ESG Annual Review

Report on the activities of Standard Life Investments for 12 months to 31 December 2017
ESG Annual Review 2017

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About Aberdeen Standard Investments

Aberdeen Standard Investments is a leading global asset manager dedicated to creating long-term value for clients.

To achieve this, we offer a comprehensive range of investment capabilities, as well as the highest levels of service.

Overall, Aberdeen Standard Investments manages £575.7 billion* on behalf of clients in 80 countries. In managing these assets, we employ over 1,000 investment professionals and provide client support from 50 client relationship offices globally.

The Aberdeen Standard Investments brand was created in connection with the merger of Aberdeen Asset Management PLC and Standard Life Plc on 14 August 2017 to form Standard Life Aberdeen plc.

*As at 31 December 2017 Source: Standard Life Aberdeen plc

Unless otherwise indicated, this document refers only to the activities, views and engagements of Standard Life Investments.

Aberdeen Standard Investments is a brand of the investment businesses of Aberdeen Asset Management and Standard Life Investments.
Foreword

This will be the last Governance and Stewardship Annual Review from Standard Life Investments. On August 14, 2017 our parent company, Standard Life plc, merged with Aberdeen Asset Management PLC to create Standard Life Aberdeen plc. The investment arm operates under the name Aberdeen Standard Investments, a brand of the investment businesses of Aberdeen Asset Management and Standard Life Investments.

From January 2018, we have been combining many of our activities including voting at company general meetings and the associated reporting.

Governance and stewardship continues to rise up our clients’ agenda. This dictates the energy and resource that we apply to the governance debates that we have with the companies in which we invest our clients’ capital.

In the UK, 2017 saw the majority of large companies submit their triennial remuneration plans to a mandatory vote and we noticed a subtle but substantial change of tone. The dissent from stakeholders to excessive pay in previous years finally seems to be having an impact, with a number of plans being moderated or withdrawn for further consideration. While this change is not universal, we welcome it and encourage companies to carefully consider their place in society and the obligations that this confers.

We continue to expand the number of engagements that we have with non-UK companies. Our new colleagues at Aberdeen have a substantial overseas investment presence and I expect next year’s review to have an even more international flavour. This brings ever greater opportunity to use our experiences around the globe to encourage higher standards everywhere that we invest our clients’ capital.

In 2016, we brought Standard Life Investments’ Governance and Stewardship team together with the Responsible Investment team to try to enhance our effectiveness across a range of issues. Notably, we are now able to challenge climate-change strategy, workforce development strategy and social issues in our board level meetings, as well as examine board leadership and effectiveness with different management layers of investee companies.

The launch of the Global Equity Impact Fund represents a significant milestone for the ESG Investing team at Standard Life Investments. This fund brings ESG considerations to the heart of the stock-selection process as we search for companies whose growth and profits are directed towards the UN Sustainable Development Goals. More details on this can be found in this review. More recently, we launched the UK Equity Impact – Employment Opportunities Fund. As the name suggests, it is focused on the positive social impact of jobs in the UK. More information can be found later in the document.

Last year was the ‘Silver Anniversary’ of the corporate governance team at Standard Life Investments. It was launched in the wake of the Cadbury Report on Financial Aspects of Corporate Governance. This report became an international benchmark used to set governance codes around the world. A review of the UK Governance Code was launched this year and it is fitting that the principles established in 1992 remain relevant to the structural considerations of how companies organise themselves and behave. We look forward to the next 25 years of building constructive relationships with companies in order to generate value for our clients.
Our approach to ESG

Investing for a better future
Integrating environmental, social and governance (ESG) aspects into our investment process is a core part of the Standard Life Investments’ process. Our foundations come from having corporate governance and stewardship at the heart of our investment philosophy for 25 years. We firmly believe that companies that demonstrate a commitment to sustainable business practices will enjoy a competitive advantage and provide long-term sustainable returns.

The companies in which we invest do not operate in isolation. A company’s behaviour, its operations, how it treats its employees and what products and services it produces all have a bearing on the environment and society around it. Irresponsible behaviour may lead to irreparable damage to a company’s reputation and the value it creates for its shareholders. Understanding how companies are governed and manage their impact on the environment and society is key to our investment process.

Our team
Standard Life Investments has one of the best resourced ESG investment teams in the industry. Our team of 14 analysts, managers and directors work alongside our investment teams, bringing expertise and independent oversight to the investments we make on behalf of our clients. The ESG Investment team is headed up by Euan Stirling. Euan is a long-time equity fund manager who, in 2016, undertook the role to head the team and enhance the integration of ESG matters across the investment process. Under his leadership, the responsible investment function and the governance and stewardship function were brought together to form a stronger and more integrated ESG Investment team. The wider team has analysts that cover environmental and social matters, as well as governance experts who undertake the analysis and voting at company annual general meetings (AGMs). In addition, high-level engagement is conducted with the board and senior executives over how our investee companies operate, structure and govern themselves.

Materiality-driven approach
The ESG Investment team conducts materiality-driven analysis of ESG issues that have the potential to affect financial performance. This analysis feeds into the investment process through regular research publications and desk meetings with the investment teams to highlight the key issues for consideration. It also drives an active engagement process, whereby we meet with executives and non-executives of our investee companies. The outcomes of discussions feed into our own fundamental analysis.

Our voice as an active shareholder encourages best practice and strong corporate behaviour from the companies in which we invest. This active approach is taken in the belief that driving better corporate behaviour will provide better returns over the longer term. These engagements also feed into our voting process, where we exercise our clients’ rights as shareholders and formally hold the boards of companies to account.

Our ESG investment professionals use our Focus on Change investment philosophy to understand how changes affect sectors and individual companies. The responsible investment function uses the four pillars of the UN Global Compact to define its work: environment, human rights & community, business ethics and employment. We analyse issues and themes on a global scale, as well as focusing on how these issues may change regionally. We are signatories to the UK Stewardship Code and the PRI and comply with their principles.
We work with our asset class teams to understand how different ESG matters affect their underlying holdings. The degree of the risks and opportunities each asset class face will vary and it is essential to work closely with the asset class investors to incorporate this at a portfolio level. For instance, our real estate team has a dedicated sustainable real estate investment policy and a member of the responsible investment function sits on the Real Estate Sustainability Focus Group. This helps the integration of ESG matters within real estate investment.

**Values-based investment styles**

Our research, analysis and engagement provides us with in-depth knowledge of ESG matters. We are able to apply this knowledge to a range of values-based investment styles, including ethical funds, sustainable & responsible investment styles (SRI) or impact investing options. We have managed values-based investment funds for over 20 years and have a strong capability to build and tailor solutions to meet the ever-growing demand from our customers. This allows our clients to align their beliefs and values with their investment portfolios.

**Transparency**

Finally, we regularly report on the ESG Investment team’s activities. As well as publishing annual reviews, we produce quarterly reports, white papers and disclose our voting activity on our website.
The year in review

Voting at the general meetings of our investee companies is a key element of our stewardship activities and provides the opportunity to hold boards to account for their actions.

Voting on the remuneration of executives has undoubtedly drawn the most attention in recent years and 2017 was no different. There is strong public opinion and political pressure on this subject in the UK, with an emphasis on curbing excessive rewards. As shareholders, we have the ability to represent our clients and influence remuneration committees when engaging on executive pay.

There were a small number of companies that failed to manage the consultation process, resulting in large votes against resolutions or the withdrawal of resolutions that were unlikely to receive support.

The largest UK companies have dedicated resource to engage with shareholders which has, in the main, resulted in supportive votes. However, votes against resolutions at the AGMs of FTSE 350 companies increased, demonstrating the growing willingness of shareholders to apply high standards to smaller companies.

In addition, following amendments to the Investment Association guidance, there was an increase in votes against individual directors.

In Europe, an annual binding vote on pay was introduced in France. We therefore engaged with a number of large French companies in advance of their AGMs, as they sought to ensure shareholder support.

Over the year, we saw the continued application of the SDGs (sustainable development goals) among companies, regulators, civil society groups and investors. Impetus behind the 17 goals, which seek to address targets ranging from education to clean energy by 2030, continues to gather pace. Standard Life Investments was at the forefront of these developments and during the fourth quarter of 2017 we launched our Global Equity Impact Fund (more details can be found later in this report).

Countries around the globe continued to tackle climate change as part of the COP21 Paris agreement. The decision of the US administration to exit the agreement led some commentators to speculate that other participants may withdraw. However, countries with heavy fossil-fuel reliance, such as India and China, along with individual US states reaffirmed their commitment to the agreement. The Financial Stability Board (FSB) established the Taskforce on Climate-related Financial Disclosure (TCFD) in 2016 to encourage and develop consistent disclosures from companies on the financial implications of climate change. It sets out what constitutes effective financial disclosure from companies in all sectors. During 2017, we submitted our views to various consultations produced by the TCFD and used its guidance to further develop our understanding of the climate change risk within our portfolios and our investee companies.
Impact investing

Developing our proposition

Impact investing involves making investments that seek to deliver a positive social and environmental outcome, alongside a financial return. This involves harnessing the power of the capital markets to direct investment into listed entities that are financially attractive, as well as having the ability to deliver intentional measurable positive environmental or social impacts.

The United Nations set an agenda for sustainable development at the start of 2016 by establishing the Sustainable Development Goals (SDGs). Through these goals, governments, companies and civil society will aim to address some of the world’s biggest environmental and social challenges, such as poverty, climate change and unsustainable production and consumption.

In order to achieve these goals, significant amounts of mainstream capital will have to be invested in solutions to the world’s problems. The estimated cost of achieving the goals ranges from $2 trillion to $7 trillion a year. This can only be done through partnerships between governments, regulators, academia, philanthropists and the corporate world.

