strategies for recommendation to the Trustee Board and oversight of the Fund’s triennial actuarial valuation process. The IIFC will also ensure that the Trustee devotes enough time and resources to addressing the financial risks to the Fund that are presented by climate change.

Report on actuarial liabilities

Under Section 222 of the Pensions Act 2004, every pension scheme is subject to the Statutory Funding Objective, which is to have sufficient and appropriate assets to cover its technical provisions. The technical provisions represent the present value of the benefits members are entitled to receive, based on pensionable service to the valuation date. The present value of those benefits is assessed using assumptions agreed between the Trustee and the Company and set out in a Statement of Funding Principles, which is available to members on request. A formal actuarial valuation of the Fund is carried out by the Scheme Actuary at least every three years.

The latest formal actuarial valuation was undertaken as at 31 March 2020 by the previous Scheme Actuary, Alastair McIntosh of Aon Solutions UK Limited. The results of this valuation and an updated position as at 30 June 2023 using equivalent assumptions are shown below.

	31 March 2020	30 June 2023
The value of the assets was:	£9,336m	£5,020.6m
The value of the technical provisions was:	£8,874m	£4,509.9m
Surplus / (deficit):	£462m	£510.7m
Funding ratio:	105.2%	111.3%

The reduction in assets and liabilities over the above period is largely due to a significant increase in UK Government bond yields.

The new Scheme Actuary is currently undertaking the next due formal actuarial valuation as at 31 March 2023 which will reassess all the assumptions used to value the Fund's liabilities as well as taking into account updated details of the Fund's membership at the valuation date. The figures above will be superseded by the results of this valuation, which is expected to be finalised in late 2023.

The method and significant actuarial assumptions used to determine the technical provisions for the formal actuarial valuation as at 31 March 2020 were as follows:

Method

The actuarial method that was used in the calculation of the technical provisions was the Projected Unit Method.

Significant actuarial assumptions

Discount rate: Term structure derived from the yields on conventional UK Government bonds appropriate to the date of each future cashflow plus an additional 0.5% per annum to reflect the allowance the Trustee has agreed for additional investment returns based on the investment strategy as set out in the Trustee's Statement of Investment Principles.

Future Retail Price inflation: Term structure derived from the difference between the yield on conventional and index-linked UK Government bonds at the date of each future cash flow.

Future Consumer Price inflation: Derived from the RPI inflation assumption with an appropriate adjustment to recognize the difference between expectations of future RPI increases and future CPI increases. At the 31 March 2020 valuation the adjustment was a deduction of 0.54% per annum.

Salary increases: Salary increases are no longer applicable following closure of the Fund to future accrual on 31 December 2020.

Pension increases in payment: Term structure derived from price inflation annual forward rates allowing for the maximum and minimum annual increase entitlements or fixed increases where known and guaranteed. Guaranteed increases, as shown on page 11, were paid as at 1 April 2023. In addition to guaranteed increases, if the Fund retains a surplus of at least 4% on a basis set out in the Trust Deed and Rules, contingent increases of up to 2% a year apply to pensions earned before 6 April 1997 and that receive no guaranteed increases under the Trust Deed and Rules or legislation. The value of these contingent increases is not included in the above technical provisions.

Mortality: SAPS S3 year of birth tables S3PMA and S3PFA_M adjusted as follows:

	Male	Female
Active members	101%	94%
Deferred members	101%	95%
Pensioners	102%	99%

Note that different adjustments are applied to contingent dependants.

The allowance for improvements is based on the actuarial profession's Continuous Mortality Investigation 2019 model with a period smoothing parameter of 7.0, "A" parameter of 0.5 and a long-term improvement rate of 1.5% p.a.

Membership

The changes in membership during the period 1 April 2022 to 31 March 2023 are shown in the table below. Opening balance adjustments take account of any retirements, leavers and deaths that occurred before the last Fund year end but which were not processed until after the Trustee's report and financial statements had been signed for that year.

Deferred members	
Members at 1 April 2022	24,196
Adjustments for movements prior to 1 April but processed after that date	(248)
	23,948
Less: Deferred members retiring	(621)
Deaths	(36)
Trivial commutations	(1)
Transfers out	(222)
No further liability ¹	(2)
Members at 31 March 2023	23,066
Pensioners	
Pensioners at 1 April 2022	14,227
Adjustments for movements prior to 1 April but processed after that date	82
	14,309
Add: Deferred members retiring	621
Dependants pensions commencing	250
Less: Deaths	(742)
No further Liability ¹	(21)
Pensioners at 31 March 2023	14,417

¹As a result of various data cleansing activities undertaken by the administrator; these members have been identified as having no further benefit entitlement from the Fund.

Statement of Trustee's responsibilities

Statement of Trustee's responsibilities for the annual report and financial statements

The financial statements, which are prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including the Financial Reporting Standard applicable in the UK (FRS 102), are the responsibility of the Trustee. Pension Scheme regulations require, and the Trustee is responsible for ensuring, that those financial statements:

- show a true and fair view of the financial transactions of the Fund during the Fund year and of the amount and disposition at the end of that year of its assets and liabilities, other than liabilities to pay pensions and benefits after the end of the Fund year; and
- contain the information specified in the Regulation 3A of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, including making a statement whether the financial statements have been prepared in accordance with the relevant financial reporting framework applicable to occupational pension schemes.

In discharging the above responsibilities, the Trustee is responsible for selecting suitable accounting policies, to be applied consistently, making any estimates and judgments on a prudent and reasonable basis, and for the preparing of the financial statements on a going concern basis unless it is inappropriate to presume that the Fund will not be wound up.

The Trustee is also responsible for making available certain other information about the Fund in the form of an annual report.

The Trustee also has a general responsibility for ensuring that adequate accounting records are kept and for taking such steps as are reasonably open to them to safeguard the assets of the Fund and to prevent and detect fraud and other irregularities, including the maintenance of an appropriate system of internal control. The Trustee is responsible for the maintenance and integrity of the corporate and financial information included on the Fund's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Trustee's responsibilities in respect of contributions

- The Trustee is responsible under pensions legislation for preparing, maintaining and from time to time reviewing and, if necessary, revising a Schedule of Contributions showing the rates of contributions payable towards the Fund by or on behalf of the employer of the Fund and the dates on or before which such contributions are to be paid; and
- The Trustee is also responsible for adopting risk-based processes to monitor whether contributions are made to the Fund by the employer in accordance with the Schedule of Contributions. Where breaches of the Schedule occur, the Trustee is required by the Pensions Acts 1995 and 2004 to consider making reports to The Pensions Regulator and the members.

Financial development of the Fund

The financial statements of the Fund for the year are set out on pages 22 to 37. The financial statements have been prepared and audited in accordance with Sections 41(1) and (6) of the *Pensions Act 1995*. A summary of the Fund's financial statements is set out in the table below:

	31/03/2023	31/03/2022
	£'000	£'000
Member related income	503	1,153
Member related payments	(291,356)	(493,683)
Net withdrawals from dealings with members	(290,853)	(492,530)
Net returns on investments	(2,375,227)	28,227
Net decrease in Fund	(2,666,080)	(464,303)
Net assets at start of year	8,076,748	8,541,051
Net assets at end of year	5,410,668	8,076,748

Transfer Payments

As a minimum, all cash equivalent transfer values (CETVs) paid during the year were calculated as prescribed by legislation and represented the value of a member's preserved benefits. No allowance for discretionary pension increases was included. CETVs paid to members of the Fund who were active when it closed to future accrual of benefits, and who have reached the UK minimum retirement age, are provided with a transfer value calculated as a Share of Fund, based on advice from the Scheme Actuary. Authorised financial advice is also provided to those members to enable them to consider their retirement options.

Pension Increases

Deferred pensions are increased in line with statutory requirements when deferred members retire. Pensions in payment were increased on 1 April 2023 as shown in the following table:

Legacy Scheme	Pension Element	Increase
Rolls-Royce Pension Fund / Rolls-Royce Ancillary Benefits Plan	Pension earned before 6 April 1997	2% (1)
	Pension earned between 6 April 1997 and 5 April 2005	5% (2)
	Pension earned after 5 April 2005	2.5% (3)
	Bridging pension	2.5% (3)
Rolls-Royce Group Pension Scheme / Vickers Group Pension Scheme	Pension earned before 6 April 1997	3% (4)
	Pension earned between 6 April 1997 and 5 April 2005 (31 March 2007 for former members of the Vickers Group Pension Scheme)	5% (5)
	Pension earned after 5 April 2005 (31 March 2007 for former members of the Vickers Group Pension Scheme)	2.5% (6)
	For managers, pension earned after 5 April 2006	2.5% (13)
	Bridging pension	2.5% (6)
Rolls-Royce Engine Control Systems Pension Scheme – Closed, SRBS and Open Sections	Pension earned before 1 April 2008	7% (7)
	Pension earned between 1 April 2008 and 30 September 2016	4% (9)
	Pension earned after 30 September 2016	2.5% (6)
	Temporary Pension	10.1% (10)
	For managers, pension earned after 30 September 2016	2.5% (13)
	Bridging pension	2.5% (6)
Rolls-Royce Engine Control Systems Pension Scheme – 2004 Section	Pension earned before 1 April 2008	5% (8)
	Pension earned between 1 April 2008 and 30 September 2016	4% (9)
	Pension earned after 30 September 2016	2.5% (6)
	Temporary Pension	10.1% (10)
	For managers, pension earned after 30 September 2016	2.5% (13)
	Bridging pension	2.5% (6)

See notes on following page.

Guaranteed Minimum Pension (GMP)

GMP earned between 6 Apr 1978 and 5 Apr 1988	N/A (11)
GMP earned between 6 Apr 1988 and 5 Apr 1997	3% (12)

Notes:

- Guaranteed 2% increases on 1 April in the years 2021, 2022 and 2023. From 1 April 2024, contingent increases of up to 2% a year will apply if the Fund retains a surplus of at least 4% on a basis set out in the Trust Deed and Rules.
- (1) Guaranteed 2% increases on 1 April in the years 2021, 2022 and 2023. From 1 April 2024, contingent increases of up to 2% a year will apply if the Fund retains a surplus of at least 4% on a basis set out in the Trust Deed and Rules.
 - (2) Annual CPI increase (September 2022) up to maximum of 5%.
 - (3) Annual CPI increase (September 2022) up to maximum of 2.5%.
 - (4) Annual RPI increase (December 2022) up to maximum of 3%.
 - (5) Annual RPI increase (December 2022) up to maximum of 5%.
 - (6) Annual RPI increase (December 2022) up to maximum of 2.5%.
 - (7) Annual RPI increase (January 2023) up to maximum of 7%.
 - (8) Annual RPI increase (January 2023) up to maximum of 5%.
 - (9) Annual RPI increase (January 2023) up to maximum of 4%.
 - (10) Increases in line with Basic State Pension.
 - (11) All increases are provided by the State.
 - (12) Annual CPI increase (September 2022) up to a maximum of 3%. Additional inflationary increases are provided by the State.
 - (13) Annual CPI increase (December 2022) up to maximum of 2.5%.
-

There were no discretionary increases applied to pensions.

Pensions Act 1995/2004

The following appointments have been made in accordance with statutory requirements:

- Scheme Actuary – Alastair McIntosh FIA - Aon plc until 21 July 2022
- Scheme Actuary – Leanne Johnston FIA, Mercer Limited from 22 July 2022
- Auditor – Deloitte LLP
- Legal advisor – Linklaters LLP
- Investment consultant – Mercer Limited

The Trustee regularly reviews the performance of its appointed advisors and service providers (including those mentioned above).

Investments

Governance

During the year the Trustee operated an investment governance framework. In accordance with this framework, significant investment matters were reserved for the full Trustee Board to enable it to consider, agree and monitor implementation of its investment strategy. To replace this framework the Trustee established an investment implementation and funding committee with effect from 1 April 2023 as described on page 5. The committee's terms of reference include regular investment risk monitoring and the development of investment and funding strategies for recommendation to the Trustee. Day-to-day management of investments is delegated to appointed investment managers in written agreements with those investment managers.

The Trustee maintains a statement of investment principles (SIP) in accordance with the *Pensions Act 1995*, which documents the principles governing the Trustee's decisions about investment. A copy of the latest SIP is appended to this annual report and financial statements. Copies are also available from the Trustee Secretary on written request. The Trustee can confirm that there were no breaches of the SIP during the year.

Custody

The Fund's assets are owned directly or indirectly by the Trustee and are entirely separate from the assets of the Company. The Trustee has appointed State Street Bank and Trust Company (State Street) to provide custody services for the safekeeping of segregated assets. The Fund's segregated assets are separately identified in State Street's records as belonging to the Trustee and State Street requires its sub-custodians to segregate the Trustee's assets from their own assets. State Street's records of securities and cash are reconciled to the Trustee's appointed investment managers' records on a monthly basis. Custody of the underlying investments in pooled investment vehicles is arranged by the managers of the pooled investment vehicles. Cash is normally held in liquid, diversified pooled investment vehicles managed by the investment managers.

Investment strategy

The Trustee's primary objective is to meet the Fund's liabilities as and when they fall due. In pursuit of this objective, the Trustee seeks to invest the Fund's assets at an appropriate level of risk relative to the Fund's liabilities.

In seeking to achieve the primary objective, the Trustee follows a low-risk investment strategy in pursuit of excess return relative to the Fund's liabilities by investing a proportion of assets in:

- A Liability-Driven Investment (LDI) portfolio, expected to match or "hedge" closely the interest rate and inflation risk profile of the Fund's liabilities.
- A credit portfolio expected to generate excess returns relative to the Fund's liabilities primarily by harvesting credit spreads above yields on "pure" hedging assets. The credit portfolio may contribute to the LDI strategy through investment in fixed interest assets but may also hold floating rate or non-matching assets. The credit portfolio may also hold a mixture of public and private assets.
- A Return-Seeking Asset (RSA) portfolio, expected to generate excess returns relative to the Fund's liabilities through investment in other non-matching assets such as equities.

Within these portfolios the Trustee invests in segregated assets and pooled investment vehicles. A summary of the assets contained in these portfolios at the end of the year is shown in the following table:

Asset Class	Segregated	Pooled investment vehicles	Total	
	£'000	£'000	£'000	%
Liability-Driven Investment (LDI) Portfolio	2,303,553	164,001	2,467,554	45
UK Government bonds - fixed interest	2,764,955	-	2,764,955	51
UK Government bonds - index-linked	1,463,027	-	1,463,027	27
Gilt repurchase agreements	(1,159,467)	-	(1,159,467)	(21)
Derivatives	406,781	-	406,781	7
Cash, liquidity funds and other net investment assets	(1,171,743)	164,001	(1,007,742)	(18)
Credit Portfolio	2,072,798	851,152	2,923,950	54
UK Government bond	7,197	-	7,197	-
Overseas Government bond	3,892	-	3,892	-
Global non-government (public and private)	1,989,174	755,787	2,741,961	50
Derivatives	(2,888)	-	(2,888)	-
Cash, liquidity funds and other net investment assets	78,423	95,365	173,788	3
Return-Seeking Asset (RSA) Portfolio	4,836	38,035	42,871	1
Private equity funds	-	38,035	38,035	1
Derivatives	7,807	-	7,807	-
Cash, liquidity funds and other net investment assets	(2,971)	-	(2,971)	-
Total net investment assets	4,381,187	1,053,188	5,434,375	100

The segregated UK Government bonds are quoted on recognised stock exchanges. The pooled investment vehicles are valued and traded daily, weekly or monthly by the investment managers. All other assets are traded in “over the counter” markets.

The Trustee has authorised the use of derivatives by the investment managers to reduce certain investment risks and for efficient portfolio management purposes. The principal investments in derivatives are:

- Collateralised interest rate swaps, inflation swaps and futures contracts within the LDI and credit portfolios.
- Forward foreign exchange contracts in order to hedge assets denominated in overseas currencies back to Sterling.

The Fund maintains a prudent level of collateral that can be accessed quickly if additional collateral needs to be posted to derivative counterparties. Consequently, the Fund was not subject to the significant, adverse impacts that rapidly rising interest rates had on some pension schemes' LDI portfolios in the second half of 2022.

A summary of the derivative contracts held within the Fund's segregated investments for this purpose at the end of the year is included under note 15 to the financial statements.

At the year end the Fund held senior debt of Credit Suisse Group valued at £6.6m and had no direct exposure to Silicon Valley Bank. Following the acquisition of Credit Suisse Group by UBS Group in March 2023, the senior debt of Credit Suisse Group became the senior debt of UBS Group and was valued at £6.7m on 30 June 2023.

Performance

The level and type of assets in the Fund was significantly changed by the transfer of assets and liabilities from three other Company pension arrangements into the Fund on 31 October 2016.

Annual performance data is therefore only available for the Fund's assets and liabilities (technical provisions described on page 6) from the Fund year ended 31 March 2018. Data for the previous three Fund years is shown below:

Year ending 31 March	Assets	Liabilities
	%	%
2023	(29.63)%	(29.80)%
2022	0.16%	(0.70)%
2021	1.07%	(1.70)%

Stewardship and responsible investment

The Trustee has considered how Environmental, Social and Governance (ESG) factors should be integrated into the Fund's investment management processes and stewardship practices, taking into account the expected time horizon of the Fund. The Trustee's policy is that the Fund's investment managers have full discretion in integrating ESG and sustainability factors into their investment processes in order to assess the potential impact on financial performance in deciding on the selection, retention and realisation of investments.

The Trustee supports the UK Stewardship Code. The Trustee has given the appointed investment managers, both segregated and pooled, full discretion when undertaking engagement activities in accordance with their own corporate governance policies and current best practice.

In addition to requiring all managers to adhere to the UK Stewardship Code, all managers are expected to be signatories to the UN supported Principles for Responsible Investment (PRI).

The Trustee is open to engaging directly, through written communication, with debt or equity issuers on a range of issues including, but not limited to, performance, strategy, risks, ESG and sustainability factors. This might take place if the manager requests the engagement and if the Trustee believes that this may be more effective than the investment manager's stewardship engagement activity on its own. Before engaging, the Trustee will seek advice from its appointed investment consultant and other appointed advisers.

The Trustee has commissioned its investment consultant to undertake an annual responsible investment monitoring framework exercise covering ESG integration, stewardship activities and carbon footprinting analysis. The Trustee will engage with its investment managers on the key findings as necessary, particularly where a manager is judged to be lagging its peers. The Trustee will use this assessment and the investment consultant's ESG ratings in decisions around selection, retention and cessation of manager appointments.

The Trustee supports the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD) as a best-practice framework to manage and report on the actions being taken to identify climate change related risks and incorporate climate change risk management into investment processes. The Fund's investment managers are expected to adopt these recommendations. Since 2019 the investment managers have been required to provide portfolio carbon risk metrics consistent with the framework and the Trustee reports these metrics on an annual basis. A copy of the current TCFD report is included in Appendix 2.

The Trustee does not currently have a policy of taking into account "non-financial matters" when considering the selection, retention and realisation of assets. For this purpose "non-financial matters" means the views of the members and beneficiaries, including their ethical views and views in relation to social and environmental impact and their present and future quality of life.

Contact details

Internal Disputes Procedure

The Trustee operates an Internal Disputes Procedure for resolving complaints by members in accordance with statutory requirements. All complaints should be made in writing to:

*The Trustee Secretary
Pensions Department
Rolls-Royce plc
Trent Hall (A90)
Victory Road
Derby
DE24 8EJ*

The Money and Pensions Service

The Money and Pensions Service (MaPS) is a UK Government funded website that provides financial information and tools for the public on a range of financial issues. The website address is: <https://moneyandpensionsservice.org.co.uk>

The Pensions Ombudsman

The Pensions Ombudsman may investigate and determine any complaint or dispute of fact or law in relation to an occupational pension scheme. The Ombudsman can be contacted at:

*10 South Colonnade
Canary Wharf
London
E14 4PU*

Pension Tracing Service

The Pension Tracing Service has been established to help individuals to keep track of benefits they may have as a result of service with former employers. The Pension Tracing Service can be contacted at:

*The Pension Service 9
Mail Handling Site A
Wolverhampton
WV98 1LU*

The registration number of The Rolls-Royce UK Pension Fund is 12001014.

