

Public Engagement Report



Money talks – Reforming executive remuneration

This report contains a summary of the stewardship activities undertaken by Hermes EOS on behalf of its clients. It covers significant themes that have informed some of our intensive engagements with companies in Q2 2016.

The report also provides information on voting recommendations and the steps we have taken to promote global best practices, improvements in public policy and collaborative work with other long-term shareholders.

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What is Hermes EOS?

Hermes EOS helps long-term institutional investors around the world to meet their fiduciary responsibilities and become active owners of public companies. Our team of engagement and voting specialists monitors our clients' investments in companies and intervenes where necessary with the aim of improving their performance and sustainability. Our activities are based on the premise that companies with informed and involved shareholders are more likely to achieve superior long-term performance than those without.

Pooling the resources of other like-minded funds creates a strong and representative shareholder voice and makes our company engagements more effective. We currently act on behalf of 42 clients and £188.9 billion* in assets under advice.

Hermes has one of the largest stewardship resources of any fund manager in the world. Our 26-person team includes industry executives, senior strategists, corporate governance and climate change experts, ex-fund managers and lawyers.

The depth and breadth of this resource reflects our philosophy that stewardship activities require an integrated and skilled approach. Intervention at senior management and board director level should be carried out by individuals with the right skills, experience and credibility. Making realistic and realisable demands of companies, informed by significant hands-on experience of business management and strategy setting is critical to the success of our engagements.

We have extensive experience of implementing the Principles for Responsible Investment (PRI) and various stewardship codes. Our chair Colin Melvin led the committee that drew up the original principles and we are actively engaged in a variety of workstreams through the PRI Clearinghouse. This insight enables us to help signatories in meeting the challenges of effective PRI implementation.

How does Hermes EOS work?

Our corporate, public policy and best practice engagement programmes aim to enhance and protect the value of our clients' investments and safeguard their reputations. We measure and monitor progress on all engagements, setting clear objectives and specific milestones for our most intensive engagements. In selecting companies for engagement, we take account of their environmental, social and governance risks, their ability to create long-term shareholder value and the prospects for engagement success.

The Hermes Responsible Ownership Principles¹ set out our fundamental expectations of companies in which our clients invest. These cover business strategy, communications, financial structure, governance and management of social, ethical and environmental risks. The engagement programme we have agreed with our clients, as well as the Principles and their regional iterations, guide our intervention with companies throughout the world. Our approach is pragmatic, company- and market-specific, taking into account the circumstances of each company.

We escalate the intensity of our engagement with companies over time, depending on the nature of the challenges they face and the attitude of the board towards our dialogue. Some engagements involve one or two meetings over a period of months, others are more complex and entail multiple meetings with different board members over several years.

At any one time around 360 companies are included within our core engagement programmes. All of our engagements are undertaken subject to a rigorous initial assessment and ongoing review process to ensure that we focus our efforts where they can add most value for our clients.

While we can be robust in our dealings with companies, the aim is to deliver value for clients, not to seek headlines through campaigns, which could undermine the trust that would otherwise exist between a company and its owners. We are honest and open with companies about the nature of our discussions and aim to keep these private. Not only has this proven to be the most effective way to bring about change, it also acts as a protection to our clients, so that their positions will not be misrepresented in the media.

For these reasons, this public report contains few specific details of our interactions with companies. Rather it explains some of the most important issues relevant to responsible owners and outlines our activities in these areas.

We would be delighted to discuss Hermes EOS with you in greater detail.

For further information please contact:

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* as of 30 June 2016

¹ <https://www.hermes-investment.com/wp-content/uploads/2015/09/the-hermes-ownership-principles.pdf>

Hermes EOS team

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Engagement professionals



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Alan Fitzpatrick
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Rochelle Giugni
Client Relations



Bram Houtenbos
Voting and Engagement
Support



Amy Lunn
Head of Business and
Client Development



Nina Röhrbein
Reporting and
Communications



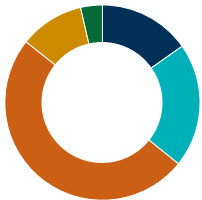
Lucy Saville
Client Relations

Engagement by region

Over the last quarter we engaged with 298 companies on 579 environmental, social, governance and business strategy issues. Our holistic approach to engagement means that we typically engage with companies on more than one issue simultaneously. The engagements included in these figures are in addition to our discussions with companies around voting matters.

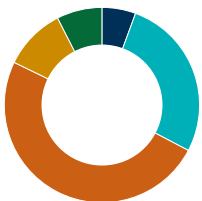
Global

We engaged with **298** companies over the last quarter.



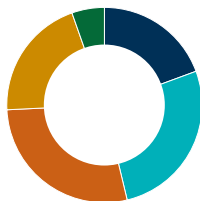
Developed Asia

We engaged with **39** companies over the last quarter.



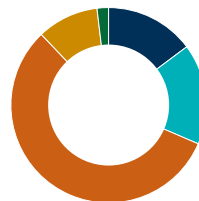
Emerging and Frontier Markets

We engaged with **40** companies over the last quarter.



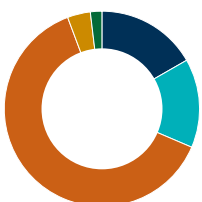
Europe

We engaged with **62** companies over the last quarter.



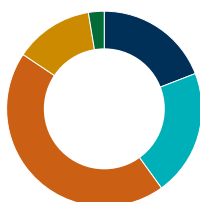
North America

We engaged with **97** companies over the last quarter.



United Kingdom

We engaged with **60** companies over the last quarter.

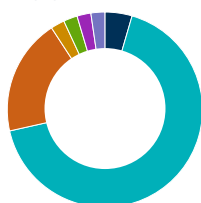


Engagement by issue

A summary of the 579 issues on which we engaged with companies over the last quarter is shown below.

Environmental

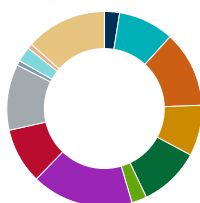
Environmental issues featured in **15.2%** of our engagements over the last quarter.



- Biodiversity **4.5%**
- Climate change/carbon intensity **67.0%**
- Environmental management **19.3%**
- Forestry **2.3%**
- Oil sands **2.3%**
- Waste **2.3%**
- Water stress **2.3%**

Social and ethical

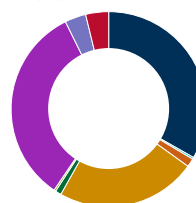
Social issues featured in **20.6%** of our engagements over the last quarter.



- Access to medicine **2.5%**
- Bribery and corruption **9.2%**
- Community relations **12.6%**
- Corporate culture **8.4%**
- Customer relations **10.1%**
- Diversity **2.5%**
- Health and safety **16.8%**
- Labour rights/employee relations **9.2%**
- Licence to operate **10.9%**
- Munitions manufacture **0.8%**
- Operations in troubled regions **2.5%**
- Political risk management **0.8%**
- Supply chain management **13.4%**

Governance

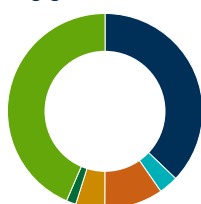
Governance issues featured in **49.9%** of our engagements over the last quarter.



- Board structure **33.2%**
- Committee structure **0.3%**
- Conflicts of interest **1.4%**
- Other governance **23.2%**
- Poison pill **1.0%**
- Related-party transactions **0.3%**
- Remuneration **33.2%**
- Separation of chair/CEO **3.5%**
- Succession planning **3.8%**

Strategy and risk

Strategy and risk issues featured in **10.7%** of our engagements over the last quarter.



- Business strategy **37.1%**
- Capital structure **3.2%**
- Reporting/disclosure **9.7%**
- Reputational risk **4.8%**
- Returns to shareholders **1.6%**
- Risk management **43.5%**

Stewardship

Stewardship issues featured in **3.6%** of our engagements over the last quarter.



- Accounting or auditing issues **19.0%**
- Shareholder communications **66.7%**
- Shareholder rights **14.3%**



Fighting fires – Pushing for sustainable palm oil production

In our longstanding engagement with producers of palm oil, we have pressed them to adopt sustainable business practices. We have also engaged with some of their customers on the issue.



