

RESPONSIBLE INVESTMENT

Stewardship priorities 2023

SPECIALISTS IN INVESTMENT MANAGEMENT

Approver: Quilter Cheviot Limited 30 November 2023.

Stewardship is a central pillar of Quilter Cheviot's responsible investment approach. 2023 will be a critical year in driving forward our engagement priorities, whether that is holding high emitting companies to their interim decarbonisation targets or understanding how UK companies will begin to implement new recommendations on gender balanced boards. Below we outline our priorities for the year ahead and a review of our 2022 activities.

Our approach

Our stewardship process is comprised of two main approaches: engagement and voting. By engagement, we mean speaking directly to companies (including investment trusts) and funds about the issues that concern us and understanding their general approach to material environmental, social and governance (ESG) issues. This can be at board, executive or manager level. Engagements can be reactive or proactive. Where engagement topics are proactively set by the responsible investment team, potentially outside of AGM activity, we use numerous data providers to identify engagement targets and track the success of these efforts over time. Any thematic engagement proposals are approved by our internal Engagement Panel.

Voting is the formal expression of approval or disapproval related to items proposed by management and shareholders at general meetings. We vote on our global equity and investment trust positions¹ – this includes the monitored equity lists, the monitored investment trust list, our AIM portfolio service, MPS Building Blocks, funds managed by Quilter Cheviot¹, and where we own more than 0.2% or £2 million of a holding in the UK. This represents around 95% assets we hold that have voting rights. Voting is undertaken alongside engagement.

Many of our interactions with companies are related to governance issues and typically take place surrounding the general meetings. While most general meeting agenda items still relate to governance topics, we are increasingly seeing items on social and environmental issues put forward by shareholders.

In addition to more reactive activities, Quilter Cheviot² has three broad thematic priorities that help to drive our approach to stewardship: climate change, human rights, and natural capital. Topics within these categories have been identified for several reasons, including:

Size: This relates to the relative size of the position and the likely access/impact we will have. This will be viewed on a total exposure and percentage of equity issued basis.

Geography: We will have more meaningful engagements in markets where we have expertise in legal processes and stewardship norms.

Research coverage: Our research teams are embedded into our engagement process. We will have more meaningful engagement where knowledge and relationships are deeper.

For more detail on our approach to stewardship or details of engagement and voting activities please visit [Stewardship | Quilter Cheviot](#).



¹ As far as reasonably possible given the local regulations regarding share voting.

² Climate Assets Balanced Fund and Climate Assets Growth Fund; Quilter Cheviot Global Income and Growth Fund for Charities; Quilter Investors Ethical Fund; Libero Balanced

Our thematic engagement priorities



Climate change

Through our stewardship process we commit to engage with companies and funds to understand their decarbonisation plans. We aim to encourage alignment with net zero pathways and disclosure against globally recognised standards such as the Science Based Targets Initiative.



Human rights

Through our stewardship process we commit to engage with companies and funds to better understand or improve performance on issues such as decent work and pay, human rights in the supply chain, and health and safety, as well as inclusion and diversity.



Natural capital

Through our stewardship process we commit to engage with companies operating, and funds investing in, high impact sectors to better understand how they are managing and mitigating risks related to deforestation, water usage and biodiversity. We commit to engage to improve company and fund performance where they are not meeting the standards we expect.

Engagement priorities 2023³

Climate change

Climate transition strategy

We continue to engage with high emitting companies on the quality of their transition plans and related disclosures. Our engagement will cover varied industry groups and sectors including industrial gases, cement manufacture and utilities, but unsurprisingly most conversations will be held with oil and gas majors and diversified miners. This is an ongoing dialogue that will require systematic monitoring to ensure companies ‘walk the talk’.

Objectives

- Assess the quality of climate transition plans among high emitters.
- Encourage alignment and disclosure towards the goal of net zero emissions by 2050.

Targets

- High emitters among investee holdings, with materiality of holding a key consideration.

Lifecycle of renewable energy infrastructure assets

Renewable energy infrastructure is often perceived to be automatically sustainable given its contribution to net zero ambitions, but there are many factors to consider. One important consideration is the end-of-life plan for these assets. The sourcing of infrastructure assets or raw materials is also important, ensuring thought is given to ethical and sustainability considerations early in the asset lifecycle.

Objectives

- Assess supply chain management and ethical sourcing of infrastructure assets or raw materials.
- Understand the end-of-cycle asset disposal process.

Targets

- Investment trust holdings, particularly those within the Climate Assets Funds (our sustainable investment strategy).