Over the past two years, Standard Life Investments has spent time developing its approach to impact investment. We have used the SDGs as the foundation for our Global Equity Impact Fund. Selecting a company for impact must first incorporate analysis of the company’s fundamentals in order to identify attractive investment opportunities. We then assess these companies on their ability to deliver against our impact investment framework.

We have identified three stages of impact maturity, which allows us to invest in a company at the early stages of developing business strategies that lead to a positive environmental and social contribution. The first stage is intentionality, where a clear strategy is set by the company’s board to pursue business opportunities that lead to measurable and positive social and environmental outcomes. The second is where the company demonstrates how it is implementing this strategy and the third is where we are able to measure the outcomes of this strategy. With the SDGs, we use the indicators for each goal to report on the outputs, and then attempt to quantify the outcomes of the company’s activities, i.e. its impact.

We have identified eight pillars of impact under which a company’s activities can be framed to meet the SDGs. We align the 15 investable SDGs with one or two of these pillars. The final two goals, focused on promoting peaceful societies and for partnerships, are not captured. These pillars allow us to identify companies that have impact through criteria such as their turnover of dedicated products, the number of lives reached and the amount of research and development funded.

Standard Life Investments ran a model portfolio for a year before launching its Global Equity Impact Fund in October 2017. The Fund is available in the UK, and EU as a Luxembourg-registered SICAV. More information about our strategy and the Fund can be found on our dedicated landing page: https://uk.standardlifeinvestments.com/ifa/funds/focus_on_funds/impact_fund.html

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<td>Education &amp; Employment</td>
<td>Access to education and skills development Quality employment and job creation</td>
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Graphic 1: Impact pillars
Reporting the outcomes of the investee companies’ activities will be essential to demonstrate impact. We published our first impact report on the model portfolio to demonstrate how we intend to report on this Fund going forward (visit our landing page for more details). This is the first impact product that we have launched. On 1 February 2018, we launched the UK Equity Impact – Employment Opportunities Fund under the Aberdeen Standard Investments brand. The Fund was developed in partnership with UK charity Big Issue Invest (a subsidiary of the Big Issue Group). Big Issue Invest receives a 20% share of revenue from the Fund’s management fee in recognition of its role in conceiving the Fund, and its significant contribution to the Fund’s advisory group. Income generated for Big Issue Invest will support the organisation in its mission to dismantle poverty and create opportunity for people and communities across the UK.

Creating a culture of social impact investing

In late 2016, the UK government set up an independent advisory group to investigate how savings, pensions and investments providers engage with individuals to enable them to support the things they care about through their savings and investment choices. The advisory group comprised senior industry representatives from across the savings and investment sectors, including Standard Life Aberdeen’s co-CEO Keith Skeoch. Its aim was to explore the barriers to the development, demand and distribution of products with social impact components and provide recommendations on helping to reduce or remove these barriers.

Standard Life Investments’ Head of Responsible Investment and the Head of Fund Governance were asked to be part of the steering group. Both were actively involved in various working groups. Aberdeen Asset Management’s Head of Distribution was also a member of the steering group.

In November 2017, the findings of the advisory group were published in its report “Growing a culture of social impact investing in the UK”. It highlighted that there is a strong and growing interest among individuals to see their savings and investments do social good, as well as produce a financial return. The report highlighted that the financial industry needs to be able to address this growing demand. It looked at the lack of investable propositions and suggested that some of the reasons for this included the issue that social impact investment opportunities can be difficult to identify and crystalise. Many impact projects are at early stages, implying material credit and liquidity risk. There is also a challenge in explaining social impact intentions to investors and a degree of inertia may be setting in. While demand appears strong for these products, the number of people actually investing in social products remains relatively limited.

Through its report, the group provided a set of practical recommendations that aim to help increase the choice of savings, investment and pension products that offer social impact. In addition, recommendations focus on broadening sources of funding for enterprises targeting social impact as well as financial return. The recommendations were grouped under five key areas of action.

1. Improve deal flow and the ability to invest at scale
2. Strengthen competence and confidence within the financial services industry
3. Develop better reporting of non-financial outcomes
4. Make it easier for people to invest
5. Maintain momentum and build cohesion across initiatives

These recommendations were lobbied to a number of different stakeholders, including government, regulators, the financial services industry, professional bodies, companies and financial advisers.

It is likely that a number of industry representatives involved in the production of this report will work on sustaining a focus on the actions needed to follow through on the recommendations.

“Impact investing involves making investments that seek to deliver a positive social and environmental outcome, alongside a financial return”
Thematic commentary

The 30% Club: engaging for better diversity on boards

The 30% Club is committed to achieving a minimum of 30% women on FTSE 350 boards and a minimum of 30% women at senior management level of FTSE 100 companies by the end of 2020. In addition, the target of one-third of FTSE 350 board positions to be held by women by 2020 is supported, as developed by the UK Government’s Women on Boards Report, the Davies Review and the continuing Hampton-Alexander Review.

We believe boards that genuinely embrace cognitive diversity, as manifested through appropriate gender representation and a broad spectrum of skills and experience, are more likely to achieve better outcomes for their investors. Intuitively, it makes sense that diverse groups will be able to draw on a wider set of experiences and broader thinking. This should lead to better decisions and, ultimately, superior financial performance over the longer term. A growing body of empirical evidence and research from different sources and geographies corroborates this intuitive argument. In that, more diverse boards and senior management teams are more effective than ‘identikit’ teams when it comes to decision-making and in reducing groupthink. Evidence also shows that firms with better gender balance at board and management levels outperform their peers on a variety of financial measures.

We believe a better gender balance is good for the economy and should be supported by public policy. However, this should not be through ‘hard’ legislation such as quotas, as we do not believe their impact filters down into companies and into organisational cultures to deliver long-term sustainable change.

The stakeholders who are in a position to really drive change are company chairs and CEOs, as well as regulators and public policymakers, such as the Financial Reporting Council (FRC), and investors.

At the time of writing, 65 FTSE 350 CEOs at 63 companies had made public commitments to the 30% Club’s aspirational targets of 30% female representation at senior management level by the end of 2020. In addition, there are 46 FTSE 350 Chair members who support the 30% Club’s targets for female board representation. Leadership and commitment from the top of organisations is paramount to long-term sustainable change and in the creation of corporate cultures that respect diversity in all its forms.

Shareholders have a major role to play in expecting their investee companies to seek out and hire the best people. This includes drawing on all of their individual strengths and experiences to produce the best possible outcomes. We recognise this responsibility. As such, we have been working with the 30% Club and its Investor Group to collaborate with other shareholders to leverage the power of investor stewardship to create long-term meritocracies in our investee companies.

The 30% Club Investor Group was established in 2011 and both Aberdeen Asset Management and Standard Life Investments are long standing members. Deborah Gilshan, who joined the ESG Investment team in May 2017, has been involved in the UK Investor Group since its inception, and is currently its co-chair. She also serves on the Steering Committee of the 30% Club. The Investor Group now has 32 members, across asset owners, asset managers and charity investors with a collective £10.9 trillion in assets under management. These investors are committed to using the leverage of their stewardship work and ownership stakes to engage with the boards and management teams of investee companies to promote the importance of diversity.

The purpose of the 30% Club Investor Group is:

• to co-ordinate the investment community’s approach to diversity, in particular to explain the investment case for more diverse boards and senior management teams
• to exercise our ownership rights, including voting and engagement, to effect change on company boards and within senior management teams
• to encourage all investors to engage on the issue of diversity with chairs of boards and senior management teams.

Members of the 30% Club Investor Group are responsible for the stewardship of the investments they make on behalf of their pension scheme members and clients. Part of that responsibility includes the assessment of the boards and senior management teams of their investee companies. While the 30% Club Investor Group focuses primarily on gender diversity, we have found that it provides a good segue into discussions about other forms of diversity and opens up the conversation with boards of companies about their nominations processes.

The 30% Club believes that appointments should always be made on merit, and that considerations on diversity can ensure that appointments are made precisely on that basis by widening the pool of talent available from which board and management appointments are made.

1 A collection of relevant research: McKinsey Women Matter: Ten Years of Insights on Gender Diversity, October 2017; MSCI Women On Boards: Global Trends in Gender Diversity on Corporate Boards, November 2015; Credit Suisse The CS Gender 3000: Women in Senior Management, September 2014; Credit Suisse Gender Diversity and Corporate Performance, August 2012; and Catalyst ‘The Bottom Line: Corporate Performance and Women’s Representation on Boards’, 2007. More research can be found on the website of the 30% Club: https://30percentclub.org/
Since 2012, the UK Corporate Governance Code has included provisions for companies to report on board diversity policy, with measurable objectives and progress towards meeting them. These Code expectations provide fertile ground for a discussion on board governance with investee companies.

Such discussions allow shareholders to better understand how the board is harnessing the power of diversity to ensure optimal board outcomes, both in terms of membership of the board and in the collective decisions that are made by them. In addition, and following on from the review by Lord Davies on women on boards of UK-listed companies, we support the brief of the Hampton-Alexander Review to focus on "improving female representation in leadership positions of British business, broadening the ambition to the entire FTSE 350 Index and raising the target to 33% of women on boards by 2020." We were encouraged by the focus on diversity in both the earlier inquiry into corporate governance from the Select Committee of the Department for Business, Energy and Industrial Strategy and in the UK Government’s Green paper on Corporate Governance. That focus on diversity is heightened further with the proposed changes to the UK Corporate Governance Code as to how the Code can further elevate the importance of diversity in investee companies and encourage companies to intensify their efforts. The introduction of annual gender pay gap reporting for UK companies\(^1\) provides opportunities for companies to explain, and investors to understand better, the drivers within organisations that are enabling or stalling progress on addressing the challenges of gender imbalances across the workforce.