Information to Members

Further information about the Fund can be requested by writing to:

*The Trustee Secretary
Pensions Department
Rolls-Royce plc
Trent Hall (A90)
Victory Road
Derby
DE24 8EJ*

Information can also be requested by e-mailing pensions.web@rolls-royce.com.

The Pensions Regulator

The Pensions Regulator (TPR) is the regulatory body for occupational pension schemes in the UK. TPR can be contacted at:

*Napier House
Trafalgar Place
Brighton
East Sussex
BN1 4DW*

This report or other information about the Fund can be provided in large print or Braille formats upon request. The Trust Deed and Rules is available for inspection by members by writing to the same address. Further information about members' benefits and the Fund in general is available at www.rolls-roycepensions.com.

Approval of Trustee's Annual Report and Financial Statements

The Trustee's Annual Report and the Financial Statements were approved at a meeting of the Trustee held on 20 September 2023.

Caroline Veitch
Trustee Secretary

Independent auditor's report to the Trustee of the Rolls-Royce UK Pension Fund for the year ended 31 March 2023

Report on the audit of the financial statements

Opinion

In our opinion the financial statements of the Rolls-Royce UK Pension Fund (the 'Fund'):

- show a true and fair view of the financial transactions of the Fund during the year ended 31 March 2023 and of the amount and disposition at that date of its assets and liabilities, other than the liabilities to pay pensions and benefits after the end of the year;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland"; and
- contain the information specified in Regulation 3A of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, made under the Pensions Act 1995.

We have audited the financial statements which comprise:

- the fund account;
- the statement of net assets (available for benefits); and
- the related notes 1 to 26.

The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards, including Financial Reporting Standard 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" (United Kingdom Generally Accepted Accounting Practice).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the Fund in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the Trustee's use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Fund's

ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

Our responsibilities and the responsibilities of the Trustee with respect to going concern are described in the relevant sections of this report.

Other information

The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. The Trustee is responsible for the other information contained within the annual report. Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit, or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

Responsibilities of Trustee

As explained more fully in the Statement of Trustee's responsibilities, the Trustee is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the Trustee determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Trustee is responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Trustee either intends to liquidate the Fund or to cease operations, or has no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Extent to which the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

We considered the nature of the Fund's industry and its control environment, and reviewed the Fund's documentation of their policies and procedures relating to fraud and compliance with laws and regulations. We also enquired of the Trustee and pension management, their own identification and assessment of the risks of irregularities, including those that are specific to the Fund's business sector.

We obtained an understanding of the legal and regulatory framework that the Fund operates in, and identified the key laws and regulations that:

- had a direct effect on the determination of material amounts and disclosures in the financial statements. These included the Pensions Act 2004, the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 and the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013; and
- do not have a direct effect on the financial statements but compliance with which may be fundamental to the Fund's ability to operate or to avoid a material penalty. These included the Fund's regulatory requirements.

We discussed among the audit engagement team including relevant internal specialists such as pensions actuarial and IT specialists regarding the opportunities and incentives that may exist within the organisation for fraud and how and where fraud might occur in the financial statements.

As a result of performing the above, we identified the greatest potential for fraud in the misappropriation of investment assets due to the significant size of investment transactions and balances. In response we have:

- obtained an understanding of the relevant controls over investment holdings and transactions;
- agreed investment holdings to independent confirmations; and
- agreed investment and cash reconciliations to independent sales and purchase reports and bank statements.

In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override. In addressing the risk of fraud through management override of controls, testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business.

In addition to the above, our procedures to respond to the risks identified included the following:

- reviewing financial statement disclosures by testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the financial statements;
- performing analytical procedures to identify unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- enquiring of the Trustee and pension management and legal counsel concerning actual and potential litigation and claims, and instances of non-compliance with laws and regulations; and

- reading minutes of Trustee meetings and reviewing correspondence with the Pensions Regulator.

Use of our report

This report is made solely to the Fund's Trustee, as a body, in accordance with Regulation 3 of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 made under the Pensions Act 1995. Our audit work has been undertaken so that we might state to the Fund's Trustee those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Fund's Trustee as a body, for our audit work, for this report, or for the opinions we have formed.

Deloitte LLP

Statutory Auditor
Birmingham, United Kingdom
Date: 20 September 2023

Financial Statements

Fund account

	Note	31st March 2023	31st March 2022
		£'000	£'000
Contributions and benefits			
Employer contributions	4	434	737
Employee contributions	4	-	-
Total contributions		434	737
Transfers in	5	69	416
		503	1,153
Benefits payable	6	(112,274)	(112,148)
Payments to and on account of leavers	7	(174,662)	(376,485)
Other payments	8	(476)	(1,764)
Administrative expenses	9	(3,944)	(3,286)
		(291,356)	(493,683)
Net withdrawals from dealings with members		(290,853)	(492,530)
Returns on investments			
Investment income	10	240,287	197,518
Change in market value of investments	13	(2,607,818)	(160,782)
Investment management expenses	11	(7,554)	(8,509)
Taxation	12	(142)	-
Net returns on investments		(2,375,227)	28,227
Net decrease in the Fund during the year		(2,666,080)	(464,303)
Net assets of the Fund at 1 April		8,076,748	8,541,051
Net assets of the Fund at 31 March		5,410,668	8,076,748

The notes on pages 24 to 37 form part of these financial statements.

Statement of net assets (available for benefits)

	Note	31 March 2023	31 March 2022
		£'000	£'000
Investment assets			
Bonds	13	6,225,245	9,010,750
Pooled investment vehicles	14	1,053,188	1,041,677
Derivatives	15	466,036	369,730
Cash	13	17,449	81,360
Other investment balances	13	1,007,352	1,614,939
		8,769,270	12,118,456
Investment liabilities			
Short sold bonds	13	(779,141)	(987,974)
Derivatives	15	(54,336)	(145,500)
Other investment balances	13	(2,501,418)	(2,887,178)
		(3,334,895)	(4,020,652)
Total investments		5,434,375	8,097,804
Current assets	22	637	830
Current liabilities	23	(24,344)	(21,886)
Total net assets of the Fund as 31 March		5,410,668	8,076,748

The notes on pages 24 to 37 form part of these financial statements.

The financial statements summarise the transactions of the Fund and deal with the net assets at the disposal of the Trustee. They do not take account of obligations to pay pensions and benefits which fall due after the end of the Fund year. The actuarial position of the Fund, which takes into account such obligations, is dealt with in the Report on Actuarial Liabilities on page 6 and these financial statements should be read in conjunction with that report.

Signed for and on behalf of the Trustee of the Rolls-Royce UK Pension Fund

Liz Airey
Director

Iain Foster
Director

20 September 2023

Notes (forming part of the financial statements)

1. Basis of preparation

The financial statements have been prepared in accordance with the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, Financial Reporting Standard 102 - The Financial Reporting Standard applicable in the UK and Republic of Ireland issued by the Financial Reporting Council and the guidance set out in the Statement of Recommended Practice (Revised 2018).

The financial statements are prepared on a going concern basis, which the Trustee believes to be appropriate as it believes that the Fund has adequate resources to realise its assets and meet accrued benefit payments in the normal course of events (continue to operate) for at least the next twelve months.

Whilst the Fund currently has surplus net assets to meet pension payments that have been accrued to date on an ongoing basis, if the Principal Employer, Rolls-Royce plc, became insolvent then the Fund would nevertheless be subject to an assessment by the Pension Protection Fund (the Pension Protection Fund is a statutory fund in the United Kingdom, intended to protect members if their defined benefits pension fund becomes insolvent. It was created under the Pensions Act 2004). This could potentially result in the Fund being wound up and its assets and liabilities transferred to the Pension Protection Fund. In such circumstances members would receive at least the level of benefits provided by the Pension Protection Fund. Alternatively, if the Fund was allowed to continue to provide members' benefits outside the Pension Protection Fund, it is possible that the Trustee would decide to wind-up the Fund and secure members' benefits immediately.

Rolls-Royce plc is a significant part of the Rolls-Royce group of companies which are ultimately owned by Rolls-Royce Holdings plc (the "Group"). The Trustee closely monitors the strength of the Group. The Trustee has considered the going concern statement included in the Group's 2023 half-year results published on 3 August 2023. This considered the period to 28 February 2025 and concluded that under "base case" and "stressed downside" scenarios, the Group expects to continue as a going concern. On this basis, whilst the impact of various factors including the macroeconomic environment and the Russian invasion of Ukraine cannot be accurately predicted, the Trustee currently considers that the Group will nevertheless continue to operate for the next twelve months, and therefore the Trustee believes that it remains appropriate to prepare the Trust's financial statements on a going concern basis. The financial statements do not include any adjustments that would result from the basis of preparation being inappropriate. It should also be noted that total investments shown in the financial statements are £5,434m within total net assets of £5,411m. Investments are recognised at fair value, which would not change if the financial statements were not prepared on a going concern basis.

2. Identification of the financial statements

The Fund is established as a trust under English law. The address for enquiries to the Fund is included in the annual report.

3. Accounting policies

The principal accounting policies of the Fund are as follows:

- a) Investments
 - i. Investments are included at fair value.
 - ii. Listed investments are stated at the bid price at the date of the statement of net assets, except as noted below.
 - iii. Bonds are stated at their clean prices (i.e. without accrued interest). Accrued interest is accounted for within investment income.
 - iv. Unquoted securities are included at fair value estimated by the Trustee based on advice from the investment managers.

- v. Pooled investment vehicles are stated at bid price for funds with bid/offer spreads, or single price where there are no bid/offer spreads are provided by the investment manager.
 - vi. Annuities purchased in the name of the Trustee which fully provide the pension benefits for certain members are excluded in these financial statements on grounds of materiality.
 - vii. Derivatives are stated at fair value.
 - Exchange traded derivatives are stated at fair value determined using market quoted prices.
 - Swaps are valued taking the current value of future cash flows arising from the swap determined using discounted cash flow models and market data at the reporting date.
 - Over the counter (OTC) derivatives are stated at fair value using pricing models and relevant market data as at the reporting date.
 - Forward foreign exchange contracts are valued by determining the gain or loss that would arise from closing out the contract at the reporting date by entering into an equal and opposite contract at that date.
 - All gains and losses arising on derivative contracts are reported within change in market value in the fund account.
 - Receipts and payments arising from derivatives are reported as sale proceeds or purchases of investments.
 - viii. Repurchase and reverse repurchase agreements:
 - Under repurchase agreements, the Fund continues to recognise and value the securities that are delivered out as collateral and includes them in the financial statements. The cash received is recognised as an asset in the financial statements and the obligation to pay it back is recognised as a liability.
 - Under reverse repurchase agreements, the Fund does not recognise the value of securities received as collateral in its financial statements. The cash delivered to the counterparty is recognised as a receivable in the financial statements.
- b) Investment income
- i. Income from fixed income securities is accounted for when it becomes payable.
 - ii. Interest is accrued on a daily basis.
 - iii. Investment income is reported net of attributable tax credits but gross of withholding taxes which are accrued in line with the associated investment income. Irrecoverable withholding taxes are reported separately as a tax charge.
 - iv. Investment income arising from the underlying investments of pooled investment vehicles is rolled up and reinvested within the pooled investment vehicles. This is reflected in the unit price and reported within change in market value.
 - v. Receipts from annuity policies held by the Trustee to fund benefits payable to members are included within investment income on an accruals basis.
- c) Foreign currencies
- i. The functional and presentational currency of the Fund is Sterling.
 - ii. Balances denominated in foreign currencies are translated into Sterling at the rate ruling at the reporting date. Asset and liability balances are translated at the bid and offer rates respectively.
 - iii. Transactions denominated in foreign currencies are translated at the rate ruling at the date of a transaction.
 - iv. Differences arising on investment balance translation are accounted for in the change in market value of investments during the year.
- d) Contributions
- i. Employee normal contributions are accounted for when deducted from pay. Employer normal contributions are accounted for in the period they are due under the Schedule of Contributions.
 - ii. Employer augmentation contributions are accounted for in accordance with the agreement under which they are being paid.

- iii. If relevant, employer deficit funding contributions are accounted for on the due dates on which they are payable in accordance with the Schedule of Contributions and any recovery plan under which they are being paid.
- e) Payments to members
 - i. Benefits are accounted for in the period in which they fall due for payment. Where there is a choice, benefits are accounted for in the period in which the member notifies the Trustee of his decision on the type or amount of benefit to be taken or, if there is no member choice, they are accounted for on the date of retirement or leaving.
 - ii. Opt outs are accounted for when the Trustee is notified of the opt out.
 - iii. Individual transfers in/out are accounted for when paid/received which is normally when member liability is accepted/discharged.

4. Contributions receivable

	2023	2022
	£'000	£'000
Employer:		
Normal	(5)	(24)
PaySave	(1)	(6)
Other	10	540
Disability benefits	430	227
	434	737
Members:		
Normal	-	-
	434	737

Following closure of the Fund to future accrual of benefits on 31 December 2020 no further regular contributions are payable in accordance with the Schedule of Contributions certified by the Scheme Actuary on 25 June 2021. Residual contributions remain payable due to backdated salary and service adjustments.

PaySave contributions related to members participating in an employee salary sacrifice arrangement. Such members accepted a reduced salary, did not pay member pension contributions and instead, the Company paid the pension contributions that would otherwise have been due from the members.

Other contributions relate to members using voluntary severance payments to fund a Bridging Pension Option.

If the Fund is less than 107% funded at the 31 March 2023 on the technical provisions basis agreed between the Trustee and the Company for the formal actuarial valuation, the employer will make additional contributions (capped at £145m) to the Fund over the period 1 January 2024 to 31 December 2026.

5. Transfers in

	2023	2022
	£'000	£'000
Individual transfers	69	416
	69	416

The individual transfers above relate to certain AVCs in the Rolls-Royce Retirement Savings Trust, which members can transfer back into the Fund to provide additional benefits at retirement.

6. Benefits payable

	2023	2022
	£'000	£'000
Pensions	(91,847)	(87,366)
Commutations and lump sum retirement benefits	(16,011)	(21,336)
Lump sum death benefits	(4,312)	(3,395)
Taxation where lifetime or annual allowance exceeded	(104)	(51)
	(112,274)	(112,148)

7. Payments to and on account of leavers

	2023	2022
	£'000	£'000
Individual transfers out to other schemes	(174,662)	(376,485)
	(174,662)	(376,485)

8. Other payments

	2023	2022
	£'000	£'000
PPF Levies	(476)	(1,764)
	(476)	(1,764)

9. Administration expenses

	2023	2022
	£'000	£'000
Actuarial fees	(722)	(467)
Audit fee	(68)	(47)
Legal and other professional fees	(399)	(530)
Administration and processing	(2,755)	(2,242)
	(3,944)	(3,286)

10. Investment income

	2023	2022
	£'000	£'000
Income from bonds	165,125	180,090
Income from pooled investment vehicles	74,682	17,408
Annuity income	149	86
Interest on cash deposits	331	(66)
	240,287	197,518

Investment income in unit-linked insurance policies and other pooled investment vehicles where income is not distributed, is accumulated, reinvested and included under change in market value in these financial statements. Overseas investment income is stated gross of withholding taxes. Irrecoverable withholding taxes are reported under taxation in the fund account.

Annuity income relates to annuities provided by Clerical Medical, Prudential, Zurich Assurance, Aviva Life and Pensions UK, ReAssure, Rothesay Life, Legal & General Assurance Society and Scottish Widows.

11. Investment management expenses

	2023	2022
	£'000	£'000
Administration, management and custody fees	(6,690)	(7,460)
Performance measurement and advisory fees	(834)	(956)
Performance related fees	(30)	(93)
	(7,554)	(8,509)

In addition to the investment management expenses charged directly to the Fund and disclosed above, the Fund incurred indirect investment management expenses through pooled investment vehicles as follows:

	2023	2022
	£'000	£'000
Administration, management and custody	(3,546)	(3,675)
	(3,546)	(3,675)

12. Taxation

The Fund is a registered pension scheme for tax purposes under the *Finance Act 2004*. The Fund is therefore exempt from taxation except for certain withholding taxes relating to overseas income. Tax charges are accrued on the same basis as the investment income to which they relate (see note 3 (b) (iii) and note 10 above).

13. Investment reconciliation

	Market value as at 01/04/2022	Purchases at cost and derivative payments	Sales proceeds and derivative receipts	Change in market value	Market value at 31/03/2023
	£'000	£'000	£'000	£'000	£'000
Bonds	8,022,776	1,611,461	(1,613,639)	(2,574,494)	5,446,104
Pooled investment vehicles	1,041,677	3,203,080	(3,137,927)	(53,642)	1,053,188
Derivatives	224,230	8,639,213	(8,468,271)	16,528	411,700
	9,288,683	13,453,754	(13,219,837)	(2,611,608)	6,910,992
Cash deposits	81,360			3,790	17,449
Other investment balances	(1,272,239)				(1,494,066)
	8,097,804			(2,607,818)	5,434,375

14. Pooled investment vehicles

The Fund's investments in pooled investment vehicles is analysed below:

	2023	2022
	£'000	£'000
Overseas open-ended investment companies	1,015,153	988,874
Shares in limited partnerships	38,035	52,803
	1,053,188	1,041,677

The asset classes for the pooled investment vehicles are summarised in the following table:

	2023	2022
	£'000	£'000
Credit	23,334	23,590
Private equity	38,035	52,803
Cash and liquidity	259,366	188,758
Sole-investor pooled investment vehicles	732,453	776,526
	1,053,188	1,041,677

The asset classes for the sole-investor pooled investment vehicles are summarised in the following table:

	2023	2022
	£'000	£'000
Credit	649,986	721,114
Futures	(13,678)	(16,540)
Cash and liquidity	96,145	71,952
	732,453	776,526

15. Derivatives

The Trustee has authorised the use of derivatives by its investment managers as part of the investment strategy described in the Trustee's report. Derivatives are primarily used to provide returns in line with changes in the value of the Fund's liabilities as a result of changes in interest rates and inflation – a strategy known as Liability Driven Investment (LDI). These assets include collateralised interest rate and inflation swap contracts.