Human rights

Fast fashion (labour standards and supply chain management)

This model of retail relies on companies catering to ever-changing consumer tastes as quickly as possible. We plan on engaging with investee companies with high human rights-related risks within their supply chains. We will look to explore if companies have mitigation practices in place such as carrying out location-specific risk assessments, providing multilingual materials for local employees, and fostering open collaboration between suppliers. We expect companies to have a recent and relevant Modern Slavery Statement that highlights awareness of supply chain risks and lays out actionable steps to address them.

Objectives

- Explore measures companies have in place to address and manage human rights-related supply chain risks.
- Explore if companies have mitigation practices in place.
- Assess the relationship between the supplier and company.
- Identify if the company has a sustainability committee or a senior member held responsible for labour standards and supply chain management.
- Ensure companies have a recent and relevant Modern Slavery Statement.
- Ensure companies have a robust auditing standard within the supply chain.

Targets

- Companies where we have material holdings in the fashion industry.
- Companies with previous poor practice in this area

³ These descriptions represent prospective engagement designs, and may be adjusted as necessary.

Cybersecurity

Cybersecurity is a material issue for companies in critical infrastructure sectors. The average annual cost of data breaches in 2022 for companies in critical infrastructure industries was \$4.82 million (£3.82 million). In addition to the potential cost for companies, data privacy is recognised as a human right by the United Nations (UN).

We have established an engagement framework following the Principles for Responsible Investment's (PRI) guide and recommendations for engaging on cyber resilience.

Objectives

- To establish best practice cyber governance and raise concerns with companies providing insufficient disclosure.
- To encourage investee companies to improve their disclosure on key cyber governance areas. These areas include legal compliance, board communication, training, business continuity and information security experience.

Targets

- Companies with good disclosure compared to peer group will be targeted to assess best practice, and companies with insufficient disclosure will also be targeted to provide an opportunity to discuss concerns and monitor improvement over time.
- Companies within critical infrastructure sectors such as banking, telecommunication and software and services. This is because cybersecurity is as a material issue according to the SASB framework.

Pharmaceuticals – litigation and product safety

Healthcare companies are especially vulnerable to product safety issues. Failure to undertake adequate testing for drugs and medical equipment can lead to recalls, which not only have an economic impact but also reputational ramifications. In the most extreme cases, the products can lead to the injury and death of customers, which may result in litigation, regulatory action, and/or reputational damage. Having

adequate risk mitigation processes in place can help reduce the likelihood of these instances and therefore improve the company's performance.

Objectives

- Understand ongoing litigation risk within the health care equipment and services, pharmaceuticals, biotechnology and life sciences sectors.
- Gain a deeper understanding of the processes that are in place to minimise the risk of litigation or product safety issues.

Targets

- Priority companies will be identified by considering ongoing litigation concerns and the materiality of holdings.

Natural capital

Agricultural commodities and deforestation

The most significant risk related to natural capital management is in supply chains. Companies tend to have more transparent practices for direct operations, which are also easier to monitor and control. However, supply chains can be complex, particularly global supply chains where companies have less visibility and regulation may be less strict in certain jurisdictions.

Objectives

- Understand companies' dependency on natural resources and their processes to ensure a sustainable supply.
- Understand companies processes and policies to minimise the environmental and social risks associated with sourcing agricultural inputs related to deforestation.
- Identify poor practice.

Targets

- Companies with high exposure to key forestry commodities using CDP forest score and other materials.

Collectives

Fund engagement priorities

In 2023 we will focus on areas including climate and diversity & inclusion as well as regional specific concerns for firm- and fund-level engagements.

Our climate-related work will focus on the approaches being taken to meet Net Zero Asset Manager initiative (NZAM) commitments and progress on implementation. We will also assess firms that are not signatories to NZAM or that are not reporting in line with TCFD (Taskforce for Climate-related Financial Disclosures) and advocate why we think net zero commitments and climate disclosures are important.

Our proprietary annual RFI questionnaires are a key source of information for our engagements with fund managers and responsible investment teams.

Firm level:

- Firms not reporting in line with TCFD.
- Firms that disclose no data or only gender data within their RFI responses at a firm and investment team level.
- Engagement with the largest 20 firms by Quilter Cheviot assets invested to discuss their approach to net zero commitments. If not signatories to the Net Zero Asset Manager Initiative (NZAM), discuss the reasons and encourage them to make a net zero commitment.
- Firms not signed up to the Principles for Responsible Investment (PRI).