As local regulators have been slow to date to introduce strict legislation on palm oil, in our engagement, we have urged companies to produce and sell only sustainable palm oil and to follow best practice guidelines. To mitigate reputational risk, we have also encouraged their customers to buy from companies producing sustainable palm oil.

Certification

In 2004, the Roundtable for Sustainable Palm Oil (RSPO), a multi-stakeholder forum, which includes palm oil producers, NGOs and banks, was set up with the aim of promoting the growth and use of sustainable palm oil products. It offers a certification scheme for growers to prove that their palm oil is produced in a sustainable manner. Producers are required to meet a number of criteria on environmental impact, including on biodiversity and carbon emissions, as well as on social matters, for example the rights of workers and local communities. However, to date approximately only 21% of global palm oil is RSPO-certified and questions have been raised about the RSPO's work and robustness of its certification criteria, for example that it does not take into account greenhouse gas emissions and that certification does not guarantee that the palm oil in a product is deforestation- or exploitation-free. Nevertheless, we believe that the organisation has helped raise awareness about the challenges of palm oil production and made meaningful changes to the way the industry operates.

If any RSPO members are negligent in their plantations, they face expulsion from the certification group. While a recently expelled member continues to sell crude palm oil without RSPO certification, several major global companies have stopped buying from it and it was placed on review for downgrade by credit ratings agency Moody's.

Setting the scene

Palm oil is a versatile commodity that can be found in everyday products from chocolate to shampoo. It is the world's most widely used vegetable oil, accounting for 65% of all vegetable oil traded internationally, according to WWF. The efficient crop produces the most edible oil per hectare of land² and so has proven profitable for its cultivators, which is why the palm oil plantation business has been expanding rapidly.

However, the development of palm oil, the vast majority of which is produced in Malaysia and Indonesia, has been accompanied by controversies. While in Malaysia the business expanded largely by converting former rubber plantations to ones growing palm oil, in Indonesia the development of palm oil plantations has involved the destruction of primary forest of native tree species. Palm-oil producing companies and small-scale farmers have been accused by NGOs and other organisations of starting fires deliberately to clear existing vegetation to make room for new palm oil plantations. The fires have become so widespread they are known as the Southeast Asian haze. In addition, producers have allegedly been involved in land-grabbing and disputes with local communities when developing new plantations. Others have faced accusations of poor working practices in and a lack of oversight of their supply chains. However, the industry also provides significant employment to local people, as well as infrastructure.

As companies were not certified when we began our dialogue on sustainable palm oil, we set objectives on RSPO certification. We are pleased that since our engagements started, the Malaysian palm oil plantations of companies we have had dialogue with and some of whose operations we were able to visit, have obtained 100% RSPO certification. However, due to land registry disputes or technical issues, full certification has been more difficult to achieve in Indonesia.

Sustainable Palm Oil Manifesto

Furthermore, pressure from asset owners and investor representatives like ourselves contributed to the Sustainable Palm Oil Manifesto, which launched in 2014 and aims to build on the existing sustainability commitments of RSPO signatories.

The manifesto seeks to achieve common objectives held by key stakeholders in the palm oil industry, such as growers, traders, processors and end-users, to ensure sustainability in the entire chain from cultivation to consumption. It commits palm oil producers and traders to refrain from deforestation of high carbon stock (HCS) forest, as defined by a study, to create traceable and transparent supply chains and to protect highly fertile peat areas. The manifesto also requires companies to ensure continuous positive economic and social benefits for the local communities living near palm oil plantations. Signatories have to prepare their own time-bound plan to implement these principles within 12 months of signing but are free to adopt a reasonable timeframe to achieve their objectives. They also have to publish their time-bound plans and file regular progress reports.

Progress in selected engagements

As a result of the pressure from investors and customers, as well as the above-mentioned initiatives, in our engagement with companies on sustainable palm oil, we have witnessed significant progress.

Golden Agri-Resources

In 2009, a report by Greenpeace alleged that Southeast Asian palm oil giant Golden Agri-Resources (GAR) was contributing to large-scale deforestation in Indonesia, where it owns nearly 500,000 hectares. This resulted in a number of its customers, including Unilever, Nestlé, Kraft and Burger King cancelling their contracts. Although they made up less than 3% of GAR's revenue, the incident tarnished the company's reputation.

We commenced engagement with GAR in 2009. We focused on the objective of ensuring RSPO certification for all of its palm oil and on putting together a credible strategy to address wider sustainability allegations, including the setting of stretching targets. We also pressed GAR to dedicate more resources to the issue of sustainable palm oil.

In 2010, the company committed to certifying all of its plantations to RSPO standard by 2015. A year later, it developed a forest conservation policy to ensure sustainable growth and gained RSPO membership. It also worked with Greenpeace and The Forest Trust on a different version of HCS, which classifies land and sets out which vegetation types have more or less carbon content than a plantation. This helps identify where palm oil development would contribute to carbon storage. In addition to these commitments, GAR pledged to oversee a wider cultural change in its attitude to environmental sustainability. This included ensuring that its lead independent director would oversee environmental and social risks and that the company's environmental commitment would be driven by a culture of awareness of the importance of sustainability at the board level. The company also nominated an executive director responsible for sustainability issues to enhance the board's reporting. Unilever and Nestlé resumed buying from GAR in 2011.

In 2012, we conducted a site visit to GAR plantations in the Riau region of Indonesia to inspect its methods of consultation with the local community and management of impacts on carbon emissions, as well as to assess whether its commitment to full RSPO certification by 2015 was sufficiently stretching. Following the visit, we engaged the company's senior independent director to urge the board to publish a time-bound action plan for implementation of its sustainability strategy. GAR understood the importance of demonstrating its commitment to sustainability and agreed to strengthen its standard operating procedures on sustainability matters.

We continue to monitor the company as it has begun palm oil operations in Africa, which raises new challenges and requires different approaches to be developed beyond those in Asia.

Kuala Lumpur Kepong

Our engagement with Malaysian multi-national Kuala Lumpur Kepong (KLK) was sparked in 2012 by allegations of illegal logging of an Indonesian peat forest in violation of a two-year moratorium by one of its subsidiaries. In addition, a contractor of KLK was accused of operating slave labour-like conditions at its palm plantations, allegations which KLK has denied. The company has also been accused of failing to respect the rights of community groups in Papua New Guinea and Liberia.

Throughout our engagement, we have pressed the company to implement better labour standards in its supply chain. While denying the allegations of labour abuses by one of its contractors, KLK confirmed that it had terminated its contract with the contractor concerned and provided us with a document intended for its customers explaining its labour practices. We welcomed its efforts to reduce the use of contract workers, improve communications with customers and engage with NGOs. We were also encouraged by the significant amount of time the board spent discussing these issues and the visits to the estates by directors to gain first-hand experience. However,

we noted the company's lack of public disclosure of this and other sustainability issues and urged it to publish a policy commitment, highlighting the significance of reputational risks facing palm oil producers. We continued our discussion on its progress in obtaining RSPO certification for all of its plantations, to ensure that the company was on track to meet its targets.

In 2014, the company became a signatory to the Sustainable Palm Oil Manifesto. This was followed by an announcement that the signatory companies would halt development of potential HCS areas while the HCS study was underway. In addition, KLK obtained RSPO certification for all of its plantations and mills in Malaysia and is working on meeting this target for Indonesia. We welcomed the publication of the company's first sustainability policy and its intention to engage with its contractors and suppliers to ensure their adherence to the policy. Furthermore, KLK has vastly improved its reporting, including the disclosure of fires within its plantations.

Public policy engagement

While we have seen improvements at the company level, it is important not to forget the role governments can play. By creating legislation and supporting a change in farming of smallholders, they can pave the way to sustainable palm oil production. As part of our engagement, we jointly signed a letter to the Indonesian government calling on it to make sustainable palm oil practices compulsory. As part of the collaborative engagement on palm oil led by the Principles for Responsible Investment, we have met indigenous community representatives from tropical forests in Indonesia, Colombia, Peru and Liberia, to listen to their concerns – related to land-grabbing, human rights violations, deforestation and contamination of land and water – and investigate their claims further.