(i) Total derivatives

The total derivatives in the Fund are summarised below:

	2023			2022		
	Assets	Liabilities	Net	Assets	Liabilities	Net
	£'000	£'000	£'000	£'000	£'000	£'000
Swaps	460,059	(53,934)	406,125	354,608	(127,965)	226,643
Futures	-	(261)	(261)	14,236	(196)	14,040
Foreign exchange forwards	5,977	(141)	5,836	886	(17,339)	(16,453)
	466,036	(54,336)	411,700	369,730	(145,500)	224,230

ii) Swaps

Swaps are used as part of the LDI strategy described in the Trustee's report. The swaps in the Fund are summarised below:

Nature	Latest maturity	Nominal amount	Asset value at year end	Liability value at year end
		£'000	£'000	£'000
Interest rate swap	05/01/2072	2,405,806	229,727	(51,923)
Inflation rate swap	15/01/2034	1,381,500	222,752	(-)
Total return swap	29/03/2024	158	7,580	(2,011)
Total 2023		3,787,464	460,059	(53,934)
Total 2022		5,188,715	354,608	(127,965)

(iii) Futures

Futures are used as part of the LDI strategy described in the Trustee's report. The futures in the Fund are summarised in the following table:

Nature	Notional Amount	Term	Asset value at year end	Liability value at year end
	£'000		£'000	£'000
Euro Bund – Euro	(1,000)	3 Months	-	(44)
Euro Buxl – Euro	(200)	3 Months	-	(17)
Euro Bobl – Euro	(4,200)	3 Months	-	(104)
US Long Bond – USD	(109,100)	3 Months	-	(96)
Total 2023	(114,500)		-	(261)
Total 2022	(385,100)		14,236	(196)

The futures are structured as exchange traded contracts, are centrally cleared and require margin to be posted by the Fund.

iv) Foreign exchange (FX) forwards

FX forwards are used as part of the investment strategy described in the Trustee's report. The FX forwards in the Fund are summarised below:

Contract	Settlement date within	Currency bought	Currency sold	Asset value at year end	Liability value at year end
		000's	000's	£'000	£'000
FX Forward	1 to 3 months	3,143 GBP	5,575 AUD	121	-
FX Forward	1 to 3 months	6,469 GBP	10,651 CAD	106	-
FX Forward	1 to 3 months	4,083 GBP	4,549 CHF	38	-
FX Forward	1 to 3 months	1,206 GBP	10,139 DKK	7	-
FX Forward	1 to 3 months	35,382 GBP	39,958 EUR	209	-
FX Forward	1 to 3 months	6,475 GBP	61,710 HKD	108	-
FX Forward	1 to 3 months	9,953 GBP	1,569,400 JPY	357	-
FX Forward	1 to 3 months	1,413 GBP	17,877 SEK	16	-
FX Forward	1 to 3 months	309,287 GBP	376,570 USD	4,957	-
FX Forward	1 to 3 months	1,963 GBP	Various	58	-
FX Forward	1 to 3 months	6,300 USD	5,215 GBP		(123)
FX Forward	1 to 3 months	Various	1,653 GBP		(18)
Total 2023				5,977	(141)
Total 2022				886	(17,339)

The table above includes separate detail for FX forwards where the amount of GBP bought or sold is £1 million or more. All other FX forwards have been combined into two "various" lines.

v) Collateral and margin

The swaps and FX forwards are structured as "over the counter" contracts. Some of these contracts are "bilateral" agreements that require daily collateral to be posted by one of the counterparties to each swap. Collateral posted and received is summarised in the following table:

2023	Posted	Received	Net
	£'000	£'000	£'000
Cash	(10,510)	15,228	4,718
UK Government bonds	(6,369)	-	(6,369)
	(16,879)	15,228	(1,651)

2022	Posted	Received	Net
	£'000	£'000	£'000
Cash	(15,060)	35,059	19,999
UK Government bonds	(27,398)	-	(27,398)
	(42,458)	35,059	(7,399)

The Fund retains economic exposure to collateral posted to counterparties. Collateral received from counterparties is not reflected in the Fund's net asset statement.

The remaining contracts and futures are "cleared" agreements that require margin to be paid to a central clearing house to support changes in the valuation of the contracts. Margin is typically paid in cash. The Fund does not retain economic exposure to cash paid to a clearing house.

16. Transaction costs

Included within purchases and sales are direct transaction costs of £31,192 (2022: £45,875) comprising commissions and stamp duty. These costs are summarised below and relate to credit.

	2023			2022	
	Fees	Commission	Stamp Duty	Total	Total
	£'000	£'000	£'000	£'000	£'000
Credit	-	33	-	33	46
2023	-	33	-	33	-
2022	-	45	1	-	46

Transaction costs are also borne by the Fund in relation to transactions in pooled investment vehicles. These costs are taken into account in calculating the bid/offer spread of these investments and are not separately reported.

17. Repurchase and reverse repurchase agreements

The value of repurchase and reverse repurchase agreements are reported at the end of the year within other investment balances. These amounts include assets of £797.9 million (£1,151.9 million as at 31 March 2022) and liabilities of £1,957.4 million (£2,122.7 million as at 31 March 2022).

Repurchase and reverse repurchase agreements are structured as "over the counter" contracts and require daily collateral to be posted by one of the counterparties. Collateral posted and received is summarised in the following table:

2023	Posted	Received	Net
	£'000	£'000	£'000
UK Government bonds	(289,433)	-	(289,433)
	(289,433)	-	(289,433)

2022	Posted	Received	Net
	£'000	£'000	£'000
UK Government bonds	(305,689)	9,633	(296,056)
	(305,689)	9,633	(296,056)

The Fund retains economic exposure to collateral posted to counterparties. Collateral received from counterparties is not reflected in the Fund's net asset statement.

18. Concentration of investment

The Fund's investments in securities from a single issuer that represents 5% or more of the Fund's net assets are shown below:

Fund	2023	2022
UK Government bonds	63.5%	63.9%
Shares in the Insight Investments Secured Multi-Asset Credit Fund V	8.6%	5.8%

19. Investment fair value hierarchy

The fair value of the Fund's investment assets has been determined using the following fair value hierarchy:

- **Level 1** - the quoted price for an identical asset in an active market.
- **Level 2** - when quoted prices are unavailable, the price of a recent transaction for an identical asset adjusted if necessary or observable market data.
- **Level 3** - where a quoted price is not available and recent transactions of an identical asset on their own are not a good estimate of fair value, the fair value is determined by using a valuation technique which uses non-observable data.

The Fund's investment assets and liabilities have been allocated to the fair value hierarchy as follows:

2023	Level 1	Level 2	Level 3	Total
	£'000	£'000	£'000	£'000
Bonds	3,459,930	1,986,174	-	5,446,104
Pooled investment vehicles	259,366	755,787	38,035	1,053,188
Derivatives	(261)	411,961	-	411,700
Cash	17,449	-	-	17,449
Other investment balances	(1,494,066)	-	-	(1,494,066)
Total	2,242,418	3,153,922	38,035	5,434,375

2022	Level 1	Level 2	Level 3	Total
	£'000	£'000	£'000	£'000
Bonds	5,186,369	2,836,407	-	8,022,776
Pooled investment vehicles	188,757	800,117	52,803	1,041,677
Derivatives	14,039	210,191	-	224,230
Cash	81,360	-	-	81,360
Other investment balances	(1,272,239)	-	-	(1,272,239)
Total	4,198,286	3,846,715	52,803	8,097,804

20. Investment risks

FRS 102 requires the disclosure of information in relation to certain investment risks. These risks are set out by FRS 102 as follows:

- Credit risk: this is the risk that one party to a financial instrument will cause a financial loss for the other party by defaulting on an obligation.
- Market risk: this comprises currency risk, interest rate risk and other price risk.
- Currency risk: this is the risk that the fair value or future cash flows of a financial asset will fluctuate because of changes in foreign exchange rates.
- Interest rate risk: this is the risk that the fair value or future cash flows of a financial asset will fluctuate because of changes in market interest rates.
- Other price risk: this is the risk that the fair value or future cash flows of a financial asset will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

The Fund has exposure to these risks because of the investments it makes to implement its investment strategy described in the Trustee's report. The Trustee manages investment risks, including credit risk and other market risks, within agreed risk limits which are set taking into account the Fund's strategic investment objectives relative to its liabilities. These investment objectives and risk limits are implemented and monitored through the agreements in place with the Trustee's appointed investment managers, investment consultant and other professional advisors.

Further information about the Trustee's approach to risk management and the Fund's exposures to credit and market risks are set out below. This does not include annuity policies because these are not considered significant in relation to the Fund's overall investments.

(i) Credit risk

The Fund is subject to credit risk as it invests in bonds, "over the counter" derivatives, money market instruments and cash deposits. The Fund also invests in pooled investment vehicles and is therefore directly exposed to credit risk in relation to the investment in the pooled investment vehicles and is indirectly exposed to credit risks arising on the financial instruments held by the pooled investment vehicles.

A summary of direct credit risk is shown in the following table (investments are categorised as rated or unrated based upon the rating of an issuer rather than a counterparty or deposit institution):

2023	Investment grade	Non-investment grade	Unrated	Total
	£'000	£'000	£'000	£'000
Bonds	6,120,428	19,856	(694,180)	5,446,104
Over the counter derivatives	-	-	411,700	411,700
Cash	-	-	17,449	17,449
Other investment balances	-	-	(1,494,066)	(1,494,066)
Pooled investment vehicles	-	-	1,053,188	1,053,188
	6,120,428	19,856	(705,909)	5,434,375

2022	Investment grade	Non-investment grade	Unrated	Total
	£'000	£'000	£'000	£'000
Bonds	8,876,558	36,491	(890,273)	8,022,776
Over the counter derivatives	-	-	224,230	224,230
Cash	-	-	81,360	81,360
Other investment balances	-	-	(1,272,239)	(1,272,239)
Pooled investment vehicles	-	-	1,041,677	1,041,677
	8,876,558	36,491	(815,245)	8,097,804

Credit risk arising on bonds is mitigated by investing in government bonds of developed countries (mainly the UK) where the risk of default is minimal or in non-government bonds that are mostly rated as “investment grade”.

Credit risk arising on “over the counter” derivatives is mitigated by daily collateralisation (see note 15).

Credit risk arising on repurchase agreements is mitigated by daily collateralisation (see note 17).

Credit risk arising on cash deposits is mitigated by investing surplus cash in liquid and diversified pooled investment vehicles.

Credit risk on repurchase agreements is mitigated through collateral arrangements. Included in Other Investment Balances are amounts of £(1,159.5) million (£970.8) million as at 31 March 2022) payable under repurchase agreements.

Direct credit risk arising from pooled investment vehicles is mitigated by the underlying assets of the vehicles being ring-fenced from those of the related investment managers and by the regulatory environments in which the vehicles are operated. Accordingly, the Trustee and its advisors undertake due diligence when investing in new pooled investment vehicles and then continue to monitor the position. Indirect credit risk arises in relation to the underlying assets in the pooled investment vehicles. These risks are mitigated as described above for direct credit risks. The pooled investment vehicles in the Fund are summarised in note 14.

(ii) Currency risk

The Fund is subject to currency risk because some of its assets are denominated in overseas currencies. Foreign exchange forwards are used to hedge currency risk where it is both desirable and practical. The Fund's exposure to currency risk at the year end is shown below:

2023	Gross Exposure	Hedged Exposure	Net Unhedged Exposure
	£'000	£'000	£'000
Bonds	204,891	204,891	-
Derivatives	405,865	445,865	-
Cash	1,142	1,142	-
Pooled investment vehicles	34,849	3,244	31,605
	646,747	655,142	31,605

2022	Gross Exposure	Hedged Exposure	Net Unhedged Exposure
	£'000	£'000	£'000
Bonds	710,399	710,399	-
Derivatives	240,683	240,683	-
Cash	9,636	9,636	-
Pooled investment vehicles	49,897	3,110	46,787
	1,010,615	963,828	46,787

The net unhedged exposure above is to USD.

(iii) Interest rate risk

The Fund maintains controlled exposure to interest rate risk through bonds and interest rate swaps as part of its LDI strategy. The assets in the Fund that are subject to interest rate risk as part of the LDI strategy are shown in the following tables:

2023	Segregated	Pooled investment vehicles	Total
	£'000	£'000	£'000
Bonds	5,446,104	-	5,446,104
Interest rate derivatives	405,865	-	405,865
	5,851,969	-	5,851,969

2022	Segregated	Pooled investment vehicles	Total
	£'000	£'000	£'000
Bonds	8,022,776	-	8,022,776
Interest rate derivatives	240,683	-	240,683
	8,263,459	-	8,263,459

The value of bonds decreased significantly over the year because of rising interest rates. Rising interest rates also resulted in the Fund being required to post additional collateral to derivative counterparties over the year. As noted on page 14, the Fund maintains a prudent level of collateral that can be accessed quickly if additional collateral needs to be posted to derivative counterparties.

(iv) Other price risk

Other price risk arises principally in relation to the Fund's return seeking assets, which includes publicly listed equity and private equity. The Fund's exposure to other price risk is mitigated by constructing a portfolio with diverse exposure across various investment markets. The Fund's exposure to other price risk is shown below:

2023	Segregated	Pooled investment vehicles	Total
	£'000	£'000	£'000
Private equity	-	38,035	38,035
	-	38,035	38,035

2022	Segregated	Pooled investment vehicles	Total
	£'000	£'000	£'000
Private equity	-	52,803	52,803
	-	52,803	52,803

21. Self-investment

The Fund's holding in employer-related investments at the end of the year was less than 0.01% of the Fund's net assets (less than 0.01% as at 31 March 2022).

22. Current assets

	2023	2022
	£'000	£'000
Contributions due from Employer	53	158
Cash held by the Trustees	238	356
Sundry debtors	346	316
	637	830

Contributions receivable from the employer are disclosed in note 4. The contributions due at the end of the year are shown above. Following closure of the Fund to future accrual of benefits on 31 December 2020 no further significant regular contributions are expected to be paid. Subject to the Fund's funding position additional contributions might be payable as described in note 4.

The accrued contributions above relate to backdated salary increases, and disability payments. They were paid in April 2023.

23. Current liabilities

	2023	2022
	£'000	£'000
Amount due to Employer	(479)	(369)
Unpaid benefits	(19,481)	(17,397)
Sundry creditors	(612)	(485)
Investment manager expenses payable	(3,772)	(3,635)
	(24,344)	(21,886)

24. Related parties

At 31 March 2023 the companies participating in the Fund were:

- Rolls-Royce plc;
- Rolls-Royce Power Engineering plc;
- Rolls-Royce Submarines Limited (formerly Rolls-Royce Marine Power Operations Limited);
- Ross Ceramics Limited; and
- Vinters Engineering Limited.

At 31 March 2023 the directors of the Trustee included:

- 1 Trustee director who is a director of a trustee of another pension arrangement related to Rolls-Royce plc;
- 1 Trustee director who is in receipt of a pension from the Fund; and
- 7 Trustee directors who are deferred members of the Fund.

Contributions in respect of the Trustee directors were paid in accordance with the Schedules of Contributions.

In the year ended 31 March 2023 the following Trustee directors had received fees for their services:

- Liz Airey - £110,000 (£80,000 for the year ended 31 March 2022);
- Will Mansfield - £15,000 (£0 for the year ended 31 March 2022); and
- Paul Butler - £5,000 (£0 for the year ended 31 March 2022).

The Fund is administered by the Pensions Department of Rolls-Royce plc. From 1 January 2018 all costs of managing and administering the Fund have been paid by the Fund. Amounts due from and payable to the Company are included in notes 22 and 23. As at 31 March 2023 a net amount of £425,000 (£311,000 was due from the Company as at 31 March 2022) is due to the Company.

25. Commitments

The Fund has commitments in respect of private equity investments amounting to approximately £15.9 million at 31 March 2023 (£15.3 million as at 31 March 2022).

26. Guaranteed Minimum Pensions

On 26 October 2018 the High Court handed down a judgment involving the Lloyds Banking Group's defined benefit pension schemes. The judgment concluded the schemes should be amended to equalise pension benefits for men and women in relation to Guaranteed Minimum Pension (GMP) benefits. The issues determined by the judgment arise in relation to many other defined benefit pension schemes. Under the judgement schemes are required to backdate benefit adjustments in relation to GMPs accrued between 17 May 1990 and 5 April 1997 and provide interest on the backdated amounts. The Trustee has obtained an estimate of the backdated benefit adjustments and related interest. The amount is £16m. This amount is based on the Trustee's view of the most likely equalisation methodology to be adopted and a top-down assessment of the likely impact on members. It also includes an estimate of the top up transfer payments for GMP equalisation for members who have taken cash equivalent transfer values since 17 May 1990 following the High Court ruling on 20 November 2020. The amount has been recognised as a current liability in note 23 to the Fund's financial statements for the year ended 31 March 2023 (the prior year amount was £15m) and has increased due to interest on the original amount owing and an extra year of back payments now due.

Summary of contributions payable under the Schedule of Contributions in respect of the year ended 31 March 2023

This summary has been prepared on behalf of, and is the responsibility of, the Trustee. It sets out the employer and member contributions payable to the Fund under the Schedule of contributions certified by the Scheme Actuary on 25 June 2021.

The auditor reports on contributions payable under the Schedule of Contributions in the auditor's statement about contributions. The contributions payable under the Schedule of Contributions in respect of the Fund year are shown below:

	£'000
Employer:	
Employer contributions in respect of disability benefits	430
Contributions payable under the Schedule of Contributions (as reported by the auditor)	430
Members' voluntary severance payments used to fund a Bridging Pension Option.	10
Normal contributions	(5)
PaySave contributions made by employee salary sacrifice	(1)
Total contributions reported in the financial statements	434

The option for active members to pay AVCs into the Fund was removed from 1 November 2016. Active members could subsequently pay AVCs outside of the Fund to a different Company pension arrangement, the Rolls-Royce Retirement Savings Trust, until the Fund closed to future accrual of benefits.

Independent Auditor's Statement about Contributions

We have examined the summary of contributions to the Rolls-Royce UK Pension Fund for the Fund year ended 31 March 2023 which is set out on page 38.

Statement about contributions payable under the Schedules of Contributions

In our opinion contributions for the Fund year ended 31 March 2023 as reported in the summary of contributions and payable under the Schedule of Contributions have in all material respects been paid at least in accordance with the Schedule of Contributions certified by the Scheme Actuary on 25 June 2021.

Scope of work on statement about contributions

Our examination involves obtaining evidence sufficient to give reasonable assurance that contributions reported in the attached summary of contributions have in all material respects been paid at least in accordance with the Schedule of Contributions. This includes an examination, on a test basis, of evidence relevant to the amounts of contributions payable to the Fund and the timing of those payments under the Schedule of Contributions.

Respective responsibilities of Trustee and the auditor

As explained more fully in the Statement of Trustee's Responsibilities, the Fund's Trustee is responsible for preparing, and from time to time reviewing and if necessary revising, a Schedule of Contributions and for monitoring whether contributions are made to the Fund by the employer in accordance with the Schedule of Contributions.

It is our responsibility to provide a statement about contributions paid under the Schedule of Contributions and to report our opinion to you.

Use of our report

This statement is made solely to the Trustee, as a body, in accordance with Regulation 4 of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 made under the Pensions Act 1995. Our work has been undertaken so that we might state to the Trustee those matters we are required to state to them in an auditor's statement about contributions and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Trustee as a body for our work, for this statement, or for the opinion, we have formed.

Deloitte LLP

Statutory Auditor

Birmingham, United Kingdom

Date: 20 September 2023

Actuarial certification of the Schedule of Contributions

Name of scheme: Rolls-Royce UK Pension Fund

Adequacy of rates of contributions

1. I certify that, in my opinion, the rates of contributions shown in this Schedule of Contributions are such that the statutory funding objective could have been expected on 31 March 2020 to continue to be met for the period for which the Schedule is to be in force.

I also certify that the rates of contributions shown in this Schedule are not lower than I would have provided for had I had responsibility for preparing or revising the Schedule, the statement of funding principles and any recovery plan.

Adherence to statement of funding principles

2. I hereby certify that, in my opinion, this Schedule of contributions is consistent with the Statement of Funding Principles dated 25 June 2021.

The certification of the adequacy of the rates of contributions for the purpose of securing that the statutory funding objective can be expected to be met is not a certification of their adequacy for the purpose of securing the scheme's liabilities by the purchase of annuities, if the scheme were wound up.