Fund level:

- Engagement with the largest fund holdings, particularly on management of climate commitments such as NZAM.
- Identify the five highest emitting fund holdings that do not have a net zero aligned transition plan and engage with the fund managers to understand their approach to these holdings.

Regional engagement:

Internal engagement with all fund analysts to understand key concerns within their geographies.

Investment Trusts

This is an ongoing engagement between Quilter Cheviot and Quilter Investors focused on improving investment trust board composition and disclosure on responsible investment-related matters, including stewardship reporting. In 2023, we will continue to focus on three main topics for engagement:

- **Board composition:** We expect a board to be independent, diverse and have the right skillset. In regard to independence, two areas are of primary focus. First, we do not believe it is acceptable for an investment trust to have a board member that has been appointed or is employed by the investment advisor. Second, we believe that tenure does impede independence and expect boards to adhere to the nine-year rule, unless there are mitigating circumstances. We expect boards to meet the FTSE Women Leaders and Parker Review targets. A board's skillset should be appropriate to challenge and support the investment adviser and represent shareholders.
- **Board effectiveness:** A board's function is to represent and act in the best interests of shareholders. Therefore, we expect boards to be willing and able to challenge an investment adviser when necessary. Additionally, boards should be accessible and prepared to meet with and consider feedback from shareholders.
- **Disclosure:** We want to see responsible investment disclosures that are pertinent to the investment trust and its holdings. This will vary depending on the asset class a trust invests in. For equities, at the minimum we want a trust to disclose how it has voted on its holdings (when applicable) and the rationale behind some of the most significant votes. Examples of how the manager has engaged with the holdings and clear examples of ESG integration are encouraged for all asset classes. Further, it is good practice to report on a board's role in managing these ESG risks.

Year in review: engagement priorities 2022

Climate change

Climate transition plans and disclosure

In 2022, we engaged some of the largest carbon emitters within portfolio holdings to better understanding corporate climate strategies and, where lacking, encourage alignment with best practice. Our engagements have spanned a variety of industry groups including industrial gases, cement manufacture and utilities. Unsurprisingly, most conversations were held with oil and gas majors and diversified miners. This is an ongoing dialogue that will require systematic monitoring to ensure companies walk the talk.

Human rights

Gender diversity in the UK and Germany

Significant progress has been made by the largest UK companies on improving gender diversity at the board level. However, improving gender representation at the executive level and in other senior positions has progressed at a slower rate. Therefore, we engaged with companies reporting the slowest progress at both the board level and at senior management levels. Regulatory approaches to gender diversity differ across geographies and the lack of consistent reporting requirements presents challenges in assessing progress at a global level.

Exploring diversity beyond the data

Our research explored both quantitative and qualitative diversity and inclusion disclosures across our centrally monitored universe of 342 companies. The goal was to gain further insight into best practices and to identify trends. We used company annual reports and website disclosures as source material rather than direct interaction with the underlying companies, which was limited to the case studies within this document. We identified 21 data points related to qualitative and quantitative factors linked to diversity and inclusion (D&I). Quantitative data provided a high-level entry point for analysis and qualitative data offered additional insights into a company's approach to diversity and inclusion. The objective was to identify and assess areas where companies are performing well, or underperforming, and what actions are successfully being put in place to attain a more diverse and inclusive workforce.

Natural capital

Water risk

We initiated an engagement with a focused group of companies in the food, beverage and tobacco industry group, one of the areas most impacted by water risk. Data on water usage at a company level are not systematically disclosed in detail. This is an engagement for information and the primary outcome is to understand how investee companies are managing and potentially mitigating these risks, and how they are using the information gathered from these conversations to form an assessment of what best practice looks like.

Collectives

We invest in funds managed by other investment firms We track the developments and outcomes over time. The engagements were split into four areas:

1. The firm-wide approach to responsible investment.
2. Manager and strategy approach to responsible investment.
3. Engagement on ESG risk and exposure.
4. The firm-wide approach to net zero.

Fund engagement – PRI Signatory Status

We contacted most funds under coverage to outline our expectation that they should be signatories to the UN-supported Principles for Responsible Investment. We followed up on initial outreach with non-signatories for more detailed engagement and communicated the growing importance of ESG integration and stewardship in our fund selection process.

Fund engagement – Net Zero Asset Manager Initiative commitments

This engagement focused on the third-party managers that we invest with on behalf of our clients. This is a long-term engagement for information as well as an engagement to drive change.