Ongoing challenges

However, challenges remain. One of the biggest is the oversight and control of small-scale farmers who often work on concessionary lands of global companies. These smallholders typically supply local customers who may not be interested in sourcing palm oil in a sustainable manner and lack investors who could pressure them on sustainability. This makes it difficult for them to see the potential economic benefits of producing sustainable palm oil. Large companies may have zero burning policies in place but smallholders on concessionary lands can still choose to ignore these.

We continue to engage with large palm oil producers to seek their help in extending best practice to smallholders, while putting pressure on the regulators to raise industry standards. We urge the laggards in the industry to catch up with its leaders and push to ensure that the companies in our engagement programme achieve full RSPO certification in Indonesia. Furthermore, we engage with the companies to ensure that they apply best practice standards in new sourcing markets where they expand their palm oil activities, such as Africa and Latin America.

For further information, please contact:



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2 Sustainable path: Who is leading palm-oil reform?, CLSA Blue Books 2016



Safety first – Update on supply chain management in Bangladesh

We have been engaging with garment retailers for stronger labour standards and supply chain management in Bangladesh and beyond.



Progress

After the 2013 Rana Plaza disaster in Bangladesh, the primary aim of retail companies and their stakeholders was to improve health and safety standards in the garment manufacturing sector.

Immediate structural safety issues, such as the provision of escape routes and exit doors in factories, negligence of which has led to companies being fined in the past, have now been addressed by the companies we have been engaging with. However, the rate of progress when looking at all outstanding remediation required ahead of the expiry of the Alliance for Bangladesh Worker Safety (Alliance) and the Bangladesh Accord on Fire and Building Safety (Accord) in 2018 has been slower than expected.

Commonly cited obstacles include the limited availability of certified specialists, such as engineers, and delays in obtaining materials and equipment such as fire doors, although we understand from the Accord that these are being overcome.

Oversight

In our engagement, we have pushed for oversight of sustainability risks in supply chains by retail companies and their boards through ambitious targets and tracking of progress at the group level.

Setting the scene

It has been over three years since the eight-storey Rana Plaza building in Bangladesh's capital Dhaka collapsed, taking with it the lives of over 1,100 garment workers that were on its premises producing clothes for global retailers. In its wake, two initiatives were set up, the Alliance for Bangladesh Worker Safety (Alliance), which was founded by North American retailers and brands, and the Bangladesh Accord on Fire and Building Safety (Accord), which has mainly Asian, Australian and European company signatories. Both initiatives set out binding, five-year undertakings that aim to improve safety in ready-made garment factories in the country through inspections and audits.

On the third anniversary of the collapse of the Rana Plaza building, we signed a joint investor statement addressed to companies that are members of the Alliance and Accord. While acknowledging the positive steps taken towards improving the safety of workers, the statement highlighted remaining concerns about the pace of progress in addressing systemic issues and called for further action from international brands. This includes the provision of financial support to suppliers where appropriate, the establishment of independent safety committees in factories to sustain improvements that have been made and the public disclosure of factories in their supply chains.

We visited a number of international brands, their suppliers and other stakeholders in Bangladesh in late 2014 to understand the issues on the ground. Three years on from the accident, we reflect on what has been happening in the sector and how the focus of our engagement with companies has shifted.

We are therefore pleased that advances have been made in the transparency of supply chains. Several companies in our engagement programme have completed the mapping of their supply chains through to tier 2 and 3 suppliers, covering ancillary processes such as washing and dyeing, as well as fabric mills.

Encouragingly, some retailers have gone beyond the requirements of the Accord and Alliance and undertaken their own auditing and structural surveys of all their suppliers, including those for which they are not the lead buyer.

Positive steps have also been taken by some retailers in response to the refugee crisis in Europe and the Middle East. Refugees entering the supply chain illegally are vulnerable to exploitation, which is why some retail companies have been working with local NGOs and auditors to identify and redress instances and provide disclosure on this matter.

Workers' rights

In view of the improvements in structural safety and oversight, our engagement focus has shifted to the rights of workers in supply chains and how the dynamics between suppliers and brands can be improved to sustain and encourage best practices.

As unions have traditionally been largely absent from Bangladesh, we have pushed for the rights of workers to organise and represent themselves collectively. Our 2014 visit to the country had given us concern about how effectively worker participation committees were functioning in factories, which we fed back to the retail companies we spent time with and called for further action on.

A couple of companies have since signed agreements with global unions to provide more effective support to workers and their representatives, such as negotiation training. However, we also want to see improvements in factory human resource processes, including the training of supervisors and the introduction of meaningful metrics which provide insights into the management of workers.

Productivity

Another significant issue in the supply chain has been the poor productivity of workers, in other words the output per employee. During our 2014 visit, two of the retail brands we met told us that productivity is lower in Bangladesh than in their other sourcing markets, in part due to faults in the production of garments.

Efforts by some retailers to increase wages indicate that this can enhance productivity, with trials finding that output and efficiency increase, while costs associated with employee turnover decrease due to investment in the training of workers, as well as supervisors, on management practices.

Order volatility also remains one of the biggest pressures on suppliers and in our engagements, we urge brands to address volatile buying practices and insecure short-term relationships.

Longer-term planning can provide suppliers with the certainty to invest in employee and processes, driving standards, while also offering more competitive pricing to buyers. Recognising this Swedish, multi-national retailer H&M is committing to five-year agreements with suppliers that perform highly on sustainability and to three-year plans for the next tier. We will continue to monitor H&M's progress in this area and encourage other brands to improve their buying practices.

Trying to address labour standards in its Bangladesh supply chain may have also led US retailer Wal-Mart to improve human capital management across its business, increasing the pay of many of its store staff and investing substantially in staff training and career development.

Reporting

In our engagements, we encourage companies to adopt the UN Guiding Principles on Business and Human Rights Reporting Framework in order to effectively communicate how they manage human rights impacts, ranging from child labour to women's rights and workplace harassment. We supported the development of the principles through our participation in the Shift Project. Speaking on a panel with several companies we engage with at an EU conference on human rights, we were pleased to hear about the benefits of the framework as an internal management tool, which supports their engagement with investors and other stakeholders. We called for consistency in the implementation and guidance of non-financial reporting across different markets, including on human rights, while cautioning against a too prescriptive focus on common metrics or data points. In our experience human rights impacts vary greatly between companies, sectors and geographies and so we suggested that companies should have the flexibility to report meaningfully and qualitatively on the risks and impacts most salient to their operations.

We have also supported the development of the Corporate Human Rights Benchmark which ranks the top 500 companies globally on the basis of their human rights risk management and disclosure. This complements a number of other initiatives seeking to drive transparency and better performance on social issues, such as the Modern Slavery Act in the UK, the above-mentioned UN Guiding Principles reporting framework, the EU directive on non-financial

reporting and the US Business Supply Chain Transparency on Trafficking and Slavery Act. We believe that the benchmark can encourage the provision of better quality and comparable information from companies to inform our engagement with and assessment of them, as well as incentivising businesses to adopt best practices from peers.

New market challenge

A key test of companies' progress is the extent to which they embed best practices in new sourcing markets and apply the lessons learned from their experience in Bangladesh and elsewhere. In Myanmar, for example, several companies entering the country have petitioned the government to introduce a living wage for the textile industry, in a demonstration of their commitment to staying there.

We will explore this issue with companies considering or already sourcing from this market and seek to visit factories on the ground at some point in the future.

We will also focus our engagement increasingly on the environmental challenges facing factories in the supply chain, such as water and waste management, as well as parts of the supply chain previously not scrutinised, such as tanneries.

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Money talks – Reforming executive remuneration

In our engagements with companies across sectors and regions, we continue to push for reforms to executive pay.