Signature: *A G McIntosh*

Date: 25 June 2021

Name: Alastair McIntosh

Qualification: Fellow of the Institute and Faculty of Actuaries

Address: 122 Leadenhall Street
London
EC3V 4AN

Name of Employer: Aon Solutions UK Limited

Appendix 1 – Statement of Investment Principles

Rolls-Royce UK Pension Fund

Statement of Investment Principles – updated September 2023

1. Introduction

The Trustee of the Rolls-Royce UK Pension Fund (“the Trustee”) has drawn up this Statement of Investment Principles (“the Statement”) to comply with the requirements of the Pensions Act 1995 (“the Act”) and subsequent legislation. The Pensions Act 1995 requires the Trustee to document the investment principles governing decisions about investments for the purposes of the Fund. These include the Trustee’s policy on choosing investments, the kinds of investments to be held, the balance between different kinds of investments, risk, the expected return on investments, the realisation of investments, and such other matters as may be prescribed by legislation. The Trustee has consulted a suitably qualified person by obtaining written advice from the Trustee’s appointed Investment Consultant (IC), currently Mercer. The Trustee, in preparing this Statement, has also consulted the Company, Rolls-Royce plc.

Overall investment policy falls into two parts: the Trustee is responsible for the strategic management of the assets, which it undertakes in accordance with advice from its appointed IC; and the Trustee delegates various operational activities in respect of the implementation of its agreed investment strategy to the Rolls-Royce pensions department and other professional service providers. The Trustee uses professional investment managers for the day-to-day management of the assets.

This Statement is consistent with the Trustee’s investment powers, which are set out within the Fund’s Trust Deed & Rules and are subject to applicable legislation. If necessary, the Trustee will take appropriate legal advice regarding the interpretation of these. The Trustee acknowledges that, according to the law, it has ultimate power and responsibility for the Fund’s investment arrangements.

The Trustee refers to this Statement when making investment decisions to ensure that the decisions are consistent with the principles set out within. In addition, the Trustee will review this Statement in response to any material changes with respect to the Fund which it judges to have a bearing on this Statement. The Trustee will also review this Statement at least once every three years and without delay following any significant change in investment policy. Before any review or revision, the Trustee will obtain and consider written advice from an appropriate investment expert and will consult with the Company. Whilst it is normally expected that there will be general agreement, the Trustee’s fiduciary obligation to Fund members will take precedence over the Company’s wishes, should these ever conflict.

This Statement sets out the Trustee’s investment beliefs and general principles underlying the investment policy.

2. **Investment Beliefs**

The Trustee holds the following investment beliefs (not in any particular order):

1. The Fund's assets should be invested at an appropriate level of risk relative to the Fund's liabilities and the strength of employer covenant.
2. Good stewardship of the Fund's investments is in the best interests of the beneficiaries, because it can contribute towards the generation of a sustainable long term return at an appropriate level of risk to meet the Fund's investment objective.
3. Integration of environmental, social and corporate governance (ESG), or sustainability, factors into investment management processes and stewardship practices has a positive impact on financial performance.
4. Long term sustainability issues, in particular climate risk, present risks and opportunities which increasingly require explicit consideration.
5. A "well-below 2°C scenario" climate warming outcome in line with the Paris Agreement represents the best result for the economy and most investors as well as a lower risk outcome for the Fund than higher levels of warming. Therefore, the Trustee supports this outcome.
6. The primary risk to the Fund is a mismatch between its assets and liabilities.
7. Exposure to risks which might not reasonably be expected to be rewarded should be mitigated where the impact on overall risk is material and where it is practical and cost-effective to do so.
8. Exposure to credit risk is expected to be rewarded and contractual cash flows from credit investments are appropriate to match the liabilities, subject to adequate consideration of default risk.
9. Equity market exposure is expected to be rewarded through higher returns and diversification of risk versus other asset classes over the long term. However, equities are not a good match for the liabilities over the short term.
10. Exposure to specific risks of individual investments can be mitigated through diversification.
11. Investments which are liquid, transparent and simple are favoured, though a degree of illiquidity and complexity may be accepted where the expected rewards are sufficient and subject to having a very high probability of the remaining liquidity being sufficient (taking into account benefit payments including transfers and collateral requirements).
12. Risk cannot be captured effectively through a single measure and is best understood using a range of approaches.
13. Active management can add value and reduce risk, but its attractiveness depends on the style of active management and the associated additional costs must be justified.

14. Effectively controlling investment management costs can have a positive impact on overall investment returns.
15. The investment approach should reflect the ability to take a long-term view and to take advantage of a strong funding position. In particular, the Fund may benefit from being able to invest in a contrarian fashion, especially in times of heightened volatility, and efforts should be sought to control value leakage from the transaction costs associated with frequent switching between investments.

3. **Investment Objective**

The Trustee's overriding objective is to meet the Fund's liabilities as and when they fall due. In addition, the Trustee wishes to improve the funding position of the Fund over time to further increase the security of members' benefits.

In pursuit of these objectives, the Trustee seeks to invest the Fund's assets at an appropriate level of risk relative to the Fund's liabilities.

In seeking to achieve these objectives, the Trustee follows a low-risk investment strategy in pursuit of excess return relative to the Fund's liabilities by investing a proportion of assets in:

- i) a Liability-Driven Investment ("LDI") portfolio, expected to match or "hedge" closely the interest rate and inflation risk profile of the Fund's liabilities;
- ii) a Credit portfolio, expected to generate excess returns relative to the Fund's liabilities primarily by harvesting credit spreads above yields on "pure" hedging assets. The Credit portfolio may contribute to the LDI or liability-hedging strategy through investment in fixed interest assets, but may also hold floating rate or non-matching assets; and
- iii) a Return-Seeking Asset ("RSA") portfolio, expected to generate excess returns relative to the Fund's liabilities through investment in other non-matching assets such as equities.

Under the Rules of the Fund, the Trustee will grant contingent increases to certain benefit tranches should certain parameters be met in respect of the funding position of the Fund and the investment strategy. From an investment perspective, the requirement for the granting of contingent increase is that the Trustee considers, having taken advice, that the Fund is invested prudently. The Trustee has adopted a strategy to invest the assets of the Fund in this way.

4. Strategic Asset Allocation

In order to achieve its investment objectives the Trustee has adopted the following broad strategic asset allocation ranges for the Fund. The Fund may deviate from this allocation due to market movements or due to strategic decisions and there is no requirement to rebalance back to these ranges. In addition, the asset allocation may be refined to take advantage of market opportunities.

Asset Class	Typical ranges %	
	Exposure	Allocation
LDI portfolio	36.0 – 86.0	36.0 – 66.0
Credit portfolio	33.0 - 53.0	33.0 – 53.0
RSA portfolio	3.5 – 8.5	0 – 8.5
Total	100.0	100.0

A modest degree of leverage is used within the investment strategy in order to maintain the interest rate and inflation hedge ratios within the rebalancing ranges below whilst also maintaining the asset class exposures within the typical ranges above. Leverage is expected be used within the LDI portfolio or to provide leveraged exposure to equity markets.

The table below sets out the typical liability hedge rebalancing ranges for interest rates and inflation as at the date on which this SIP has been updated. The hedge ratios are monitored by the Trustee on a regular basis and rebalancing may be undertaken if the ranges are breached, although there is no requirement for the hedge ratios to be automatically rebalanced back within these ranges. The Trustee expects to increase the rebalancing ranges as the funding level improves in future.

	Rebalancing ranges (%)
Interest rate hedge ratio *	90 – 100
Inflation hedge ratio *	90 – 110

*Measured on a gilts flat basis.

5. Expected Return and Risk

The Trustee expects to generate a return on total assets, over the long term, of circa gilts+ 0.7% to gilts + 1.0% p.a. (net of investment management expenses). It is recognised that over the short term, performance may deviate significantly from the long term target.

The Trustee regularly monitors the level of investment risk and aims to keep this to a prudent level.

6. Risk Management and Measurement

The primary risk upon which the Trustee focuses is that arising through a mismatch between the Fund's assets and its liabilities.

The Trustee recognises that modern financial instruments make it possible to select assets with interest and inflation rate sensitivities that are similar to those of the estimated liability cash flows; a strategy known as liability-driven investment ("LDI"). A significant proportion of the Fund's assets have been invested in this way.

However, in order to meet the Fund's long-term objectives while controlling the level of contributions required from the Company, the Trustee has agreed to take a modest amount of investment risk relative to the liabilities. This is done in order to target a greater return than the LDI Portfolio would provide, whilst maintaining a prudent approach to meeting the Fund's liabilities.

In arriving at its chosen investment strategy and the production of this Statement, the Trustee has considered (amongst others) the following risks, which it believes may be financially material over the Fund's anticipated lifetime:

Risk	Description and mitigations
Market risk	Fluctuation in market prices and/or future cashflows of financial instruments. The Trustee adopts only a limited allocation to return seeking assets such as equities, and holdings are diversified by geography and sector. Currency risk is also monitored and, where appropriate, hedged.
Interest rate and inflation risk	Changes in market implied interest rates and inflation can affect the value of the Fund's assets and liabilities. The Trustee pays close attention to matching the interest rate and inflation exposures of its liabilities with those of its assets, maintaining high hedge ratios. A significant proportion of assets are allocated to liability-matching asset classes.
Credit risk	Direct credit risk arising from pooled investment vehicles is mitigated by the underlying assets of the pooled arrangements being ring-fenced from the pooled managers. Credit risk arising from direct debt holdings such as corporate bonds is mitigated by diversification limits specified in the investment management guidelines, by requiring investment to be predominantly in investment grade rated or equivalent quality instruments, as well as the skill of the managers in instrument selection.
Counterparty risk	The risk of default by the counterparty to a derivative or similar transaction. The Trustee has set limits diversifying exposure across different counterparties and monitors the total exposure to counterparties against specified risk limits. Derivative positions are predominantly collateralised daily to mitigate counterparty risk.
Investment manager risk	The risk inherent in the day-to-day running of the asset portfolio by investment managers, including underperformance of portfolios against the objectives set. The Trustee selects its managers carefully and, where appropriate, diversifies across a number of managers.

Concentration risk	<p>The failure of any one of the Fund's investments could jeopardise the Trustee's ability to meet its objectives if it constituted a significant proposition of the assets.</p> <p>The Trustee aims to ensure that the Fund is not unduly exposed to asset class, market or manager specific risk.</p> <p>There is some concentration of the Fund's assets in holdings of government bonds held by the LDI investment manager. The Trustee is of the view that these assets are the best available matching assets for the Fund's liabilities, and this risk reduction more than offsets the concentration risk.</p>
Cash flow and liquidity risk	<p>Cash flow and liquidity risk relates to the realisation of investments in order to meet the benefit payments.</p> <p>The Trustee and its advisors manage the Fund's cash flow requirements over the short-term in order to minimise the possibility that this occurs.</p> <p>The Trustee mitigates liquidity risk by ensuring investment in illiquid assets is kept at an appropriate level, and a prudent approach is taken to maintaining suitable levels of collateral to support derivative programmes.</p>
Custody risk	<p>The Trustee has appointed a leading custodian bank which is independent of the investment managers to act as global custodian to the assets. The Trustee has satisfied itself that the financial security, procedures and controls available justify this as a prudent, efficient and cost effective procedure. Pooled funds will have their own custody arrangements and the global custodian's function in this regard is therefore limited to the safekeeping of any relevant unit certificates, the custodian designated by the pooled fund manager retaining the remaining responsibilities in respect of the underlying securities and cash of the pooled funds.</p>
Leverage risk	<p>The Trustee has considered the risks from the use of leverage, such as a potential need to raise additional collateral and roll risks, and has implemented controls to reduce these risks.</p>
ESG factors	<p>Environmental, social and corporate governance (ESG), or sustainability, factors can have an impact on financial performance.</p> <p>The Trustee's policy is that the Fund's investment managers should integrate ESG and sustainability factors into their investment processes, to assess the potential impact in deciding on the selection, retention and realisation of investments, and should engage in stewardship activity which complements this analysis.</p>
Climate change	<p>Climate change is a systemic risk that may materially affect the financial performance of investments. Since 2020, the Trustee has adopted the Financial Stability Board's Task Force on Climate-Related Financial Disclosures (TCFD) framework recommendations and reports against them on an annual basis. The Fund's investment managers are expected to adopt these recommendations and since 2019 they have been required to provide portfolio carbon risk metrics consistent with the framework. In order to further mitigate climate change risk, the Fund's listed equity exposure tracks a low carbon equity index (subject to ongoing liquidity) and the Trustee has set targets for reducing the Fund's carbon exposure as set out in Section 11.</p>

7. Rebalancing and Cashflow Policy

The Trustee monitors the allocations to the LDI, Credit and RSA portfolios and the hedge ratios against the ranges set out in section 4 and considers rebalancing accordingly. Rebalancing is not automatic and the Trustee may choose not to rebalance if the limits of the ranges have been reached. The Trustee may also rebalance, if judged appropriate, where the limits of the ranges have not been reached.

The Trustee monitors leverage-related metrics and may rebalance the asset allocation if it deems that it is appropriate to do so in the context of these metrics. The Trustee may also make decisions about the realisation of assets based on the liquidity of an asset or class, its performance, and the extent to which investments must be in readily realisable form to meet the Fund's outgoing liabilities.

8. Day-to-Day Management of the Assets

The Trustee delegates the day-to-day management of the assets, including the realisation of assets, to a number of professional investment managers. The Trustee has taken advice from its appointed IC that the managers have the appropriate skill and experience for managing the Fund's investments and that they are carrying out their work competently.

The Trustee regularly reviews the continuing suitability of the Fund's investments, including the appointed managers, both of which may be adjusted from time to time. However, any such adjustments would be carried out with the aim of ensuring an overall level of risk that is consistent with the Fund's investment objective.

9. Appointment and Monitoring of Investment Managers

The Trustee looks to its appointed IC for a forward looking assessment of a manager's ability to meet its investment objectives over a full market cycle. This view will be based on the IC's assessment of the manager's idea generation, portfolio construction, implementation, business management and ESG capabilities, in relation to the particular investment fund that the scheme invests in. The IC's manager research ratings assist with due diligence and questioning managers during presentations to the Trustee and are used in decisions around selection, retention and realisation of manager appointments.

If the investment objective for a particular manager's fund changes, the Trustee will review the fund appointment to ensure it remains appropriate and consistent with the Trustee's wider investment objectives.

Some appointments, such as the private equity mandates, are for actively managed mandates and the managers are incentivised through remuneration (via performance related fees) and performance targets. The Trustee reviews the appropriateness of active management as part of its strategic management of the assets.

The documents governing the manager appointments include a number of guidelines which, among other things, are designed to ensure that only suitable investments are made by the Fund. The managers are prevented from investing in asset classes outside

their mandate without the Trustee's prior consent. The Trustee restricts managers from investing in employer-related investments where possible.

Where the Trustee has invested in pooled investment vehicles, it accepts that it has no ability to specify the risk profile and return targets of the manager, but appropriate mandates can be selected to align with the overall investment strategy. Additionally, specific exclusions may not be possible to be included in pooled funds and limited employer-related investments may occur.

Arrangements are in place to monitor the Fund's investments to help the Trustee check that nothing has occurred that would bring into question the continuing suitability of the current investments. To facilitate this, the Trustee's appointed IC provides the Trustee with a quarterly investment monitoring report. The appointed investment managers provide quarterly investment reports. The Trustee also employs an independent performance measurer that reports on a quarterly basis. These reports support the production of the quarterly investment monitoring report.

The quarterly investment monitoring report allows the Trustee to review absolute performance, relative performance against a suitable comparator index used as the benchmark, and against the manager's stated target performance (over the relevant time period) on a net of fees basis. The Trustee's focus is on long term performance but it may put a manager 'on watch' if there are short term performance concerns. If a manager is not meeting performance objectives, or their investment objectives for the mandate have changed, the Trustee may ask the manager to review any element of their fees. The Trustee does not currently monitor portfolio turnover costs but is looking to do this in future. The Trustee will ask investment managers to include portfolio turnover and turnover costs in their presentations and reports to the Trustee. The Trustee will engage with a manager if portfolio turnover is higher than expected.

The safe custody of the Fund's assets is delegated to professional custodians (either directly or via the use of pooled vehicles).

Additionally, the Rolls-Royce pensions department holds regular meetings or calls with the IC, investment managers and other professional service providers to support implementation of the Trustee's investment strategy.

10. Responsible Investment

The Trustee has set out its responsible investment beliefs in relation to ESG integration, including climate change, and stewardship earlier in this statement.

The Trustee has considered how ESG factors should be integrated into the Fund's investment management processes and stewardship practices, taking into account the expected time horizon of the Fund. The Trustee's policy is that the Fund's investment managers have full discretion in integrating ESG and sustainability factors into their investment processes to assess the potential impact on financial performance in deciding on the selection, retention and realisation of investments.

The Trustee supports the UK Stewardship Code (the "Code"). The Trustee has given the appointed investment managers, both segregated and pooled, full discretion when undertaking engagement activities in accordance with their own corporate governance policies and current best practice.

In addition to requiring all managers to adhere to the UK Stewardship Code all managers are expected to be signatories to the UN supported Principles for Responsible Investment (PRI).

The Trustee is open to engaging directly through written communication with debt or equity issuers on a range of issues including, but not limited to, performance, strategy, risks, ESG and sustainability factors. This might take place if the manager requests the engagement and if the Trustee believes that this may be more effective than the investment manager's stewardship engagement activity on its own. Before engaging the Trustee will seek advice from its appointed IC and other appointed advisers.

The Trustee produces an Engagement Policy Implementation Statement on an annual basis which documents how the Trustee has adhered to its policies with respect to engagement over the prior year. This statement provides detail on the voting activity of the investment managers, as well as examples of how they have engaged with the investee companies over the period.

The Trustee's IC produces an annual responsible investment monitoring report for the Trustee covering ESG integration, carbon footprinting analysis and stewardship activities including investment managers' adherence to the UK Stewardship Code. The Trustee engages with its investment managers on the key findings as necessary, particularly where a manager is judged to be lagging its peers. The Trustee uses this assessment and the IC's ESG ratings in decisions around selection, retention and realisation of manager appointments.

The Trustee does not currently have a policy of taking into account "non-financial matters" when considering the selection, retention and realisation of assets. For this purpose "non-financial matters" means the views of the members and beneficiaries, including their ethical views and views in relation to social and environmental impact and their present and future quality of life.

11. Climate-related risk and opportunities

The Trustee supports the recommendations of the TCFD as a best-practice framework to manage and report on the actions being taken to identify climate change related risks and incorporate climate change risk management into investment processes. Therefore, since 2020, the Trustee has adopted the TCFD framework recommendations and reports against them on an annual basis via its TCFD Statement. The Fund's investment managers are also expected to adopt these recommendations. Since 2019 the investment managers have been required to provide portfolio carbon risk metrics consistent with the framework and the Trustee reports these metrics on an annual basis.

The Trustee has a Climate Change Governance Policy document which sets out the detailed approach and processes that the Trustee and other stakeholders follow in respect of climate-related risks and opportunities.

The Trustee has agreed to target a net zero investment portfolio by 2050 or earlier. This target includes all assets.

The Trustee has also set a shorter-term target of a 50% or more reduction in greenhouse gas emissions intensity between the end of 2021 and the end of 2030. This target covers all assets except for the LDI portfolio and the private equity portfolio.

These targets are broadly consistent with the degree of decarbonisation required to limit global warming to 1.5°C according to the Intergovernmental Panel on Climate Change (IPCC).

In order to achieve the 2030 target, the Trustee has agreed specific targets relating to its corporate bond holdings, seeking to reduce the greenhouse gas emissions intensity of these portfolios between the end of 2021 and the end of 2025 by 50% or more and between the end of 2021 and the end of 2030 by 55% or more.

The targets are based on the Weighted Average Carbon Intensity metric and include Scope 1 and 2 emissions.

The Trustee will review its targets at least annually and intends to set specific targets for other asset classes and include Scope 3 emissions, when the available data has improved and there are suitable methodologies.

