



**NORTHERN TRUST**

ASSET MANAGEMENT

# NORTHERN TRUST ASSET MANAGEMENT ENGAGEMENT POLICY

Since 1889, Northern Trust Asset Management has been guided by our principles of service, expertise and integrity.

At Northern Trust Asset Management, our primary objective as an asset manager is to create long-term value for our clients. This objective applies to all of our portfolio management decisions, including operating as a responsible investor and engaging with company management and boards of directors. Northern Trust Asset Management believes that being an active owner will help portfolio companies produce sustainable value, and that companies' long-term financial returns are connected to their strategic, environmental, social and governance performance.

This policy is designed to provide guidance for engagements with any company we are invested in on behalf of our clients.

## GOVERNANCE AND OVERSIGHT

Northern Trust's Proxy Voting Committee is responsible for oversight of the *Northern Trust Asset Management Engagement Policy*.

## SCOPE AND OBJECTIVES FOR ENGAGEMENT

We consider engagement to be an open and ongoing dialogue with investee companies and other market participants to encourage adoption and execution of practices consistent with sustainable long-term value creation.

Northern Trust Asset Management’s investment analysts engage with hundreds of companies annually on a range of objectives across four principle themes:

**ENGAGEMENT THEMES FOR 2019-2021**

<b>ENVIRONMENT</b>	<b>CLIMATE CHANGE</b>	<b>NATURAL RESOURCE MANAGEMENT</b>	<b>WASTE, RECYCLING AND BIODIVERSITY</b>
	Strategic alignment to 1.5D	Water scarcity, use and pollution	Pollution and waste management
	Climate lobbying	Deforestation	Recycling opportunities
<b>SOCIAL</b>	<b>HUMAN RIGHTS</b>	<b>HUMAN CAPITAL MANAGEMENT</b>	<b>CONDUCT, CULTURE &amp; ETHICS</b>
	TCFD-based disclosure	Sustainable food and agriculture	Biodiversity impacts
	Modern slavery	Occupational health and safety	Fraud and bribery
<b>GOVERNANCE</b>	Child labour	Diversity and inclusion	Employee engagement
	Community rights	Recruitment and retention	Product safety
	<b>BOARD COMPOSITION AND EFFECTIVENESS</b>	<b>COMPENSATION</b>	<b>SHAREHOLDER RIGHTS</b>
<b>RISK MANAGEMENT &amp; STRATEGY</b>	Independence	Pay for performance alignment	Shareholder responsiveness
	Structure and attentiveness	Disclosure	Proxy access
	Diversity		One share one vote
	<b>RISK MANAGEMENT</b>	<b>BUSINESS STRATEGY</b>	
	Financial prudence	Analysis of opportunities	
	Enterprise risk management	Scenario planning	
	Independence of external auditor	Business purpose and mission	

The details of our engagement principles on specific topics can be found in Appendix 1.

Output from these engagements is used to inform investment conclusions with the aim of delivering positive long-term investment outcomes for clients, and helps to inform our proxy voting decisions.

**USE OF THIRD PARTY PROVIDERS**

Northern Trust has entered into an agreement with Hermes Equity Ownership Services (Hermes EOS) to provide additional monitoring and engagement services for select portfolios. Details of the covered portfolios and approach used by Hermes EOS are described in Appendix 2, the *EMEA and APAC Supplement to the Northern Trust Engagement Policy*.

## ENGAGEMENT PROCESS

Engagements are made on a case-by-case basis where Northern Trust Asset Management, or Hermes EOS acting on behalf of Northern Trust Asset Management, identifies events or decisions on the part of the investee company's management or board which raise significant environmental, social or governance concerns or identifies serious weaknesses with respect to strategy, risk and corporate communications.

In most instances, engagements will be conducted telephonically or in person with members of management or the board of directors. Engagements may also be conducted in the form of formal letter to the company's board or management detailing our issues and advocating our recommended solutions, or by attending company briefings, etc.

While we generally refrain from submitting shareholder proposals at companies annual meetings, before a proposal is put on the ballot a good faith effort to engage with management or the board should first have been made.