FTSE 100 CEO received to average employee 2002 – 2014

| Year | CEO total remuneration received as multiple of average employee earnings | Shareholder voting % dissent (abstain + oppose) on remuneration |
|------|--|---|
| 2002 | 69.51 | 16.19 |
| 2003 | 77.08 | 12.83 |
| 2004 | 94.16 | 7.38 |
| 2005 | 97.62 | 5.19 |
| 2006 | 98.75 | 6.08 |
| 2007 | 139.16 | 7.14 |
| 2008 | 124.32 | 10.06 |
| 2009 | 151.68 | 9.38 |
| 2010 | 132.22 | 9.07 |
| 2011 | 117.50 | 11.34 |
| 2012 | 114.35 | 7.55 |
| 2013 | 125.38 | 9.08 |
| 2014 | 149.58 | 8.38 |

Source: Manifest, High Pay Centre 'Pay ratios – Just do it'
<http://highpaycentre.org/pubs/pay-ratios-just-do-it>

The annual bonus and long-term incentive plans of executives typically pay many multiples of their base salary, even in years where companies underperform. Often the root cause of overly generous pay and reward for failure lies in the remuneration policies of companies which are supposed to align the remuneration of the CEO with the performance of the company he or she is leading. Executive pay plans have become increasingly – and unnecessarily – complex and difficult to understand even for members of remuneration committees. At the same time, remuneration committees have mostly failed to fulfil their responsibilities by using their discretion to reign in ever-increasing pay awards.

Voting season 2016

In the 2016 voting season, similar to 2012, a large number of shareholders opposed the pay policies and reports of companies and called for reforms, reflecting the public anger to high levels of pay. We at Hermes EOS played a part in this, by complementing our

Setting the scene

In 2012, UK companies found themselves caught up in the so-called shareholder spring. Unhappy with what they perceived to be excessive amounts of executive pay or packages that were too complex or out of sync with the economic climate and value creation, shareholders started voicing their frustration by voting more frequently against remuneration reports at company AGMs.

The shareholder spring was perceived to be a game-changer. In the UK, it led to new legislation in 2013, resulting in a binding vote on a company's pay policy by shareholders at least every three years. Together with the Pensions and Lifetime Savings Association, the BT Pension Scheme, Railpen Investments and the Universities Superannuation Scheme, Hermes EOS developed a set of remuneration principles for executives in the aftermath of the shareholder spring.³

However, the impact of the 2012 shareholder spring turned out to be short-lived and executive pay has continued to increase, particularly in comparison with the rest of the workforce [see table]. Often this has led to higher levels of remuneration for average performance and reward for failure. To the ultimate beneficiary of institutional investors this trend has been difficult to justify and frustration about the widening pay gap and related divisions in society may have contributed to the decision made by UK voters to leave the EU.

engagement on high pay with votes against management proposals on remuneration.

Although remuneration frameworks vary by country – most notably with regard to disclosure, pay caps and, crucially, the existence and legal effect of shareholder votes on pay policies and reports – and concerns differ accordingly, several trends have stood out this voting season.

First, we observed the misalignment of executive pay to the experience of shareholders and creation of long-term value. Due to the downturn in the commodities sector, this applied especially to extractives companies, such as Anglo American and BP, and those providing goods or services to the industry, such as Weir Group. Secondly, we witnessed the overuse of discretion upwards by remuneration committees when it should not be used or lack of discretion when it needed to be applied, for instance where quantum is already large. We, for example, opposed the pay package at Tullow Oil for failure to use discretion downwards in a year, which, in our view, displayed poor performance. In addition, we recommended voting against remuneration policies where the assessment and stress-testing of pay packages and policies by remuneration committees was in our view flawed and quantum was inappropriate and unacceptable to us.

One of the most controversial votes cast against in the 2016 voting season was at the AGM of UK multinational advertising agency WPP, with which we have a longstanding engagement on independent board leadership, succession planning and the responsibilities of its remuneration committee. The proposed £70 million pay package for 2015 has to date been the second-highest pay package ever received by a FTSE CEO. The large quantum could primarily be attributed to a legacy equity incentive plan introduced in 2009 which is to be phased out in 2017. However, while we appreciate that the quantum was primarily a result of the company's strong performance in recent years, we had historic concerns about board composition and the remuneration committee's apparent lack of vigour and stress-

testing when the legacy plan was devised. We urged the chair of the remuneration committee to draw the right lessons from this controversy when developing a new remuneration policy in 2017 and, like last year, opposed the proposed pay package for assessment and quantum reasons.

Another highlight of the voting season was the AGM of Deutsche Bank, where we commended the supervisory board for not paying any bonuses to the members of the management board in 2015. However, we were concerned about the significant increases in base salaries in recent years, the apparent lack of consultation on the proposed changes to the management board remuneration system, the inadequate transparency in relation to performance criteria and targets of the proposed division performance award, as well as the high level of discretion of the supervisory board with regard to variable remuneration. We were therefore part of the 51.9% of shareholders who opposed the new remuneration system.

Reform proposals

At the beginning of this year's AGM season, we issued additional guidance to clarify our expectations of remuneration committees. We highlighted that developing, thoroughly assessing and stress-testing, implementing and – if necessary – adjusting the outcomes of remuneration policies is the responsibility of remuneration committees – not of investors.⁴

To effectively discharge their stewardship role, remuneration committees must take a more robust view on pay.

They must improve their assessment and stress-testing of remuneration policies and the disclosure and communications of outcomes of different, even unlikely, scenarios. If their members are unable to do so, this suggests that remuneration policies have become far too complex and unnecessarily complicated. A simplification of remuneration policies and plans – which allows outcomes to be understood by investors, boards and executives – has thus become necessary. If remuneration committees do not understand the potential outcomes of a pay policy, or would struggle to rationalise proposed quantum, they should veto it. And if the actual outcomes of a policy cannot be explained convincingly to the average member of the public or implementation leads to results that contradict the underlying purpose of a remuneration policy, they should use their discretion to adjust them. At all times, they should use discretion to safeguard their company's reputation and social licence to operate in a given market.

Remuneration committees must also balance the desire to set some targets that can be controlled by executives with the need to ensure alignment of remuneration and long-term value creation. We have long argued that paying a significant part of remuneration to executives in shares and requiring them to hold these well beyond their tenure with companies is a natural starting point to ensure the desired alignment. In addition, remuneration committees must form a view on what they regard as appropriate and acceptable quantum for executives in different scenarios and clearly disclose and communicate this to shareholders. Shareholders can then take a view on this important matter.

Pay escalation is often linked to succession plans, as companies believe they can hold onto their CEO by paying excessive amounts to the individual. However, in our view the head of a company should not be purely incentivised by money, as this is neither in the interests of shareholders nor the company. At times this excuse has been used to increase pay when there was little chance of the CEO leaving. While we recognise that companies want to pay their CEOs more than their competitors, businesses need to realise that remuneration alone does not attract great talent. Ideally, some form of fairness test should be

applied to explain CEO pay and how it compares to the rest of the workforce and why it is justified.

In short, the objective of remuneration policy is no longer to attract, retain and motivate an individual but to pay what is necessary while rewarding delivery of great performance.

Stewardship

We believe that there is a significant appetite for change and urge companies to consider how they might align pay more closely with the interests of their long-term owners in order to position themselves best for future success.

The ownership chain should endeavour to understand and reflect the views and interests of the ultimate beneficiaries, including with respect to the question of what executive remuneration levels are acceptable. In the absence of direct involvement of beneficiaries, boards or trustees of asset owners could develop a clearer view on executive remuneration, including on quantum, and instruct their fund managers to communicate this to companies and exercise voting rights accordingly.

The conflicts asset managers can face, specifically when they are listed or are part of a financial group, ought to be addressed, for example through better disclosure on how published policies on executive remuneration can be implemented through voting at AGMs.

Fresh thinking

To address inequalities and the rise in quantum, pay ratios, which will come into effect for US companies in 2018, should also be considered. Under the rule adopted by the US Securities and Exchange Commission as required by the Dodd-Frank Act, large companies will have to disclose how salaries at the top compare to their median compensation level for employees worldwide.

Furthermore, pay-for-performance ought to be disentangled, in other words it has to be clearly defined as to whether it is about individual or company performance.

Engagement and voting

However, engagement reinforced by voting is likely to be the most effective means of bringing about positive change when it comes to remuneration. With another round of binding shareholder votes on pay policies taking place in the UK in 2017, we will continue our intensive engagement on remuneration for the remainder of 2016.

We seek to support companies and their directors embracing change as we believe pay arrangements that reward long-term value creation instead of average performance – and are acceptable within the wider society – are in the interests of companies and their investors.

