



WHEB

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Responsible Investing: Engagement Report Q2 2017

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Introduction

The second quarter is always the busiest period of the year for voting. In the past three months we voted at 46 company meetings representing over three-quarter of the Annual General Meetings of the portfolio companies. A summary break-down of how we voted at the meetings is available at the back of this report. For those with a passion for the full details, a complete list of how we voted on every ballot is available as an appendix on the WHEB website¹.

WHEB's voting 'Red-lines'

Last quarter, following our pilot-testing of the Association of Member Nominated Trustee's (AMNT's) Red Line Voting policies, we reported on our decision to strengthen our voting policies. This included strengthening policies on the independence and diversity of company board directors, executive and non-executive remuneration and on the management and disclosure of performance on social and environmental issues.

We are currently implementing these stricter policies in full in our UK and European holdings with a view to rolling them out more broadly across other geographies in due course. It is clear though, that there is a significant difference in the standards of corporate governance between Europe on the one hand and the US and Japan on the other. For example, we now consider non-executive Board Directors non-independent after being ten years on the board. This is broadly in-line with definitions in Europe and is based on a judgement that after ten years, a Board Director will have had an important role in shaping the strategy of a business. As a consequence, we do not believe that he or she is in a position to independently assess the validity of that strategy. There is scope for Board Directors with longer tenures to remain in post, but we do not believe that they can be considered independent.

This perspective is at odds with a view that is typical in the US where Director tenure is not generally considered to have a bearing on independence. It is therefore not uncommon in the US for a majority of non-executive Board Directors to have tenures that are significantly in excess of ten or even twenty years. Our voting in this quarter reflects this with votes against management on at least one Director election at 80% of US companies. For European companies, the equivalent number is approximately 50%.

Other prominent issues that we have addressed in our voting and in subsequent engagement with companies includes auditor independence, executive remuneration as well as non-executive remuneration and share schemes, and reporting of Greenhouse Gas Emissions.

Company engagement

■ The environmental impact of Viscose production at Lenzing AG

Lenzing AG is an Austrian-based business that uses wood pulp to manufacture a variety of wood-based cellulose fibres (WBCF) that are increasingly widely used in apparel. The materials that Lenzing manufactures include viscose as well as Lyocell and Modal. These materials are popular with clothing manufacturers because they have a number of superior characteristics including their softness, breathability and because they have a radically lower environmental footprint when compared with the cotton that they typically replace. The FP WHEB Sustainability Fund invested in Lenzing in early 2017 as part of the 'Environmentally Preferable Products' sub-theme within Environmental Services.



Lenzing is widely regarded as a leader in the environmentally responsible production of WBCF, however, poor practices have been found at one of their operations in Indonesia.

The cultivation and manufacture of cotton for use in apparel has a very significant negative environmental impact. Cotton requires huge volumes of water to grow (up to 6,860m³ per tonne of fibre) and also uses significant amounts of pesticide and fertilizer in its production². In contrast, the production of Viscose, Modal and Lyocell use radically lower levels of these inputs (<10% of the water and chemical inputs on average).



Lenzing is widely regarded as a leader in the environmentally responsible production of WBCF and has had their manufacturing operations certified by several non-governmental organisations (NGO) including the Rainforest Alliance and Canopy³. However, Lenzing was criticized in a more recent report by the NGO the Changing Market Foundation⁴. While this report confirmed much of Lenzing's strong performance highlighted in other reports, they did find evidence of poor practices at one of Lenzing's operations in Indonesia. This included reports of local river pollution, pressure on local villagers not to disclose information and local air pollution.

The factory in question is the only Lenzing operation that is not considered to employ the European Union's standard for best available technology in producing viscose. The factory had already been highlighted by Lenzing itself as an operation where performance needed to be improved. While we do not believe that the report undermines the inherent advantages of WBCF, we have spoken to the business to encourage them to review the report and determine if further improvements need to be made at their Indonesian operations. We have also contacted the NGO to understand their concerns more precisely. We plan to discuss these issues further with the company in the coming weeks.

Market Engagement

Calculating the positive impact of investing

The concept of investing in a way that has positive impact on the world is central to WHEB's investment proposition. Until recently though it has not been possible to measure and quantify this impact in a way that enables investors to understand and connect with the impact that their money is having in the real world. In our view, this has prevented people from appreciating the importance and role of finance generally in generating positive impact.