Northern Trust Asset Management actively participates in a number of investor groups.<sup>1</sup> As members of these initiatives, we regularly engage collectively with other investors through both formal and informal ad hoc collaborations. We typically do this as part of the process of escalation of a significant concern where we believe the collaborative approach will make success more likely, this is also a way of managing the workload involved in our engagements with companies where we are invested solely on a passive or quantitative basis and raising their efficiency.

## EXERCISE OF VOTING AND OTHER RIGHTS

As with other stewardship activities, in exercising voting and other rights attached to companies we hold investments, (where we have been given authorisation to exercise such rights as proxy on behalf of a client) our primary concern is to act in the best interest of clients/beneficiaries and the value of the investment. To that end Northern Trust Asset Management has adopted global Proxy Voting Policies, Procedures and Guidelines (the Proxy Guidelines),<sup>2</sup> setting out how we engage in such activity.

## CONFLICTS OF INTEREST

Northern Trust Asset Management has established, implemented and maintains effective arrangements for identifying and managing potential and actual conflicts of interest and inducements, in accordance with internal policies and applicable regulatory requirements. Such management includes in relation to potential conflicts around engagement activity.

The specific elements of the conflicts of interest management for Northern Trust's proxy voting activities are incorporated within the Proxy Guidelines.<sup>2</sup>

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Our primary concern is to act in the best interest of the clients/beneficiaries and the value of the investment.

## COMMUNICATION WITH CLIENTS

We acknowledge that our stewardship activities are carried out on behalf of our clients and that we have a clear obligation to be as transparent as possible about them. We produce an annual public report on our stewardship activities,<sup>3</sup> including company-specific case studies. We are transparent to our clients on our voting decisions, and disclose publicly all voting activity of our pooled funds on our website.<sup>4</sup>

Where a client delegates responsibility for proxy voting to Northern Trust, we provide reports on all voting activity taken on their behalf on a quarter, semi-annual or annual basis as directed by the client.

## COMMUNICATION WITH INVESTEE COMPANIES AND THIRD PARTIES

Our Proxy and Engagement team respond to company requests for engagement on corporate governance and related issues. Companies seeking such a dialogue may send requests to:

**NT\_CorporateEngagement@ntrs.com**

## SOURCES

1. Full list of investor groups we participate in can be found in our *Sustainable Investing Philosophy*  
<https://cdn.northerntrust.com/pws/nt/documents/white-papers/asset-management/sustainable-investing-policy-26Apr2018.pdf>
2. [https://cdn.northerntrust.com/pws/nt/documents/fact-sheets/mutual-funds/institutional/nt\\_proxy\\_policy.pdf](https://cdn.northerntrust.com/pws/nt/documents/fact-sheets/mutual-funds/institutional/nt_proxy_policy.pdf)
3. <https://cdn.northerntrust.com/pws/nt/documents/fact-sheets/mutual-funds/institutional/annual-stewardship-report.pdf>
4. <https://www.northerntrust.com/united-states/what-we-do/investment-management/sustainable-investing/proxy-voting-and-engagement>

### About Sustainable Investing

At Northern Trust Asset Management ("NTAM"), we define Sustainable Investing as encompassing all of NTAM's investment strategies and accounts that utilize values based and norms based screens, best-in-class and ESG integration, or thematic investing that may focus on a specific ESG issue such as climate risk. NTAM's Sustainable Investing includes portfolios designed by NTAM as well as those portfolios managed to client-defined methodologies or screens. As the data, analytical models and aforementioned portfolio construction tools available in the marketplace have evolved over time, so too has NTAM. NTAM's Sustainable Investing encompasses strategies and client assets managed in accordance with client specified responsible investing terms (historically referred to as Socially Responsible), as well as portfolios that leverage contemporary approaches and datasets, including ESG analytics and ESG thematic investing.