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³ <https://www.hermes-investment.com/wp-content/uploads/2016/03/Remuneration-Principles-PLSA-NAPF-March-2016-update.pdf>

⁴ <https://www.hermes-investment.com/ukw/blog/2016/04/21/executive-remuneration-in-the-spotlight/>



Aiming for change – Stewardship in the mining sector

In our engagement with mining companies, we focus on a variety of issues, ranging from climate change to health and safety and governance.



Disclosure of climate change risks

Mitigating the risks mining companies face from climate change has been a core part of our engagements with companies. We have focused on improving corporate reporting of climate risks, setting an objective relating to the disclosure of asset portfolio resilience to climate change for several of the mining companies in our engagement programme.

We have asked companies to stress-test their portfolios – analysing their assets to see how they would perform in different circumstances – using recognised greenhouse gas emissions scenarios, such as those developed by the International Energy Agency. This includes analysis of their existing portfolios, as well as the new pipeline of products over a period to at least 2035. Furthermore, they should assess the impact of changes in demand for commodities on the supply curve and develop price implications before communicating the impact of the resulting scenarios qualitatively and quantitatively and describe their response to the scenarios and the implications for strategy.

One notable example has been the publication of climate change portfolio analysis by Anglo-Australian multinational mining company BHP Billiton in 2015. It set a welcome precedent in transparency by a

Setting the scene

Much of the world's higher grade mineral resources can be found in the more remote parts of developing nations, where there is frequently poor infrastructure and weak governance. Operators can therefore face significant local environmental and social risks. While best practices can help mitigate many of these risks, climate change presents a number of structural challenges that require a whole-business response. The first of these is the energy and therefore carbon-intensive nature of mining itself, which involves shifting large quantities of bulky materials, followed by their processing and smelting. The threat of carbon pricing is a significant business risk and mining companies must focus on energy efficiency and renewable energy solutions. The second threat is to the demand of the products, which often are the cause of emissions, such as coal, or which may be substituted by other, lower-carbon and lighter materials, for example aluminium for steel. The good news for mining companies is that while some commodities appear threatened by the move to a low-carbon economy, others should do better, such as copper, which supports better grid infrastructure and the electrification of transport, uranium, which is used in nuclear power generation and lithium and cobalt, which are used to make batteries for electric vehicles.

major company regarding preparedness for the challenges of climate change. The scenario-based analysis underpinning this publication was the result of a successful engagement by Hermes EOS in 2014. Somewhat reassuringly for investors, due to BHP Billiton's well-diversified portfolio, the work set out that even in a more extreme 2°C scenario with a cost of carbon of \$80/tonne – the latest cost of carbon in the EU emissions trading scheme was €5.60/tonne on 30 June 2016 – climate change is estimated to reduce the operating margins of the company over a 20-year period by approximately only 5%. While demand for some commodities is anticipated to fall in a lower-carbon economy, the company expects it to rise for others. We have used this precedent to encourage the company's peers to carry out a similar exercise.

Shareholder resolutions

As part of the Aiming for A coalition of investors, we filed climate change-related shareholder resolutions at oil and gas majors BP and Shell in 2015 in the belief that carefully crafted, supportive but stretching shareholder proposals can play a positive role in encouraging best practice during the transition to a low-carbon economy. Such resolutions also highlight the need to balance the short- and longer-term aspects of shareholder value creation. Throughout 2015, we raised the idea of filing similar resolutions on the disclosure of asset portfolio resilience to climate change with the chairs of three major diversified mining companies, namely Anglo American, Glencore and Rio Tinto, all of which are listed in London.

Board support increases the likelihood that a resolution will be passed and ensures management will be committed to implementing the resolution. While each chair indicated his informal personal backing during the engagement, formal board support could not be guaranteed. It was necessary to demonstrate the scale of long-term institutional investor support by meeting the required thresholds for co-filing required by company law.

The shareholder resolutions we recommended our clients to co-file asked for enhanced disclosure of the companies' approach to climate change risks, including management of operational greenhouse emissions, their strategic portfolio resilience to low-carbon scenarios,

research and development into low-carbon solutions, their public policy position on climate change, as well as their overarching corporate governance framework and link to key performance indicators.

Support

In the end, we successfully met the required thresholds by bringing together over 100 supportive institutional investors for the shareholder proposal submitted at Rio Tinto and 50 for the resolution at Jersey-based Glencore. We eventually also managed to pass the required 5% alternative threshold for the shareholder proposal at Anglo American. In total, investors responsible for more than \$8 trillion, including clients of Hermes EOS, were involved in filing the resolutions.

At the AGMs of the respective companies, the shareholder proposals received overwhelming support, namely 99% at Glencore, 98% at Rio Tinto and 96% at Anglo-American.

Anglo American committed to finalising energy efficiency targets at its AGM, following the restructuring of the business. It also agreed to carry out further analysis of the resilience of its principal commodities to low-carbon scenarios, as well as to explore the link between remuneration and climate change-related key performance indicators.

Rio Tinto meanwhile promised to work with institutional investors to explore new ways of analysing climate change risks.

With the shareholder resolutions all passed, we are now working with the companies to help define the nature of the additional disclosure required to meet the requirements of the shareholder resolutions, which ideally should be part of the strategy section of their annual reports, and give feedback on first drafts. Glencore has already published its view of the robustness of its business to low-carbon scenarios and committed to conducting this analysis on the basis of a 2°C scenario, which is particularly important given the company's relatively high exposure to thermal coal.

Public policy work

As part of our engagement, we collaborated with the Institutional Investors Group on Climate Change (IIGCC) to produce the document called Investor Expectations of Mining Companies – Digging deeper into carbon asset risk⁵ which outlines the approach and disclosure that investors expect of mining companies concerning climate change risks.

We are also working with the Task Force on Climate-related Financial Disclosures, set up by the chair of the Financial Stability Board, to establish guidelines for standardised risk disclosures by companies on climate change. This will help to increase the scope of reporting across more companies, as well as its comparability. It should also mean that we do not have to use the administratively cumbersome approach of using more shareholder resolutions to achieve the disclosure required by investors across the industry.

Social engagements

In addition to the focus on environmental issues over the last year, we continue to engage on social issues. This has entailed ensuring that during the cost-savings programmes introduced at many mining businesses following the downturn in commodities, companies are not cutting corners on health and safety, environmental protection and investment in their social licence to operate. It includes programmes on community relations, as tension with local communities can lead to significant reputational, operational and financial risks.

While acknowledging that fatalities are difficult to eliminate, in our engagements we have pushed for effective and culturally sensitive health and safety training and that systems and procedures are in place across all operations globally and audited and updated regularly. In general, we have seen health and safety standards improve across the sector, reflected in, for example, lower lost time injury frequency rates.

Good governance

We also continue to engage with mining companies on good governance. In the wake of the Bento Rodrigues dam disaster in Brazil in November 2015, where a dam burst as a result of mining operations by Samarco, a joint venture between BHP Billiton and Brazilian mining company Vale, we have stepped up our engagement efforts on the governance of joint venture-operated mines. Above all, we want to make sure that lessons are learned and applied to future mining operations across the industry.

So while the activities of mining companies naturally have an impact on the environment, locally and globally, as well as on communities living or working near mines, in our engagement we have pressed for better environmental, social and governance standards in their operations. We are pleased about the steps the mining companies have taken on climate change, for which we have helped pave the way, and will continue our engagements in that and other areas.

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⁵ http://www.iigcc.org/files/publication-files/IIGCC_2015_Mining_Report_FINAL_WEB.PDF



Engagement on strategy

Many of our most successful engagements include discussions on business strategy and structural governance issues.

Overview

We adopt a holistic approach to engagement, combining discussions on business strategy and risk management, including social, environmental and ethical risks, with structural governance issues. We challenge and support corporate management in their approach to the long-term future of the businesses they run, often when there is minimal outside pressure for change. We are generally most successful when we engage from a business perspective and present environmental, social and governance issues as risks to the company's strategic positioning. Companies may benefit from new perspectives on the board and from promoting fresh thinking at the head of the company. An independent chair or change of CEO is frequently the key to improving performance and creating long-term value for shareholders.

