Sarasin & Partners

Policy outreach, company engagement and voting report

Q4 2018

January 2019

Introduction

Investors in companies have an important shared responsibility in holding the board to account for the management of the business.

On behalf of our clients we are active in voting on matters put to shareholders, and we closely monitor investee companies and engage on issues of concern relating to corporate governance, capital structure and strategy. We do this because we believe that poor governance can adversely affect the returns for investors and, equally, good stewardship can lead to better returns over the long term.

As long-term investors, we also take an interest in the broader market environment in which companies operate. Where we perceive problems, and believe we can catalyse positive change, we will reach out to policy-makers and other key market participants to promote reform. Our objective is to shape the regulatory and market environment to support more sustainable economic growth.

Given the emphasis we place on responsible and active ownership, we aim to communicate openly with our clients and other interested parties about our activities. This report offers a window into our recent company engagement, policy outreach and voting activities.

Stewardship: Policy and company engagement

Our engagement work with companies aims to address governance failures or strategic challenges with a view to protecting and enhancing shareholder value. It often takes place in confidence, but we aim to share key points and goals of recent engagements to ensure transparency and insights on our stewardship activities to our clients.

Alongside our company dialogues, we often have a unique opportunity to engage with policy makers to improve the regulatory and market environment in which companies operate. In these cases our aim is to promote rules and market-wide practices which encourage long-term and sustainable behaviour, which in turn will underpin sustained and equitable wealth creation.

Company Engagement: Glencore

This quarter we exited our position in Glencore following an involved engagement with the Chairman, Tony Hayward, and Chair of the Audit Committee, Leonard Fischer, on bribery and corruption allegations over the past 6 months.

To ensure a bigger voice, we reached to other investors, including the Church of England Commissioners, the UK's Local Authority Pension Fund Forum and Royal London Asset Management, to build a joint engagement position. Specifically, we asked for five actions:

1. An independent review of Glencore's internal controls;

2. A change of their auditor, Deloitte, who has been in situ for over 25 years, and during the period in question;

3. The suspension of implicated executives until the investigation has been completed;

4. The ending of payments to Mr. Gertler until cleared;

5. Increased transparency around Glencore's business dealings, including beneficial ownership of related entities.

Notwithstanding positive commitments to us by the Board to undertake an independent review of Glencore's internal controls, and to change the auditor (and more recent announcement that the former Head of Copper would step down - implicated in financial irregularities at Glencore's subsidiary, Katanga Mining), they were not prepared to suspend Glencore's business dealings with Mr. Gertler.

Whilst we understand the contractual obligations Glencore has with entities controlled by Mr. Gertler, having reviewed detailed evidence compiled by Global Witness, we believe that Glencore has failed to take contractual opportunities in the last two years to distance itself from Mr. Gertler. Consequently, the ongoing relationship, in our view, runs contrary to the Board's commitment to shareholders to ensure they minimise bribery risks.

In the end, as we put it in our letter to the Board, we believe that a failure to act decisively on bribery leaves the company and its shareholders exposed not just ethically and reputationally, but also financially.

Company engagement: Swedbank

Anti-money laundering controls have also been a focus in our engagement with banks this quarter. This builds on our work on ING Groep, which we reported on last quarter, and takes place against the backdrop of a money laundering scandal which has dogged Danske Bank, a company we do not invest in, over the course of this year.

Over €200bn is alleged to have passed through Danske Bank's Estonian operations in recent years, leading to the departure of its CEO and Chairman among others, as well as criminal investigations in Denmark and the US. The consequences are likely to be severe. Some smaller local regional banks could lose their banking licenses, or may fail under the pressure of international sanctions.

While not implicated in the scandals, we met with Swedbank's Deputy Chair and Head of Investor Relations this quarter. Our goal was to assess whether it may be exposed to similar risks due to its dominant position in Estonia and other Baltic markets. We discussed in detail the structure and oversight of the Bank's IT and anti-money laundering systems, as well its share of cross-border payments and the profitability of non-resident customer portfolios in these markets (indictors of lax money laundering controls at Danske Bank).

Company engagement: Swiss Re

Climate-related risks were a focus of our discussions this quarter with the Chairman and Lead Independent Director of Swiss Re, as well its in-house climate change specialists.

