

QUARTERLY ENGAGEMENT REPORT

JULY TO SEPTEMBER 2017



LAPFF focusses on human capital standards during company engagement meetings

Employment practices at Sports Direct remain a concern

Cybersecurity rises up the agenda of LAPFF engagements

The Forum exposes legal inaccuracies and inconsistencies of the Financial Reporting Council

Company Engagement



GOVERNANCE RISK

HOLDINGS-BASED ENGAGEMENT

Voting Alerts

LAPFF's engagement with **Sports Direct International** continued through correspondence over voting recommendations for the 2017 AGM. Sports Direct has been embroiled for some time in a controversy over poor corporate governance and workplace practices at its Shirebrook warehouse. The Forum was concerned about the Chairman, Mr Hellawell's ability to address workplace issues in an appropriate and timely manner. An oppose vote was also recommended for the re-election of the CEO, Mike Ashely and the Senior Independent Director, Simon Bentley. A recommendation to oppose the annual report was due to continued workplace and corporate governance concerns and inadequate reporting on steps undertaken by Sports Direct to rectify these problems. In recognition of executive remuneration being restricted solely to fixed pay, with no variable element, benefits or pensions paid, the Forum advised a vote in favour of the remuneration report.



This is not to say that no progress has been made on governance and workplace concerns. Sports Direct has appointed an employee representative to its board, which is a welcome development. The Forum was pleased that the Company Secretary was willing to provide comments prior to the issuance of the voting alert, in the context of the failure of Mr Bentley to attend a meeting with LAPFF.

At the AGM, employment practices remained a focus. Cllr Richard Greening thanked the board for their efforts in addressing the Shirebrook issues and requested a clarification on the election process of the newly appointed staff representative. He then called for an independent review of employment practices. Mr Hellawell subsequently addressed questions regarding the new representative, the feedback system and employee satisfaction; however, he seemed reluctant to further expand on the possibility of an independent review. LAPFF will continue to push the company for an independent review of its workplace and corporate governance practices to ensure it fully captures and addresses its social risks. LAPFF has written to ask to meet the new employee director.

Remuneration

LAPFF representative, Michael Marshall, attended **Ashtead Group's** AGM to discuss the company's remuneration in light of the new Department for Business, Energy and Industrial Strategy's green paper. The Forum was pleased that the company listened to shareholders following the 2016 AGM by changing the leverage incentive in the Performance Share Plan (PSP) pay scheme. The Forum further inquired whether the company welcomes the Government's Green Paper proposals, specifically in regards to executive pay and whether the company thinks that comparisons of CEO pay to median worker pay is a useful disclosure item for the company's stakeholders.

The Chairman personally thanked LAPFF for attending and briefly spoke to Michael Marshall about the issues he raised.

Finance and Accounting

Cllr Toby Simon of LAPFF met with **Lonmin Plc** to obtain an explanation of how the company will meet its commitments to its Social Labour Plan (SLP), to understand the company's position on carbon price and to confirm the company's ability to sustain long-term performance. The Forum was pleased with Lonmin's openness to dialogue and asked about the poor conditions of the platinum market, the company's ability to increase its net cash under these conditions, and the effectiveness of the recent rights issues.

Mergers & Acquisitions

A successful meeting took place between Dave Lewis, the CEO of **Tesco**, and LAPFF Chair, Kieran Quinn. LAPFF met with Mr Lewis to discuss the merger with Booker in order to further understand the rationale behind the deal, as well as the potential risks which may emerge. The Forum was pleased to hear the strong rationale behind the merger and has expressed support to Mr Lewis for the deal.



Cybersecurity

Cllr Alasdair Rankin raised cybersecurity at the **SSE** AGM, asking the Chairman, Richard Gillingswater, for greater detail on cybersecurity protections and how they will protect both SSE and its customers from an attack on the network and systems failures. He further asked about the results and the following recommendations of the company's internal audit on cybersecurity risks. SSE has now separately classified cybersecurity as a risk in its risk register and is managing the risk with a high priority level. A great deal of investment had taken place over the past three to four years, after the company had acknowledged its need to tighten up.

LAPFF has written to the Chairmen of **HSBC Holdings**, **Standard Chartered**, **WPP**, **Aviva** and **International Consolidated Airlines Group SA**, seeking meetings to better understand each company's respective approaches

to cybersecurity and how this issue is managed at the board level.

Public Health

The Forum met with Richard Burrows, the Chair of **British American Tobacco** to understand the role public health plays in influencing the company's business strategy and business model. The meeting followed a previous meeting in 2013 on similar concerns and followed up with discussions about the necessary steps taken to address public health issues and comply with anti-smoking regulations, including the introduction of new next generation products.