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# APPENDIX 1

## GLOBAL ENGAGEMENT PRINCIPLES

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When engaging with investee companies and voting on proxies, Northern Trust Asset Management, or Hermes EOS acting on behalf of Northern Trust Asset Management, routinely review:

- **Risk oversight** by the board. Northern Trust believes that the most sustainable companies have a holistic approach to sustainability and risk. In addition, companies should have an enterprise-wide approach to risk management. Companies which address sustainability as a legal risk compliance exercise or which treat each business unit individually in terms of risk management, in our view, may not be in a position to identify the most salient risks to business. It should be considered good practice to involve the board in both establishing and overseeing risk management structure. If there is a lack of risk management structure within the board, Northern Trust may vote against certain board or committee candidates.
- **Environmental and social risks and opportunities.** Northern Trust believes that sustainable companies embrace uncertainty and proactively prepare for and minimize the impact of threats through effective planning. This should include market, reputational and financial risks associated with environmental and social concerns. We therefore routinely examine and analyse the policies and processes that companies have put in place to protect, elevate and strategically position their organisation. In our engagement with companies, we regularly discuss how a company assesses and discloses the environmental impact of their operations and products. In our voting, we generally support proposals requesting the issuance of corporate sustainability reports and disclosures concerning the emission of greenhouse gases and other negative impacts.
- **Board composition and structure**, including what processes are used for board succession planning and board refreshment. Northern Trust will engage with companies and express concerns where they arise as to the attentiveness or competency of individual directors or the board as a whole. Northern Trust will vote against director nominees when there are concerns around independence (depending on committee representation), attendance of board meetings, overboarding and diversity of skills, experience and attributes of board. Northern Trust also votes in favour of proposals requiring women and minorities to be included in the pool of board candidates.
- **Executive compensation programme**, including how companies structure executive incentive compensation. Northern Trust believes that compensation plans should be well designed to motivate executives to achieve strong results for stakeholders while mitigating the motivation to take excessive risks. In examining compensation proposals, NTAM takes into account pay-for-performance alignment, effectiveness of governance practices, and the company's overall transparency and level of responsiveness to shareholder concerns.

Northern Trust will vote against executive compensation plans that we believe are not designed to enhance shareholder value, or where there is a lack of disclosure around performance goals. Northern Trust will vote against compensation committee members where the board and company management have failed to take reasonable action over concerns raised by a majority of the company's shareholders.

We have created supplemental guidance for companies on our approach to compensation which can be found on our website here.<sup>1</sup>

## SOURCES

1. <https://www.northerntrust.com/united-states/what-we-do/investment-management/sustainable-investing/proxy-voting-and-engagement>

### About Sustainable Investing

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## APPENDIX 2

EMEA AND APAC POOLED FUNDS  
SUPPLEMENT TO NORTHERN  
TRUST ASSET MANAGEMENT  
ENGAGEMENT POLICY

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## EMEA AND APAC SHAREHOLDER ENGAGEMENT POLICY STATEMENT

### GENERAL APPROACH

At Northern Trust, we have aligned our corporate social responsibility efforts with our guiding principles of service, expertise and integrity. We are dedicated to meeting the evolving needs of our clients, shareholders and other key stakeholders through innovative and ethical business practices.

Northern Trust advocates high environmental, social and governance (ESG) standards. We fully acknowledge that the long-term financial success of our clients and shareholders is dependent upon a healthy global environment, a stable society and well-functioning companies. In our daily operations and strategic planning, we strive to mitigate our environmental impact and improve our social and governance procedures. As a leading investment manager and financial service provider, we recognise our additional influence and responsibility.

Our core mission is to enable global investors to achieve their most important goals by providing insights, solutions and an exceptional client experience. We believe sustainability is central to all investment areas as investors increasingly demand solutions that fulfil a complete ESG portfolio. Sustainable investing is integral to our product development and implementation processes, aligning with our clients' objectives. The foundation of Northern Trust's Sustainable Investment Philosophy, as with our entire decision making process, is that we will act in a manner to protect our client's financial well-being throughout the time period and strategy they have set forth.<sup>1</sup>

Northern Trust believes that being an active owner on behalf of the shareholders of strategies covered by this document will help portfolio companies produce sustainable value, and that companies' long-term financial returns are connected to their strategic, environmental, social and governance performance. In line with the European Shareholder Rights Directive II, the UK Stewardship Code and the Dutch Stewardship Code, we integrate shareholder engagement in our investment strategy and process.

Northern Trust's equity research analysts engage with hundreds of companies annually. The focus of these engagements is to accumulate and interpret facts to reach sound investment conclusions with the aim of delivering positive long-term investment outcomes for clients. In addition to strategy, risk, and sustainability of financials, analysts also monitor corporate governance, environmental and social factors that are of material concern to the long-term sustainability of the investment. The Proxy and Engagement team supplements the analysis performed by equity analysts with additional research on corporate governance and environmental and social matters that contribute to the long-term value of the investment and reflects Northern Trust's commitment to Sustainable Investing Philosophy.