With this in mind, WHEB has developed an 'impact calculator' that is intended to reveal the positive impact associated with an investment in the FP WHEB Sustainability Fund. The impact calculator is based on research undertaken as part of WHEB's third Annual Impact Report and involved calculating the positive impact generated by different companies in the fund. Depending on the company, the impacts were quantified in terms of carbon emissions avoided, water treated and waste collected and recycled as a result of their activities⁵.

The impact calculator then calculates, based upon the amount of money invested in the fund, what the associated impact is in terms of avoided carbon emissions, water treated and so on. Figure 1 illustrates the impacts associated with investing £1 million in the fund. An on-line calculator available on WHEB's homepage (www.whebgroupp.com) can be used to calculate the positive impacts associated with any amount invested in the fund.

Figure 1:



WHEB has developed an 'impact calculator' that is intended to reveal the positive impact associated with an investment in the FP WHEB Sustainability Fund.

As part of the IIGCC we have written to Energy Ministers of the European Union to encourage them to adopt a strong Clean Energy Package

- **Lobbying on energy efficiency in Europe**

As part of the Institutional Investors Group on Climate Change (IIGCC) we have written to Energy Ministers of the European Union to encourage them to adopt a strong Clean Energy Package including ambitious targets on greater energy efficiency. We heard at the end of June that the EU's Energy Council had come to an agreement on the Energy Efficiency Directive. Disappointingly, as a result of lobbying from the UK and eastern European countries, the Council elected to support a more modest level of ambition including making key targets voluntary and eliminating longer-term energy savings targets. The European Parliament will now agree its position before a final version is negotiated.

- **The RE100 reaches its 100th member**

Working with the NGO ShareAction, WHEB has been an investor signatory supporting the RE100 initiative to encourage businesses to commit to using 100% renewable energy. The campaign has targeted a range of businesses across the world. WHEB has been a signatory to many of the letters sent to encourage companies to commit to the initiative. Among the businesses that have now signed up include large companies across almost all sectors of the economy including Apple, BMW, BT, Coca-Cola, Diageo, GM, Google, IKEA, LEGO, Mars, Nestle, Nike, Tesco and Unilever. Together these companies account for 107 Twh of renewable electricity, equivalent to the power consumed by the Netherlands⁶. In early July, the 100th company Philips Lighting signed up to the initiative.

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End-Notes

¹ <http://www.whebgroupp.com>

² http://www.lenzing.com/fileadmin/template/pdf/konzern/lenzinger_berichte/ausgabe_88_2010/LB_88_2010_paper_1.pdf

³ <http://canopyplanet.org/wp-content/uploads/2016/10/The-Hot-Button-Issue-The-CanopyStyle-Report-2016.pdf>

⁴ <https://changingmarkets.org/portfolio/dirty-fashion/>

⁵ <http://www.whebgroupp.com>

⁶ <http://media.virbcdn.com/files/69/ddbfa4d36e1b8bd4-RE100AnnualReport2017.pdf>

Voting record: Q2 2017

The table below summarises the voting record for the FP WHEB Sustainability Fund from 1 April – 30 June 2017. 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 rationales for votes against management and abstentions and where we supported shareholder resolutions.

Meetings	# of meetings	%
# votable meetings	46	N/A
# meetings at which votes were cast	46	100%
# meetings at which we voted against mgmt. or abstained	37	80%
Resolutions	# of resolutions	%
# votes cast with management	402	70%
# resolutions where votes cast were against mgmt. or abstained (see list in appendix)	174	30%
# resolutions where votes were withheld	0	0%

Company engagement activity

Company	Topic	Comment	Outcome
Acuity Brands	Sustainability reporting	Conference call	Company is currently working on its sustainability report for 2017.
Cerner Corp.	Related-party transactions / Director independence / Auditor independence	AGM Voting letter	Company correspondence set out why they disagree with our views.
Cooper Companies	Sustainability reporting	Letter	Arranging date for conference call during the Summer.
Lenzing AG	Environmental impact of viscose production	Letter following NGO report	Arranging date for conference call during the Summer (see above).
Orpea	Related-party transactions / Remuneration / Share capital repurchase	AGM Voting letter	Company responded stating that Board Director has retired resolving the related-party transaction issue, and disagreeing with other points.
Wabtec	Sustainability reporting	Conference call	Company is currently working on its sustainability report for 2017.
Ecolab Inc.	'Overboarding*' / Director independence / Auditor independence	Conference call	Conference call set out why the company disagrees with our views.
Grand Canyon Education	Director independence / Sustainability reporting	AGM Voting letter	Arranging conference call to discuss.