A wide range of factors will affect whether the Trustee achieves its targets and the Trustee has varying degrees of control over these factors. For example, the progress of the UK government will have a significant influence over the timing of reaching net zero, the quality and availability of data means that the quoted greenhouse gas emissions are likely to change. Ultimately achieving the desired level of decarbonisation will depend on economies overall successfully decarbonising. Notwithstanding that there are factors outside of the Trustee's control, the Trustee's intention is to meet its targets and it engages with its investment managers to make clear its requirements.

12. Compliance with this Statement

The Trustee will monitor compliance with this Statement regularly, and in any event will review this Statement at least once every three years or sooner if there is any significant change in investment strategy. The Statement will also be reviewed in response to any material changes to any aspects of the Fund and its liabilities, finances and attitude to risk of the Trustee and Company which they judge to have a bearing on the stated investment policy. Any such review will be based on written expert investment advice and will be in consultation with the Company.

Updated September 2023

Appendix 2 – Taskforce on Climate-related Financial Disclosures report

Chair's introduction

Climate change is one of the most defining challenges of our time. The response to climate change will influence the health and prosperity of the world now and in future; its impacts are already being felt and observed around the globe.

The Trustee of the Rolls-Royce UK Pension Fund ("the Fund") has a legal fiduciary responsibility to invest the Fund's assets in the best way possible for its members. The Trustee recognises climate change as a risk that could impact the financial security of members' benefits if it is not properly measured and managed. It also presents an opportunity, through investment in companies or assets that are expected to perform well in an economy that is positioned to address climate change.

The Trustee supports the recommendations of the Task Force on Climate-related Financial Disclosures ("TCFD"), and has prepared this report accordingly and in compliance with relevant legislation. The TCFD framework helps to manage and report on the actions the Trustee, and others involved in the management of the Fund, take to identify, assess and manage climate change related risks and opportunities.

This is the fourth year that the Trustee has produced a TCFD report, and this report builds on last year's with several additional areas covered. As the availability of data improves, and as best practice continues to develop, the Trustee's reporting will continue to evolve.

Steps taken over the year

Over the year to 31 March 2023, the key steps taken by the Trustee have been:

- Engaging with investment managers to ensure progress against the climate targets set last year.
 - o Last year, the Trustee agreed to target a net zero investment portfolio by 2050 or earlier including all assets of the Fund.
 - o The Trustee also set a shorter-term target of a 50% or more reduction in greenhouse gas emissions between the end of 2021 and the end of 2030, covering all assets except for the LDI portfolio and the private equity portfolio.
 - o In order to achieve the 2030 target, the Trustee agreed specific targets relating to its corporate bond portfolio, seeking to reduce greenhouse gas emissions intensity between the end of 2021 and the end of 2025 by 50% or more and by the end of 2030 by 55% or more.
 - o As at the end of 2022, greenhouse gas emissions intensity for the corporate bond portfolio had been reduced by 48%, demonstrating good progress against the Trustee's target.
- Carrying out a climate scenario analysis exercise, covering the potential impact on assets and liabilities (including longevity impacts).
- Carrying out carbon metrics analysis which provide an indication of the Fund's greenhouse gas emissions exposure. Additional climate metric data is also now available and included in this report (for example covering the liability driven investment portfolio).

- Producing an Engagement Policy Implementation Statement (which can be found online appended to the Trustee's annual report [here](#)) which outlines the considerations of climate change-related voting and engagement practices of the Fund's investment managers.

Regulatory and industry responses to climate change and its impacts are subject to significant development and change. Addressing climate change related risks to the Fund is a significant challenge for the Trustee, particularly given developments in the collection, disclosure and analysis of relevant data. The Trustee has reviewed its governance structure to ensure, amongst other things, that it devotes the necessary time and focus to reviewing and addressing climate change related risks. Consequently, after the year end, the Trustee set up a sub-committee, the Investment Implementation and Funding Committee (the "IIFC") whose primary purpose is to support the Trustee on a wide range on investment and actuarial matters, including climate change. The IIFC has responsibility to review the potential impacts of climate change on the Fund and report them to the Trustee alongside activities to address risks where possible. This TCFD report is backwards looking and many of the actions taken by the Trustee during the period covered by the report will be undertaken by the IIFC in future.

This report is appended to the Trustee's annual report and is available in the Help and resources tab at www.rolls-roycepensions.com.

Members are encouraged to contact the Trustee if there are comments they wish to raise and they can contact the Trustee at www.rolls-roycepensions.com.

We hope you enjoy reading this report.

Liz Airey, Chair – Rolls-Royce UK Pension Fund

Executive Summary

This report sets out the disclosures of the Trustee of the Rolls-Royce UK Pension Fund under the Task Force on Climate-related Financial Disclosures (“TCFD”) framework, and covers the Fund year ending 31 March 2023. As such, it focuses on the areas of Governance, Strategy, Risk Management and Metrics and Targets.

In addition to updates to the reporting provided in the 2022 report, this report also includes:

- Updates to the climate scenario analysis, following developments in modelling capabilities and assumptions, including modelling of potential impacts on longevity.
- Inclusion of liability driven investment (“LDI”) metrics following improvements in reporting from the LDI manager.
- Details on progress towards the Fund’s climate targets set in 2022.

In summary, this report details:

- The Trustee’s decision to target a net zero investment portfolio (covering all assets) by 2050 or earlier.
- The Trustee’s shorter-term target of a 50% or more reduction in greenhouse gas emissions intensity between the end of 2021 and the end of 2030. This target covers all assets except for the LDI portfolio and the private equity portfolio.
- The Trustee’s targets relating to its corporate bond holdings, seeking to reduce greenhouse gas emissions intensity between the end of 2021 and the end of 2025 by 50% or more and between the end of 2021 and the end of 2030 by 55% or more.
- The Fund’s progress over the first year against the targets set as part of last year’s report. In particular, as at the end of 2022, greenhouse gas emissions intensity for the corporate bond portfolio had been reduced by 48%, demonstrating good progress against the Trustee’s target.
- The steps taken by the Trustee in response to the risk posed by climate change and its impact on the long-term funding objective for the Fund.
- Achieving the targets in the long-term will require the global economy to decarbonise and this is especially relevant since the Fund’s low risk investment strategy, which dictates that the majority of the Fund’s assets are invested in (or have exposure to) UK Government bonds, means reaching the Fund’s target is highly reliant on the UK Government meeting its own net zero goals.
- The five metrics identified by the Trustee to inform its understanding of climate-related risks and opportunities: (1) carbon emissions, (2) carbon footprint, (3) weighted average carbon intensity (“WACI”), (4) implied temperature rise and (5) data quality.
- The Trustee’s decision to review the metrics on an annual basis as part of its responsible investment framework. To date, the Trustee has liaised with its investment managers and collated data where available. The Trustee notes that data availability and available methodologies has been better for

some asset classes (for example equities and buy and maintain credit) compared to others (for example secured finance). The Trustee will continue to work with the investment managers to improve data availability of the reported metrics.

- The key findings from the Trustee's climate change scenario analysis and carbon metric analysis.
- The Trustee's processes to identify, assess and mitigate climate change risk.
- Key aspects of the Trustee's Climate Governance Policy, which outlines the roles and responsibilities of the Trustee, Pensions Executive and professional advisers with respect to climate-related activities.
- The Trustee's beliefs with respect to environmental, social and corporate governance ("ESG") considerations, including in the area of climate change.
- The training received by the Trustee over the year from its investment adviser and investment managers.

The TCFD Framework

The Financial Stability Board, an international body established by the G20 that monitors and makes recommendations about the global financial system, created the Task Force on Climate-related Financial Disclosures (“TCFD”) framework in 2015. TCFD was created to improve and increase reporting of climate-related financial information that can promote more climate-informed investments.

Figure 1: TCFD Framework

The recommendations are in four key areas:



Governance

The organization's governance around climate-related risks and opportunities

Strategy

The actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning

Risk Management

The processes used by the organization to identify, assess, and manage climate-related risks

Metrics and Targets

The metrics and targets used to assess and manage relevant climate-related risks and opportunities

In 2021 legislation¹ was introduced to ensure there is effective governance by pension schemes with respect to climate change and there is appropriate disclosure regarding the identification, assessment and management of climate risk. The legislation is accompanied by statutory guidance that sets out how the Trustee should meet the requirements and report in line with the TCFD recommendations.

¹ The Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021 (“the Climate Change Governance and Reporting Regulations”) introduced new requirements for certain trustees relating to reporting in line with the TCFD recommendations. The Occupational Pension Schemes (Climate Change Governance and Reporting) (Miscellaneous Provisions and Amendments) Regulations 2021 amended the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 to introduce disclosure requirements relating to the reports required by the Climate Change Governance and Reporting Regulations.

Governance

The Trustee's approach to climate-related risks and opportunities

The Trustee has ultimate responsibility for ensuring effective governance of climate-related risks and opportunities. The Trustee's approach to the oversight and management of climate-related risks and opportunities is consistent with its approach to considering other financially material risks and opportunities facing the Fund. The Trustee's Statement of Investment Principles (the "SIP") details the key objectives, risks and approach to considering environmental, social and corporate governance ("ESG") factors, including climate change, as part of its investment decision making. The SIP is reviewed on an annual basis or more frequently as required.

The Trustee's overall investment beliefs on sustainability are:

- Climate change poses a systemic risk that may materially affect the financial performance of investments.
- ESG, or sustainability, factors can have an impact on financial performance. The Trustee's policy is that the Fund's investment managers should integrate ESG and sustainability factors into their investment processes, to assess the potential impact in deciding on the selection, retention and realisation of investments, and should engage in stewardship activity which complements this analysis.
- Good stewardship of the Fund's investments is in the best interests of the beneficiaries, because it can contribute towards the generation of a sustainable long term return at an appropriate level of risk to meet the Fund's investment objective.

The Trustee has reviewed in detail the roles and responsibilities of those undertaking or advising the Trustee on the Fund's governance activities and produced a Climate Governance Policy, which outlines the roles of the Trustee, Pensions Executive and professional advisers in respect of climate-related risks and opportunities, and the governance processes around this; please see the Appendix for further details of the roles and responsibilities of those parties advising or assisting the Trustee. Ongoing actions are embedded into the Trustee's business plan, and climate-related risks are included in the Trustee's risk register. All TCFD items and training are tabled at full Trustee Board meetings.

After the year end, the Trustee set up a sub-committee, the Investment Implementation and Funding Committee (the "IIFC") whose primary purpose is to support the Trustee on a wide range on investment and actuarial matters, including climate change. The IIFC meets at least four times a year. The Fund's Climate Governance Policy has since been updated to reflect the responsibilities of the IIFC in ensuring effective governance, monitoring and reporting on climate-related risks and opportunities.

The Trustee expects all advisers to act with integrity and diligence in fulfilling the set objectives and uses meetings with the advisers to assess and challenge them. Where relevant, this includes discussion of the steps taken by advisers to identify and assess any climate-related risks and opportunities.

The Trustee has set objectives for advice provided on climate change, risk and opportunities for its investment consultant, scheme actuary and covenant advisers. All professional advisers were formally assessed against the objectives set over the year. The Trustee has agreed to review its professional advisers annually against these objectives.

Key Trustee responsibilities and oversight of climate change risks

The Trustee takes independent advice from its professional advisers and input from its investment managers to help assess and manage climate risks and opportunities. The Trustee considers, discusses, questions and challenges the advice provided to ensure that any decisions continue to be integrated into a coherent investment strategy that supports the Fund's ability to provide pensions.

The Trustee agreed the Fund's strategic asset allocation and funding strategy in view of climate risk. The Trustee also agreed to greenhouse gas emissions targets and changes to investment mandates to ensure that the Fund's portfolio is aligned to meet its climate related targets.

The Trustee also considered the short, medium and long term impacts of climate change on the Fund's assets, funding level and covenant. More detail on the results is provided below under the 'Strategy' section.

The Trustee allocated a substantial amount of time and resource to reporting on TCFD regulations over the year. The Trustee meets at least quarterly (and more frequently, as deemed necessary) where investment performance and risk management are reviewed, and where climate-related risks form part of the wider assessment. The Trustee ensured that it allocated appropriate time in these meetings to discuss climate governance and reporting. When appropriate, over the year, the Trustee also set up additional ad-hoc meetings to discuss climate-related risks and opportunities. The Trustee undertakes training on climate-related risks and opportunities at least annually. The Trustee considers the time and resources spent on climate-related risks and opportunities to be proportionate to the overall level of risk associated with climate-related issues in the context of other risks, noting the large size and low-risk investment strategy of the Fund. Following the set-up of the IIFC noted above, many of the Key responsibilities and oversight of climate change risks will be managed by the IIFC with reporting and significant decisions tabled at full Trustee meetings.

Regular monitoring

The Trustee has commissioned an annual Responsible Investment report from its investment consultant covering ESG integration, stewardship and climate metric analysis (see 'Metrics' section for more detail). The Trustee engages with its investment managers on the key findings as necessary and monitors progress on at least an annual basis. The Trustee uses the annual Responsible Investment report to monitor progress against the targets set (see 'Targets' section for more detail).

In addition, the Trustee receives quarterly performance reports, which include ESG ratings (which includes considerations for climate change and active stewardship) for relevant investment mandates.

The Trustee reviewed and published its Engagement Policy Implementation Statement during the year, detailing how it has implemented its approach to climate change as laid out in the SIP.

The Trustee will also review the climate scenario analysis (see 'Strategy' for further detail) at least once every three years.

Training and climate competency

Research into how climate-related risks and opportunities impact financial markets is constantly evolving and expanding. Responsible Investment topics may also form stand-alone agenda items at meetings. The Trustee's investment managers are also asked to explicitly cover ESG and climate issues when presenting to the Trustee. The Trustee has allocated time and resources to reproducing the Fund's climate scenario analysis, reflecting developments made with respect to modelling capabilities and the inclusion of the impact of the climate scenarios on longevity.

Day-to-day implementation

The implementation of the management of climate change-related risk with respect to specific securities is delegated to third party portfolio managers. Each manager's approach to ESG issues and how these are integrated into their investment process is assessed as part of the manager selection and monitoring process. The terms of reference forming part of the contracts with a number of the Fund's listed corporate bond and secured income portfolio managers reflect their agreement to integrate ESG and sustainability factors into their investment processes and adhere to the UK Stewardship Code. In addition, the Fund's investment managers are also expected to be signatories to the UN supported Principles for Responsible Investment ("PRI").

Strategy

The Trustee's approach to managing strategic climate change risks and opportunities

Summary of Fund's Assets

This section sets out the Fund's strategic asset allocation, which has been considered as part of the scenario analysis.

Figure 2: Current Strategic Asset Allocation

Asset Type	Current Strategy
Liability Driven Investment	46.0%
Buy and Maintain Credit	38.0%
Secured Finance	10.0%
Return Seeking Assets	6.0%

Return Seeking Assets includes exposure to synthetic equities (c.5.3%), private equity (c.0.6%) and infrastructure (c.0.1%). LDI assets are predominantly UK Government bonds or derivatives.

The Fund's current strategic asset allocation is set out in Figure 2. In practice, the Fund's illiquid holdings have now been set to run-off over time and in the climate scenario analysis the secured finance, private equity and infrastructure mandates have therefore been assumed to linearly decrease over time and completely run-off by 2030.

Climate change timescales

The Trustee believes that sustainability issues, including climate change, present risks and opportunities which increasingly require explicit consideration. Climate change is identified and described as a systemic risk which may materially affect the financial performance of the Fund's investments. More specifically, the Trustee supports a "well-below 2°C scenario" climate warming outcome in line with the Paris Agreement as it represents the best result for its members as well as a lower risk outcome for the Fund than higher levels of warming.

The Trustee has considered the following time horizons:

Figure 3: Timeframes of short, medium and long-term horizons to identify relevant climate-related risks and opportunities.

Short term	4 years	Aligns with the Fund's next actuarial valuation date of 31 March 2026.
Medium term	13 years	Timescale over which the Fund may be able to achieve its long-term funding objective and materially de-risk.
Long term	28 years	This is chosen to be after the Fund is expected to achieve its long-term funding objective and materially de-risk. Aligns with long-term objective to achieve net zero by 2050.

Over the short term, **transition risks (i.e. risks and opportunities relating to transitioning the economy to emit lower levels of greenhouse gasses) are expected to dominate** and may present themselves through rapid market re-pricing as:

- The likelihood of different levels of global warming occurring, and different approaches to transitioning the economy, change.
- Market awareness of climate risks grows. For example, the implications of the physical impacts of climate change become clearer to markets.
- If policy changes catch markets by surprise. For example, if a carbon price is introduced across key markets to which the portfolio is exposed, at a sufficiently high price to impact behaviour.

Over the medium term (13 years), transition risks are also expected to dominate and will be associated with the transition to a low carbon economy. These include the development of technology and low carbon solutions (i.e. transition risks can also present opportunities). Policy, legislation and regulation are likely to also play a key role at the international, national and subnational level. Technology and policy changes are likely to produce winners and losers both between and within sectors and lead to stranded asset risks.

Over the long term (28 years), **physical risks are expected to come to the fore**. This includes the impact of natural catastrophes leading to physical damages through extreme weather events. Availability of resources is expected to become more important if changes in weather patterns (e.g. temperature or precipitation) affect the availability of natural resources such as water.

The greatest climate-related exposure in the short and medium term for the Fund is through the public equity and buy and maintain credit allocations as these asset classes were identified as those most sensitive to valuation impacts under different climate scenario assumptions. Over the long-term the position is expected to be similar, although changes in investment strategy may affect this. The climate scenario analysis (and climate metrics) thus helped the Trustee to understand how the Fund was exposed to climate-related risks and how it could be best positioned for the move to a low carbon economy.

The Trustee will continue to consider approaches to further manage climate change risks and opportunities as part of its ongoing investment strategy.

Climate change scenarios

This section of the report summarises the analysis of three climate scenarios in addition to a base case. The three climate scenarios are constructed to explore a range of plausible futures, rather than exploring tail risks (i.e., risks with a low probability but significant impact). In shorter time frames, transition risk tends to dominate while over longer time frames physical risk is expected to be the key driver of climate impacts. A key strength of the scenarios is that they allow for climate impacts to be “priced-in” before they happen. This reflects likely market dynamics and means climate impacts are more likely to materialise within investment timeframes.

The three climate scenarios are defined below:

- **1.5°C Rapid Transition** – Average temperature increase of 1.5°C by 2100 in line with the Paris Agreement. This scenario assumes sudden large-scale downward re-pricing across multiple securities in 2025. This could be driven by a change in policy or realisation that policy change is inevitable, consideration of stranded assets or expected cost. To a degree the shock is sentiment driven and is therefore followed by a partial recovery across markets. The physical damages are most limited under this scenario.
- **<2°C Orderly Transition** – Average temperature increase of less than 2°C by 2100. This scenario assumes political and social organisations act in a co-ordinated way to implement the recommendations of the Paris Agreement to limit global warming to below 2°C. Transition impacts do occur but are relatively muted across the broad market.
- **4°C Failed Transition** – Average temperature increase above 4°C by 2100. This scenario assumes the world fails to co-ordinate a transition to a low carbon economy and global warming exceeds 4°C above pre-industrial levels by 2100. Physical climate impacts cause large reductions in economic productivity and increasingly negative impacts from extreme weather events. These are reflected in re-pricing events in the late 2020s and late 2030s.

Climate scenario analysis is an ever evolving space and, as such, the scenarios modelled and reported may be subject to review in future periods. The Appendix of this report summarises the key assumptions and limitations of the climate scenario modelling. It is important to note that the modelling may understate the true level of risk due to the uncertainty around the future economic impacts of climate change. Results are expressed relative to a “climate-aware” baseline projection with the following weights, assuming scenarios are already partly price-in to markets: 10% to a Failed Transition, 40% to an Orderly Transition, 10% to a Rapid Transition and 40% to a range of low impact scenarios.