In addition to this, in EMEA, we appointed Hermes Equity Ownership Services ('Hermes EOS') to act as agent of the majority of our pooled funds in EMEA

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This policy covers the EMEA and APAC funds which can **viewed here**.

and some funds in APAC (together the 'Funds' – see the list here) and SMA strategies to carry out public policy, best practice and corporate sustainability engagement.

Our engagement policy covers both our passive and quantitative equity pooled funds. It is implemented through consistent efforts by our Proxy and Engagement team, Equity Analyst team and Hermes EOS. Whenever we see significant risk coming from an investee company's behaviour, we will make sure it is addressed by engagement – either through Hermes EOS, or directly by our specialist team. If the issue is not resolved, we may consider divesting from such securities, except the situations when they are part of the index strategies, or when investment strategies do not permit us to do so.

Hermes EOS is a leading stewardship provider with a focus on achieving positive change. Its dedicated team of engagement specialists supports its clients in achieving their fiduciary responsibilities and being more active owners of companies.

Hermes EOS typically conducts engagement-related dialogues with companies in confidence and will not disclose the Funds' involvement in such engagements, unless specifically agreed in advance.

The basis for Hermes EOS' approach in carrying out engagement activities on behalf of the Funds, is their Responsible Ownership policy as described in this document together with the Hermes Responsible Ownership Principles and regional policies.<sup>2</sup>

In certain cases, Hermes EOS engagements may inform our proxy voting activities.<sup>3</sup> Northern Trust Proxy Voting policies and procedures are designed to meet our clients' needs and ensure that Proxy Voting is used in their best interest.<sup>3</sup>

Northern Trust Sustainable Investing Council and the Product Governance Committee (a subcommittee of NTGIL's board of directors) is responsible for oversight of this supplement to the NTAM Engagement Policy.

## **ENGAGEMENT PROCESS**

Proposals for engagement, whether generated by Hermes EOS or the Funds directly, usually involve risks and concerns relating to the strategic, operational, legal, social, environmental, ethical or governance principles set out below, or a breach of the Hermes Responsible Ownership Principles or its regional policies. Engagements may relate to longer-term strategic, environmental, social or governance issues, which may not have immediate stock-specific impacts, for example where the company's shares are fully valued and the intent is to preserve that value. Hermes EOS will escalate its engagement according to the nature and severity of the concerns.

Hermes EOS conducts engagements with companies that are constituents of the Funds to seek positive change for investors, the companies and the societies in which they operate. Hermes EOS adopt their three-year engagement plans to explain their short-and-medium-term priorities and the links to the United Nations' Sustainable Development Goals (SDGs).<sup>5</sup>

Hermes EOS shall undertake portfolio company-specific engagements where it is believed that:

1. Engagement will lead to an increase in the value of a company's shares over the long term; or
2. Engagement will prevent or limit a decrease in the value of a company's shares over the long term.

In determining whether and how the engagement is taken forward, due regard is given to the level of the company's exposure to the identified concerns, the likelihood of engagement success and the potential to bring about positive change. Such considerations are based around an assessment of the likely impact of the engagement and the ultimate benefit to the value of the Fund's holding. Engagements may involve:

- Meetings with executive and non-executive directors
- Meetings with other company representatives
- Discussions with other shareholders of the company
- Participation in collaborative investor initiatives
- Submission of shareholder resolutions at general meetings as appropriate
- Use of public media
- Advocacy of or support for public policy or regulatory intervention
- Monitoring of engagement impact

Hermes EOS takes part in various collaboration initiatives, such as Institutional Investor Group on Climate Change (IIGCC) and Climate Action 100+, Responsible Business Alliance, CDP Water Initiative, Farm Animal Investment Risk and Return (FAIRR) initiative, and the Roundtable on Sustainable Palm Oil (RSPO). Hermes EOS usually plays a prominent role in leading collaborative company and policy engagements.

## SPECIFIC ENGAGEMENT TOPICS

### GOVERNANCE

#### Board behaviours and composition

The board should comprise individuals with relevant and diverse skills and traits, knowledge of the company and experience in the sectors and regions in which the company operates.