The UK Investor Group published a “Statement of Intent” in October 2016, which signals the collective voice of the 30% Club Investor Group to companies and the wider marketplace. It also demonstrates the ways in which members can use their ownership rights and undertake stewardship to encourage progress on gender diversity.

The Statement of Intent includes supporting the following achievements by the end of 2020:

- 30% women on FTSE 350 boards
- 30% women at senior management level in FTSE 100 companies.

Commitments, as set out in the Statement of Intent, include:

- engagement with investee companies
- exercise of ownership rights
- recognising exemplars of best practice, as well as engaging with laggards.

The 30% Club launched the Statement of Intent at an event to open the market at the London Stock Exchange with CEOs of asset owners and asset managers, as well as regulators and other stakeholder bodies. This demonstrated the importance of the investor voice in the diversity debate. It held a further event at the London Stock Exchange on 2 February 2018 to mark the growth of the UK Investor Group and to further enforce the use of stewardship by shareholders to progress better diversity on boards and in senior executive management teams.

As with all of the initiatives of the 30% Club, this is a group of ‘men and women working together for real change’. Diversity is not a social issue, it is a financial issue and should be treated like any other business imperative, with targets that are regularly measured and reported. What gets measured gets managed, and what gets managed gets done. Our Investor Groups are growing in AUM globally and we intend to harness the power of stewardship to work together to hold investee companies to account on this important issue.

**Promoting diversity at Standard Life Aberdeen plc**

Both Aberdeen Asset Management and Standard Life Investments have been strong supporters of the wider efforts of the 30% Club in promoting diversity. This will continue, with Sir Gerry Grimstone, Standard Life Aberdeen plc’s chair, remaining a member of the 30% Club. In addition, co-CEOs Martin Gilbert and Keith Skeoch have signed up to the 30% Club’s aspirational targets. Both Martin and Keith are committed to continuing to accelerate progress on gender diversity as part of our broader inclusion strategy. This is reinforced by both heritage businesses being initial signatories of the HM Treasury Women in Finance Charter in 2016 and the combined action plan, as published in 2017. We have been active members of the 30% Club’s ‘Balancing the Pyramid’ initiative, through which we sponsored research aligned to our efforts in building a sustainable gender-balanced talent pipeline. We are also supporters of the Diversity Project, which seeks to accelerate progress towards an inclusive culture across the investment and savings industry.

An edited version of this article was originally published in November 2017 by the Financial Reporting Council in recognition of the 25th anniversary of the UK Corporate Governance Code.

Standard Life Investments released a number of thematic papers throughout 2017 covering our views on, among other things, the Workforce Disclosure Initiative, executive remuneration, the taskforce on climate-related financial disclosure, and ESG and the corporate bond investor. Please click on the link below in order to see these, and many of our other publications: https://www.standardlifeinvestments.com/esg_themes

\(^1\)From 6 April 2017, employers in the UK with more than 250 employees are required by law to publish the following four types of figures annually on their own website and on a government website: (i) gender pay/salary gap (mean and median averages); (ii) gender bonus gap (mean and median averages); (iii) proportion of men and women receiving bonuses; and (iv) proportion of men and women in each quartile of the organisation’s pay structure.
Engagement overview

During the year, our programme of targeted engagement with investee companies continued. We now have a single process which screens portfolios on the basis of ESG factors. As a result, we are conducting more joint engagement on these issues.

During 2017, we had 302 one-to-one ESG engagements with investee companies. Of these, 180 were planned on the basis of our engagement priorities and 122 were organised in reaction to ESG change. In total, 111 were with overseas companies. We were particularly pleased to note that our engagement with US companies continues to increase as we build our ESG relationships and it is encouraging that more of these engagements involved independent board members.

One of the key topics for engagement in the US this year was the backlash against companies that have different classes of shares with unequal voting rights. This started with strong investor opposition to Snap’s IPO which listed shares with zero voting rights. On a positive note, Facebook recently dropped its plans to issue a new class of shares with no voting rights, something that we had previously discussed with the company. The Facebook decision reflects pressure on Silicon Valley companies to limit the use of unequal voting rights intended to cement founder control. The index providers have been considering this issue and recently S&P Dow Jones decided to ban new multi-class companies from its key US stock indices. The move means that Snap, and other new public companies with share classes that have differential or no voting rights for certain investors, will be barred from inclusion in indices such as the S&P 500.

Investors are becoming increasingly concerned about the trend of companies holding ‘virtual AGMs’. A rising number of US companies, including Ford, HP, Duke Energy and PayPal, are moving to virtual meetings, claiming it saves costs and provides greater accessibility for investors. However, opponents argue online-only meetings disadvantage shareholders, particularly smaller investors for whom the annual meeting is often their only opportunity to speak to management and the board. There are also concerns that by moving to virtual AGMs, companies will escape scrutiny over controversial issues. The acceptable alternative would be to hold “hybrid” meetings where both physical and online participation is possible. We expect to engage more on this issue with our US holdings over the coming year.

Board nominations and the work of the nominations committee was an important focus. We reported last year on our participation in the nominating committee of Swedish Match, the first time that we had done this. As long-term and significant shareholders of Swedish Match, we were approached by the company and asked to join the committee. One of the senior members of our European fund management team agreed to participate. The committee comprised a total of four shareholder representatives along with the chairman of the board. Its role is to consider proposals for candidates to serve as directors and as auditors. Ahead of the AGM, the committee reviewed overall board composition, interviewed two potential candidates to replace an independent director who was stepping down and were also involved in decisions regarding the level of director fees and the appointment of the auditor. All the relevant resolutions were subsequently passed at the AGM. Overall, we believe that this was a valuable opportunity to fulfill our shareholder responsibilities and have agreed to take part in the committee again this year.

We engaged with a number of companies on their nominations process. Finnish food retailer Kesko and Portuguese oil & gas company Galp Energia are examples. Galp is included in the Engagement Highlights section which follows. At Kesko, the major shareholder, the K-Retailers Association, is in control of the board nominations process. The Association owns 15% of the votes and nominates three of the seven-person board from its own ranks and also selects the four independent directors. This is not uncommon in Finland but the nature of the relationship between Kesko and its major shareholder is not a simple financial investment or even that of a founder shareholder. The Association has a strong trading relationship with Kesko: Kesko effectively franchises its stores to the retailers who, among other things, must then lease property and buy goods from Kesko. This obviously presents the potential for conflicts of interest. As a result, the lack of clarity around the nomination process is a concern and we encouraged Kesko to consider setting up a formal nominations committee in order to improve both the process and its disclosure.

We have reported in the past on our participation in a collective engagement in Japan aimed at improving the level of board independence. This initiative continues to deliver results. When we started in 2014, our objective of one third board independence was seen as very ambitious but, three years on, 12 of the 33 companies targeted have achieved this level and 15 have made some progress. Only six companies still have 10%, or fewer, independent directors. It is clear that the debate on board independence has moved on significantly, which we believe will have a positive impact on governance standards in Japan.
In terms of key environmental and social themes, we continued to see increased attention on employees and how companies manage what is ultimately their key resource. Our engagement considered employees throughout organisational structures, ranging from gender and ethnic diversity at board level to the contracts afforded to frontline staff. How a company treats its workforce can be a source of reputational, operational and regulatory risk for businesses and their investors. In the UK, there has been considerable media focus on working conditions in the retail industry over the past two years, most notably warehouse conditions at Sports Direct. There have also been issues with factories that supply retailers such as River Island and Boohoo, with many allegedly only paying their workers £3 an hour. We have engaged with numerous companies over the year on these issues (including Boohoo and River Island) in addition to carrying out several site visits to better understand how companies are treating employees. This year, in collaboration with civil society group ShareAction and other investors, we took part in the creation of the Workforce Disclosure Initiative (WDI). While we recognise the increasing pressure on businesses to respond to a number of surveys, in our view there is scope for a more standardised employee reporting framework. We believe that the WDI offers this through a robust framework that references existing reporting standards, such as the 2015 UK Modern Slavery Act, as well as voluntary guidelines such as those of the Pensions and Lifetime Savings Association.

Throughout the year, we engaged with several extractive companies with significant environmental footprints including Coal India, Shell, Suncor, Total and BP. All companies rely on natural capital. Their ability to operate, deliver products and services depends on a range of raw material inputs. Mismanagement of environmental impacts, wherever they may occur along the value chain, threatens the going concern of a business and can lead to reputational damage, operational disruption, and a loss of licence to operate. In many countries, increasingly stringent environmental legislation is in place to promote the sustainable use of common resources and mitigate adverse environmental impacts. Even though the focus of this legislation is generally on downside risks, it is equally important to stress the potential opportunities available as companies adapt and develop solutions to environmental challenges. Our engagement has become more focused on solution-based initiatives and across companies we are starting to witness a move away from simple measurement of current environmental impacts toward strategic decision making to address future impacts.