Impact on financial assumptions (funding and investments)

The analysis shows the annualised return and funding level impact of the three climate scenarios compared to their respective baseline on the asset allocation modelled.

Figure 5: Summary results of climate change scenario analysis.

	Climate impact *	
	Funding level	Annualised returns (% p.a.)
Rapid Transition		
Impact at 4 years	-1.2%	-0.3%
Impact at 13 years	-0.9%	0.0%
Impact at 28 years	-0.4%	0.0%
Orderly Transition		
Impact at 4 years	-0.3%	-0.1%
Impact at 13 years	+1.1%	+0.1%
Impact at 28 years	+4.3%	0.0%
Failed Transition		
Impact at 4 years	+0.2%	0.0%
Impact at 13 years	-1.3%	-0.1%
Impact at 28 years	-11.6%	-0.1%

*Relative to the baseline

Over the short and medium terms, the impact of climate change on funding level and returns is expected to be relatively muted and broadly similar across all scenarios considered.

- **Short term (4 years)** – Over this time period, transition risk dominates. The Rapid Transition is the most impactful scenario. Under this scenario there is a shock to financial markets in year 3 followed by a partial recovery the following year. Overall, the funding level at year 4 is reduced by 1.2% due to the impacts of Rapid Transition relative to the baseline projection. The Failed Transition is marginally positive due to transition costs not materialising.
- **Medium term (13 years)** – At this time period, the Rapid Transition and Failed Transition have impacts of similar magnitude. The Rapid Transition reduces funding level by 0.9% and the Failed Transition reduces funding level by 1.3%. The impact of the Orderly Transition is small on the basis that transition costs and impacts are smaller and largely priced in.

The risks in the long-term could be greater than in the short and medium term, particularly in relation to physical damage under a Failed Transition scenario. Over **the long term (28 years)**, physical damages are the dominant driver and the Failed Transition is the worst scenario. The Failed Transition reduces the funding level by 11.6%.

Overall, the Fund demonstrates robustness with respect to the potential impact of climate change on the investment strategy though a failed transition could present a significant risk over the long term.

It is important to note that these results are based on future projections of global financial metrics sourced from third-party data which may produce output that differs materially from actual impacts to the Fund. In particular, the model is expected to be less reliable the further in time the projections extend, and it is likely that physical impacts are significantly underestimated due to feedback loops or “tipping points”. The results are set out for informational purposes only and should not be used for any other purpose. The model uses a number of assumptions as set out in Appendix 3.

Impact on mortality

The Trustee has carried out analysis of potential mortality impacts from climate-related scenarios, including:

- **Transition risks** – risks from policy changes, reputational impacts and shifts in market preferences, norms and technology. For example, these may impact on GDP, with consequent impact on well-being and longevity.
- **Physical risks** – dangers or perils related to the physical or natural environment that pose a threat to people. This includes the direct impact on changes to heat/cold related deaths.

The balance between transition and physical risks will vary over different time horizons.

In modelling scenarios for mortality impacts, the Trustee's advisors have made use of:

- Representative Concentration Pathways (RCPs) and Shared Socioeconomic Pathways (SSPs) as defined by the UN Intergovernmental Panel on Climate Change (IPCC), including estimated projected temperatures.
- Relationships between each SSP and a range of socioeconomic and other variables as published by the UK Climate Resilience Program, and modelling of how changes to those variables would affect UK mortality rates.
- UK-based climate projections from the Met Office, with correlations between past climate data and mortality rates being used to predict future influences.

The modelling indicates the following scenario outcomes, each compared to mortality assumptions constructed with no explicit allowance for climate-related risks:

- A temperature rise of 1.5-2°C from pre-industrial levels might mean 5.3% higher Fund liabilities and 20 months higher life expectancy for older generations.*
- A temperature rise of around 3.5-4°C from pre-industrial levels might mean 3.8% lower Fund liabilities and over 5 years' lower life expectancy for younger generations.*

Based on this analysis, mortality changes arising from the direct and indirect impact of climate change may be material to the funding strategy longer term. The Trustee will keep this under review as part of monitoring its long-term strategy.

** It is important to note that these results are based on longevity projection models and third-party data which may produce output that differ materially from actual outcomes. The results are set out for informational purposes only and should not be used for any other purpose. In particular, the results should not be relied upon and they are not suitable for repurposing, copying, redistributing or modifying. The model provider disclaims all liability and makes no representations about the suitability for any purpose of the results and such content is supplied on an as is basis, without any warranty of any kind.*

Impact on covenant strength

In assessing the impact of climate change from a covenant perspective, the Trustee has considered the potential financial impact on the Sponsor (including cash flow generation and ability to raise capital) over the time horizons outlined in this report, the degree of reliance on the covenant and the relative scale of the covenant and the Fund. The Trustee has reviewed the Sponsor's climate disclosures and taken advice from its covenant adviser, taking into account the Sponsor's public disclosure and third party assessments. The Trustee noted that:

- The risks facing the Sponsor range from shorter term risks, in particular commodity market disruption, reputational risks and potential regulatory impacts, to longer term risks including a possible step change in the Sponsor's fundamental business model (e.g. new technology makes Rolls-Royce's engines redundant).
- At this stage, based on its internal risk assessment under two scenarios, the Sponsor has assessed the potential impact on the business as greater under the Accelerated Transition Scenario (1.5°C) than under the Accelerated Physical Scenario (3.6°C) given the regulatory changes and increased investment required to meet an accelerated transition towards a low carbon economy in the former. These two scenarios are broadly comparable to Mercer's Rapid Transition and Failed Transition scenarios respectively.
- Overall, the Trustee's covenant adviser concluded that, from a covenant perspective, climate change related risks are Low in the near term.
- In addition, over the longer term:
 - Although the potential financial impact of climate change risks on the covenant is not fully disclosed publicly, there is significant covenant headroom;
 - While the civil aerospace industry needs to address the issue of carbon emissions, the longevity of the Rolls-Royce covenant is supported by the likely longer time horizons to find alternative solutions for long haul travel as well as its diversified portfolio;
 - The Sponsor's carbon reduction and sustainable technology investment targets are in line with its peers; at this stage there is no evidence of environmental factors being a barrier to the civil aerospace industry's ability to attract capital; and
 - The impact of various climate change scenarios on the Fund's funding is limited in the short term and although the funding impact at 28 years is greater under certain scenarios, funding levels are expected to be materially above 100%.

Having taken advice and based on the information currently available, the Trustee remains of the view that its long term funding strategy and the likely timescale taken to achieve it remain appropriate in the context of the potential impact of climate change on the covenant provided by Rolls-Royce.

The Trustee will continue to consider the potential impact of climate change on Rolls-Royce in future.

Risk Management

The Trustee recognises that climate-related risks can be financially material and that due consideration of climate risk falls within the scope of the Trustee's fiduciary duty. Given the long-term nature of the Fund's investments and the timeframe in which climate risks could materialise, a total portfolio approach to risk management covering all sectors and all relevant asset classes has been taken, coupled with funding and covenant analysis.

This section summarises the primary climate-related risk management processes and activities of the Trustee. These help the Trustee understand the materiality of climate-related risks, both in absolute terms and relative to other risks to which the Fund is exposed.

Governance

The Trustee reviews climate change developments to identify risks and opportunities for the Fund regularly. In particular the Trustee reviews quarterly the investment managers' ESG ratings and an annual Responsible Investment report covering ESG integration, stewardship and carbon metric analysis. In addition, climate-related risks are referenced in the Trustee's risk register.

The Trustee has set objectives for advice provided on climate change, risk and opportunities for its investment consultant, scheme actuary and covenant advisers. All professional advisers were formally assessed against the objectives set over the year. The Trustee has agreed to review its professional advisers annually against these objectives.

Strategy

The Trustee carried out climate change scenario modelling which provides a top down strategic assessment of climate change risks and opportunities at the total Fund level. This focussed on the Fund's potential exposure to both transition and physical risks and the impact these could have on the funding level and the covenant of the Fund's sponsor. The covenant analysis was carried out by Penfida. On the basis of this analysis, the Trustee does not believe its investment or funding strategies have excessive exposure to climate-related risks.

Metrics and Targets

As set out later, the Trustee has measured the Fund using a number of climate-related metrics to identify potential areas of risk.

Reflecting the relative importance of climate risk relative to the other risks that the Fund faces, the Trustee has set multiple targets to reduce greenhouse gas emissions. The Trustee will monitor progress annually and challenge managers should they not meet the agreed targets. The Trustee believes that this will reduce climate-related risk over time.

The Trustee recognises the challenges with various metrics, tools and modelling techniques used to assess climate change risks. The Trustee aims to work with its investment consultant and investment managers to improve its approach to assessing and managing risks over time.

Manager selection, monitoring and retention

As the Trustee relies on third party investment managers to manage its assets, the day-to-day assessment of climate change related risks on specific assets has been delegated to them. They in turn are regularly assessed using the investment consultant's ESG ratings and as part of the annual Responsible Investment report framework and Engagement Policy Implementation Statement.

Where relevant, managers are invited to present to the Trustee to explain their approach to climate change risk management, amongst other topics. The Trustee will engage with managers where they are perceived to be lagging their peers in terms of ESG integration or active ownership, including where this relates to climate change risks.

Active stewardship

The Trustee recognises that active ownership by the investment managers will continue to be a very important part of the Fund's approach to managing these risks. The Trustee has agreed to assess investment managers' approaches to stewardship and engagement on an annual basis and summarises its findings in the Engagement Policy Implementation Statement. The Trustee expects companies in its portfolio to manage climate change risks. Stewardship activities can help hold companies to account and ensure they are taking a meaningful approach in this area.

The Trustee delegates stewardship engagement activity to the underlying investment managers.

Metrics

Key metrics for climate change related risks

Climate risk metrics aid the assessment of potential climate-related risks to which the Fund is exposed and help to identify areas for further risk management, including engagement and fund manager monitoring.

The Trustee recognises that the availability of accurate data for some asset classes or methodology is an industry-wide issue and will engage with the investment managers to improve their climate (and greenhouse gas) reporting.

The Trustee has chosen to report on the following metrics:

Metric type	Description
1. Absolute emissions: Total greenhouse gas emissions	The total greenhouse gas emissions (in metric tons) of the Fund's investments
2 Emissions intensity: Carbon Footprint	Total greenhouse gas emissions (in metric tons) of the Fund's investments divided by the value of the Fund's investments (in \$million)
3. Alternative emissions intensity: Weighted Average Carbon Intensity ("WACI")	The average, based on the size of the Fund's holding in each investment, of the greenhouse gas emissions (in metric tons) divided by revenue (in \$million) associated with each investment
4.Portfolio Alignment: Implied temperature rise ("ITR")	An estimate of the level of global warming consistent with the Fund's investments
5. Additional metric: Data Quality	The proportion of the portfolio for which the Trustee has verified, reported or estimated carbon emissions data

In addition to the emissions intensity metric proposed by the Department for Work and Pensions (carbon footprint), the Trustee has also selected to report the WACI. This is the primary metric to monitor the short-term decarbonisation target set for the buy and maintain credit managers and has been chosen given the higher levels of data coverage for this metric (see the Target section for further details). Both carbon footprint and WACI are reported in \$ terms in this report, consistent with the format the data is provided to the Trustee by its managers.

The Trustee has chosen the ITR because of its simplicity in presentation and as it is a useful way to see, at a glance, the positioning of a Fund towards a low carbon economy. Investments with high ITR metrics are likely to have a greater transition risk.

The Trustee has also chosen data quality as an alternative metric as it quantifies the overall quality of the data available and helps identify mandates where the Trustee should work further with its investment managers to increase the quality of data reported.

The Trustee recognises the challenges with various metrics, tools and modelling techniques used to assess climate change risks. The Trustee aims to work with its investment adviser and investment managers to continuously improve the approach to assessing and managing risks over time as more data becomes available.

The Trustee reports all Scope 1 and 2 emissions and Scope 3 where available.

The Appendix of this report sets out in further detail the metrics selected by the Trustee, including the data limitations and assumptions used in collating these metrics.

Results

Overall summary

The greenhouse gas emissions analysis includes scope 1, 2 and 3 emissions (where available). The Trustee has excluded the private equity (c.0.6% of total assets) and infrastructure (c.0.1% of total assets) mandates due to lack of available data.

Data coverage numbers are as provided by the managers. In some cases, managers have provided the split between reported and estimated (see appendix for further detail). For secured finance coverage is currently low. Across the other portfolios, the Trustee understands that missing or estimated data can have an impact upon investment decision making. The Trustee is working with its investment managers to improve quality and coverage over time and will be reactive to such changes. The Trustee is working with its investment consultant to stay abreast of emerging net zero and carbon metric methodologies as well.

Figure 6: Metrics summary.

Manager	Value at 31 December 2022 (£m)	Asset Class	Absolute emissions (tCO ₂ e based on value of investment)			Carbon Footprint (tCO ₂ e/\$million investment)			WACI (tCO ₂ e/\$million sales)			Implied Temperature Rise (°C)
			Coverage scope 1+2	Scope 1 + 2	Scope 3	Coverage scope 1+2	Scope 1 + 2	Scope 3	Coverage scope 1+2	Scope 1 + 2	Scope 3	
LGIM	(5.2) ¹	Synthetic equity	97.4%	11,424	Not available	97.4%	29	Not available	99.7%	111	Not available	3.2
LGIM	628.9	Buy & maintain credit	40.0%	44,049	Not available	40.0%	58	Not available	49.0%	144	Not available	2.4
RLAM	999.2		100.0%	50,603	165,332	100.0%	42	138	86.8%	93	Not available	1.7
Insight	471.3		59.0%	24,142	161,326	59.0%	42	284	87.0%	105	549	2.0
Aggregate	2,099.4		Not available	118,794	Not available	72.8%	47	Not available	75.5%	111	Not available	Not available
Insight	459.9	Secured finance	Not available									
M&G	312.6		14.8%	4,912	Not available	14.8%	11 ²	Not available	26.8%	17 ²	Not available	Not available
LGIM	2,308.2	LDI	100.0%	275,969	Not available	100.0%	72 ³	n/a	100.0%	140 ⁴	Not available	1.9

Source: Investment managers. As at 31 December 2022. Private equity mandates excluded due to lack of data availability

¹Net value of synthetic instruments. Equity market exposure at same date was c£332.2m.

²Figures provided on available data and are not normalised to reflect the whole portfolio.

³Units tonnes CO₂e/\$m Total Capital Stock

⁴Units tonnes CO₂e/\$m GDP

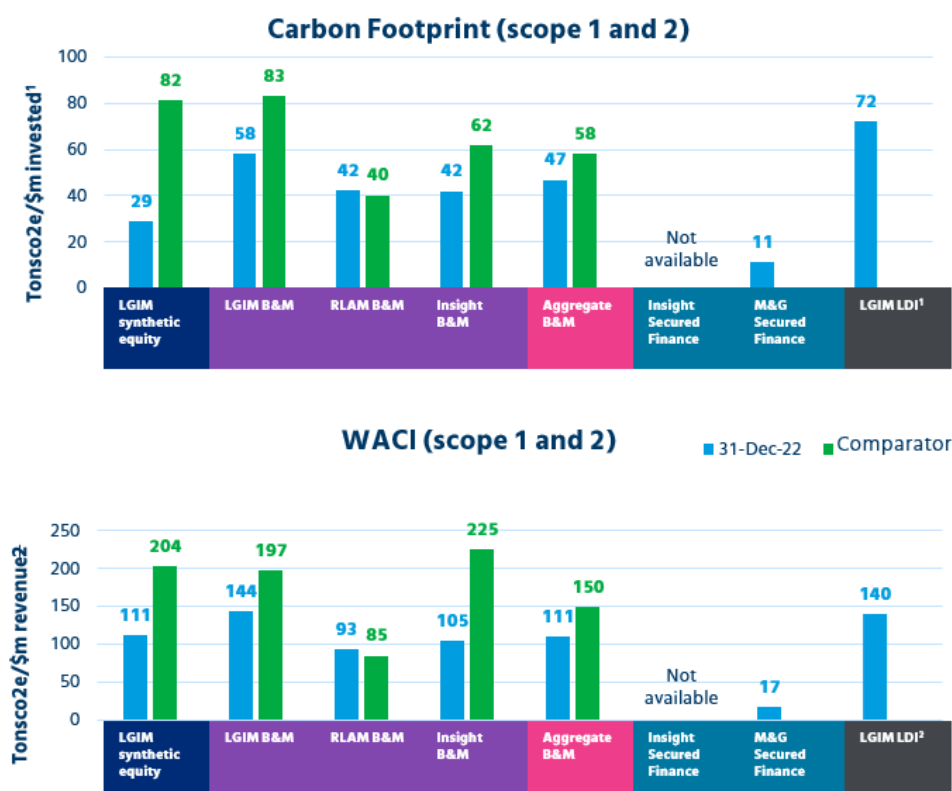
Emissions intensity metrics

Carbon footprinting metrics aid the Trustee in assessing the potential climate change related risks to which the Fund is exposed. The Trustee monitors the mandate's scope 1 and 2 carbon metrics against a benchmark or comparator index which helps in identifying areas for further risk management, including company engagement and investment manager monitoring. The graph below shows the carbon footprint and WACI against the comparator.

The synthetic equity mandate has a lower carbon footprint and WACI compared to the comparator. The LGIM and Insight buy and maintain credit portfolio WACIs are lower than their respective comparators this is also true for their carbon footprint. RLAM has a WACI and carbon footprint which is marginally higher than that of its comparator.

The WACI of the M&G secured finance is also shown; however they have low coverage and no obvious comparator. Data availability on Scope 3 remains limited and the most of the Fund's investment managers were not able to provide it this year.

Figure 7: Emissions intensity metrics.

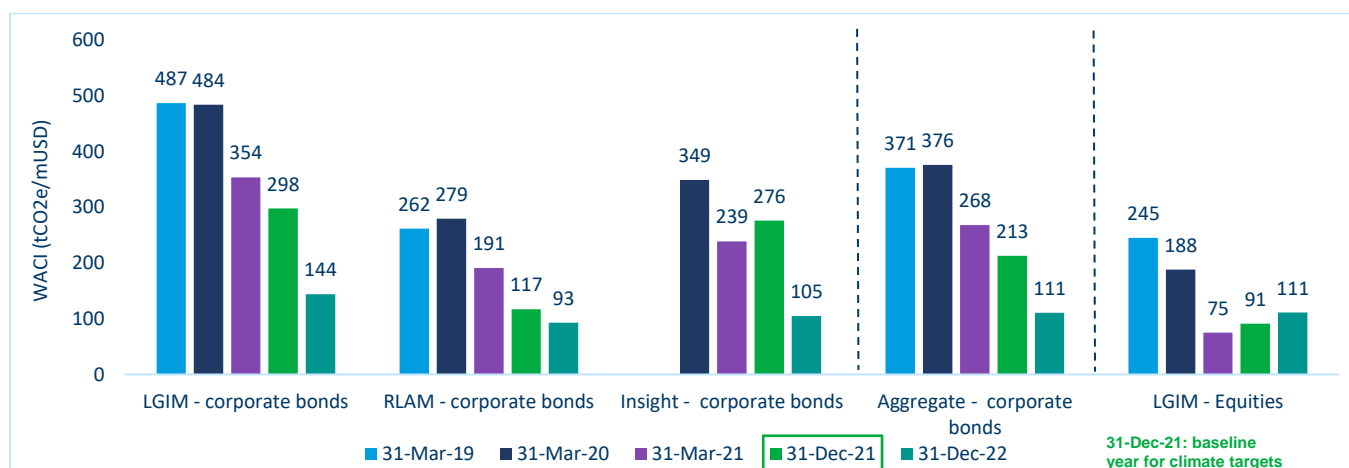


Source: Investment managers. Please see Appendix for further details including comparator details

The Trustee also monitors the year-on-year change in portfolio WACI, as can be seen below. The Fund has seen a broad decrease in carbon emissions (as measured by WACI) since 31 March 2019, with all

corporate bond and equity mandates making significant progress over longer time periods. However, the synthetic equities mandate has seen a slight increase in WACI since last year's analysis.