Appropriate board behaviour and the development of individual directors and the whole board is encouraged, and open disclosure on individual directors' contributions to the board and the work of the board as a whole is expected.

No individual director or small group of directors should be in a position to dominate the decision making process. Independence should be a mindset rather than a box-ticking exercise.

Board committees should be set up for audit, nomination and compensation and appropriately constituted to effectively undertake their role.

Active and open dialogue between the board and shareholders is encouraged. While the first point of contact in most cases will be the chairman, the appointment of a lead independent director is advocated to facilitate this process where a conversation with the chairman is not appropriate.

The board as a whole should act in the best interests of all shareholders and should establish appropriate channels of communication to facilitate this.

#### Remuneration

Remuneration structures should be designed to incentivise executives to promote the long-term, sustainable performance of the company with the view that:

- Compensation structures should directly link pay with performance, avoiding the possibility of reward for failure and incorporating risk management to ensure practices that promote sustainable performance.
- Significant consideration should be given by the remuneration committee as to how performance criteria and hurdles accurately represent the long-term goals and ambitions of the company. In particular, performance metrics should include company-specific measures and assessments of operational and financial risk and other risk factors, such as environmental and social risks, which could affect the long term health of the company.
- The interests of key executives should be aligned with those of shareholders through material direct long-term investment in the company's equity.
- Clear disclosure of remuneration structures and their rationale should be made annually with board consultation with major shareholders on material changes.

- Independent directors' pay should not be structured such that it could impair their independence.
- Shareholders should be granted the right to vote on the company's remuneration policy and report.
- In order to ensure corporate transparency and accountability of the directors, the remuneration report should be clear and understandable and should provide a comprehensive overview of the remuneration of individual directors during the most recent financial year.

### **Risk management and audit**

An important function of the board is to ensure that risks are appropriately managed and that company reporting accurately represents the financial position of the business and the material risks to it. Independent board-level oversight process should be in place through the audit committee and should include information sharing, insightful discussions, decisions and monitoring. If appropriate, a separate risk committee should be established to ensure adequate supervision and accountability.

Regular reports on the effectiveness of risk management should be made to the full board with the audit or risk committee taking ownership of risk oversight and supervision of any risk management functions such as internal audit.

Risk management should cover all areas of a company's operations. Risk management should be treated as integral to a company's business strategy and values rather than simply as a compliance issue. Those responsible for any risk management function within the business should be given the necessary status and have sufficient personal authority to enable them to effectively carry out their role.

The underlying risks to which a company is exposed should be clearly communicated to shareholders along with the structures in place to manage these risks. This should be done in a way which highlights the most material risks.

### **Promotion of equitable shareholder rights**

Engagements are undertaken to protect shareholder rights, including regarding issues of excessive dilution through share issuances and the establishment or maintenance of inequitable shareholding practices such as double voting rights.

### **Shareholder Proposals**

Where shareholder proposals are submitted at portfolio companies, a full analysis of the benefits of each proposal to the long-term value of the company is made. This takes into account the aims of a good owner and supports shareholder objectives that are consistent with promoting long term sustainable shareholder value at portfolio companies. Shareholder proposals that encourage full and timely disclosure of all policies, practices and matters that materially affect shareholder value are normally supported.

## **Company Culture**

Companies should establish and maintain strong internal culture which focuses its staff on sustainable value creation. Such a culture will ensure that employees act cohesively to promote the long-term success of the business. Boards should establish, maintain and oversee mechanisms of monitoring corporate culture and ensure that related objectives are reflected in arrangements such as job responsibilities, performance measurement, and remuneration.

## **BUSINESS PURPOSE AND STRATEGY**

Companies should articulate a corporate purpose that envisages long-term sustained benefits to their customers, acknowledging the needs of other key stakeholders, which may include shareholders, employees, communities, suppliers or the environment. Companies should have coherent strategies for each business unit and the corporation as a whole, aligned when applicable with their sustainability strategy. It should ensure that it is the 'best parent' of each of the businesses it runs. Engagement is undertaken with companies to ensure that capital is allocated appropriately to business units and investments whether organically or through acquisition. These allocations should be based on an assessment of where the deployment of capital will deliver the maximum, sustainable risk adjusted return. Companies are encouraged to give sufficient management focus to core businesses and the opportunities to exploit the company's core capabilities for growth and enhanced economic returns. Engagement is also carried out to challenge companies to employ an appropriate capital structure taking into account the cyclical nature of the industries in which they operate and the growth opportunities available.

