RESPONSIBLE INVESTMENT AND STEWARDSHIP REPORT

2022

SCOTTISH WIDOWS

CONTENTS

CEO LETTER

Climate change is undoubtedly the biggest crisis we face as a planet. Governments around the globe are increasingly taking bold steps to address this emergency head on, spurred on by activists, and individuals are increasingly playing a part in changing the way we live to preserve the planet for future generations. It is incumbent on the corporate world to be a trail blazer and lead this charge – radically changing its practices and priorities will have a hugely positive impact. As Scottish Widows' new CEO it is my privilege to join an organisation which has such a pivotal role to play in shaping the behaviours of the firms we invest our customers' pension funds in. Being bold and acting in our customers' and societies' best interests, is part of Scottish Widows' DNA. The challenges the world faced when Scottish Widows was set up in 1815 were entirely different, but we are resolute in our determination to address the challenge of climate change.

Millions of customers entrust us with their pension savings and we have a duty to them to make good decisions, which will aid their long-term prosperity and help to build their financial resilience. Our role is to deliver good investment outcomes to our customers, which extends to us considering the impact of our decisions on the planet and Britain's transition to net zero.

Scottish Widows is committed to striving for sustainable financial outcomes for our customers and a more inclusive and sustainable future for people and businesses. This report sets out the progress we've made through 2022 in working with our partners and the firms we invest in to work towards a brighter future together.

Our Values

Scottish Widows' parent Lloyds Banking Group recently launched a refreshed strategy and set of values, to help us better meet the needs of our customers in an ever changing and dynamic market. This saw us step up our role in helping our local communities and supporting people from every background, to face into the biggest challenges we face as a society and developing profitable solutions that help both people and the planet.

Putting our values into action is recognised across Scottish Widows as the key to how we deliver against our strategy. By being Bold we can challenge the status quo and building Trust will empower colleagues to speak up and take action. We will support our colleagues by putting People First, arming them with the right products, services, tools and skills to go further for customers. Being Inclusive demonstrates that we value everyone and have programmes in place to support development and opportunity for our under-represented groups.

For the purposes of this report the key value is Sustainability – caring for our planet, taking responsibility for the impact of our actions on nature and Britain's transition to net zero. We will use our scale, expertise and influence to be a positive force in shaping the role finance plays in reaching this goal. We are also investing in engagement, sentiment tracking and development interventions that demonstrate how we can live our values every day to enable us to get things right for our customers and colleagues.

Our Actions

These ambitions have informed our focus on Responsible Investment and Stewardship activity during 2022. We have deepened and expanded our thematic stewardship priorities, adding a third stewardship priority on 'Human Rights', and expanding 'Climate' to 'Climate and the Environment', so as to encompass nature and biodiversity. These sit alongside our priority on 'Board Diversity'. These improvements empower us to influence more investee companies, on a greater range of issues, allowing us to manage risks and returns in a more effective way, safeguard our customers' long-term savings and ultimately improving the chances of a sustainable transition to net zero. We have made significant progress in our Climate Action Plan – our climate-aware strategies investment assets increased by £12 billion in 2022. This brings us to a cumulative £17.5 billion, well on the way to meeting our £20-25 billion goal by end of 2025. Our investment in climate solutions within these same strategies amounted to £1.3bn, achieving our 2025 goal of at least £1bn.

As one of the industry's major players, we are an active member of a growing number of collaborative investor and policy advocacy activities, amplifying our voice to encourage companies to engender positive change across a host of environment, social and governance factors, and take greater action towards net zero emissions before 2050, extending that to include nature and biodiversity. We were an early stakeholder in the development of government policy to allow asset owner directed voting, and during 2022 we worked with key managers to develop functionality allowing us direct key votes. This enables us to use our voice to influence companies and deliver better long-term sustainable value for our customers. Similarly, we are contributing to giving social factors the importance and focus they need through our participation in DWP's Taskforce on Social Factors.

As long-term investors, we encourage our investee companies to foster cognitive diversity at all levels of their business. This is something whose value Scottish Widows recognises in our own operations, for example through our Colleague Advisory Panel.