Examples of recent engagements

Board nomination process

Lead engager: Jaime Gornsztejn

In a meeting at the head office of an emerging markets company, we were encouraged by the positive development in the board nomination process. We commended the company for disclosing the board nominees for the first time in advance of its 2016 AGM and challenged its board composition and evolution, in line with our engagement objectives. Although three new independent directors have joined the board over the last three years, it still comprises three independent directors with tenures exceeding 20 years. The company sought to reassure us that it has formal procedures in place to verify the independence of these directors, consistent with the country's regulations, which does not set a limit on tenure. We shared with the company best practice in board evaluation and discussed the possible benefits to the group's effectiveness in discharging its duties resulting from such an assessment. The company was receptive to our engagement and we agreed to follow up with the board secretary. In a separate meeting, we were pleased to learn that the company has begun preparations to produce its first integrated report in 2017.

Climate change risk management

Lead engager: Natacha Dimitrijevic

We spoke at the AGM of an oil major on behalf of our clients and 10 other institutional investors who together have assets under management of over \$3 trillion. Following our intensive engagement with the company, which led to the publication of its climate change report at the shareholder meeting, we highlighted publicly the work it has undertaken on climate change to date and the quality of dialogue we have had with the company over the past year. We also outlined the remaining challenges on strategy, reporting and lobbying. In line with our constructive engagement, we had informed the company in advance of our intervention. The chair welcomed our approach and input in his main speech and in his response to our questions. Positively, he announced enhanced transparency on lobbying practices. In a subsequent meeting with the chair, we gained reassurance that the company is committed to addressing the risk of climate change by including renewables in its energy mix, allocating the appropriate capital and research and development expenditure.

Cyber security

Lead engager: Dominic Burke

A European company has made significant advances since our first conversation on data and cyber security in 2015, recognising the significant shift in emphasis from traditional sources of communications revenue to data and that its management of security concerns will be key to its future success. The company has appointed chief data and security officers with backgrounds in military intelligence and cyber security who, as members of the executive committees, report to the chair/CEO. We discussed the need to ensure non-executive directors develop sufficient knowledge to effectively challenge and oversee management in these areas. The company welcomed our suggestion that an independent director sit on the security committee with management. It also acknowledged the importance of planning for effective communication of cyber incidents with stakeholders as part of its incident response plan and explained that effective communication with clients on data matters is a priority during product and service development. We also challenged the company on its management of cyber security risk arising from its more than 12,000 suppliers and were reassured that additional security measures are contractually required from the small number of critical suppliers that have privileged access to the company's data and systems. On the related matter of protecting the human rights of customers when handling government data requests, the company was able to illustrate a clear legal process and from next year will publish a transparency report detailing the number of requests it receives by operating markets, something we have pushed for in line with many of its peers. The company also offered us a visit to its cyber security business.

Proxy access

Lead engager: Darren Brady

Through discussions with several senior representatives, we advanced our engagements with a US company seeking a robust proxy access right for long-term shareholders and a strengthening of the pay-for-performance relationship within executive compensation plans. Following intensive consultation with the company on how it should structure its proxy access policy over the past few months, we were pleased to learn that it has implemented our suggestions and approved a proxy access policy in line with our best practices guidance. While there are a few deviations made by the company that are appropriate to its individual circumstances, the resulting proxy access right is a meaningful enhancement to shareholder rights. We commended the company for its earnest engagement efforts and uptake of investor

feedback. We also challenged it on its executive remuneration practices. While we do not have major concerns with its pay practices, we have been pushing for a higher percentage of long-term awards to be based on objective performance criteria to strengthen the alignment of interests between executives and shareholders. The company informed us that from next year it will base at least 60% of its long-term awards on disclosed performance goals and enhance the transparency on how these targets are determined. We will continue to engage on this issue as it implements these enhancements. Furthermore, we questioned the company's attempts to promote gender pay equality among its staff and learned of significant efforts already underway. This gave us more than ample comfort to support management by not backing a shareholder proposal on this topic, as the company is already able to demonstrate robust action in this area.

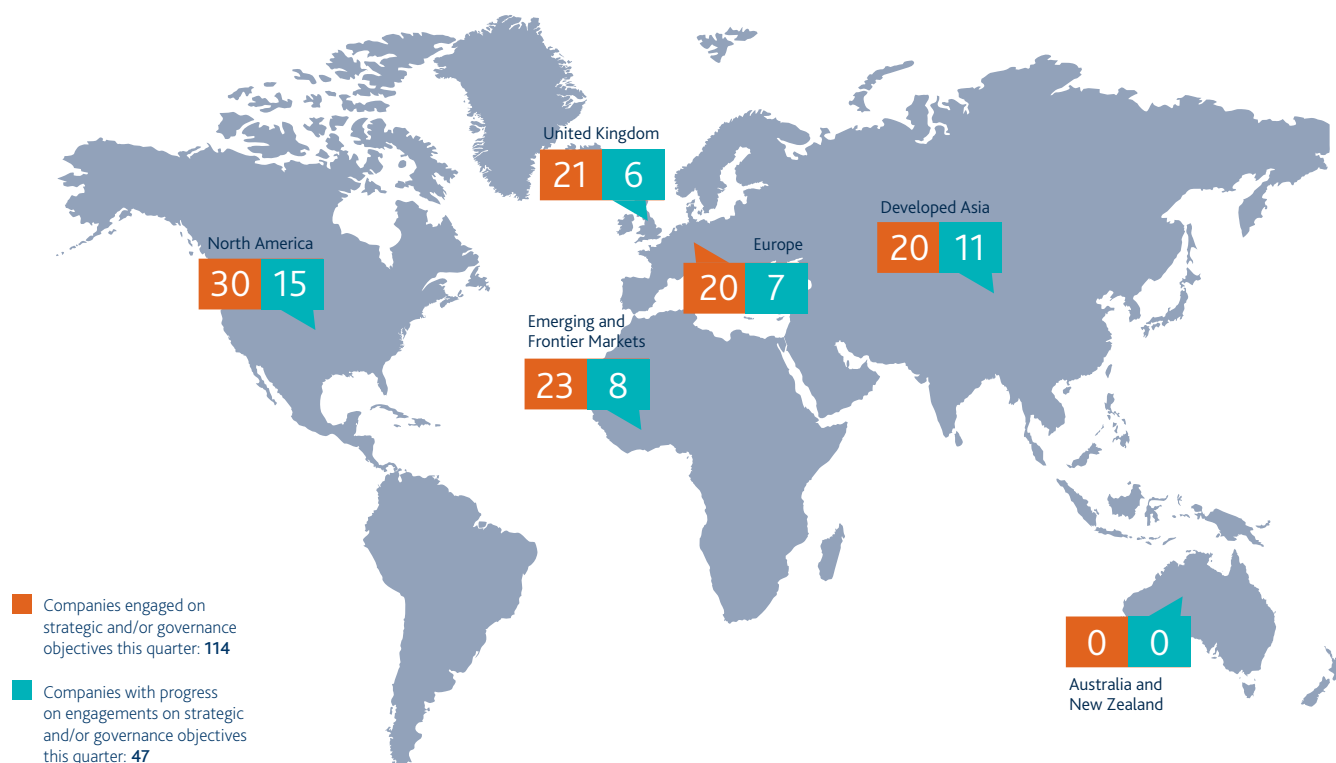
issues at its AGM. We requested a further meeting to discuss board leadership arrangements and the company's governance of political and lobbying donations, noting that we had voted by exception against the shareholder proposals on these issues. The board had discussed its governance of political and lobbying donations and while we believe that it has reasonable approaches in place, its disclosures could be improved. We subsequently participated in a survey organised by a consultant to the company in which we called on the company to focus on the issues that we see as most material to it, such as data protection, privacy and safe use of the internet and technology, reduction in its own environmental footprint and helping its customers with theirs, as well as human and labour rights within its own operations and supply chain.