Figure 8: Year on year change in WACI.



Source: Investment managers, Rolls-Royce and Refinitiv.

Asset valuation provided by Rolls-Royce and includes cash and accruals, government bonds, FX and derivatives and corporate bonds'.

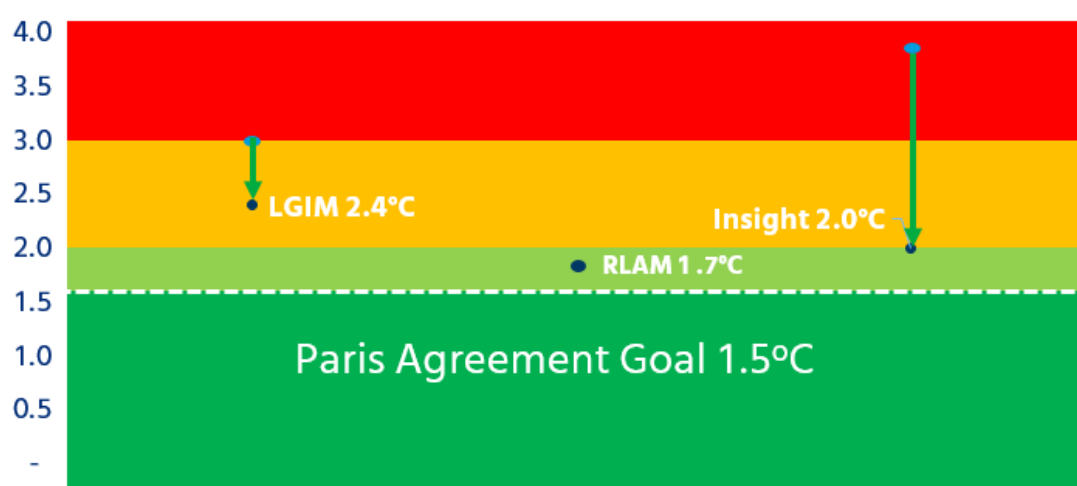
WACI figure provided by managers if data has been provided in £, Mercer have converted to USD using the spot rate at the appropriate date.

RLAM 2019 WACI figure calculated using holding data as at 30 September 2018.

Carbon intensity coverage has broadly improved over time.

Implied temperature rise

Figure 9: Implied Temperature Rise (ITR).



Source: Investment managers, as at 31 December 2022.

The buy and maintain credit portfolios have an ITR of between 1.7°C and 2.4°C, reflecting a range of methodologies for computing ITR and underlying companies at different stages of transitioning towards a low carbon future.

Only RLAM has an ITR broadly consistent with the goals of the Paris Agreement (although coverage is only 56%) and it is not yet 1.5°C aligned.

Targets

The Trustee has agreed to target a net zero investment portfolio by 2050 or earlier. This target includes all assets.

The Trustee has also set a shorter-term target of a 50% or more reduction in greenhouse gas emissions intensity between the end of 2021 and the end of 2030. This target covers all assets except for the LDI portfolio and the private equity portfolio.

These targets are broadly consistent with the degree of decarbonisation required to limit global warming to 1.5°C according to the Intergovernmental Panel on Climate Change (IPCC).

The LDI portfolio is excluded from the shorter-term target since this portfolio predominantly holds UK Government bonds which are an integral part of the Trustee's wider risk management approach. The Trustee notes that the UK Government is targeting being net zero by 2050 and achieving emissions reductions of 68% by 2030 and 78% by 2035 against a 1990 baseline. The Trustee will monitor progress and consider its next steps if these targets are not achieved. The private equity and infrastructure portfolio is excluded as it constitutes less than one percent of assets and these assets are being run off over time.

In order to achieve the 2030 target, the Trustee has agreed specific targets relating to its corporate bond holdings, seeking to reduce greenhouse gas emissions intensity between the end of 2021 and the end of 2025 by 50% or more and between the end of 2021 and the end of 2030 by 55% or more. These are in the process of being implemented through a mix of active portfolio decisions and stewardship undertaken by the managers.

The targets are based on the Weighted Average Carbon Intensity metric and include Scope 1 and 2 emissions.

The Trustee will review its targets at least annually and intends to set specific targets for other asset classes and include Scope 3 emissions, when the available data has improved and there are suitable methodologies.

A wide range of factors will affect whether the Trustee achieves its targets and the Trustee has varying degrees of control over these factors. For example, the progress of the UK Government will have a significant influence over the timing of reaching net zero, the quality and availability of data means that the quoted greenhouse gas emissions are likely to change. Ultimately achieving the desired level of decarbonisation will depend on global economies overall successfully decarbonising. Notwithstanding that there are factors outside of the Trustee's control, the Trustee's intention is to meet its targets and it engages with its investment managers to make clear its requirements.

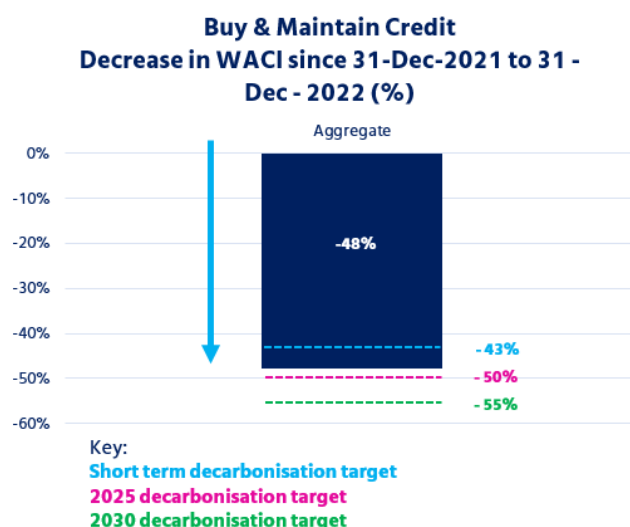
Progress Against Targets

In 2022, the Trustee set a number of targets as part of its TCFD requirements, relative to a baseline date of 31 December 2021 and agreed with its buy and maintain credit managers on a pathway towards decarbonisation (represented c40% of the Fund's net assets at 31 December 2022).

Following the adoption of these targets, a significant reduction in WACI was achieved across the Fund's B&M credit managers. This is depicted in the chart to the below, showing progression vs targets over 2022.

Figure 10: Progress against targets (Buy and maintain credit).

In aggregate, the WACI of the Fund's buy and maintain holdings decreased by 48% since last year, ahead of the decarbonisation pathway set by the Trustee. The Trustee notes that a wide range of factors will cause the WACI metric to vary from year to year and so the position against the target could oscillate over time. Notwithstanding this, the Trustee considers that good progress has been made to date.



Appendix 1: The roles of those undertaking or advising the Trustee on Fund governance activities

The Trustee has a **Pensions Executive** (which comprises certain individuals employed by the sponsor to assist the Trustee in managing the Fund) which assists the Trustee and its committees with these governance activities, including:

- Liaising with professional advisers on the Trustee's proposed objectives;
- Ensuring appropriate time and resource is allocated to climate governance and reporting; and
- Facilitating information sharing between the Trustee, its committees, professional advisers and investment managers as appropriate.

Over the reporting period, the Trustee's relevant **professional advisers** were:

- **Mercer, as the investment consultant, who:**
 - Advises on strategic asset allocation taking into account climate risk, advises on greenhouse gas emissions targets, advises on changes to investment mandates and monitors investment managers through the annual Responsible Investment report;
 - Provides climate related scenario analysis, advice and training on the selection of climate-related metrics for the Fund;
 - Produces the annual Responsible Investment report for the Trustee which outlines climate related risks or opportunities on an ongoing basis and monitors progress against climate related targets; and
 - Liaises with investment managers and other professional advisers to provide training to the Trustee and Pensions Executive on climate change, as appropriate.
- **Penfida, as the covenant adviser who:**
 - Assesses the Sponsor's ability and willingness to continue to support the Fund. Climate-related exposures are considered alongside other factors that could have a positive or negative impact on the strength of the Sponsor's covenant; and
 - Provides input into scenario analysis and advises on covenant implications.

- **Mercer, as the Scheme Actuary** who:

- Advises on the funding position including an understanding of the potential funding impact resulting from changes to financial or demographic assumptions driven by climate change;
- Advises on funding strategy robustness to climate risk. Provides input to enable strategic asset allocation decisions to be made considering impact of climate risks on funding strategy; and
- Provides input into scenario analysis and advises on funding implications.

In addition, Mercer assists the Trustee in producing the Fund's TCFD report on an annual basis and will work in conjunction with the Trustee's other advisers.

Appendix 2: Climate related risks and opportunities

We are already experiencing climate change and its associated physical impacts today. The average global temperature in 2022 was about 1.2°C above pre-industrial levels. Most of this warming has occurred in the past 35 years, with the seven “warmest” years on record taking place since the start of 2015. The overwhelming scientific consensus is that the observed climatic changes are primarily the result of human activities including electricity and heat production, agriculture and land use change, industry and transport.

In order to mitigate the worst economic impacts of climate change, there must be a large, swift, and globally co-ordinated policy response. Despite this, the majority of climate scientists anticipate that given the current level of climate action, by 2100 the world is estimated to be between 2°C and 4°C warmer than pre-industrial levels, with significant regional variations. This is substantially higher than the 2015 Paris Climate Change Agreement objectives, which reflects a collective goal to hold the increase in the climate’s average global surface temperature to well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase to 1.5°C.

There is considerable uncertainty regarding the future warming pathway, which is highly dependent on the actions of governments, industries, businesses and individuals.

The effects of climate change will be felt over many decades. There are two broad types of climate-related risks and opportunities that have been considered by the Trustee in its climate scenario analysis: transition risk (and opportunities) and physical risks (and opportunities).

Transition risks and opportunities

These cover the potential financial and economic risks and opportunities from the transition to a low-carbon economy (i.e. one that has a low or no reliance on fossil fuels), such as:

- Policy and legal
- Market
- Technology
- Reputation

These risks cover the possibility of future bans, or high costs, associated with high carbon activities or products as well as opportunities that may come from the development of low-carbon technologies.

In order to make a meaningful impact on reducing the extent of global warming, most transition activities need to take place over the next decade and certainly in the first half of this century.

Physical risks and opportunities

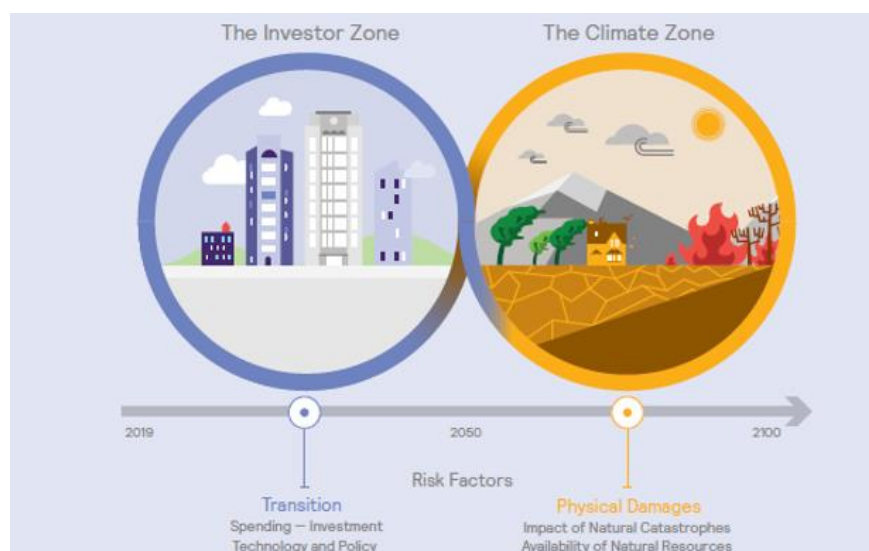
The higher the future level of global warming, the greater physical risks will be in frequency and magnitude. Physical risks cover:

- Physical damage (storms, wildfires, droughts, floods)
- Resource scarcity (water, food, materials, biodiversity loss)

The Trustee expects physical risks to be felt more as the century progresses though the extent of the risks is highly dependent on whether global net zero greenhouse gas emissions are achieved by 2050.

There are investment opportunities in newly constructed infrastructure and real estate that are designed to be resilient to the physical impacts of climate change, as well as being constructed and operated in a way that has low or no net carbon emissions. There are also opportunities for investment in those companies or industries that focus on energy conservation and resource efficiency.

Transition and physical damages.



Source: Mercer.

Appendix 3: Scenario analysis assumptions

Assumed Strategic Asset Allocation Over Time

Modelling Asset Class	Strategic Asset Allocation								
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9 - 28
MSCI Paris Aligned Equity	5.3%	5.4%	5.5%	5.6%	5.7%	5.7%	5.8%	5.9%	6.0%
UK Investment Grade Credit	31.7%	31.5%	31.0%	30.4%	30.8%	31.7%	32.6%	33.6%	34.5%
US Investment Grade Credit	4.3%	5.8%	7.5%	9.4%	10.3%	10.6%	10.9%	11.2%	11.5%
Global Senior Private Debt	10.0%	8.8%	7.5%	6.3%	5.0%	3.8%	2.5%	1.3%	0.0%
World Private Infrastructure	0.1%	0.1%	0.1%	0.1%	0.0%	0.0%	0.0%	0.0%	0.0%
LDI	48.0%	48.0%	48.0%	48.0%	48.0%	48.0%	48.0%	48.0%	48.0%
Private Equity	0.6%	0.5%	0.4%	0.4%	0.3%	0.2%	0.1%	0.1%	-

Note: figures may not sum to 100% due to rounding

The analysis has been completed based on an analysis date of 31 December 2022 and using the latest assumptions:

- *Mercer's capital market assumptions as at 31 March 2023*
- *Ortec's climate scenarios as at 31 December 2022*

Overview of Climate Scenarios Modelled

	Failed Transition	Rapid Transition	Orderly Transition
Summary	The world fails to meet the Paris Agreement goals and global warming reaches 4.3°C above pre-industrial levels by 2100. Physical climate impacts cause large reductions in economic productivity and increasing impacts from extreme weather events.	Sudden divestments in 2025 to align portfolios to the Paris Agreement goals have disruptive effects on financial markets with sudden repricing followed by stranded assets and a sentiment shock.	Political and social organizations act quickly and predictably to implement the recommendations of the Paris Agreement to limit global warming to below 2°C.
Temperature change	Expected increase of 4.3°C, with a high-likelihood range of an increase between 3.4°C and 5.6°C by 2100.	Average temperature increase stabilises at 1.5°C around 2050.	This scenario includes additional economic damage consistent with 1.8°C of average temperature rise – peaking in 2070.
Cumulative emissions	c5,000 GtCO ₂ (2020-2100)	c400 GtCO ₂ (2020-2100)	The additional damage under this scenario could be associated with further human emissions or greater impacts from feedback loops and tipping points.
Key policy & tech assumptions	Existing policy regimes are continued with the same level of ambition.	An ambitious policy regime is pursued to encourage greater decarbonization of the electricity sector and to reduce emissions across all sectors of the economy. Higher carbon prices, larger investment in energy efficiency and faster phase out of coal-fired power generation. This is earlier and more effective under a Rapid Transition than the Orderly Transition, which allows for less investment in energy efficiency and bioenergy with carbon capture and storage.	
Financial climate modelling	Physical risks are priced in two different periods: 2026-2030 (risks of first 40 years) and 2036-2040 (risks of 40-80 years).	Pricing in of transition and physical risks of the coming 40 years occurs within one year in 2025. As a result of this aggressive market correction, a confidence shock to the financial system takes place in the same year.	Pricing in of transition and physical risks associated with 1.5°C up to 2050 takes place over the first 4 years. The additional damage, beyond 1.5°C, impacts asset performance on a year-by-year basis with no advance pricing in.
Physical risks considered	Physical risks are regionally differentiated, consider variation in expected temperature increase per region and increase dramatically with rising average global temperature. Physical risks are built up from: • Gradual physical impacts associated with rising temperature (agricultural, labour, and industrial productivity losses) • Economic impacts from climate-related extreme weather events Current modelling does not capture environmental tipping points or knock-on effects (e.g., migration and conflict).		

Climate Scenario Impacts on Expected Return Assumptions

	Failed Transition			Rapid Transition			Orderly Transition		
Asset Class	31/12/2022								
	4 Years	13 Years	28 Years	4 Years	13 Years	28 Years	4 Years	13 Years	28 Years
MSCI Paris Aligned Equity	1.8%	-5.6%	-31.6%	-6.0%	-4.1%	-0.7%	-2.8%	-2.3%	-3.3%
UK Investment Grade Credit	0.2%	0.4%	-0.1%	-2.2%	-2.8%	-2.0%	-0.3%	0.1%	0.7%
US Investment Grade Credit	-0.1%	0.5%	-0.2%	-1.2%	-2.9%	-2.1%	-0.2%	0.2%	0.6%
Global Senior Private Debt	-0.1%	-0.7%	-1.5%	-2.1%	-1.8%	-1.9%	0.2%	1.2%	0.1%
World Private Infrastructure	2.9%	-5.4%	-28.3%	-4.2%	0.5%	4.0%	-3.9%	-0.7%	-0.2%
Cash	0.1%	-1.9%	-3.2%	-0.2%	1.9%	2.6%	0.0%	2.0%	1.9%
Private Equity	5.3%	-6.5%	-48.5%	-10.5%	-8.0%	-2.5%	-7.4%	-7.7%	-10.1%

Capital Market Assumptions

	CMA's		
Asset Class	Expected Return as at 31/12/2022		
	4 Years p.a.	13 Years p.a.	28 Years p.a.
MSCI Paris Aligned Equity	8.8%	9.0%	9.3%
UK Investment Grade Credit	5.5%	5.7%	5.9%
US Investment Grade Credit	5.1%	5.1%	5.3%
Global Senior Private Debt	7.9%	8.3%	8.3%
World Private Infrastructure	7.9%	8.2%	8.2%
Cash	4.2%	4.3%	4.7%
Private Equity	11.2%	11.3%	11.7%

Treatment of liabilities

Liability projections **allow for interest rate and inflation expectation impacts** across the scenarios. To the extent interest rate and inflation exposures are unhedged, this will feed through to funding level projections.

Changes to interest rates and inflation expectations at a constant liability duration of 20 years are set out below:

Assumption	Failed Transition			Rapid Transition			Orderly Transition		
	31/12/2022								
	Year 4	Year 13	Year 28	Year 4	Year 13	Year 28	Year 4	Year 13	Year 28
UK Interest Rates	-0.04%	-0.09%	-0.09%	0.00%	0.10%	-0.01%	0.06%	0.09%	-0.11%
UK Inflation Expectations	-0.04%	-0.03%	-0.03%	0.02%	0.05%	-0.01%	0.05%	0.04%	-0.05%

Assumptions underlying the liability calibration such as financial (e.g. RPI/CPI wedge) and demographic assumptions (e.g. lack of transfers and long term improvements in mortality) are expected to play out as expected.