Finally, following the merger between Standard Life and Aberdeen Asset Management, our approach to engagement will continue to evolve. However, as an asset manager, we remain deeply committed to engagement on ESG issues, which we view as a key aspect of our investment process.
Engagement highlights

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<td>Mattioli Woods</td>
<td>Founder and Chairman moves to a sub-board role</td>
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<td>Coal India</td>
<td>Unearthing the sustainability issues at Coal India</td>
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<td>Accesso Technology Group</td>
<td>Recent board and executive changes</td>
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<td>Wells Fargo</td>
<td>Sales scandal and the steps taken to mitigate it</td>
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<tr>
<td>BT Group</td>
<td>Concerns about its management of relationships with regulators and the control environment that allowed fraud in the Italian business to go unnoticed for so long</td>
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### Key

<table>
<thead>
<tr>
<th>Engagement driver</th>
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<tr>
<td>Internal mandate</td>
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<tr>
<td>Client mandate</td>
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<tr>
<td>Performance-based engagement</td>
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<tr>
<th>Engagement outcome</th>
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<tr>
<td>Influential in achieving change</td>
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<td>On track to meet objectives</td>
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<tr>
<td>Escalation candidate</td>
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**National Express**

National Express is a UK-listed mass passenger transport company. It operates express coaches, buses and trains in regions including the US, UK and Germany. It has a fleet of over 26,000 vehicles.

We last spoke to the company in the second quarter of 2016 to discuss various allegations in relation to human capital management and its approach to health & safety. Subsequent to the meeting, National Express highlighted that it was applying the European Foundation for Quality Management framework across the group, initiating an independent review of its employee practices and that it would issue an independently produced report.

We were reassured by the steps taken by the company and the findings of the independent report. However, issues remained around safety standards. At the end of 2016, a Durham School Services bus (a subsidiary of National Express) crashed in Tennessee, killing six children and injuring 20. A preliminary report by the National Transportation Safety Board (NTSB) indicated that the crash was a result of driver error.

We engaged with the company to gain further details on the causes of the accident and the company's response. National Express advised that its CEO (Dean Finch) went to the US, met with the CEO of the US business (David Duke) and reported back to the board within 48 hours. The company is awaiting the outcome of a full report from regulators. As it stands, the company is already accelerating numerous activities relating to safety standards, which are listed below.

- Implementing a secure cloud-based complaint management system to directly connect all schools that the company serves. It is available in Chattanooga and will be rolled out to the entire customer base by end-2017.
National Express (Continued)

- Installing smart cameras/drive-cam in all 16,000 Durham buses, which will record the driver and road whenever “unusual driving is sensed”. It is available in Chattanooga and will be rolled out to the entire US customer base by end-2017.

- Appointing chief data and safety compliance officers by the end of Q1 2017. They will work directly with the senior vice-president of safety and report to the president and CEO.

This tragedy in Tennessee highlights the important responsibilities that transport service providers have. We await the final findings of the US Federal Motor Carrier Safety Administration and the NTSB investigation. We will continue to engage with the company and measure its progress on this and other issues.

Galp Energia

Galp Energia is Portugal’s only oil and natural gas integrated operator. It has global activities that span from the exploration and production of oil and natural gas through to refining and marketing oil products, natural gas marketing, and sales and power generation.

We have been a shareholder in Galp for many years and have engaged with it on governance matters in the past. In July 2015, we had a call with the head of group secretariat. The conversation focused on the nominations process for new board appointments and on board composition. We encouraged the company to improve transparency around board nominations and subsequently wrote to the chairman to follow up on board composition more generally. The board is large and we believe there is potential to reduce the number of directors and increase independence.

In October 2016, the company announced that the 82-year-old chairman, and 33% shareholder, was standing down in favour of his daughter. We subsequently requested a call to discuss this change and, in April 2017, were able to speak to the vice-chairman. While we took positive note of the recent appointment of the vice-chairman, an experienced individual who will be able to support the new chair, we reiterated our view that the board, with 19 members, was large and lacked independence. As such, we repeated our call for better disclosure around the nominations process. Independent directors comprise 26% of the board, and while this meets the requirements of the Portuguese governance code, we believe that, given the shareholder structure, a minimum of 50% independence would be appropriate.

The next director elections will be in 2019 and we intend to continue engaging between now and then with a view to seeking improvements in the nominations process and in overall board composition. Unless there are improvements in board independence, we will consider taking voting action on director elections in 2019.
<table>
<thead>
<tr>
<th>Key</th>
<th>Joules</th>
</tr>
</thead>
<tbody>
<tr>
<td>Engagement driver</td>
<td>Joules is a UK-based premium lifestyle brand that designs and sells own-branded lifestyle clothing, accessories and homeware.</td>
</tr>
<tr>
<td>Internal mandate</td>
<td>In May, we visited the Joules head office and distribution centre in Market Harborough. The meeting was part of a wider engagement with UK retailers to address labour risks in warehouse operations. We had previously spoken to Joules following its initial public offering in May 2016 to discuss the inclusion criteria for Standard Life Investments’ ethical funds.</td>
</tr>
<tr>
<td>Client mandate</td>
<td>Joules seems less exposed than other retailers to reputational and operational risks associated with working conditions in its warehouse. This is in part due to its size but also because it does not produce ‘fast fashion’, which reduces the pressure on employees to meet targets. As the company and online retail grows, management of Joules’s distribution is likely to become more complex. Joules currently employs around 1,500 people in total, of which 90 are permanent staff working at the warehouse.</td>
</tr>
<tr>
<td>Performance-based engagement</td>
<td>Joules does not use zero-hours contracts, and works with just one agency onsite to provide additional headcount during peak times. We met with the warehouse manager who outlined the work that had been done to make improvements at the facility, including more flexibility around shifts. We welcome these improvements, but also noted that unlike other retailers, Joules does not pay its employees for the time spent undergoing security searches.</td>
</tr>
<tr>
<td>Engagement outcome</td>
<td>We also spoke in more detail about Joules’s approach to sourcing, which we had already discussed during our first engagement. Joules produces 85% of its clothes in China. It employs 10 Shanghai-based quality controllers who visit factories in between audits. Other sourcing countries include India, Myanmar and Cambodia. We questioned the company about due diligence in countries where the risk of human rights violations is higher. Joules confirmed it would not go into production in these countries on its own but with trusted suppliers. Going beyond tier one, Joules also has a number of textile mills it works with and encourages suppliers to source from.</td>
</tr>
<tr>
<td>Influential in achieving change</td>
<td>As Joules only listed last year, reporting on sustainability is limited. We highlighted the reputational benefits from greater transparency and encouraged the company to be more open about some of the positive practices it demonstrates. Joules was open to our suggestions and agreed to consider greater disclosure of its sustainability practices. We will continue to monitor the company’s progress.</td>
</tr>
<tr>
<td>On track to meet objectives</td>
<td>Escalation candidate</td>
</tr>
</tbody>
</table>
LafargeHolcim is headquartered in Switzerland and produces building materials. The company, through its subsidiaries, operates in more than 80 countries and has 90,000 employees. The company was formed from a merger of Lafarge and Holcim in 2015.

We have had ongoing engagement with LafargeHolcim regarding allegations that its Syrian operations provided facilitation payments to so-called ‘Islamic State’ to allow employees access to work and to continue production at its plant. LafargeHolcim commenced production in Syria in 2010 with a plant that had taken three years to build and cost $680 million to produce. As armed conflict escalated in the region, the decision was taken to evacuate the site in 2014. When these allegations initially came to light, a French parliamentary report found the allegations to be unsupported; however, the company chose to embark on an internal investigation. It has been found that LafargeHolcim made payments to intermediaries in furtherance of its Syrian operations. These payments were made without regard to the identity of the groups involved.

We engaged with the company regarding these findings and to inform it of our voting position. We decided that, in light of the seriousness of these actions, we were unable to vote in favour of the discharge of LafargeHolcim's board and senior management. Although the formal discharge of the board is largely a routine request, we believed that due to the issues raised, the potential for legal proceedings and as a symbolic gesture to highlight our concerns, we could not support the resolution.

LafargeHolcim announced that its CEO, Eric Olsen, would step down from his position on 15 July 2017, as a result of the issues arising from historic Syrian operations. The company highlighted that Mr Olsen was found not to be aware or linked to the wrongdoings identified in Syria. Mr Olsen claimed that his resignation would “bring back serenity” to the company. LafargeHolcim has subsequently appointed the former CEO of chemical group Sika, Jan Jenisch, as its new CEO.

We are supportive of LafargeHolcim’s openness and ongoing engagement over this period. We recognise the active steps taken by the company to investigate this incident, disclosure of its findings and the remedial actions it is taking. The actions of its ethics, integrity and risk committee to enhance the group’s compliance procedures are also a welcome step.

LafargeHolcim has continued to take positive steps in its reporting practices, operations and production of sustainable products to support the transition to a low carbon economy. We welcome the steps it has taken in light of this very serious incident and will continue to engage with the company to track its business conduct and other sustainable performance targets.
We attended Royal Dutch Shell's annual sustainable responsible investment (SRI) roundtable in April. In the morning, there was a general presentation by the executive team on the company’s sustainability challenges. Three consecutive panel sessions (technology, upstream safety & environment, and strategy) followed in the afternoon. We have had ongoing engagement with Royal Dutch Shell and also attended its 2016 SRI event.

The first item on the agenda was an update on the OPL 245 investigation, given by Shell’s Legal Director. In 2011, Shell and ENI paid $1.1 billion to the Nigerian government for the purchase of the offshore OPL 245 oil block in Nigeria, the licence of which was held by Malabu Oil & Gas. Allegations were later made that a significant amount of this money went directly to Malabu, the owner of which was a former Nigerian oil minister suspected of awarding himself the licence to the block in 1998.

Prior to the meeting, we took note of various media reports detailing allegations of corruption carried out by the company. This included transcripts of email conversations, which seem to show that a few Royal Dutch Shell executives were aware that the deal money would be used to pay-off intermediaries and officials in the Nigerian government. We continue to monitor the situation closely and will augment our company research/view as new information becomes available.