Sustainability targets

Lead engager: Tim Goodman

The suggestions we made two years ago for a North American company to report on mid-term and long-term sustainability targets have directly influenced its sustainability programme and latest reporting, according to its sustainability head. This has in turn enabled us to progress our sustainability objective. Positively, two more of the company's longstanding directors are to step down in the next few months in line with what we have called for in our engagement on board composition. The general counsel provided a detailed account of how governance at the company functions, how the lead independent director is performing and how the committee chairs work together. He also described the company's processes for controlling its political and lobbying activity in light of two shareholder proposals on these

Engagements on strategy and/or governance





Public policy and best practice

Hermes EOS contributes to the development of policy and best practice on corporate governance, sustainability and shareholder rights to protect and enhance the value of its clients' shareholdings over the longer term.

Highlights

Climate deal signing ceremony

Lead engager: Tim Goodman

We were honoured to be invited to the signing ceremony of the 2015 Paris climate change agreement at the UN building in New York. It is a testament to the commitment of our clients and the work that we have done and continue to do in fighting the risks to the value of their portfolios from climate change that we were part of the small non-state delegation invited to witness the beginning of the agreement being put into formal legal effect. We intend to continue working vigorously to ensure that the agreement marks a significant milestone in the successful fight to limit climate change to 2°C. The fact that nation states and other actors are taking brave steps now, without waiting for a perfect solution to solve climate change, was evidence of the historic day.

Cyber risk

Lead engager: Dominic Burke

In the latest of our series of dinners with non-executive directors and clients, we discussed cyber risk with representatives from banking, pharmaceuticals and defence among other sectors. Board members said that while cyber security is distinctive due to the maliciousness of the threat, they, as well as investors, should not be overwhelmed by the technical nature of the topic. As well as assigning responsibility to senior executives, including chief information security officers, some companies have convened advisory committees of experts which can help boards evaluate and understand mitigation efforts. It was clear that collaboration within and across sectors is critical to developing best practice defences and that certain industries have benefited from government input, which others might learn from. As part of their preparation for incidents, companies must also consider a communications strategy, including identifying a suitable spokesperson who can articulate technical and business dimensions to stakeholders. We will adopt many of the key points in our engagements on cyber risk.

We were also the sole investor representative at a roundtable meeting of audit committee chairs to discuss cyber security. Participants shared

Overview

We actively participate in debates on public policy matters to protect and enhance value for our clients by improving shareholder rights and boosting protection for minority shareholders. This work extends across company law, which in many markets sets a basic foundation for shareholder rights, securities laws, which frame the operation of the markets and ensure that value creation is reflected in value for shareholders, and developing codes of best practice for governance, management of key risks and disclosure. In addition to this work on a country-specific basis, we address regulations with a global remit. Investment institutions are typically absent from public policy debates even though they can have a profound impact on shareholder value. Hermes EOS seeks to fill this gap. By playing a full role in shaping these standards we can ensure that they work in the interests of shareholders instead of being moulded to the narrow interests of other market participants – particularly companies, lawyers and accounting firms, which tend to be more active than investors in these debates – whose interests may be markedly different.

the view that the high-profile breach at TalkTalk in 2015 marked a sea change in the way their organisations deal with the issue, which is now recognised as a principal risk and matter for board-level oversight. Directors were concerned about the appropriate level of disclosure on cyber risk. We suggested that an appropriate starting point would be confirmation that a documented cyber security strategy has been signed off by the board, covering critical assets and access, clear senior level accountability, appraisal of supply chain risk, as well as investment in technical capabilities and culture awareness.

Executive pay

Lead engager: Bruce Duguid

We hosted a special meeting of the UK Corporate Governance Forum, which comprises corporate governance representatives of leading UK-based asset managers, to discuss potential new approaches to executive pay. The discussion was based on the interim proposals of the Investment Association's working group on remuneration. In relation to the new structures for remuneration proposed in the paper, many asset managers now support simplification, together with more reliance on higher long-term executive shareholding requirements to ensure alignment of interests. Support is growing for a structure that is based on a one-year bonus scheme with a significant proportion of the bonus being withheld for a number of years in the form of shares. There was appetite to also explore the granting of shares to executives either together with a moderated bonus scheme or even as an alternative to bonuses.

Proxy advisory legislation

Lead engager: Tim Goodman

We co-signed a letter from the Council of Institutional Investors (CII) addressed to the US Congress committee on financial services opposing proposed legislation which would constrain significantly the ability of proxy advisory firms to act on behalf of their clients in the US. The legislation, if passed, would likely have a powerful knock-on effect elsewhere in the world because of the size of the US capital market. To add heft to the letter, we encouraged our clients to sign the letter as well and the CII was grateful for our efforts to do so.

Other work in this quarter included

Promoting best practice

- We spoke with a representative of the **Access to Nutrition Index** which assesses and ranks the world's largest food and beverage manufacturers on their nutrition-related commitments, practices and performance globally. Following the launch of the 2016 Index, we expressed an interest in joining a collaborative initiative to push companies to take account of nutrition in their product formulation, pricing and distribution, as well as to encourage responsible marketing and labelling.
- At the quarterly **Aiming for A members** meeting, our contribution to help coordinate the mining sector climate change resolutions and lead the engagement at oil and gas majors was acknowledged by other members. Work is now underway to expand the Aiming for A coalition to some larger asset owners and managers in continental Europe. We seek to explore the potential for supportive but stretching resolutions at utilities and automotive players to reduce long-term risks and enhance the alignment with the move towards building a low-carbon economy.
- We participated in the launch of the **Corporate Human Rights Benchmark** which will rank the top 500 companies globally on the basis of their human rights risk management and disclosure. This complements a number of other initiatives seeking to drive transparency and better performance on social issues, such as the Modern Slavery Act in the UK, the UN Guiding Principles Reporting Framework and the EU non-financial reporting directive.
- At the UK launch of the next phase of the **ESG integration** initiative as part of the fiduciary duty project by the Principles for Responsible Investment and UNEP Finance Initiative, we promoted the role effective stewardship can play in asset owners – and asset managers as their agents – discharging their fiduciary responsibilities. We recognised the resource constraints of smaller funds in carrying out stewardship and explored different solutions, including industry consolidation, outsourcing of stewardship activities and participation in investor fora such as the UK's Investor Forum.
- We were one of the few investor representatives to participate in the **EU Roadmap to Business and Human Rights Conference**. We encouraged companies to adopt the UN Guiding Principles on Business and Human Rights Reporting Framework, the development of which we have supported, in order to effectively communicate how they manage human rights impacts.
- We had an initial meeting with the CEO and a senior researcher of the **High Pay Centre**, a not-for-profit research and lobbying association. We discussed some of the trends in executive remuneration, such as increasing CEO packages and an ever-widening pay gap, and their underlying reasons. We then focused on some of the potential solutions and the role of key stakeholders, such as investors and employees.
- We took part in a multi-stakeholder roundtable regarding the payment of **living wages in global supply chains**. There was consensus that progress in this area has been slow and we expressed interest in a collaborative initiative with other investors to address the challenges at an industry level.
- We participated in a call with **Malaysia's Institutional Investor Council** and provided final input into its main project for 2016, a practical corporate governance toolkit for companies, investors

and regulators. The outcome of the project seems well suited to provide at least a common starting point for dialogue between the key players. We are pleased to have made a contribution to this important project.

- In our consultation response to the **Task Force on Climate-related Financial Disclosures**, we explained that disclosure should seek to improve the understanding of climate risks. This means publishing the risks arising as the economy moves to lower carbon, together with the physical risk of climate change, as well as the low-carbon alignment, in other words the progress made and future plans to align value-creation with building a lower-carbon economy. We advocated companies use the Aiming for A framework which we have supported in our engagement with oil and gas and mining firms, including the results of a stress-test of the value and performance of each materially exposed investment to a range of climate change scenarios. We also advocated voluntary reporting by including investment intermediaries, such as asset managers reporting to their clients and, ultimately investors reporting to beneficiaries.
- We welcomed the idea by the **Tokyo Stock Exchange** to develop an online engagement platform for listed companies and shareholders and made suggestions for it to be beneficial for investors. As the current plan is to make participation voluntary, we expressed concerns that the platform might be of limited use to investors should only a small number of companies participate and encouraged the exchange to promote the benefits of the system to attract many joiners. We also highlighted the importance of gaining the full support from Japan's Financial Services Agency.