ENVIRONMENTAL AND CARBON RISK

LAPFF attended the **National Grid** AGM, and asked the Chair, Sir Peter Gershon, how the final recommendations of the Taskforce on Climate-Related Financial Disclosure (TCFD) would affect the company's reporting on climate change and in particular on scenario planning. Notably the Finance Director responded, who is aiming to see if other finance directors can commit to the TCFD and noted that there will be a statement around the release of next year's annual report.

During the meeting with **Lonmin**, the Forum asked about the company's position on carbon pricing. Brian Beamish, the Chair, spoke about carbon price discussions under way in South Africa, both at the governmental level and the company level. Any carbon tax would be applicable to Eskom, the national electricity company, and would thus be transferred directly to Lonmin.

Cllr Toby Simon met with **Total's** Senior Vice President for Strategy and Climate, to determine the company's objective for energy spreads and whether this is consistent with strategic resilience for Total's portfolio. Total's view is that climate is fully integrated into the business and that recent acquisitions align with the company's strategic ambitions on climate. This is not only to shift the energy mix but to reduce high-cost parts of the business and focus on low-cost sections in the upstream business. This aligns

with the company's shift to a 60% gas, 40% oil mix from 50-50 split. Both company reporting and direct engagement evidence that the company is serious about the implications of climate change for shareholder value, through changes to its portfolio and further moves into low carbon technologies, but that Total still considers itself an oil and gas business.

The Forum also met with legal counsel at **Southern Company** along with other US investors. The conversation covered climate change and carbon risk, and explored how the company is best positioning itself to report its strategy for a two-degree scenario in the context of the 2017 shareholder resolution to the company, which received 46% of support from shareholders. While Southern has been proactive in moving towards renewables, it is still the third largest carbon emitter in the US. The meeting was co-ordinated via the Forum's partnership with the 50/50 Climate Project.

SOCIAL RISK



Human Rights

A letter was sent to the Chief Executive Officer and the Chairman of **Hanwha Corporation** raising concern around the production and sale of cluster munitions, which cause indiscriminate death of civilians in conflict and post-conflict zones. Subsequent to some institutional investors disinvesting from the company, the Forum was exploring the extent to which Hanwha has stopped producing and selling cluster munitions, or intends to do so.

The meeting with the **British American Tobacco (BAT)** Chairman, also investigated whether supply chain risks, as well as monitoring and enforcement practices, are taken into consideration by BAT's board. The Forum's Deputy Chair, Ian Greenwood, raised concerns about cited instances of alleged poor labour practices and asked how these were dealt with by management. He also discussed the possibility of the company appointing a board member with a sustainability background to help reduce the risk of human rights abuses in the supply chain.



Employment Standards

Employment standards were again raised by LAPFF at the **Sports Direct International** AGM, as the situation in Shirebrook hasn't been fully resolved, with individual investors and Unite questioning the board. LAPFF member, Cllr Richard Greening, asked about a fully independent assessment of corporate governance practices and work place conditions at the Shirebrook warehouse, as well as information on the process used to select the current worker representative on the board.

The Forum had concerns about the method of selection of the representative, who holds a relatively high position (store manager) and who was elected by only half of the staff. While this individual claimed that all staff can communicate with him, Unite has informed the Forum that the representative has not contacted Unite and employees working in Shirebrook were not asked to participate in the election. At the AGM, Cllr Greening pointed out that unresolved problems with labour rights still exist, such as money owed to agencies. Overall, the Forum was disappointed to see that Sports Direct has not progressed very far to resolve concerns over its workplace and corporate governance practices.

At the **SSE** annual meeting, LAPFF also asked about human capital management, particularly how the company's human capital measure is being updated and when the outcomes will be disclosed. SSE had committed to producing a further report on the position.

Employment standards were also raised during the meeting with the **Lonmin** Chair, in light of criticism of the company's failure to adequately address employee housing problems and implement provisions of its existing SLP. While the Forum recognises the company's commitment to rectify the situation, there has been extensive press coverage regarding the company's failure to meet its SLP obligations.

RELIABLE ACCOUNTS

LAPFF has long held that the Financial Reporting Council (FRC) has been setting accounting standards that are not aligned with the law, in particular the requirement to reflect the solvency of a company. A Freedom of Information Act request (FOI) by PIRC revealed that the Government has not confirmed that LAPFF's is wrong, nor that the FRC position is right. That is contrary to what the FRC had said publicly, including to Parliament.

Given that, LAPFF has written to the Senior Partners of the six largest accounting firms and the Chairs of their public interest committees to set the record straight as well as the three FRC board members, setting out the catalogue of problems and legal inaccuracies and inconsistencies. Both letters were then intercepted by the FRC. In the case of the accounting firms the FRC convened a closed meeting to co-ordinate a response which repeats existing FRC assertions. That said, some of the Big 4 replies are marginally better than others, and follow-up letters have been sent, with no replies as yet. In the case of the LAPFF letter to FRC NEDs a letter was written by the FRC Chairman stating that the points would be considered by the FRC board. No reply has yet been received. All letters sent include new information and evidence not previously addressed by the FRC which is wholly contradictory to the FRC's position, including documents and guidance from the FRC itself.