## **ENVIRONMENTAL**

### **Climate change**

Companies should ensure that their operations take account of environmental constraints and the rising prices of carbon where trading schemes or taxes are in place or planned. Investment decisions need to build in realistic cost of plausible climate scenarios in order that they will be made in the best interests of long-term shareholder value creation.

### ***Energy use / CO2 emissions***

Companies, particularly in energy intensive industries, increasingly take steps to manage and minimise fossil fuel energy use for financial and environmental reasons. This constitutes an important part of their long-term strategy and requires analysis of specific climate scenarios. Engagement activities focus on climate governance and risk management process. Key sectors are all major CO2 users including extractives, utilities, heavy industry and transport.

***Renewable energy and carbon capture & storage (CCS)***

Engagement activities on this theme make sure companies improve their economic resilience, competitive advantage and overall sustainability. This can be done via increased use of renewable energy or developing CCS. The key industry is power generation.

***Extractives and stranded assets***

Companies in the oil and gas and mining sectors are among the heaviest users of energy and generator of carbon emissions. Stranded assets have become an issue for the industry when long term investments are initiated but risk becoming obsolete as a result of carbon taxation, increased competition from renewable or other changes to demand. Engagement is carried out with those companies most exposed to this area to ensure that they are effectively managing the risks involved.

***Transparency and disclosure of climate related information***

The Taskforce on Climate Related Financial Disclosures (TCFD) established by the Financial Stability Board (FSB) in 2015 adopted its final recommendations in June 2017. Under the recommendations, all companies should disclose key climate-related risks and opportunities through the lens of climate scenario analysis. Such disclosures should be an integral part of companies' financial statements and annual reports and should contain financially material, decision-useful information in four areas: governance, strategy, risk management, and metrics and targets.

***Disaster avoidance and business continuity preparedness***

Companies, particularly in the extractives and utilities sectors, are engaged with to ensure that they have robust plans to minimise the risk of environmental disasters, such as those experienced at Fukushima and in the Gulf of Mexico.

***Water stress***

Companies in water scarce regions are facing the need to minimise water use for economic as well as environmental reasons. Key sectors for engagement are extractives, food and drink manufacturers / agricultural and some heavy industries such as cement. Engagement is also carried out with utilities companies in this area where they have failed to live up to their obligations.

***Pollution and waste management***

Companies increasingly need to comply with regulations and respond to stakeholder pressures to minimise their emissions to air and other pollution.

They respond with policies and procedures in place to avoid using unnecessary resources, minimise waste, maximise recycling and reuse. Engagement is undertaken with companies to encourage them to maximise both financial savings from such practice but also to enhance their reputations by behaving in line with evolving best practice. Such behaviours include re-use and recycling of products and by-products, minimising the use of plastic and contribution to plastic waste, control over the use of antibiotics that can penetrate to food chains and develop resistance, and noise pollution management.

### **Biodiversity**

Companies should manage their impact on the local environment as part of maintaining their licence to operate in any particular country. Engagement is undertaken with companies that fail effectively to do this. Key sectors are food companies, the agricultural and extractives sectors.

### **Forest Sustainability**

Companies should understand and manage their contribution to deforestation. Responsible for up to 20% of global carbon emissions, deforestation is becoming a vital public policy issue. Companies should be ready for future legislation and ensure the sustainability of their supply chains. Furthermore companies who do not manage their deforestation impact appropriately face increasing reputational and 'licence to operate' risks given growing public awareness of the issue. Highlighted areas are: forestry, cattle, agriculture (particularly palm oil) and biofuels.

### **Animal Welfare**

Proposals requesting increased disclosure or reporting regarding animal treatment issues that may impact a company's operations and products, especially in relation to food production, are supported unless sufficient information on that topic has already been disclosed to shareholders or is otherwise publicly available.