Since joining Scottish Widows I have been struck by the commitment and focus of our colleagues, collaborating internally and externally to achieve a sustainable future. There is of course much more work still to be done – and it won't be easy – but it is imperative that we advance the sustainability agenda, to ensure that we take a holistic look at all ESG factors and integrate them more deeply into every aspect of our decision-making, and in the process influence the industry and the companies we invest in to up their game and strive to do better.

True wealth is realising a future which we all want to live in and we have an opportunity to make that happen, but the clock is ticking. Over the course of this report you will read more about the journey we are on, what we have achieved and what we still aspire to achieve, brought to life through examples and case studies.

Chirantan Barua
CEO, Scottish Widows

OUR KEY AREAS OF ACTIVITIES ACROSS 2022

Enhance

We integrate ESG factors, including stewardship activity, across our investments. In 2022, we developed a range of Scottish Widows funds which has a bias towards investing in companies that are adapting their businesses to be less carbon intensive and developing climate solutions. These 'building block' strategies are aimed at helping us achieve our net zero targets to benefit our customers and complement the external climate-aware funds we also invest in.

Reduce

We launched our Climate Action Plan – a roadmap of how we aim to halve the carbon intensity of all our investments by 2030, and to achieve net zero emissions by 2050 or sooner. It includes investing up to £25bn in climate-aware investment strategies by 2025 through allocations to specialist funds, with at least £1bn in climate solutions. As of the end of 2022, we had invested £17.5bn in climate-aware investment assets, of which £1.3bn was in climate solutions.

Challenge

We challenge the companies we invest in to make positive changes to their business practices to create sustainable benefits in the long term for our customers, the economy, the environment and society. We also regularly review and challenge the engagement activities carried out by our appointed investment managers to ensure their approach is aligned with ours. To do this we focus on key themes to ensure our engagement activity is effective. In 2022, we added human rights as a new social theme and extended our climate and carbon theme to include broader environmental factors like biodiversity and deforestation, and explicitly added the 'just' element of the low carbon transition.

Lend

We currently lend around £7.5bn from our annuity fund to support social housing, and sustainable energy and infrastructure projects, supporting the transition to a low-carbon future and making a contribution to the Lloyds Banking Group ambition of Helping Britain Prosper. In 2022, we invested a total of £328m to support housing associations initiatives, including the development of affordable, energy efficient housing, as well as financing retrofitting existing homes to improve energy efficiency.

Vote

We're a significant shareholder in many of the world's large listed companies, and we've produced our Voting Guidelines to help us, and the investment managers we work with, use our voting rights to encourage companies we invest in to improve their ESG performance. In 2022, we began directing votes in pooled funds managed by BlackRock, using a policy which most closely aligns with our own approach. We also began trialling the ability to direct votes with our appointed active investment manager, Schroders.

Exclude

We've divested c.£3bn from companies that haven't met our ESG criteria since introducing our Exclusions Policy in November 2020. In 2022, we evolved our policy with the addition of tobacco exclusions and lowering the threshold for maximum permitted revenues from extraction of thermal coal and tar sands. To apply exclusions in our passive index funds, we worked with FTSE Russell to create a range of custom ESG screened indices*.

Collaborate

We're involved in collective UK and global activity to support responsible investment. By working with others, we strengthen our hand in challenging for change. We're actively involved in a broad number of Initiatives, often taking a leading role. New memberships and initiatives for 2022 included: UNPRI Advance, Just Transition Finance Challenge, Deforestation Guidance, FTSE 100 Pension Emissions Report, DWP Taskforce on Social Factors, Farm Animal Investment Risk and Return (FAIRR), and the Workforce Disclosure Initiative (WDI).

* In the event that an existing holding exceeds a revenue threshold, a review will be carried out by our Investment team. If the review deems that this is likely to persist for the foreseeable future, we would look to exit the holding, taking into account market conditions and any other investment impact to the funds.