Modeling limitations

Climate scenario modelling is a complex process, with associated modelling limitations. In particular:

- The further into the future the projection extends, the less reliable any quantitative modelling may be.
- There is a reasonable likelihood that physical impacts are significantly underestimated. Feedback loops or ‘tipping points’, like permafrost melting, are challenging to model particularly around the timing of such an event and the speed at which it could accelerate.
- Financial stability and insurance ‘breakdown’ is not modelled. A systemic failure may be caused by either an ‘uninsurable’ 4°C physical environment, or due to the scale of mitigation and adaptation required to avoid material warming of the planet.

- Most adaptation costs and social factors are not priced into the models. These include population health and climate-related migration.

Appendix 4: Key metrics for climate change related risks

Total carbon emissions

This metric measures the total absolute carbon emissions attributable to a portfolio. This metric represents the underlying investee company's or issuer's reported or estimated greenhouse gas emissions, where available.

There are seven recognised greenhouse gases, as defined by the GHG Protocol. In order to simplify reporting, each greenhouse gas is calibrated relative to carbon dioxide and is reported as 'carbon dioxide equivalent' emissions (CO₂e).

To determine total exposure for this metric: The share of a given company that the Fund holds (the weight) is multiplied by the company's emissions (by Scope), effectively measuring the Fund's share of the company's emissions.

Carbon Footprint

This metric measures the carbon emissions (in Metric tons) divided by size of investment made (per \$invested). It seeks to answer how carbon intensive the portfolio is. This means that for the Fund, for example, a company with a very high carbon intensity but a low Fund weighting might contribute to the carbon footprint measure to a lesser extent than a company with a lower carbon intensity but a higher weighting in the Fund.

Weighted Average Carbon Intensity (WACI)

This is also an emissions related metric that measures the carbon emissions (in Metric tons) divided by revenue (per \$million of revenue). This involves multiplying percentage holding or exposure to a company by the carbon intensity (the company's total emissions per \$million revenue).

The Trustee has selected to report the WACI as an alternative emissions metric to the carbon footprint metric. The Trustee has also selected this metric as the primary metric to monitor the short-term decarbonisation target set for the buy and maintain credit portfolio (see the 'Target' section for further details).

Implied temperature rise (ITR)

A forward-looking assessment of how aligned the Fund's portfolios are relative to the Paris Agreement's 1.5°C target. This is estimated based on the activities and decarbonisation targets of portfolio companies / issuers, relative to what global decarbonisation needs to be to achieve 1.5°C.

The Trustee has chosen this metric to include in this report because of its simplicity in presentation and a useful way to see, at a glance, the positioning of a fund towards a low carbon economy. High Implied Temperature Rise metrics at the Fund level would imply it is invested in companies or issuers that are not transforming their businesses or activities quickly enough in order to reduce their reliance on fossil

fuels. This is also a measure of climate transition risk with greater transition risk highlighted in funds with a higher Implied Temperature Rises.

The Trustee notes that there are currently multiple methodologies used by its investment managers for computing this metric and these can have variable results. The Trustee will work with its investment managers to improve the scope and consistency of the implied temperature rise metric.

Data Quality

This is an alternative non-emissions metric that aims to represent the proportions of the portfolio for which the Trustee has verified, reported, estimated or unavailable carbon emissions data.

The Trustee has chosen this metric to include in this report as it quantifies the overall quality of the carbon data available and helps identify mandates the Trustee should work further on with its investment managers to increase the quality of data reported.

Appendix 5: Benchmarks / Comparators

Manager	Asset class	Benchmark (or comparator)
LGIM	Synthetic equity	MSCI All World Equity Index (GBP)
LGIM		Bloomberg Corporates 1% Issuer Capped
RLAM	Buy & maintain credit	50% iBoxx Sterling Non-Gilts All Maturities Index, 50% iBoxx Sterling Non-Gilts Over 15 Years Index.
Insight		Bloomberg Barclays Global Aggregate – Corporate Index
Insight	Secured Finance	N/A
M&G		N/A

Appendix 6: Data coverage and quality

Manager	Asset class	Data coverage	Data quality (in relation to WACI)			
			Reported	Estimated	Reported or estimated	Missing
LGIM	Syn. equity	99.7%	N/A	N/A	N/A	N/A
LGIM	B&M credit	49.0%	N/A	N/A	N/A	N/A
RLAM	B&M credit	86.8%	66.2%	20.6%	86.8%	13.2%
Insight	B&M credit	87.0%	68.0%	20.0%	87.0%	13.0%
Insight	Secured finance	N/A	N/A	N/A	N/A	N/A
M&G	Secured finance	26.8%	9.9%	16.9%	26.8%	73.2%
LGIM	LDI (gilts only)	100%	N/A	N/A	N/A	N/A

Only RLAM, Insight and M&G have been able to report data quality. LGIM have advised that they are unable to provide data quality metrics as at 31 December 2022.

The Fund's private equity and infrastructure mandates have not reported emissions data as at 31 December 2022 for various reasons and have therefore been excluded. Insight could not provide data in respect of their secured finance mandate.

Data coverage for the M&G secured finance mandate is currently low and may impact the reliability of the results quoted.

Appendix 7: Climate Change Glossary

Carbon footprint: The amount of carbon dioxide (or other greenhouse gasses) released into the atmosphere as a result of the activities of a particular individual, organization or community. Carbon footprint is calculated for each company as (Scope 1 and 2 carbon emissions / \$m investments). See also Scope 1, 2, 3 emissions and Weighted Average Carbon Intensity (WACI).

Carbon intensity: The amount of emissions of carbon dioxide (or other greenhouse gasses) released per unit of another variable such as revenue, gross domestic product (GDP), per \$1million invested etc. See also Weighted Average Carbon Intensity (WACI).

Carbon price: The price for avoided or released carbon dioxide (CO₂) or CO₂-equivalent emissions. This may refer to the rate of a carbon tax, or the price of emission permits. In many models that are used to assess the economic costs of mitigation, carbon prices are used as a proxy to represent the level of effort in mitigation policies.

Carbon neutrality: Achieved by offsetting emissions by paying for credits (usually certified via new forestry equivalents that provide carbon removal). Carbon neutrality is similar to net zero targeting – the latter requires actual emissions reductions to meet targets though (rather than purchasing offsets). See also Net Zero CO₂ emissions.

Decarbonisation: The process by which countries, individuals or other entities aim to achieve zero fossil carbon existence. Typically refers to a reduction of the carbon emissions associated with electricity, industry and transport.

Global warming: The estimated increase in global mean surface temperature expressed relative to pre-industrial levels unless otherwise specified. See also Pre-industrial.

Greenhouse gases: Gases in the planet's atmosphere which trap heat. They let sunlight pass through the atmosphere but prevent heat from leaving the atmosphere. Greenhouse gases include: Carbon Dioxide (CO₂), Methane (CH₄), Nitrous Oxide (N₂O), Hydrofluorocarbons (HFCs), Perfluorocarbons (PFCs), Sulphur Hexafluoride (SF₆), Nitrogen Trifluoride (NF₃).

Inevitable policy response: A scenario that expects an acceleration of climate-related policy announcements in 2023–2025, which has been supported by the Principles for Responsible Investment (PRI).

Mitigation (of climate change): A human intervention to reduce emissions or enhance the sinks of greenhouse gases.

Mitigation strategies: In climate policy, mitigation strategies are technologies, processes or practices that contribute to mitigation, for example, renewable energy (RE) technologies, waste minimization processes and public transport commuting practices.

Net zero CO2 emissions: Net zero carbon dioxide (CO2) emissions are achieved when CO2 emissions are balanced globally by CO2 removals over a specified period. The term “net zero” is also typically associated with the 2050 date or earlier, as this is aligned with the scientific recommendations to achieve a 1.5°C scenario. See also Carbon neutrality (which differs slightly).

Paris Agreement: The Paris Agreement under the United Nations Framework Convention on Climate Change (UNFCCC) was adopted on December 2015 in Paris, at the 21st session of the Conference of the Parties (COP) to the UNFCCC. The agreement, adopted by 196 Parties to the UNFCCC, entered into force on 4 November 2016 and as of May 2018 had 195 Signatories and was ratified by 177 Parties. One of the goals of the Paris Agreement is “Holding the increase in the global average temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C above pre-industrial levels”, recognising that this would significantly reduce the risks and impacts of climate change. Additionally, the Agreement aims to strengthen the ability of countries to deal with the impacts of climate change.

Physical risks: Dangers or perils related to the physical or natural environment that pose a threat to physical assets e.g. buildings, equipment and people. Mercer’s scenario analysis grouped these into the impact of natural catastrophes (for instance sea level rise, flooding, wildfires, and hurricanes) and resource availability (particularly water). See also Transition risks.

Pre-industrial: The multi-century period prior to the onset of large-scale industrial activity around 1750. The reference period 1850–1900 is used to approximate pre-industrial global mean surface temperature.

Principles for Responsible Investment (PRI): Non-profit organisation which encourages investors to use responsible investment to enhance returns and better manage risks. It engages with global policymakers and is supported by, not but part of, the United Nations. It has six Principles for Responsible Investment that offer a menu of possible actions for incorporating ESG issues into investment practice.

Resilience: The capacity of social, economic and environmental systems to cope with a hazardous event or trend or disturbance, responding or reorganising in ways that maintain their essential function, identity and structure while also maintaining the capacity for adaptation, learning and transformation.

Scope 1, 2, 3 emissions: Scope 1 emissions are direct emissions from owned or controlled sources. Scope 2 emissions are indirect emissions from the generation of purchased energy. Scope 3 emissions

are all indirect emissions (not included in scope 2) that occur in the value chain of the reporting company, including both upstream and downstream emissions.

Stranded assets: Assets exposed to devaluations or conversion to “liabilities” because of unanticipated changes in their initially expected revenues due to innovations and/or evolutions of the business context, including changes in public regulations at the domestic and international levels.

Transition risks: Risks from policy changes, reputational impacts and shifts in market preferences, norms and technology as the economy moves to a low carbon approach. See also Physical risks.

Weighted average carbon intensity (WACI): The carbon intensity of a portfolio, weighted by the proportion of each constituent in the portfolio. Carbon intensity is calculated for each company as (Scope 1 and 2 carbon emissions / \$m revenue). See also Carbon footprint.

Appendix 3 – Annual engagement policy implementation statement

Annual Engagement Policy Implementation Statement

Rolls-Royce UK Pension Fund ('the Fund')

Introduction

This statement sets out how, and the extent to which, the Engagement Policy in the Statement of Investment Principles ('SIP') produced by the Trustee, has been followed during the year to 31 March 2023. This statement has been produced in accordance with the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013, as amended, and the guidance published by the Pensions Regulator.

Investment Objectives of the Fund

The Trustee believes that it is important to consider the policies in place in the context of the investment objectives it has set. The Trustee's overriding objective is to meet the Fund's liabilities as and when they fall due. In pursuit of this objective, the Trustee seeks to invest the Fund's assets at an appropriate level of risk relative to the Fund's liabilities. The objectives of the Fund are included in Section 3 of the SIP.

Policy on ESG, Stewardship and Climate Change

Section 10 of the SIP (dated July 2022) sets out the Trustee's policy on Environmental, Social and Governance ("ESG") factors, stewardship and climate change. This policy sets out the Trustee's beliefs on ESG and climate change and the processes followed by the Trustee in relation to voting rights and stewardship.

The following sections set out how the Trustee's engagement and voting policies were followed and implemented during the year. The LDI mandate has been excluded as voting and engagement activity is less relevant as the mandate is largely invested in UK government bonds and derivatives. The residual private equity and infrastructure mandates have also been excluded as the allocation to these mandates is small (less than 1% of Fund assets) and they are now in the run-off stage.

Voting

The Trustee has delegated its voting rights to the investment managers. The SIP states "The Trustee has given the appointed investment managers, both segregated and pooled, full discretion when undertaking engagement activities in accordance with their own corporate governance policies and current best practice". It is the Trustee's view that the policy has been followed during the Fund year.

The majority of voting activity will generally arise in public equity funds. The Fund was not invested in physical public equities over the year ending 31 March 2023 and the majority of the Fund's assets were invested in bonds for which investment managers do not usually have voting rights. All managers have confirmed that there were no voting opportunities for the Fund in the reporting period and no votes have been cast.

Over the prior 12 months, the Trustee has not actively challenged the managers on their voting activity and the Trustee does not use the direct services of a proxy voter.

Significant votes

The Department of Work and Pensions released a set of Implementation Statement requirements on 17 June 2022 which are to be adopted in all statements for schemes with years ending on or after 1 October 2022. The requirements are set out in the “Reporting on Stewardship and Other Topics through the Statement of Investment Principles and the Implementation Statement: Statutory and Non-Statutory Guidance” report.

The most material change is that the Statutory Guidance provides an update on what constitutes a “significant vote”. As all of the Fund’s investment managers confirmed that there were no voting opportunities over the year, the Trustee has not reported on any significant votes or stewardship themes in this statement. The Trustee is looking to review their key stewardship themes and will report on these next year.

Engagement

The Trustee requested that the investment managers confirm compliance with the principles of the UK Stewardship Code. All managers, with the exception of private equity and infrastructure, have confirmed that they are signatories of the current UK Stewardship Code (2020 version) and are signatories of the UN Principles for Responsible Investment.

As part of its quarterly review of investment performance, the Trustee receives reporting from its investment consultant including ratings (both general and specific ESG) for its investment managers. In addition, the Trustee receives an annual report on the responsible investment activities of its managers, which includes a comparison of manager ESG ratings against their peer group and a review of each manager’s engagement activities. On average, the Fund’s investment managers had better ESG ratings (as determined by the investment consultant) than the average of their respective peer groups.

The Trustee expects its fund managers to engage regularly with the companies in which they invest on the Fund’s behalf. Whilst this is more commonplace amongst equity mandates where the investor has voting rights (i.e. investments in physical shares, not derivatives-based equity exposure such as the Fund has), there are still elements of engagement practices which can be incorporated by fixed income managers. A summary of the Trustee’s review of the managers’ engagement activity is set out below.

The SIP states that the Trustee may under certain circumstances engage directly with investee companies; the Trustee did not do so over the year.

The SIP states that the Trustee does not currently take into account “non-financial factors” when considering the selection, retention and realisation of assets and it did not do so over the year.

Legal and General Investment Management (LGIM) – Buy and maintain credit mandate

The firm has developed a proprietary ESG rating approach for the buy and maintain credit mandate. This is made publicly available to companies along with the methodology, with a clear method of linking these ratings to the engagement agenda and voting policies.

Engagement example: Living wage

LGIM is a member of two collaborative engagement groups: ShareAction’s Good Work Coalition and the Platform for Living Wage Financials. The Good Work Coalition aims to encourage UK companies to pay their employees a real living wage and to become accredited living wage employers. LGIM have been working with

this coalition since 2015. They joined the Platform for Living Wage Financials (PLWF) in 2022, to encourage, support, assess and monitor investee companies on their commitment to enable living wages and incomes for workers in their supply chains.

LGIM carried out the assessment, scoring and led engagement with three large companies from the retail sector (engaging overall with 23 companies on the living wage during 2022, of which 12 were collaborative engagements). One of these three companies, a significant employer in the UK, has raised rates twice in 2022 for inner/outer London based employees, therefore LGIM decided at this time not to escalate the issue by filing a shareholder resolution, but will continue to engage with the company and with their peers on the living wage as the cost of living crisis and economic backdrop continues to evolve. LGIM will vote against the annual report of those companies that fail to disclose their living wage strategy by 2025.

Although LGIM ask all companies to adopt a strategy to ensure workers internally and in their supply chain are paid a living wage (or the real living wage in the UK), their voting sanctions will initially be applied to the largest companies in the UK, Europe and the US.

Royal London Asset Management (RLAM) – Buy and maintain credit mandate

In 2022 RLAM engaged with 52 investee companies on 108 separate occasions in respect of assets held in the Fund's portfolio. The engagement activity covered a wide range of themes including: climate transition risk, labour and human rights, cybersecurity and corporate governance.

Engagement example: Housing associations

During 2022, RLAM sent emails to several housing associations to better understand the governance structure and processes that issuers have in place around damp and mould, in reaction to a request by the Regulator of Social Housing.

As long-term investors, RLAM want to encourage greater explanation of exposure to this issue and assurance of approaches to mitigate this risk. They are awaiting responses from the housing associations. Once received, they will be assessing what best practice looks like and will be engaging for further information if the disclosures are not adequate.

Insight Investment – Buy and maintain credit and secured finance mandates

Insight engage with companies on broad topics, using their Quarterly Risk Review for idea generation. This is typically done when the team believes the outcome could have a potential impact on the method by which they analyse issuers.

Insight's credit analysts and ESG specialists frequently engage with senior management representatives of issuing companies globally with the objective of shaping the nature of bond issuance and improving investment outcomes. On such occasions they aim to discuss their existing and future funding needs, corporate strategy and performance, as well as any ESG-specific issues. This includes a meaningful focus on environmental issues including climate change.

Engagement example: Energy services

Insight engaged with a company which is a provider of midstream energy services to producers and consumers of natural gas, natural gas liquids (NGLs), crude oil, petrochemicals and refined products in North America. The company's material issues include carbon emissions, occupational health and safety, community relations, opportunities in clean technology and biodiversity and land use.

As part of Insight's Climate Action engagement program, they engaged with the company with the intention to monitor the company's progress as the energy sector is at high risk from climate change, and the company does not have a robust climate transition plan or carbon emissions reduction targets. Governance may also be contributing to the company's relatively weak climate action plan since it has a controlling shareholder and limited transparency on executive compensation incentives.

During their discussion, Insight advocated for the company to establish a robust climate transition plan with quantitative carbon emissions targets and shared examples from peers who have done so. Insight suggested that adding timebound targets would help to illustrate the company's emissions trajectory and allows investors to integrate them into portfolios. Developing a target focused on scope 1 and 2 emissions where the company has the most direct influence and purchasing power would align with many of the company's peers.

Insight intend to monitor the company's progress on climate action and pay disclosures due to limited transparency. They are optimistic that the company will take action to improve their climate-related disclosures, plans and targets.

M&G – Secured finance mandate

M&G incorporate ESG issues into their investment decisions wherever they have a meaningful impact on risk or return. They apply this approach to ESG analysis across all sectors in which they invest and ESG factors are therefore incorporated into M&G ratings to which they assign all debt assets.

M&G has developed a proactive approach to engagement across a wide variety of asset classes, with engagement within fixed income typically led by the credit analyst teams with the support of the Stewardship and Sustainability team. The degree to which engagement is conducted in relation to the secured finance holdings will depend on each individual circumstance.

Across the private debt business at M&G, they have developed ESG scorecards to align with their public corporate exposures and to provide portfolio managers with mapping of ESG issues across their portfolios.

Engagement example: Diversity, Equity & Inclusion policies (leveraged loan issuer)

M&G met with the Head of Sustainability and Investor Relations at the company involved to make their expectations known relating to diversity and inclusion and related reporting. The company informed M&G that they are planning to expand their Diversity, Equity and Inclusion ("DEI") efforts into disability, ethnicity and sexual orientation but are facing challenges due to GDPR limitations and variation in regulations across markets. The company does not currently produce a gender pay gap report in the UK due to lack of data but are looking to report on this from 2023 onwards. By the end of 2022 the company plans to conduct a taxonomy review of all suppliers and create risk metrics. For 2023, the company will go one level deeper and establish a specific plan for different categories of suppliers, which includes both social and environmental aspects.

The company runs an Early Women in Leadership Programme and M&G voiced that it would be useful to see the successes of these programmes publicly disclosed. The company noted and said that they will endeavour to do so in their upcoming reports. Overall, M&G are happy that the direction of travel for the company is positive, but they will continue to monitor the situation to ensure that disclosure is improved and their asks are implemented. They await the company's 2024 report.