



WHEB

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Responsible Investing: Engagement Report Q2 2016

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In advance of the UK's referendum on membership of the EU we engaged with two of our UK holdings that we believed were particularly exposed to a changing trade relationship with Europe.

Introduction

We engage with companies and policy makers on a wide range of issues to understand better the quality of the businesses that we invest in, how they are positioned for future challenges and to encourage progressive approaches to environmental, social and governance issues. This quarter, in advance of the UK's referendum on whether to remain part of the European Union (EU), we spoke to some of our most exposed names to understand how they were positioned for a potential UK exit from the EU. We've also trialled a new set of voting guidelines in the UK and have been supporting the CDP¹ in their efforts to encourage more companies to respond to their climate change questionnaire. We report these and other initiatives below.

Ramping up assertive voting in UK companies

WHEB is the only asset manager that has volunteered to trial a new set of voting guidelines that focus on ESG issues at UK listed companies. The guidelines were developed by the Association of Member Nominated Trustees (AMNT), a 600 member strong group of pension fund trustees, which sets out guidelines on how they want their asset managers to vote at company meetings.² We used the guidelines to inform our voting positions on two UK companies; ARM Holdings in our Resource efficiency theme, and Intertek in our Safety theme.

Both companies have relatively strong approaches to ESG issues and so we were comfortable supporting management on most of the votes in a way that was consistent with the guidelines. However, there were a few areas where we ended up voting against management. For example, we voted against the Chairman of the Board at Intertek because we felt that the company would benefit from a higher profile governance structure on key ESG issues such as climate change and employee diversity. We also voted against the Chairman at ARM on the basis that the company's approach to employee diversity – a critical issue to the long-term success of the business in our view – was inadequate. We are communicating these views to the companies and seeking further engagement with them.

We plan to trial the guidelines in our voting at the meetings of other UK companies during the third quarter and will report back to the AMNT on our experience

What does 'BREXIT' mean for our UK holdings?

Given the huge focus in recent months on 'BREXIT' and what this means for our investment outlook, we've included a brief summary of some work we did in advance of the UK's referendum on membership of the EU when we spoke to two of our UK holdings to gauge the likely impact of BREXIT on their businesses. This initiative wasn't intended to provide a comprehensive view on the likely impact of a BREXIT, but to give an indication of what the impact might be, particularly for UK exporters.

For Johnson Matthey, the view was that the impact should be minimal because the company manufactures globally with facilities servicing their own local markets. The main impact therefore is in translating profits back into sterling and the company would therefore likely be a beneficiary of a weak pound.



¹ The CDP was formerly known as the Carbon Disclosure Project (<https://www.cdp.net>).

² See <http://amnt.org>

During the second quarter we supported the CDP's efforts to achieve a higher response rate from medium sized businesses that have so far not responded.

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Oxford Instruments made similar points though indicated that their exposure to European funded research contracts might create some challenges for the business in the medium-term as the UK would likely need to re-negotiate their involvement in these projects. They stressed though that these issues would likely affect only future research projects following a UK exit from the EU.

Company Engagement

■ Promoting CDP engagement to companies

WHEB has been a signatory to the CDP for more than four years and has been actively engaged in helping the initiative develop new criteria on political lobbying and in promoting the questionnaire to corporate audiences. During the second quarter we supported the CDP's efforts to achieve a higher response rate from medium sized businesses that have so far not responded. Given WHEB's focus on mid-sized businesses, we led the engagement work with several companies in our portfolio which were either receiving a request for the first time, or which had not responded to previous requests. This group included the US businesses Ansys, Cooper Companies, Henry Schein, Kansas City Southern, Quanta Services, Roper Technologies, Stericycle and Wabtec. We also wrote to China Longyuan, and the European businesses Hella and Orpea.

Several of these businesses have recently started disclosing sustainability information publicly (eg. Kansas City Southern, Stericycle) and have indicated that they are not yet ready to provide the detailed disclosures that the CDP requests. Some, such as Henry Schein and Wabtec, have indicated that they have an ambition to provide more comprehensive disclosures on climate issues, and are considering whether to expand this in 2016 or to wait until their internal resources and systems are better established.

■ Reducing the impact of paper bleaching at Smurfit Kappa

We were asked by one investor to investigate the approach that Smurfit Kappa, one of our portfolio holdings, takes to minimise the environmental impacts associated with bleaching processes in paper and cardboard production. Smurfit Kappa is one of our investments that has a relatively heavy environmental footprint. The company provides recycled cardboard packaging³ and fits in our Environmental Services theme. The company also owns a bleached paper pulp production line in Colombia with a capacity of 10,000 tonnes per month producing liner and boxboard that is used as part of a small portion of the business that produces virgin paperboard.

Since 1994 the facility has used a process for bleaching known as Totally Chlorine Free (TCF). This avoids the use of chlorine which is highly toxic and also leads to the production of dioxin and furans in the production process. Instead, of chlorine, Smurfit Kappa uses oxygen and pressurised peroxide in their bleaching process in order to address the environmental (and safety) concerns associated with using chlorine.

TCF processes are considered to represent a Best Available Technology for bleaching processes in paper manufacture, and more broadly Smurfit Kappa is widely regarded as a leader in addressing many of the key environmental impacts associated with cardboard packaging production. Nonetheless, the company's activities still have sizeable impacts and we continue to work closely with them to understand these impacts and encourage the company to further reduce them.



Public policy:

■ Letter to the US Securities and Exchange Commission

During the quarter we co-signed a letter to Mary Jo White the Chair of the US Securities and Exchange Commission (SEC). The letter, which was signed by a variety of US and European asset managers, pension funds and foundations called on the Commission to issue further guidance to companies on how to disclose their approach to addressing risks to their businesses from climate change. The letter also encourages the Commission to scrutinise financial filings from carbon intensive sectors such as oil and gas and electric power companies to ensure that their existing disclosures adequately address the risks of climate change to their operations.