In our engagements we considered the following:

- whether the approach being taken to net zero is focused solely on specific emissions reductions targets or if the emphasis is on real world change.
- whether the asset manager has data systems to support the methodology it has chosen.
- how much AUM has been initially committed and how this measures up with the approach being taken.
- whether there is a focus on strategy, governance and engagement.

As at the end of 2022, 40.7% of the third-party managers Quilter Cheviot invests in are NZAM signatories or are in the process of setting targets. We will continue this engagement in 2023.

Investment Trusts

We are focused on working to improve investment trust disclosure on ESG-related matters and stewardship. We want to understand the board is managing ESG risks and opportunities within the investment trust itself. Additionally, we are interested in board composition from a diversity and an independence perspective. This will be a long-term engagement for change.

Collaborative engagement

Many of the collaborative engagements outlined below are either ongoing or annual.

Signatory of:



CDP SBTi Campaign (Climate change)

The latest Intergovernmental Panel on Climate Change report makes it clear that without immediate and deep emissions reductions across all sectors, limiting global warming to 1.5°C will be impossible. Science-based targets provide a roadmap for reducing emissions at the pace and scale that science tells us is necessary to avoid the most catastrophic effects of climate change. We joined a coalition of 274 financial institutions representing \$36.5 trillion to ask specific companies to commit to a target. Of the companies targeted, 47 are holdings within our direct equity centrally monitored list.

IIGCC Net Zero Initiative (Climate change)

The Net Zero engagement initiative aims to enable net portfolio alignment by supporting investor engagement and seeking the disclosures investors need from companies to determine if they are aligned with net zero. These expanded collaborative engagements therefore seek Net Zero Investment Framework (NZIF)-aligned transition plans from companies. Quilter is participating as a signatory supporting the initiative. For Quilter Cheviot, of the 108 companies targeted initially, 19 are within the centrally monitored universe and we will have exposure to others through our third-party fund holdings.

30% Club (Executive Search Firms) (Human rights)

In discussing gender diversity performance with investee companies at board and executive levels, it is not uncommon for laggards to claim the talent pool “just isn’t there” or their recruitment consultants “struggle to find qualified women”. Most observers would admit there are clear gender imbalances in certain sectors, but we decided to test the extent and prevalence of this common refrain by directly engaging with recruitment consultants. As part of the 30%, we engaged five global consultants to better understand their processes, challenges and plans to contribute to a more gender diverse leadership. This was an engagement for information and our findings have been summarised and shared with the 30% Club Investor Group.

We have also engaged with UK executive recruitment firms to understand the diversity challenge.

Find it, Fix it, Prevent it (Human rights)

Regulation outlawing forced labour, human trafficking and slavery is to be found in international human rights law and in the legislation of many sovereign states. Further, eradicating modern slavery is one of the UN Sustainable Development Goals (SDGs). Quilter Cheviot has joined this collaborative engagement, which will focus on UK-listed companies in specific industry groups identified as being higher risk in this area.

Votes Against Slavery (Human rights)

In 2021, we joined a group of UK investors through the UN-backed Principles for Responsible Investment platform. The purpose was to engage companies that have not met reporting requirements under the 2015 Modern Slavery Act. All 44 target companies have responded and as at September 2022 there are eight committed to releasing new statements and three amending statements to become fully compliant.

Conflict Minerals (Human rights)

Quilter is an investor signatory to a letter asking semiconductor companies to take leadership roles in improving best practice for sourcing conflict minerals. We also engaged with some of our third-party managers to encourage further investor support for this letter. The letter represented a collective total of \$6.59 trillion in AUM.

PRI Advance (Human rights)

As part of Quilter plc, we endorse this initiative to drive positive change on human rights and broader social issues.

Investor statement on the Seasonal Worker Scheme (Human rights)

As an adjunct to the Find it, Fix it, Prevent it campaign, asset manager CCLA brought together ten long-term institutional investors with £806 billion assets under management and advisory with investments across UK-listed retail, hospitality and food production. The statement outlined our concern that migrant workers in the UK, recruited and employed through the government’s Seasonal Worker Scheme (SWS), are obliged to pay excessive fees to agents and middlemen in addition to other fees, travel and visa costs for crucial, but temporary roles, supporting the UK’s food sector. This results in a high risk of debt bondage, one of the key indicators of forced labour.

CDP Non-Disclosure Campaign (Natural Capital)

The campaign’s objective is to drive further corporate transparency around climate change, deforestation and water security by encouraging companies to respond to CDP’s disclosure request. We have joined other investors in a targeted campaign to collaboratively call for improved disclosure on environmental matters where information is lacking.



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