The meeting was also an opportunity for investors to understand Royal Dutch Shell's strategic positioning with regards to low carbon transition. Its objective is to increase the share of natural gas in its portfolio. According to the company, the world has now arrived at an inflection point and is on the brink of a systemic change to existing energy models. The company is advocating a holistic approach, which includes all stakeholders (competitors, regulators, investors, etc.).

Carbon capture and storage will be essential to achieve low carbon objectives, but the amount of capital expenditure allocated on these types of initiatives is still relatively marginal and commercial deployment seems a long way out. It is clear that one of Royal Dutch Shell’s ambitions is to grow its downstream oil and gas business, along with its chemicals division. We find Royal Dutch Shell one of the most transparent companies on the subject. It is one of the few to recognise that the low carbon transition will cause a systematic shock to energy systems.

This discussion has also been relevant from a voting perspective. A number of investors and organisations have voiced concern over Royal Dutch Shell’s strategic alignment with a 2°C objective, from a remuneration standpoint and with a separate climate change resolution.

Despite some notable progress on how the company is maturing its climate change response, the financial incentives to deliver this strategic change have been questioned. The company’s remuneration package has faced criticism for not encouraging a corporate behaviour aligned with a ‘2°C world’. In our view, the sustainability component of the bonus element perhaps errs on the weaker side, even though we welcome the inclusion of sustainability-related metrics in the compensation plan.
### Royal Dutch Shell (Continued)

The bonus element includes objectives for the management of greenhouse gas emissions from direct operations. However, the delivery of the low carbon strategy is perhaps less evident (other than through gas production volumes). We believe investors would benefit from greater clarity on how the incentives could be designed in order to deliver the strategy.

Royal Dutch Shell also urged its investors to vote against the climate resolution to adopt and publish science-based targets for its Scope 1, Scope 2 and Scope 3 emissions. The company already reports on its Scope 1 and Scope 2 emissions, and is very vocal on its wider strategy to adjust its operations to a lower carbon environment. We acknowledge that absolute emissions reduction targets could be difficult in the context of segment growth; however, we believe relative targets can be set in accordance with strategic objectives. In addition, we are supportive of the disclosure of Scope 3 emissions (or estimates thereof) but recognise it could put the company under considerable strain should it apply targets at this level.

Therefore, we have voted in line with management and against the proposed resolution. We will monitor how the company proposes to address some of these investor concerns, and continue to encourage a form of transparency that benefits both Royal Dutch Shell and its investor base.

### Mattioli Woods

Mattioli Woods is a leading UK provider of wealth management and employee benefits services. It was founded in 1991 and both founders, Bob Woods and Ian Mattioli, have been instrumental in the growth and success of the company.

We contacted the company to request a meeting with Joanne Lake, the company's chairperson. This was our first detailed governance engagement with the company and followed the announcement last year that Bob Woods would step down from the role of chairman and from the board in October 2016. It was also announced that he would be succeeded by non-executive director Joanne Lake, who had been on the board since 2013. Woods remains as a full-time employee, but with a client-facing role; while his co-founder, Ian Mattioli, remains CEO. Founder-led companies often face challenges when transitioning to the next generation of leadership, and that is why we approached the company.

During our most recent visit with the company, we were reassured regarding Woods’ new role, including confirmation that he would not attend board meetings. Meanwhile, Joanne Lake provided a good account of how resources and systems are being strengthened as the company grows. Mattioli Woods has a small board, consisting of the chairperson, three executive directors and two non-executives. In terms of board composition, we like to see an appropriate balance of executive and non-executive directors. As such, we suggested that the company consider adding a further independent non-executive director to the board.
Coal India

An Indian state-controlled coal mining company, Coal India is the largest coal producer in the world. It accounts for more than 80% of India's total coal production and feeds 98 out of the country's 101 coal-based thermal power plants. This is the first time we have engaged with Coal India on material issues relating to the energy transition, human capital management and water scarcity.

After the US withdrew from the Paris Agreement earlier this year, numerous observers pointed to China and India as the natural heirs of climate leadership. India has made a number of pledges concerning the penetration of renewable energy in the total electricity mix, with a target to install 200GW of electricity by 2050. Electricity demand will grow and we expect coal to continue to meet a significant part of that demand. However, renewable energy ambitions – driven in part by a commitment to fight air pollution and its associated health impacts – may see the country revise its approach. At present, Coal India does not see any constraint in that respect and presents a confident coal outlook.

Water is becoming an increasingly rare and precious resource in India. It is also essential to coal-mining operations.

Coal India's latest sustainability report highlights the numerous initiatives in relation to resource conservation (for example, rainwater harvesting) but it is difficult to assess vulnerability to water risk and how scarcity and/or flooding affects production. The report offers little sense of community engagement on the issue, and how different stakeholders (including farmers) may be competing for the water resource.

Coal India reported 38 fatalities for 2016. This is a high number, but we noted the dramatic decrease in both fatalities and serious accidents over the past five years. In 2011, Coal India was reporting close to 120 fatalities and over 400 serious accidents. The good progress on safety has mostly come from a change of mining methods. Indeed, 93% of production is open-pit mining, which is less dangerous than underground mining. There seems to be some focus on training and best practice co-operation with international peers, but Coal India is not yet able to articulate the benefits of these approaches.

Another of Coal India's challenges is its production output per man-shift. It is a company renowned for its inefficiencies, as well as its employee absenteeism. It manages a workforce of over 300,000 people and we were surprised to hear that there were no labour disputes or human capital challenges in relation to either working conditions or wages. Non-government agency reports and press coverage tends to suggest otherwise. For example, in May 2017, five trade unions called for a three-day strike to demand early settlement of wage negotiations. Coal India mentioned that salaries were negotiated at the national level for a period of five years, thereby limiting the scope for demands outside this timeframe. Wages are the biggest cost component for Coal India, and it is still unclear how wages are likely to evolve over time, and how this may affect the company's margins.
Coal India (Continued)

- **Internal mandate**: The age pyramid of the workforce is also a concern: 64% of employees are older than 45, which poses problems in terms of knowledge transfer and recruitment. We could not obtain any information on how this is likely to be managed.

- **Escalation candidate**: We were pleased to be able to speak directly to Coal India about environmental and social issues, and noted the significant improvements achieved over the past few years, especially on reporting quality and safety performance. On the latter, we encouraged the company to provide more details on its initiatives and to adopt targets to drive further performance improvements. We also asked for more details on how issues like the energy transition, water management and labour relations will affect the business.

Accesso Technology Group

- **Internal mandate**: UK-listed technology company Accesso designs and integrates ticketing and virtual queue systems in amusement parks, water parks and other attractions. We have been in regular contact with Accesso regarding voting issues since 2012.

- **Escalation candidate**: We had a discussion with the executive chairman around some of the governance practices at the company. At the time of the meeting, Accesso used a system of staggered board elections where only a certain proportion of directors were put up for renewal every year. While we realise this is more typical in smaller companies, we mentioned that as Accesso aspires to best practice in governance, then this would be an area to reconsider.

Subsequent to our meeting with the company, it was announced that as from the 2017 AGM all directors will now face annual re-election.

We have previously asked the company to give shareholders a vote on the remuneration report, but the board has not been supportive of this. We will continue to press the company on this in future engagements. At the 2017 AGM, the company asked shareholders to support a number of proposals regarding changes to remuneration schemes. We had a number of issues with the proposed changes. For example, we highlighted the lack of disclosure of the bonus and long-term incentive plan (LTIP) performance targets and also the impact of the increased level of dilution to shareholders. As a result, we voted against the changes to the company’s share option and LTIP plans, as well as the chairman of the remuneration committee, to highlight our ongoing concerns.

At a subsequent meeting, we met the senior independent director and the chair of the remuneration committee and reiterated our view that they should provide shareholders with a vote on remuneration matters. We provided details of example AIM companies that do this and agreed to talk again before the next AGM.
Wells Fargo & Company is a diversified financial services company providing banking, insurance, investments, mortgage, leasing, credit cards and consumer finance. It operates through physical stores, the internet and other distribution channels worldwide.

The company has faced a number of misconduct issues, including the unauthorised creation of deposit accounts on behalf of customers by Wells Fargo employees in a bid to achieve sales targets. The creation of these accounts resulted in three government lawsuits, which were settled for US$185 million. As a result of these issues, at the AGM we voted against the re-election of 12 board directors that were linked to audit and human resource committees during the period. Since the AGM, the company has had a number of director changes including the appointment of Betsy Duke as its new chair.

Following our voting position, we sought further engagement with the company to understand what steps it is taking to re-build trust in the bank and address the misconduct issues it is facing. During our meeting, Wells Fargo highlighted that its relatively new CEO, Tim Sloan (around one year in the post), is focused on addressing the issues arising from misconduct, and engaging with internal and external stakeholders, including employees, regulators and investors. Subsequent to the meeting, it has been reported that he will testify before a US Senate Committee regarding the bogus accounts scandal.

The company hired a third-party firm to analyse accounts opened over an eight-year timeframe, covering 165 million accounts. It identified that around 3.5 million potentially unauthorised accounts had been created to-date, with approximately 190,000 accounts incurring fees and charges. These practices were largely driven by cross-selling incentive schemes applied by the bank and a focus on revenue growth. Subsequent to the scandal – and in addition to changes at board level – over 5,000 Wells Fargo employees have been dismissed and a new head of its retail banking division has been appointed. The company has also changed its incentive scheme and moved to a service incentive model from a growth one.

We welcome the levels of disclosure from the group regarding its actions to address the scandal and the use of third-party providers to investigate potential misconduct in the business. However, we remain concerned about the culture of the organisation and the potential for further misconduct issues, including the mis-selling of car insurance.