## SOCIAL & ETHICAL

### People

#### *Labour relations*

Best-practice companies in the area of social responsibility tend to grant or recognise their workers' important rights such as the entitlement to collective representation. Where such activity is barred or where there are other poor labour practices, employee performance and labour turnover is likely to suffer over the long-term with resultant recruitment and training costs likely to increase, affecting company performance. Target companies for engagement include those in the retail and hotel sectors and any industry with large workforces. In addition, company engagement encourages companies to unlock the value of human capital to develop sustained value.

#### *Health and safety*

Engagement is undertaken with companies that fail effectively to implement appropriate health and safety measures and procedures. Key sectors are mining and construction.

#### *Diversity and inclusion*

Companies should develop and implement appropriate policies and programmes for an effective and inclusive culture, pursuing equal opportunities and pay by gender, ethnicity and other relevant demographic criteria.

#### *Employee Remuneration*

Engagement will be undertaken where employee remuneration is misaligned with long-term shareholders' interests. Examples include commercial and investment banking, sectors where pay incentives have led to employee wrongdoings and increased risks for shareholders.

#### *Community relations*

Businesses need to manage their relations with local communities on whose goodwill they are dependent. This will involve minimising negative impacts on communities and ensuring changes are communicated appropriately.

## **Ethics**

### ***Supply chain /ethical sourcing***

World class companies should manage effectively the reputational and business risks in their supply chains. Benefiting financially from poor labour practices in the short-term can lead to misleading and unsustainable levels of profit, potentially skewing investment decisions. One particular issue in this area is child or forced labour. Some of the key sectors for these engagements are textile companies, the iron and steel sector, food manufacturing and agriculture as well as those companies, particularly in the retail sector, that have supply chains that are exposed to such risks. There is a significant difference between seasonal child labour at small (particularly family) agricultural operations and more long-term systematic use of child or forced labour, for example in mining.

Companies should act to minimise the externalisation of costs either directly or indirectly via their supply chain. They should not source goods from suppliers that fail to safeguard the environment in their production processes. Engagement is undertaken with companies across all sectors that do not adhere to these standards to encourage them to seek more sustainable sources.

### ***Presence in troubled regions***

Engagement is carried out with companies operating in conflict regions or oppressive regimes to determine whether their continued presence is in the best long-term interests of shareholders.

### ***Bribery & Corruption***

Shareholder funds should not be diverted to pay bribes. Where it is believed that company executives are implicated in corrupt practices, engagement will continue in an effort to persuade these companies to adhere to governance best practice.

### ***Human Rights***

Companies must ensure that the human rights not only of their employees and people within their supply chain are protected but also the rights of their customers. Engagement is undertaken with technology companies, in particular, and other sectors to ensure that their customers' data is secure and used properly.

## **Sector specific issues**

### ***Production of cluster munitions/landmines (defence)***

The production of cluster munitions and landmines is facing high level of international opposition and has been made illegal in many jurisdictions. Engagement is undertaken with companies involved in the manufacture of such weapons, or components of such weapons, to encourage them either to cease production or, where this is not practicable, to disclose their position to shareholders.

### ***Banking***

Whilst under significant pressure since the financial crisis began in 2008, the banking industry remains fraught with issues. Engagements with banks and their regulators focus on securing improved corporate structures (including where appropriate ring-fencing of the retail banks), putting in place appropriate risk management and better governance, encouraging more insightful investor communications, engaging in socially useful banking activities, in particular support for the sustainable economy, seeking meaningful changes in culture and behaviours and ensuring pay structures where risk and quanta are aligned to investors. Board structure and director quality, experience and capability are also foci.

### ***Access to medicine (pharmaceuticals)***

Pharmaceutical companies are at risk of reputational damage if they seek to limit the availability of medicine to the most in need, particularly in the developing countries, through rigid pricing and patent protection. At the same time, it is recognised that such companies need to invest in research and make good returns for shareholders. Engagement is carried out with companies in this sector to encourage them to find appropriate solutions that meet both of these requirements. Other areas of engagement in this sector include the shift of clinical trials to less developed markets, regulatory and political risk, and animal testing.

### ***License to operate (tobacco, alcoholic beverage and food manufacturers)***

Companies in these sectors have particular responsibilities with regard to maintaining their social licence to operate, and managing the reputational risk associated with the use and misuse of their products. Engagement is undertaken on such companies' marketing and promotional practices, in particular, to ensure that they are managing these risks appropriately.