* 'Overboarding' is the term given to a Board Director who is a member of four or more Boards which we view as excessive, compromising their ability to be an effective Board member.

Company	Topic	Comment	Outcome
Hannon Armstrong Sustainable Infrastructure	Director independence / Shareholder rights / CEO remuneration	AGM Voting letter	Acknowledgement of receipt of letter.
Henry Schein Inc	Director independence / Remuneration	AGM Voting letter	Company correspondence set out why they disagree with our views.
IPG Photonics Corp	Director independence / Auditor independence	AGM Voting letter	Acknowledgement of receipt of letter.
Lennox International Inc.	Director independence / Auditor independence / Compensation	AGM Voting letter	Board Directors have now retired. Company disagrees with our other points.
Littelfuse Inc.	Director independence / Sustainability reporting	AGM Voting letter	Arranging conference call to discuss.
MSA Safety Inc.	Director independence / Share option scheme	AGM Voting letter	Company correspondence set out why they disagree with our views.
Praxair Inc.	Board independence / Auditor independence / Remuneration	AGM Voting letter	Company correspondence set out why they disagree with our views.
Rockwell Automation Inc.	Auditor independence	AGM Voting letter	Company believes it has rigorous auditor selection processes.
Xylem Inc.	'Overboarding' / Tax position / Remuneration	AGM Voting Letter	Company correspondence set out why they disagree with our views.
Wabtec Corp	Director independence / Auditor independence	AGM Voting letter	Company correspondence set out why they disagree with our views.
Acuity Brands Inc.	Auditor independence / Remuneration	AGM Voting letter	No response as of 5 th July
AO Smith Corp.	Director independence / Auditor independence /	AGM Voting letter	No response as of 5 th July
China Everbright Int. Ltd.	Director independence / Equity issuance	AGM Voting letter	No response as of 5 th July
Cooper Companies Inc.	Director independence / Auditor independence / Remuneration	AGM Voting letter	No response as of 5 th July
CVS Health Corp	Director independence / 'Overboarding' / Auditor independence / Remuneration / Renewable energy	AGM Voting letter	No response as of 5 th July
Danaher Corp	Director independence / Auditor independence / Share options / Remuneration / GHG reporting	AGM Voting letter	No response as of 5 th July
Dassault Systemes SA	Remuneration / Director independence / Auditor independence	AGM Voting letter	No response as of 5 th July

Company	Topic	Comment	Outcome
Gamesa Corp Tecnologica SA	Director independence	AGM Voting letter	No response as of 5 th July
Hera SpA	Remuneration	AGM Voting Letter	No response as of 5 th July
Intertek	Remuneration / Political donations	AGM Voting letter	No response as of 5 th July
JB Hunt Services Inc.	GHG reporting / Director independence / Auditor independence	AGM Voting letter	No response as of 5 th July
Johnson Controls Int.	Remuneration / Director independence / Share buy-back / Auditor independence	AGM Voting letter	No response as of 5 th July
Keyence	Director independence / Low pay-out ratio	AGM Voting letter	No response as of 5 th July
Kingspan	Director independence / Buyback authorisation	AGM Voting letter	No response as of 5 th July
Lenzing SA	Director independence & lack of gender diversity / Remuneration	AGM Voting letter	No response as of 5 th July
Mednax	Director independence / Auditor independence / Remuneration	AGM Voting letter	No response as of 5 th July
National Instruments Corp	Director independence / Auditor independence	AGM Voting letter	No response as of 5 th July
Nautilus Inc.	Director independence	AGM Voting letter	No response as of 5 th July
Roper Technologies Inc.	Director independence / Remuneration / Auditor independence	AGM Voting Letter	No response as of 5 th July
Shimano	Director independence / Remuneration	AGM Voting letter	No response as of 5 th July
Stantec	Remuneration / Auditor independence	AGM Voting letter	No response as of 5 th July
Suez	Director independence	AGM Voting letter	No response as of 5 th July
Thermo Fisher Scientific Inc.	Director independence / 'Overboarding' / Auditor independence / ESG incentives	AGM Voting letter	No response as of 5 th July
Varian Medical Systems Inc.	Auditor independence	AGM Voting letter	No response as of 5 th July

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