³ Approximately 75% of the cardboard sold by the company comes from recycled sources.

■ Letter to the G20 Leaders on Ratification of the Paris agreement

As part of the Institutional Investors Group on Climate Change (IIGCC), we also wrote to the leaders of the G20 nations to encourage them to ratify the Paris agreement on climate change as soon as possible. The letter also encouraged leaders to double their investment in clean energy and urged financial regulators to work to improve company disclosure standards on climate change risks.

Voting record: Q2 2016

The table below summarises the voting record for the FP WHEB Sustainability Fund from 1 April–30 June 2016. Full details of how we voted on each of the individual votes are detailed in Appendix 1 (<http://www.whebgroupp.com/investment-strategies/listed-equity/fund-governance/engagement-and-voting-records/>) including with rationales for votes against management and abstentions and where we supported shareholder resolutions.

Meetings	# of meetings	%
# votable meetings	49	100%
# meetings at which votes were cast	48 ⁴	98%
# meetings at which we voted against mgmt. or abstained	38	78%

Resolutions	# of resolutions	%
# votes cast with management	515	86%
# resolutions where votes cast were against mgmt. or abstained (see list in appendix)	77	13%
# resolutions where votes were withheld	5	1%

Summary of other areas of work

The following section details the range of engagement work that we have done bilaterally with individual companies in our portfolio and in the wider investment themes as well as our voting at annual general meetings that were held during the quarter.

Company	Topic	Comment	Outcome
Agilent	Auditor independence	AGM voting letter	Company acknowledged our letter
ARM Holdings	Sustainability reporting / Diversity strategy	Redlines voting review	Initial conversation revealed strong approach, though this is currently unpublished
CT Environmental	Excessive equity issuance	AGM voting letter	Company acknowledged our letter
Dassault Systemes	CEO compensation / pay-out ratio and stock option proposals /Director independence	AGM voting letter	Company acknowledged our letter and has proposed conference call

⁴ We did not vote at the China Singyes meeting as we had already sold our position in the company.

Company	Topic	Comment	Outcome
Ecolab	Shareholder proxy access / Auditor independence / CEO remuneration	AGM voting letter	Company acknowledged issues but believes its approach is robust.
Fresenius SE	Low pay-out ratio / Manufacturing safety	AGM voting letter	Company has previously acknowledged issues but believes its approach is robust.
Henry Schein	Auditor independence / CDP	AGM voting letter / CDP	Company is actively reviewing CDP response and acknowledged other concerns
Johnson Matthey	Impact of Brexit	Phone call before UK referendum	See section above
Lennox International	Auditor independence	AGM voting letter	Company acknowledged issues but believes its approach is robust
Littelfuse	Sustainability disclosure	Company meeting	Company agreed to look into how to improve sustainability disclosures
Orpea	CDP	CDP (as above)	Company has agreed to review involvement and discuss with CDP
Oxford Instruments	Impact of Brexit	Phone call before UK referendum	See section above
Praxair	CEO remuneration / Auditor independence	AGM voting letter	Company has previously acknowledged issues but believes its approach is robust.
Quanta Services	CDP	CDP (as above)	No response this year but indicated previously that it doesn't plan response
Shimano	Board independence / Sustainability disclosures	AGM voting letter	Company has improved sustainability reporting including providing English language version
Smurfit Kappa	Environmental impact	Use of low impact bleaching technology	Positive response from company (see above)
Stericycle	CDP	CDP (as above)	No response but did respond to these points last year
Varian Medical Systems	Board Director attendance	AGM voting letter	Company has accepted concern and is expecting the issue to be addressed in 2016-17
WABTEC Corporation	Auditor independence / Sustainability disclosure	AGM voting letter	Will be reviewing sustainability disclosure in the Autumn
Xylem	Auditor independence / ESG incentive structures	AGM voting letter	Company acknowledged concerns
Ansys	Auditor independence / CDP	AGM voting letter and CDP (as above)	No response as of 08/07/2016

Company	Topic	Comment	Outcome
AO Smith	Jurisdiction of incorporation / Auditor independence / Shareholder rights	AGM voting letter	No response as of 08/07/2016
Borgwarner	Minority shareholder rights / Proxy access / CEO remuneration	AGM voting letter	No response as of 08/07/2016
Cerner	Auditor independence / CDP	AGM voting letter and CDP (as above)	No response as of 08/07/2016
China Longyuan Power	CDP	CDP (as above)	No response as of 08/07/2016
Cooper Companies	Auditor independence / CDP	AGM voting letter and CDP (as above)	No response as of 08/07/2016
Hella	CDP	CDP (as above)	No response as of 08/07/2016
Horiba	Auditor independence	AGM voting letter	No response as of 08/07/2016
Kansas City Southern	Auditor independence / CEO Remuneration / CDP	AGM voting letter and CDP (as above)	No response as of 08/07/2016
Keyence	CDP / Low pay-out ratio / Auditor independence / Board independence	AGM voting letter / CDP	No response as of 08/07/2016
Kingspan	CEO remuneration	AGM voting letter	No response as of 08/07/3016
Mednax	Auditor independence	AGM voting letter	No response as of 08/07/2016
Rockwell Automation	Auditor independence	AGM voting letter	No response as of 08/07/2016
Roper Technologies	Auditor independence / CEO Remuneration	AGM voting letter	No response as of 08/07/2016
Suez	Director 'overboarding'	AGM voting letter	No response as of 08/07/2016
Thermofisher Scientific	CEO Remuneration / Auditor independence	AGM voting letter	No response as of 08/07/2016

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