PIRC on behalf of LAPFF has had two meetings with BEIS officials as a result of the Freedom of Information Act discoveries. The position has been reiterated that the problems with the FRC run so deep that the FRC should be disbanded and that a proper competent authority should be set up to replace it. LAPFF have been asked to supply a position paper on IFRS for the UK post-Brexit and then for possible endorsement bodies and criteria after Brexit.



The FRC decision not to pursue KPMG for its HBOS audit has triggered a very negative response from the mainstream press. The FRC analysis that the HBOS collapse was caused by the events of October 2008 (liquidity) is contrary to the conclusions of the Parliamentary Commission for Banking Standards, which was that October 2008 was the occasion of the collapse, but the bad lending and poor balance sheet was the cause of the loss (insolvency). The FRC position that KPMG could not have been expected, in spring 2008 when signing the December 2007 HBOS accounts, to have predicted a going concern, is also contrary to contemporaneous evidence from December 2007 where KPMG partner was at an investor meeting and admitted that the FRC itself was aware that banks had going concern issues.

MEDIA COVERAGE

[Pension fund group calls for corporate governance review at Sports Direct](#) – CityAM, 7 September 2017

[Council pension funds call for review of working conditions at Sports Direct](#) – LocalGov, 7 September 2017



NETWORKS AND EVENTS

The following lists some of the events and meetings attended by LAPFF representatives during the quarter:

- Attendance at the Sports Direct Investors Roundtable to discuss the Company's new business strategy, *Selfridges of Sport*, and the year's financial results.
- Participation in Trade Union Shareowners event to discuss poor working conditions in the UK hotel sector and the risks these create for investors.
- Participation in the FAIRR Initiative event on the financial impact of intensive meat production.
- Participation in a webinar organised by CDP Sector on diversified miners and a seminar organised by Ceres on water risks in the food and beverage industry.
- Participation in a call on the OECD National Contact Point process and how best to use this mechanism for investor purposes.

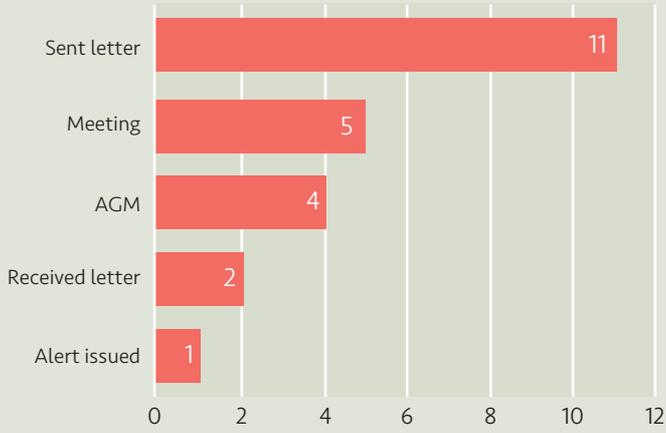
COMPANY PROGRESS REPORT

20 companies engaged over the quarter

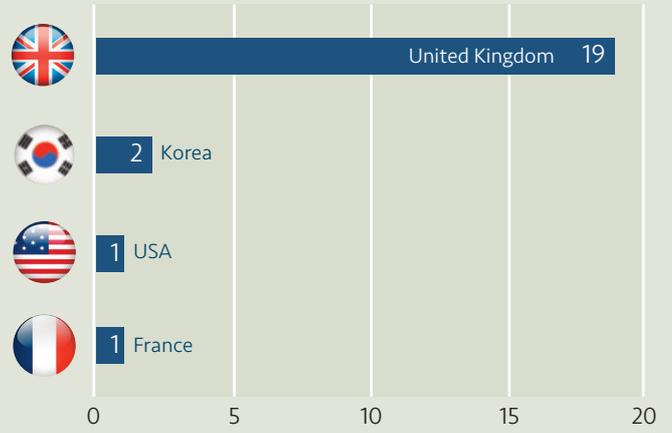
Q3 2017 ENGAGEMENT DATA				
	Company	Topics	Activity	Outcome
1	Ashtead Group Plc	Remuneration	AGM	Satisfactory Response
2	Aviva Plc	Governance (Cybersecurity)	Letter/Letter Received	Dialogue
3	British American Tobacco	Public Health/Supply Chain Management/ Board Composition	Meeting	Small Improvement
4	Hanwha Corp	Human Rights	Letter/Letter Received	No Improvement
5	HSBC Holdings Plc	Governance (Cybersecurity)	Letter/Letter Received	Dialogue
6	International Consolidated Airline Group SA	Governance (Cybersecurity)	Letter	Dialogue
7	ITV Plc	Governance (Cybersecurity)	Letter	Awaiting Response
8	Lonmin Plc	Employment Standards/ Climate Change/ Finance and Accounting	Meeting	Substantial Improvement
9	Marks & Spencer Group Plc	Governance (Cybersecurity)	Letter	Awaiting Response
10	National Grid Plc	Climate Change	AGM	Dialogue
11	Prudential Plc	Governance (Cybersecurity)	Letter	Dialogue
12	Sainsbury Plc	Governance (Cybersecurity)	Letter	Awaiting Response
13	Segro Plc	Board Composition	Letter	Awaiting Response
14	Southern Company	Climate Change	Meeting	Moderate Improvement
15	Sports Direct International Plc	Employment Standards/ Board Composition/ Governance	AGM/Alert Issued/ Roundtable	No Improvement
16	SSE Plc	Employment Standards (Cybersecurity)	AGM	Change in Process
17	Standard Chartered Plc	Governance (General)	Letter	Awaiting Response
18	Tesco Plc	Mergers & Acquisitions	Meeting	Moderate Improvement
19	Total SA	Environmental Risk	Meeting	Substantial Improvement
20	WPP	Governance (Cybersecurity)	Letter/Letter Received	Dialogue