As one of the world's largest reinsurers, the company is highly exposed to the financial impacts of extreme weather and natural catastrophes. We sought to understand how analyses of physical and energy transition risk are integrated into its risk management process, and were impressed to hear that it has c.50 climate scientists working on its models and forecasting.

This in-house expertise gives Swiss Re a high degree of confidence in its proprietary modelling, enabling it to assist clients in their efforts to adapt and increase resilience to climate change, including by meeting a growing demand for private insurance to cover related losses.

Market Outreach

Accounting & audit

This quarter saw the publication of Sir John Kingman's Independent Review of the Financial Reporting Council (FRC), the regulator responsible for accounting, audit and corporate governance matters in the UK. The Review's terms of reference had reflected many of the concerns raised in our October 2017 paper, ''Investors require a robustly independent audit regulator', and we are pleased that the final report has reached similar conclusions to our own analysis.

Among the proposals which echo our written submission to his inquiry, Kingman recommends that the FRC be replaced by a new, independent regulator with a proper statutory status, with extended powers and accountability to the Government.

He calls for significant changes to be made to the regulator's governance, funding arrangements and broader transparency, which should help to address concerns about conflicts of interest with the audit industry it oversees.

We also met and submitted a written response to the Competition and Markets Authority (CMA) as part of its study of the UK audit market, which also took place during the quarter. The CMA's preliminary report refers to Sarasin & Partners' work in a number of places, most importantly in calling for a review of whether audits are currently aligned with company law provisions designed to protect investors' capital.

While it is frustrating that this central question about the purpose of accounts and audit has not been dealt with head on by these two initiatives, it seems clear that the Government must now resolve the issue. To that end, we will be submitting feedback on the two reports' conclusions to the parliamentary Committee for Business, Energy and Industrial Strategy, as well as to the CMA ahead of its final report. The Financial Times also published a letter during the quarter in which we make this point alongside other like-minded investors.

Climate Risk

Quarter 4 was a busy period from a climate perspective. The International Governmental Panel on Climate Change (IPCC) produced its first major report in four years in October on meeting the 1.5°C goal, which highlighted in more concrete terms than ever before the enormity of the climate challenge that we face.

While the IPCC's warnings have become more shrill (though many argue still understate the problem), it failed to deliver the breakthrough at the December United Nations COP24 meeting in Poland. While the centre of gravity is slowly moving towards tougher action, the United States, Saudi Arabia and Russia continue to dilute these efforts.

Against this backdrop, we believe our work to drive better climate risk reporting by companies becomes ever more important. If governments are unable to act, companies (driven by shareholders) must. Last quarter we outlined the key conclusions from our analysis of eight European oil and gas company financial statements (Royal Dutch Shell, BP, Total, Equinor, Eni, Repsol, Cairn Energy and Soco International). Essentially, we raised concerns that companies could be overstating their capital strength and profitability due to overly optimistic long-term oil price assumptions.

We published the results from this work and were pleased to see a parallel Opinion piece appear in the Financial Times over the summer. The paper was also profiled in the Economist magazine, and in October, it was referred to again by Jonathan Ford, one of the FT's more senior journalists, as a matter worthy of greater scrutiny[1].

The public coverage of our paper has helped to ensure the concerns we identify with oil and gas company financial statements are picked up by others. In the end, this is critical to moving the market towards more disclosure of climate risks, and ultimately better management of these risks.

With this in mind, we have been pleased to take up a formal role as co-coordinator (alongside the Church of England Commissioners) for the European oil and gas engagements undertaken as part of the Climate Action 100+ initiative. This initiative matters because it is supported by over $30 trillion in assets under management, so that we are able to help shape the broader investor engagements being undertaken by the investment community.

Under the CA100+ initiative, Sarasin & Partners was pleased to support an investor letter to the FT in December calling for power companies to show more determined leadership in driving the transformation away from fossil fuels[2].

There is little doubt that pressure is growing on a broader range of companies to act to tackle climate change. Shareholders are no longer just waiting for politicians to act. We will continue to act on your behalf.

[1]Ford, J. "What big oil can learn from Exxon's curious case", Financial Times, 28th October 2018.

[2]https://www.ft.com/content/8d80c8e4-02f7-11e9-99df-6183d3002ee1

Key votes and engagements Q4 2018

Investors in companies have an important shared responsibility in holding the board to account for the management of the business. On behalf of our clients we are active in voting on matters put to shareholders, and we closely monitor investee companies and engage with companies on issues of concern relating to corporate governance, capital structure and strategy.