We have encouraged the company to further integrate its 'Vision and Values' statement into its strategy. We continue to engage with the company.
BT Group is one of the world's leading communications services companies. Its main activities are the provision of fixed-line services, broadband, mobile, and TV products and services, as well as networked IT services. It provides these services primarily in the UK, but also has customers through its Global Services business unit in 180 countries worldwide.

The company issued a significant profit warning in January 2017, of which approximately one-third was caused by fraud at its Italian business. In addition to meetings held with executive management, we were offered and accepted a meeting with the chair of the audit committee. He explained the steps taken by the audit committee subsequent to the discovery of the fraud and the remedial action taken to address any shortcomings discovered in the review of the control environment.

Although the profit warning raised questions mostly about the fraud in Italy, it also raised concerns regarding the performance of management in a number of areas. These included the development of relations with regulators and the maintenance of an appropriate balance between cost controls and the provision of a high-quality service.

At the company's AGM in July, our analysis of the resolutions was coloured by the events at BT Italia. However, it was also undertaken on the basis of our overall view on the recent performance of management, and what we believe would be best for the company's future delivery of its strategy and long-term value.

We had significant concerns regarding the overall performance of management and the oversight of the control environment that allowed the fraud in BT Italia to remain undiscovered over a number of years. We therefore voted against the reappointment of the CEO, the chair of the audit committee and the auditors.

As a result, the company has taken the time to seek further details of our concerns that led to these voting outcomes. In the spirit of a continued long-term open relationship, we have provided additional details. We will also engage further with the current and future chairman so that our position is fully explained and understood, in an effort to improve long-term financial performance.
Global voting overview

Voting at the general meetings of our investee companies is a key component of Standard Life Investments’ stewardship activities. Through voting our clients’ shareholdings, we have the opportunity to hold boards to account for their actions. In 2017, Standard Life Investments voted at 1,497 shareholder meetings. Of these meetings, 29% included one resolution where we voted against management recommendations. Key areas of focus when voting included board composition, risk & control, remuneration, environmental & social management, capital issuance authorities and audit matters.

Among the range of topics voted on at a general meeting, executive remuneration has drawn the most attention (and headlines) in recent years - and 2017 was no different. In the UK, the first application of a binding vote on remuneration policy occurred in 2014 and, as the rules require this is approved for a maximum of three years, 2017 brought the second vote on remuneration policy at many UK companies. The AGM season was therefore preceded by detailed consultations from companies on planned amendments to their remuneration policies, with Standard Life Investments providing feedback to consultations from 71 companies. In the majority of cases, often following feedback and subsequent revisions to proposals, this process led to shareholder support. However, this outcome was not the case for all consultations. Examples where we remained opposed to remuneration policies at the end of the consultation process were Morgan Sindall, PageGroup and GlaxoSmithKline. There were also a small number of companies that failed to manage the consultation process in order to obtain the support of shareholders for their remuneration report or remuneration policy. This resulted in either large votes against remuneration report resolutions, as shown in cases such as Crest Nicholson (where the remuneration report received a 58% vote against), and Pearson (where the report received a 65% vote against), or the withdrawal of remuneration policy resolutions that were unlikely to receive the require shareholder support, as was the case for Imperial Brands and Safestore. Nevertheless, there was a notable development with the first examples of some of the UK's largest companies significantly reducing the maximum remuneration available – notably at BP and WPP. We hope the actions of these companies will be replicated by others across the market.

In Europe, one significant development in relation to executive remuneration was the introduction of an annual binding vote on pay in France. A formal consultation process on remuneration is not yet common practice in markets outside of the UK; however, in the lead up to the AGM season, we engaged with a number of French companies as they sought to ensure shareholder support, in order to discuss their remuneration arrangements. We were encouraged by instances, in France and elsewhere, where it is clear that our views have been taken into account through revisions to policies and disclosures. Examples include Renault and Partners Group.

Other factors may also impact our voting on remuneration – for example, whether sufficient downwards discretion has been used in relation to formulaic outcomes. We did not consider this to be the case at National Express or Reckitt Benckiser and so voted against their remuneration reports (see voting examples section).

While the subject of executive remuneration is high profile, we regularly monitor, engage and vote on other governance topics in order to protect and enhance the value of our clients’ investments. While the level of dissent on board-related resolutions is lower than on remuneration, votes against the members of the board can signal serious concerns regarding a company’s governance. The board has ultimate responsibility for a company’s affairs and is primarily accountable to shareholders for ensuring that appropriate and effective processes are in place for carrying out the key tasks that enable it to fulfil that responsibility. This includes the identification and management of risk, the setting of the company’s risk appetite and the oversight of operations and control. Where we consider there to have been a serious failure of these responsibilities, we have taken action to emphasise our concern. During 2017, we voted against board-related resolutions where we had serious concerns regarding the board’s oversight of risk and control. This was the case at BT, Wells Fargo and LafargeHolcim.

The role and responsibilities of a company’s auditor are crucial to company control and oversight. Although it is unusual for us to vote against the reappointment of auditors, we did so on two occasions in the UK during 2017. At the AGM of BT, we voted against the reappointment of PwC following the fraud that was uncovered in the company’s Italian business. A different type of concern was underlined through our vote against the reappointment of PwC at Vodafone’s AGM. We were of the opinion that its appointment as auditors to Phones4U after its appointment as auditors of Vodafone created a conflict. We attended the company’s AGM to raise our concerns and, in this instance, the board publicly indicated that they agreed with our concerns.

We are strongly of the view that boards must contain a balance of independent directors; one region of focus in this regard for several years has been Japan. Standard Life Investments has been part of an initiative led by a group of 20 institutional investors, which called for companies to aim for an ambitious board independence standard of one-third by 2017. There has been improvement in recent years, aided by investor pressure and the
introduction of the Corporate Governance Code in 2015. However, to reflect the view, which was first set out in 2014, we strengthened our voting policy on Japanese board independence for the 2017 voting season and, for Nikkei 225 companies, we took voting action on the non-independent directors of boards who did not meet the one-third independence threshold.

In continuing to encourage sufficient independent minority shareholder representation on boards in Italy, Standard Life Investments participated in the ‘voto di lista’ process for the third consecutive year. We were signatories to the minority slates presented by Assogestioni for the election of directors to the boards of Mediolbanca, Marr and Enel.

Diversity on boards remains high on the corporate agenda, most notably gender diversity. In 2017, both France and Belgium reached deadlines regarding gender quotas. In Belgium, boards of large companies must have at least one-third male or female representation. In France, the gender quota is higher – at 40%.

Gender diversity is a topic that we primarily address through our engagement rather than voting activity. However, following engagement, we voted against members of the Governance Committee of Hudson Pacific at the company’s AGM due to the lack of gender diversity on the board.

As shareholders, we value pre-emption rights highly as we do not want to suffer significant dilution of our holdings. In 2015, the UK’s Pre-Emption Group issued new guidelines regarding share issuance authorities to enable companies to request up to 10% of their share capital without pre-emption rights, as opposed to the previous 5%. In 2016, guidance was issued stating that companies should request 10% through two resolutions: the first for a general 5% authority, and a second to request 5% for the purposes of an acquisition or capital investment. While the guidance does not apply to AIM-listed companies, we nevertheless expect companies of a sufficient size to voluntarily follow the guidance. We voted against the relevant resolutions of the meetings of AIM companies Fusionex, Rockhopper Exploration and Gamma Communications where this expectation was not met.

Over the past few years, we have seen a growth in the number of resolutions that focus upon the environmental & social (E&S) pillars of ESG, and this continued in 2017. Two areas where we saw the greatest growth were in resolutions addressing the transition to a low carbon economy and resolutions supporting gender and ethnic diversity. Consistent with our principle of transparency, we disclose all our votes on our website on a monthly basis and continue to provide a rationale for all votes against, abstentions and selected votes in favour. Our voting disclosure can be found on our website at: https://www.standardlifeinvestments.com/governance_and_stewardship/what_is_corporate_governance/our_voting_records.html

“We among the range of topics voted on at a general meeting, executive remuneration has drawn the most attention (and headlines) in recent years - and 2017 was no different.”
## Voting highlights

### 2017 ESG Investment Annual Review Voting Statistics*

<table>
<thead>
<tr>
<th>Voting Statistics</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shareholder meetings at which our clients' shares were voted</td>
<td>1,497</td>
</tr>
<tr>
<td>Number of resolutions voted</td>
<td>18,793</td>
</tr>
<tr>
<td>Shareholder meetings at which our clients' shares were voted against management on one or more resolution</td>
<td>427</td>
</tr>
<tr>
<td>Number of resolutions voted against management recommendations</td>
<td>954</td>
</tr>
<tr>
<td>Shareholder meetings at which our clients' shares abstained on one or more resolution</td>
<td>158</td>
</tr>
<tr>
<td>Number of resolutions abstained</td>
<td>383</td>
</tr>
</tbody>
</table>

### Geographical Breakdown of Votes Against Management Recommendations

- **Europe (ex UK)** (23%)
- **UK** (22%)
- **Asia Pacific (ex Japan)** (21%)
- **US & Canada** (18%)
- **Rest of world** (10%)
- **Japan** (6%)

### Reasons for Votes Against Management Recommendations

- **Remuneration** (32%)
- **Director Elections** (25%)
- **Dilution & Control** (21%)
- **Environmental & Social** (3%)
- **Audit matters** (2%)
- **Other** (18%)

*Data reflects 12 months from 1 January 2017*
## Global voting highlights

### BT Group

In January 2017, the company issued a significant profit warning, of which approximately one-third was caused by a fraud in its Italian business. At the company’s AGM, our analysis of the resolutions was coloured by the events at BT Italia. We also held an unfavourable view on the recent management and company performance, and had doubts the team could deliver the company’s future strategy and generate long-term value. We had significant concerns regarding the overall performance of management and the oversight of the control environment that allowed the fraud in BT Italia to remain undiscovered over a number of years. We therefore voted against the reappointment of the chief executive officer, the chair of the audit committee and the auditors.