COMPANY ENGAGEMENT ACTIVITIES

Company engagement activities



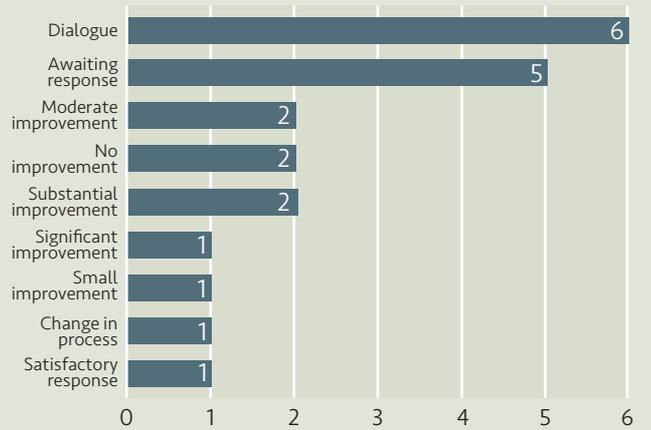
Company domiciles



Position engaged



Outcomes



LOCAL AUTHORITY PENSION FUND FORUM MEMBERS

- Avon Pension Fund
- Barking and Dagenham LB
- Bedfordshire Pension Fund
- Cambridgeshire Pension Fund
- Camden LB
- Cardiff and Vale of Glamorgan Pension Fund
- Cheshire Pension Fund
- City of London Corporation
- Clwyd Pension Fund
- Croydon LB
- Cumbria Pension Scheme
- Derbyshire CC
- Devon CC
- Dorset County Pension Fund
- Dyfed Pension Fund
- Ealing LB
- East Riding of Yorkshire Council
- East Sussex Pension Fund
- Enfield LB
- Falkirk Council
- Gloucestershire Pension Fund
- Greater Gwent Fund
- Greater Manchester Pension Fund
- Greenwich Pension Fund RB
- Gwynedd Pension Fund
- Hackney LB
- Haringey LB
- Harrow LB
- Hertfordshire County Council Pension Fund
- Hounslow LB
- Islington LB
- Lambeth LB
- Lancashire County Pension Fund
- Lewisham LB
- Lincolnshire CC
- London Pension Fund Authority
- Lothian Pension Fund
- Merseyside Pension Fund
- Newham LB
- Norfolk Pension Fund
- North East Scotland Pension Fund
- North Yorkshire CC Pension Fund
- Northamptonshire CC
- Northumberland CC
- Nottinghamshire CC
- Powys County Council Pension Fund
- Redbridge LB
- Rhondda Cynon Taf
- Shropshire Council
- Somerset CC
- Sheffield City Region Combined Authority
- South Yorkshire Pensions Authority
- Southwark LB
- Staffordshire Pension Fund
- Strathclyde Pension Fund
- Suffolk County Council Pension Fund
- Surrey CC
- Sutton LB
- Teesside Pension Fund
- The City and County of Swansea Pension Fund
- The Environment Agency Pension Fund
- Tower Hamlets LB
- Tyne and Wear Pension Fund
- Waltham Forest LB
- Wandsworth LB
- Warwickshire Pension Fund
- West Midlands ITA Pension Fund
- West Midlands Pension Fund
- West Yorkshire Pension Fund
- Wiltshire CC
- Worcestershire CC