Poor governance can adversely affect the returns for investors and, equally, good stewardship can lead to better returns over the long term. The table below shows how we voted on four company resolutions during the period under review. It also explains the way we voted, and whether the resolution was approved by the shareholders or not.

Key votes for 4th Quarter 2018

Company	Date	Resolution	How we voted for you	Result
Alibaba Group Holding Ltd	31 Oct 2018	Elect Directors	Against	Passed

We continue to vote against the non-independent directors because the majority of the Board are not independent. Additionally the governance structure (the “Alibaba Partnership” structure and related voting agreements with other larger shareholders) does not support the principle of one-share-one vote, limiting directors’ accountability to shareholders. Minority shareholders do not have an effective mechanism.

Percentage of votes cast for the resolutions: 87-90% for, 10-13% against

Company	Date	Resolution	How we voted for you	Result
EssilorLuxottica SA	29 Nov 2018	Approve remuneration policy of executive corporate officers	Against	Passed

We voted against EssilorLuxottica’s remuneration proposals because of a significant increase in total compensation (a 736% increase for the Executive Chair and 43% for the Executive Vice-Chair) following the completion of the merger between Essilor and Luxottica in October.

EssilorLuxottica argues that its increased size justifies the pay increase. We believe pay increases should come following promised synergies and improved returns, not before. Moreover, the pay scheme permits retesting against performance thresholds, something we view as poor practice.

Our concerns are also linked to wider governance issues. As part of the merger, the Chairs of Luxottica and Essilor were appointed co-Chairs. While a search will start for a CEO, it is not expected to be concluded until 2020, leaving the co-Chairs as Executive Chairs in the interim. We find this arrangement unsatisfactory, and have particular concerns over the influence of Luxottica founder Del Vecchio.

We will be engaging with the company in the coming months to push for clearer and more stable governance.

Percentage of votes cast for the approval of the remuneration policy: 62% for, 38% against.

Key votes continued

Associated British Foods Plc	7 Dec 2018	Approve remuneration report	Against	Passed

As in previous years, we have expressed concerns regarding the company's remuneration practices to the Chair of its Remuneration Committee. While we welcome the Committee's decision to provide more detailed and timely disclosure around management's achievement of short-term bonus targets (something we have called for) we decided to vote against the remuneration report once again at the AGM. This is consistent with our decision not to support the 2015-2018 long-term incentive plan in 2014. We view the targets as insufficiently stretching.

We also disagreed with the Committee's decision this year to continue awarding the CFO a pension contribution which is significantly higher than that available to other employees. This is not only inconsistent with our remuneration principles, but is also contrary to the updated guidance in the UK Corporate Governance Code. Other companies have reduced pension contributions for serving executives in order to align them with other employees. We encouraged ABF's Remuneration Committee to address this next year.

Where we have had cause to vote against a company's remuneration report over two or more consecutive years without seeing improvements, we typically also vote against the re-election of the Remuneration Committee Chair. However, ABF's Remuneration Committee Chair is new and planning to put forward a revised remuneration policy for shareholder approval next year. We decided to support her appointment to give her time to address our concerns. Positively, the Committee is no longer chaired by the Board Chairman, who is considered non-independent, and we hope to have constructive discussions around the new policy.

We have continued to engage with Associated British Foods this year, addressing strategy, culture, supply chain practices and climate change in our discussions with both management and the new Chairman.

Percentage of votes cast for the approval of the renumeration report: 96.2% for, 3.8% against

Voting Summary Q4 2018

		2012	2013	2014	2015	2016	2017	2018
Total number of company meetings		636	638	741	969	968	1,165	1,072
Total number of proposals		7,448	7,184	8,090	11,102	10,387	13,244	13,433
Votes cast	for	4,720	4,986	5,807	8,288	7,728	8,570	11,152
	against	1,312	1,418	1,332	1,631	1,681	2,354	2,611
	abstain	5	56	63	118	61	101	181
	withhold	171	173	126	85	84	83	79
	did not vote[1]	1,240	551	762	980	833	2,136	1,420

[1]We do not currently vote in jurisdictions in which share blocking and power of attorney requirements apply.

Further details are available upon request.

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