### Crest Nicholson

During 2016, we had discussions and consultation with Crest Nicholson on remuneration matters. The company informed us that it was not minded to make changes to its existing remuneration policy, which was due to be renewed in 2017. We were comfortable with the existing policy and were supportive of the structure of remuneration arrangements. However, on reviewing the annual report in preparation for voting at the company's AGM, we found that the profit before tax targets used in the long-term incentive plan had been revised downwards by a significant amount, without prior consultation with shareholders. After due consideration, we concluded that the revised targets were not sufficiently stretching in the context of the prospects of the company and we therefore voted against the remuneration report.

### CSX

In March 2017, the company appointed a new chief executive officer. Upon appointment, he received a grant of nine million stock options as an equity award. Only half of the options are subject to performance conditions, but these are undisclosed. The remaining options are time-based only, vesting annually over four years. The potential value of the options is significant, and appeared to be a one-off sign-on award. We did not consider this grant to be aligned with long-term value creation and therefore voted against the resolution to approve the CEO's compensation.

### Deutsche Telekom

At the company’s AGM, approval was sought for a general authority to issue shares. This included up to 20% of the company's issued share capital, which could be issued on a non-pre-emptive basis. We considered the level of authority to be too high, and the five-year duration of the authority to be too long. We therefore voted against the relevant resolution.

### GlaxoSmithKline

We were consulted by the company on remuneration matters. However, during our discussions, we became concerned by the structure of the revised Performance Share Plan (PSP). The new scheme was to have a more generous grant policy than the previous one and the amount of vesting for threshold performance would increase. The 2017 award to the new CEO allowed 165% of salary to vest for threshold performance, which we considered to be too high. Having discussed remuneration matters with the company in recent years, and having been previously supportive, we were disappointed that remuneration changes did not reflect our guidelines and longstanding views. We therefore voted against resolutions to approve the PSP, the remuneration policy and the members of the remuneration committee.

### Lafarge Holcim

We have had ongoing engagement with LafargeHolcim regarding allegations that its Syrian operations provided facilitation payments to so-called Islamic State to allow employees access to work and to continue production at its plant. The company conducted an internal investigation and it was found that payments were made to intermediaries in furtherance of its Syrian operations. These payments were made without regard to the identity of the groups involved. We decided that, in view of the seriousness of these actions, we were unable to vote in favour of the discharge of LafargeHolcim's board and senior management at the AGM. Although the formal discharge of the board is largely a routine request, we believed that due to the issues raised, the potential of legal proceedings and to make a symbolic gesture to highlight our concerns, we could not support the resolution.
Mitchells & Butlers

During 2016, the representation of both major shareholders increased from two to four non-executive directors. It was difficult to see how this would be a good development for independent shareholders although it may keep a balance of power between the two major shareholders. The increased representation of majority shareholders is not in the best interests of independent shareholders as there is the potential for these individuals to dominate the deliberations of the board. We were not sufficiently convinced that this would be in the best interests of all shareholders and therefore voted against the election/re-election of the shareholder representatives.

National Express

The company had a year of good financial performance and its chief executive was awarded a bonus of 87% of maximum for 2016. However, in November 2016, one of the company’s US school buses crashed. The crash resulted in the loss of the lives of six children and another 20 were injured. It seemed inappropriate for such a bonus to be paid by the company given that there had been significant loss of life during the course of its operations. At the AGM, we therefore voted against the remuneration report.

Orpea

At its AGM, the company presented backward-looking, non-binding votes on executive remuneration outcomes and forward-looking, binding votes on executive remuneration policy, which is in line with new French legislation. We noted that the company had improved the disclosure within its remuneration report, particularly around the metrics used to determine annual bonus outcomes. We welcomed changes made to remuneration policy, which removed the provision for exceptional remuneration to be paid, and the lengthening of the performance period under the Long-Term Incentive Plan (LTIP), from one year to two years. While remuneration arrangements are still not fully in line with our expectations, we considered it appropriate to abstain on the relevant resolutions. This outcome balanced our remaining reservations with the improvements made. We have engaged with the company to set our expectation that the LTIP performance period be lengthened to three years.

Reckitt Benckiser

In 2016, the company admitted responsibility for the sale of a product by one of its acquired businesses which caused the deaths of around 100 people in South Korea. In response to this, the company decided that its CEO should not receive the bonus earned for the year and that the vesting of the Long Term Incentive Plan (LTIP) award due this year should be reduced by 50%, from £28 million to £14 million. While we respect that some action was taken in respect of remuneration outcomes, we nevertheless felt that it would have been more appropriate for none of the LTIP to vest. We were also concerned that, during a year of poor performance, such a bonus award and generous LTIP vesting were due to be paid. We therefore were not convinced that the performance targets are sufficiently challenging. To reflect these views, we voted against the remuneration report.

Sports Direct

At the company’s AGM in 2016, the Chairman, Keith Hellawell, failed to receive majority support for his re-election in the separate vote by minority shareholders. In line with regulatory requirements, the board convened an EGM to submit his re-election for another vote. We did not support Mr Hellawell’s re-election at the AGM and our views remained unchanged at the time of the EGM in January 2017. We had concerns regarding the oversight of the board and were of the view that a structural change in the way the company organises itself and operates was required. We also believed that a substantial strengthening of the non-executive members of the board was required, particularly in the role of chairman. On this basis, we again voted against his re-election.

Syrah Resources

The company appointed a new chief executive officer in February 2017. At May’s AGM, shareholder approval was sought to grant him an award of one million share options, which would vest after one year subject to share price performance conditions. While we were supportive in principle of a grant to provide an incentive for the new CEO, we did not consider a performance period of one year to be sufficient. We were of the view that the performance period should be a minimum of three years to provide long-term alignment with shareholders. For this reason, we voted against the grant of options to the CEO.
TUI

We were disappointed that the 2017 AGM agenda did not provide shareholders with a vote on the company's annual report or remuneration report. The ability to vote on these reports is a valuable mechanism for shareholders to express their views to the board, particularly where there are areas of concern. In respect of executive remuneration, we had concerns regarding the structure and outcomes for 2015/16. Key concerns were the provision for, and payment of, discretionary bonuses in connection with the merger of TUI AG and TUI Travel; the absence of retrospective disclosure of annual bonus targets; and the vesting of a portion of the Long-Term Incentive Plan (LTIP) for below median relative total shareholder return (TSR). As we were unable to direct our concerns regarding remuneration through a vote on a remuneration-related resolution, we decided to vote against the discharge of the Supervisory Board Chairman, Klaus Mangold. This also underlined our disappointment at not being presented with a vote on the annual report or remuneration report. When the company's 2017 annual report was published, we welcomed changes to the structure of remuneration including the removal of discretionary bonuses, the introduction of earnings per share as a second LTIP performance metric, and the removal of vesting for below median TSR performance. We were also pleased that the company included a vote on the remuneration system at the 2018 AGM, and that it committed to do so going forward.

Thomas Cook

The company consulted us on changes to its remuneration policy and, while there were some improvements, we were concerned that our views on a number of matters were not reflected in the final policy. We were opposed to a Performance Share Plan (PSP) award in excess of the annual normal award of 150% of salary, as we believed that arrangements for exceptional circumstances should only be used for scenarios such as recruitment. We therefore voted against the remuneration report. We were also opposed to the introduction of a new additional long-term incentive, the Strategic Share Incentive Plan (SSIP), as we were of the view that the existing PSP should be sufficient to provide alignment with strategic goals. We therefore voted against introduction of the new incentive scheme and the remuneration policy which incorporated the new incentive scheme.

We had previously abstained on the re-election of remuneration committee members at the 2016 AGM and given that there were new issues of concern this year, we voted against the re-election of these directors at the 2017 AGM.

Following further discussions with the company on these matters later in 2017, we were satisfied that some changes have been made that reflect our views. We also felt that there was a change of tone in the approach taken by the company. The company has now committed not to use the Strategic Share Incentive Plan without having consulted and received support from shareholders first and that all future LTIP awards will use performance targets that are disclosed in advance. These changes have enabled us to vote in favour of all of the resolutions at the 2018 AGM.

Vodafone

During the 2016/2017 financial year, Vodafone's audit and risk committee was notified by the PwC partner leading the audit of Vodafone that a company, for which a number of PwC partners were acting as administrators, was considering litigation against Vodafone. In our opinion, the appointment of PwC as administrators to this company after its appointment as auditors of Vodafone created a conflict, regardless of whether litigation against Vodafone is pursued. PwC considered that no actual conflict exists to its position as Vodafone's auditors, but we disagreed with this view. We therefore opposed the re-appointment of PwC as auditors at the AGM. To escalate our concerns we attended and spoke at the AGM of the company and highlighted the concern about the material conflict created by PwC. From the responses, it was clear the board and company agreed with our concerns. The chair of the board stated during the AGM that while Vodafone was happy with the quality of PwC's audit and the work performed, the leadership of PwC “could have avoided this potential conflict of interest and should have done so.”