Public policy

- We lent our support to a bill being introduced in the US Congress that takes aim at the lack of transparency in relation to **corporate ownership in the US**. This includes convoluted ownership structures, opaque reporting and complex transactions, which can compromise good governance and raise red flags for investors. The bipartisan Incorporation Transparency and Law Enforcement Assistance Act would require US companies, with some exemptions, to disclose the individuals who own or control the businesses they incorporate and to keep that information up to date. Currently, in all 50 states companies can be created anonymously, effectively removing personal responsibility and accountability from the corporate equation.
- We co-signed the investor statement on climate change supporting the announcement by the US and Canadian governments to work together to reduce **methane emissions** in the oil and gas industry by 40-45% in the next decade. Target-setting like this is an important public policy initiative to tackle fugitive methane leaking into the atmosphere.
- We met the CEO of Stewardship Asia, the local think tank owned by one of the local sovereign wealth funds leading the development of **stewardship principles in Singapore**. A final draft of the principles was completed in 2015 by a working group, of which we are a member. However, the planned launch for the first quarter this year has been pushed back as the principles are under review by local regulators and major asset owners. We offered our support in the conversations taking place but it seems that any remaining issues need to be resolved locally. A launch is still likely this year.

Hermes EOS makes voting recommendations at general meetings wherever practicable. We take a graduated approach and base our recommendations on annual report disclosures, discussion with the company and independent analyses. At larger companies and those where clients have significant interest, we seek to have dialogue before recommending a vote against or abstention on any resolution.

In most cases of a vote against at a company in which our clients have a significant holding or interest, we follow up with a letter explaining our clients' concerns. We maintain records of voting and contact with companies, and we include the company in our main engagement programme, if we believe further intervention is merited.



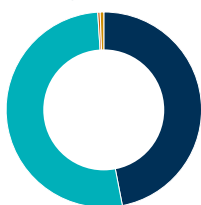
Hermes EOS makes voting recommendations at companies all over the world, wherever its clients own shares.

Overview

Over the last quarter we made voting recommendations at 6,006 meetings (69,056 resolutions). At 3,127 of those meetings, we recommended opposing one or more resolutions. We recommended voting with management by exception at 35 meetings and abstaining at 24 meetings. We supported management on all resolutions at the remaining 2,820 meetings.

Global

We made voting recommendations at **6,006** meetings (**69,056** resolutions) over the last quarter.



- Total meetings in favour **47.0%**
- Meetings against (or against AND abstain) **52.1%**
- Meetings abstained **0.4%**
- Meetings with management by exception **0.6%**

Australia and New Zealand

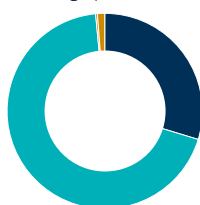
We made voting recommendations at **47** meetings (**220** resolutions) over the last quarter.



- Total meetings in favour **74.5%**
- Meetings against (or against AND abstain) **25.5%**

Developed Asia

We made voting recommendations at **1,019** meetings (**11,940** resolutions) over the last quarter.



- Total meetings in favour **29.7%**
- Meetings against (or against AND abstain) **68.8%**
- Meetings abstained **0.3%**
- Meetings with management by exception **1.2%**

Emerging and Frontier Markets

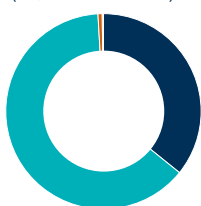
We made voting recommendations at **1,134** meetings (**11,618** resolutions) over the last quarter.



- Total meetings in favour **45.4%**
- Meetings against (or against AND abstain) **54.5%**
- Meetings with management by exception **0.1%**

Europe

We made voting recommendations at **908** meetings (**13,507** resolutions) over the last quarter.



- Total meetings in favour **35.8%**
- Meetings against (or against AND abstain) **63.3%**
- Meetings abstained **0.7%**
- Meetings with management by exception **0.2%**

North America

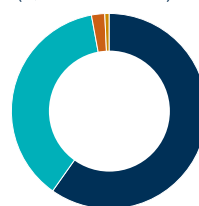
We made voting recommendations at **2,450** meetings (**25,209** resolutions) over the last quarter.



- Total meetings in favour **56.1%**
- Meetings against (or against AND abstain) **43.0%**
- Meetings abstained **0.2%**
- Meetings with management by exception **0.7%**

United Kingdom

We made voting recommendations at **448** meetings (**6,562** resolutions) over the last quarter.

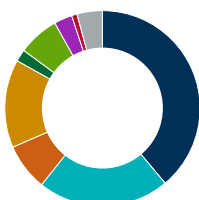


- Total meetings in favour **59.8%**
- Meetings against (or against AND abstain) **37.3%**
- Meetings abstained **2.2%**
- Meetings with management by exception **0.7%**

The issues on which we recommended voted against management or abstaining on resolutions are shown below.

Global

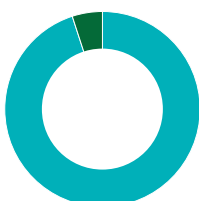
We recommended voting against or abstaining on 7,889 resolutions over the last quarter.



- Board structure 38.9%
- Remuneration 21.8%
- Shareholder resolution 7.8%
- Capital structure and dividends 14.6%
- Amend articles 2.0%
- Audit and accounts 6.8%
- Governance 3.0%
- Poison pill/Anti-takeover device 0.9%
- Other 4.2%

Australia and New Zealand

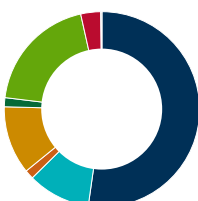
We recommended voting against or abstaining on 20 resolutions over the last quarter.



- Remuneration 95.0%
- Amend articles 5.0%

Developed Asia

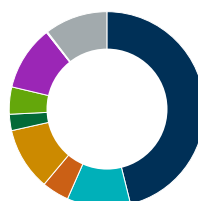
We recommended voting against or abstaining on 1,651 resolutions over the last quarter.



- Board structure 52.3%
- Remuneration 10.4%
- Shareholder resolution 1.5%
- Capital structure and dividends 11.3%
- Amend articles 1.5%
- Audit and accounts 19.6%
- Poison pill/Anti-takeover device 3.3%
- Other 0.2%

Emerging and Frontier Markets

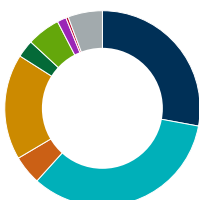
We recommended voting against or abstaining on 1,650 resolutions over the last quarter.



- Board structure 46.1%
- Remuneration 10.5%
- Shareholder resolution 4.5%
- Capital structure and dividends 10.4%
- Amend articles 2.7%
- Audit and accounts 4.5%
- Governance 10.7%
- Investment/M&A 0.1%
- Poison pill/Anti-takeover device 0.1%
- Other 10.4%

Europe

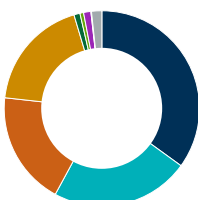
We recommended voting against or abstaining on 2,089 resolutions over the last quarter.



- Board structure 27.9%
- Remuneration 33.8%
- Shareholder resolution 4.8%
- Capital structure and dividends 17.5%
- Amend articles 2.9%
- Audit and accounts 5.5%
- Governance 1.5%
- Poison pill/Anti-takeover device 0.4%
- Other 5.7%

North America

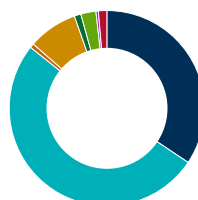
We recommended voting against or abstaining on 2,197 resolutions over the last quarter.



- Board structure 34.9%
- Remuneration 22.9%
- Shareholder resolution 18.8%
- Capital structure and dividends 18.6%
- Amend articles 1.0%
- Audit and accounts 0.6%
- Governance 1.2%
- Poison pill/Anti-takeover device 0.1%
- Other 1.7%

United Kingdom

We recommended voting against or abstaining on 282 resolutions over the last quarter.



- Board structure 34.4%
- Remuneration 51.4%
- Shareholder resolution 0.7%
- Capital structure and dividends 8.2%
- Amend articles 1.1%
- Audit and accounts 2.5%
- Governance 0.4%
- Poison pill/Anti-takeover device 1.4%

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