### ***Cyber security***

Privacy and Data Security issues in the IT, Financial, Retail and some other sectors have come at the forefront of sustainability agenda, particularly in light of high-impact data security breaches by large corporates. Companies in these sectors should strengthen their policies and systems in place to evaluate the extent to which they may face reputational damage, regulatory risks or cost increases from controversial use of personal data. Strength of data security management systems are a key area of focus of engagements with management and board directors of such companies.

## **EVALUATION AND REPORTING**

On a quarterly basis Hermes EOS provides a report on the engagement activity undertaken on each Fund's behalf. On an annual basis it produces a detailed evaluation of the progress and impact of engagements on companies in each Fund's portfolio.

On-going review of Hermes EOS' results will be undertaken by Northern Trust's Sustainable Investing (SI) Council (the "Council"), a group of partners across all business units that support Northern Trust's business plan and strategy around sustainable investing initiatives. The Council will evaluate reports received from Hermes EOS on a quarterly and annual basis, and consider the feedback provided by Hermes EOS.

## **CONFLICTS OF INTEREST**

NTGIL has established, implemented and maintains effective arrangements for identifying and managing potential and actual conflicts of interest, in accordance with our EMEA Conflicts of Interest and Inducements Policy and applicable regulatory requirements. Such management includes in relation to potential conflicts around engagement activity.

Relationships between Northern Trust Asset Management and Hermes EOS is carried out on arms-length basis, where Hermes EOS is not exposed to, and not aware of potential conflicts of interest that may happen within or relating to Northern Trust Corporation, either in relation to engagement with the company acting on behalf of the funds, or with regard to engagements with specific companies, their executives or directors. Conflicts of Interest within Hermes Investment Management or Hermes EOS that may arise while pursuing engagement activities will be handled by Hermes EOS according to their Conflicts of Interest policy.<sup>6</sup>

## SOURCES

1. Please see a link to *NT Sustainable Investment Philosophy*:  
<https://cdn.northerntrust.com/pws/nt/documents/white-papers/asset-management/sustainable-investing-policy-26Apr2018.pdf>
2. Please see the links to *Hermes Responsible Ownership Principles*:  
<https://www.hermes-investment.com/wp-content/uploads/2018/10/final-responsible-ownership-principles-2018.pdf>  
And regional policies:  
<https://www.hermes-investment.com/uki/stewardship/eos-literature/>
3. Records of our proxy voting activities, including the *Annual Report on ESG Engagement and Proxy Voting*, can be found at:  
<https://www.northerntrust.com/united-kingdom/what-we-do/investment-management/stewardship/proxy-voting-policies>
4. Please see the link to our Proxy Voting Policy:  
[https://cdn.northerntrust.com/pws/nt/documents/fact-sheets/mutual-funds/institutional/nt\\_proxyvotingpolicy.pdf](https://cdn.northerntrust.com/pws/nt/documents/fact-sheets/mutual-funds/institutional/nt_proxyvotingpolicy.pdf)
5. Please see a link to the current Hermes EOS three-year engagement plan:  
<https://www.hermes-investment.com/ukw/wp-content/uploads/2019/01/hermes-eos-engagement-plan-2019-2021-public-version.pdf>
6. Please see the link to Hermes EOS *Conflicts of Interest* policy:  
[https://www.hermes-investment.com/wp-content/uploads/2018/09/hermes-stewardship-conflicts-of-interest\\_2017.pdf](https://www.hermes-investment.com/wp-content/uploads/2018/09/hermes-stewardship-conflicts-of-interest_2017.pdf)

### About Sustainable Investing

At Northern Trust Asset Management (“NTAM”), we define Sustainable Investing as encompassing all of NTAM’s investment strategies and accounts that utilize values based and norms based screens, best-in-class and ESG integration, or thematic investing that may focus on a specific ESG issue such as climate risk. NTAM’s Sustainable Investing includes portfolios designed by NTAM as well as those portfolios managed to client-defined methodologies or screens. As the data, analytical models and aforementioned portfolio construction tools available in the marketplace have evolved over time, so too has NTAM. NTAM’s Sustainable Investing encompasses strategies and client assets managed in accordance with client specified responsible investing terms (historically referred to as Socially Responsible), as well as portfolios that leverage contemporary approaches and datasets, including ESG analytics and ESG thematic investing.