Wells Fargo

In 2016, the company announced that it had incurred $185 million in fines relating to its retail banking sales practices. The settlement was the result of investigations into unsound sales practices that occurred within Wells Fargo's Retail (Community) Banking operation. It was disclosed that certain employees opened unauthorised deposit accounts, submitted applications for credit cards without consent and enrolled customers in online banking services that they did not request. The company has made numerous management and board changes since September 2016. These include the appointment of a new chief executive officer, designating an incumbent director as independent chairman and appointing a vice chair. The board had a responsibility to set and oversee the risk profile of the company and we considered there to have been a significant failure of risk oversight. We therefore voted against the re-election of 12 board directors who were on the audit, risk and human resource committees during the period in question – as these committees are tasked with risk oversight.
Influencing governance change

As in previous years, we have remained involved in the debate and development of policies around the world which we believe are relevant to our role as the stewards of our clients’ investments. During the year, policies were being developed and consulting underway on a number of changes relating to sustainable finance and corporate governance. Below, we detail the key developments in which we have been involved, either through direct input or through the various industry associations with which we interact.

United Kingdom

During 2017, the UK government and regulators had a number of relevant proposals that look to tackle governance issues. The government had placed great importance on introducing additional corporate governance requirements and we reported our involvement on this in our ESG Annual Review of 2016. Following the general election in 2017, in which the Conservative government lost its parliamentary majority, the proposed changes (examples below) were scaled back. Although we welcome change, we are concerned that it will not radically alter the current environment.

• The creation of a public list of companies that received a significant vote against resolutions at general meetings. This would bring added scrutiny to such situations and the actions that companies take to address them. However, our preference was for an escalation process that would require companies to take action and to seek additional shareholder approval on relevant resolutions.
• The introduction by the FRC of additional company reporting to demonstrate how they achieve the requirements of Section 172 of the Companies’ Act, which defines some of the duties of directors. We are not convinced that the three methods for boards to comply with the need to consider the interests of employees are the right ones in all cases. We would like to see companies explain the consideration of employee interests no matter which method they use.

The FRC has begun a review of the Corporate Governance Code (CGC) and we took various opportunities through individual and group meetings to provide our views on how the code should be developed. We feel that the structure of the CGC is generally appropriate, but that expectations on companies were different compared to when the CGC was last reviewed in 2012. Therefore, it is an opportune time to review the detail and language of the CGC to ensure that companies are clearly able to demonstrate how they meet the expectations of shareholders and broader stakeholders. The revision of the CGC will also incorporate the additional requirements of the government corporate governance changes mentioned above.

There have also been a number of initiatives seeking to improve wider aspects of investing responsibly. These have included Her Majesty’s Treasury’s (HMT) patient capital review focusing on the financing of technology firms. Standard Life Investments provided input directly to HMT through attendance at a roundtable and written input providing suggestions regarding government activity that may assist in increasing the levels of investment allocated to this area by pension funds, insurance companies and other long-term investors.

Standard Life Investments also took part in the advisory group created by the UK government to investigate and suggest actions to grow a culture of social impact investing in the UK. The advisory group published its report in November this year identifying a number of key actions that it felt would encourage providers of pensions, savings and investments to engage with individuals to enable them to support the things they care about in their investments. Five key action areas were defined which we will continue to support.

Europe

In 2016, the European Commission (EC) appointed a High Level Expert Group (HLEG) on sustainable finance to provide advice on developing a comprehensive EU strategy on sustainable finance. The HLEG issued an interim report in July 2017 seeking input from interested parties. We provided input through the UK Sustainable Investment and Finance Association (UKSIF) and through our own input. We were supportive of the overall direction of the debate on sustainable finance and have subsequently discussed our impact investing methodologies to provide some insight into how we use the sustainable development goals to assess companies and to provide report on impact to clients.

The EC also sought input on the duties of institutional investors and asset managers regarding sustainability. This sought input on an impact assessment in December 2017 and broader consultation for input in early 2018. We will provide input to both of these pieces of work to contribute to the development of policy that will have a positive impact on investing in a sustainable manner.
Japan

We submitted a response to the Financial Services Agency consultation on proposed revisions to the Stewardship Code in Japan. We were broadly supportive of the changes put forward, particularly the requirement to disclose votes at individual company AGMs, which would improve transparency and accountability of asset managers’ voting decisions.

Standard Life Investments, in conjunction with a number of other international investors, also provided a report explaining why board independence is important to global investors. Although there has been movement towards our goal of having one-third of Japanese boards being independent, we felt that pressure needed to be sustained to ensure that progress was maintained.

US

Standard Life Investments endorsed the Investor Stewardship Group’s (ISG) new US governance & stewardship code. The ISG is a collective of some of the largest US-based institutional investors and global asset managers, along with several of their international counterparts. The ISG was formed to bring all types of investors together to establish a framework of basic standards of investment stewardship and corporate governance for US institutional investors and boardroom conduct. The result is the ‘Framework for US Stewardship and Governance’, a set of stewardship principles for institutional investors and corporate governance principles for US-listed companies.

https://www.isgframework.org/signatories-and-endorser/

“We have remained involved in the debate and development of policies around the world which we believe are relevant to our role as the stewards of our clients’ investments.”
As we move through 2018, we will continue to build on all the good work carried out last year. This includes the management of water risk, development of the SDGs and tackling the effects of opioid addiction. We will develop our own work and our collaboration with the Principles for Responsible Investment to manage water risks faced by investee companies. We believe this is one of the most significant risks facing certain companies’ operations, as well as the communities affected by their corporate footprints. However, while there has been positive work in this area, we believe it still lacks the rigour of measurement evident in areas such as carbon emissions. It also lacks the appropriate infrastructure investment. Water is generally considered a financial externality, which can exacerbate these issues. Our engagement and research will focus on how, or if, investee companies assign a financial value to water and how the resource is managed.

We will also continue to lead approaches on the application of the SDGs through the Standard Life Investments Global Impact Investment Fund and the Standard Life Investments UK Equity Impact Employment Opportunity Fund. JP Morgan research estimates demand for impact investing strategies could reach $1 trillion by 2020. We believe that finance is an important and powerful catalyst of change and that through this work and our investments we can support the SDGs goals for 2030.

The FSB (Financial Stability Board) Task Force on Climate-related Financial Disclosure (TCFD) released its final recommendations in June 2017, and delivered its findings at the G20 Summit in Hamburg, Germany. Chaired by Michael Bloomberg, the TCFD seeks to encourage disclosure on financially material climate impacts. For us, this presents an opportunity to consider the environmental impacts of our portfolios. It also allows us to create better strategies to manage these portfolios and support the transition toward a low carbon economy. We have followed the development of the TCFD closely and taken part in its public consultation. As members of the Transition Pathway Initiative, we have also worked with fellow asset managers and asset owners to develop mechanisms to evaluate the quality of companies’ disclosure on climate impacts. Following the TCFD’s final recommendations, we have begun to apply them across our investment practices and will develop this process in 2018.

In addition, we will continue to advance the work we started in Q3 2017 that focused upon the risks that opioid addictions pose, particularly in the US, and what the pharmaceutical sector, insurers and pharmacy benefit managers (PBMs) can do to address the issue. We continue to engage with companies on the issue and will consider the various resolutions that have been raised against companies relative to their practices.

The FRC’s review of the UK Corporate Governance Code will introduce significant change for companies and shareholders in the UK. We will engage actively in the process of change focusing on key areas to us, which include improved reporting on broader aspects of diversity, greater demonstration of boards’
consideration of the interests of stakeholders (including employees and suppliers), and increased transparency on boards’ role in defining and assessing culture. We are supportive of the changes but we are concerned about the speed of change. We will endeavour to encourage companies to make appropriate changes to their practices and disclosure in advance of the timeline set by the FRC.

Gender diversity on boards is already improving; however, we are committed to ensuring these positive changes continue. We support the proposals of the Hampton-Alexander review and are members of the 30% Club UK Investor Group. We will design our voting policy to reflect our views on companies’ progress in creating appropriate diversity on boards and more widely in their workforce, particularly focusing on the management levels below the board. Our wider stewardship work will reinforce this. In early 2018, companies began to report their gender pay gaps for the first time. To date, disclosure has revealed significant differences on the average pay gaps across salary and bonus. We will ask companies to provide disclosure, if they have not done so, on the actions they will be taking to address the gaps identified, and we will hold them to account on those action plans, as well as seeking appropriate reporting on progress in closing any pay gap.

We remain concerned about various aspects of the audit market. Our focus is on the delivery of high-quality audits on which we as shareholders can rely to ensure that reporting by companies is true and fair. The aspects of the audit market that we believe may have an impact on the quality of audits include: the lack of choice of audit providers with the majority of audits undertaken by the ‘Big Four’ audit firms; the increasing level of non-audit services, which can introduce conflicts of interest; the inappropriate management of conflicts leading to situations where relationships exist that create apparent conflicts of interest; and the levels of audit fees leading to questions about the ability of audit firms to deliver high-quality audits. As company accounts have increasingly included significant adjustments and judgements, the quality of auditor challenge has become even more important to us as investors. We will continue to engage with audit firms, audit committee chairs and regulators to assist in developing a trusted and transparent audit industry.

The EC will develop its policy response to create a sustainable finance system, including increasing asset managers’ transparency on the use of ESG factors. This is likely to drive additional analysis and reporting on environmental exposures in portfolios. France introduced additional ESG and climate change reporting for asset managers in 2017. It is likely the EC will use the French requirements as a basis for future European policy. We will continue to engage with various entities active in Europe to provide input into these developments, which we believe will further raise the focus on the role played by asset managers in the development of a sustainable finance system.

“Gender diversity on boards is already improving; however, we are committed to ensuring these positive changes continue.”
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