ABOUT SCOTTISH WIDOWS

1.1 OUR PRODUCTS AND CUSTOMERS

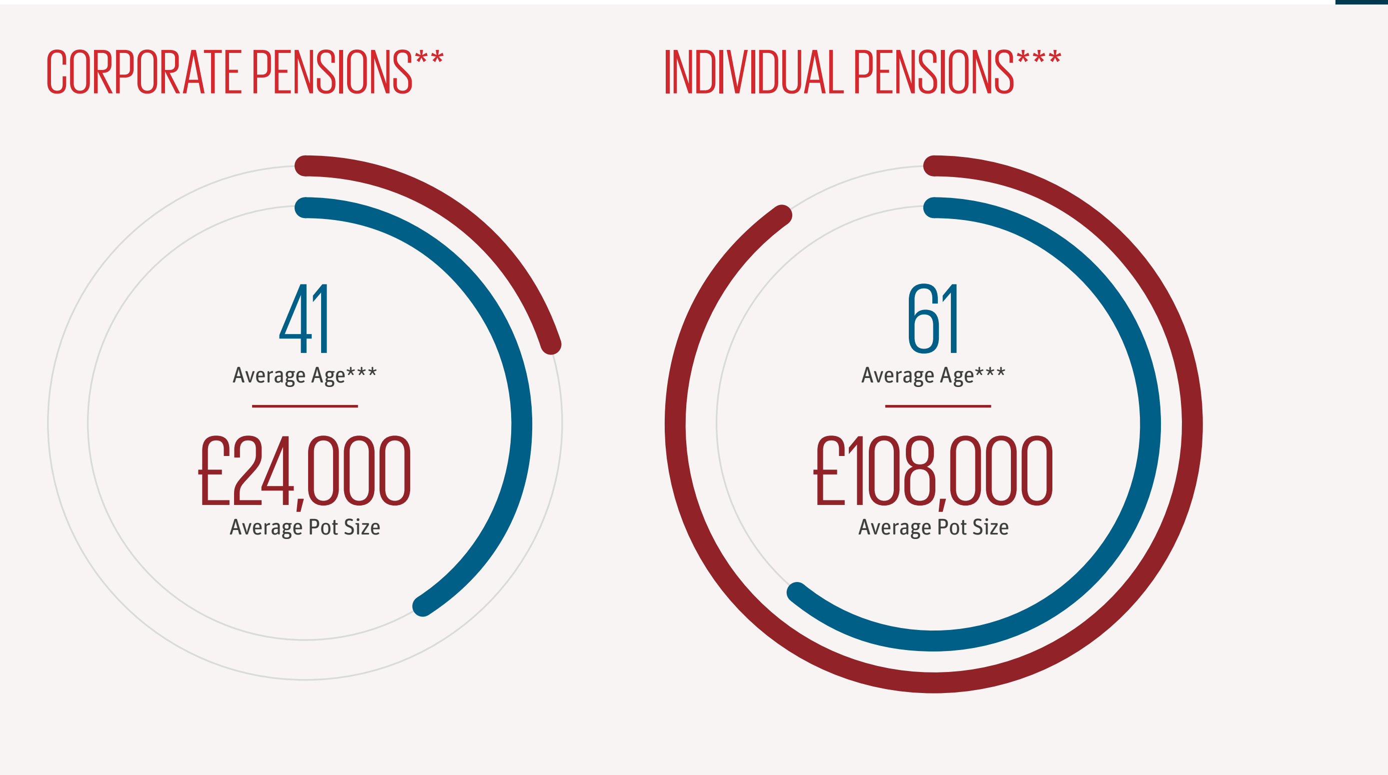
Scottish Widows Group Limited (Scottish Widows), a major insurance, investment and long-term savings provider, is part of Lloyds Banking Group (LBG), which has an overarching purpose of Helping Britain Prosper. At Scottish Widows, this means helping our customers to plan and prepare for their financial futures. We recognise that each of our customers are different and we are committed to working to understand them, putting them at the centre of the decisions we make and helping ensure they have a future worth retiring in. Scottish Widows manages and supports a large number of Defined Contribution contract-based and trust-based pension schemes, and works with many employers, employee benefits and investment consultants, and financial advisers in the process.

By the end of 2022, Scottish Widows' assets under management were c.£166bn*. Included in this is c.8.5m live customer policies across pensions life and savings channels, well over half of which are pensions policies. Other customer investments include life insurance and retail and institutional investment into Scottish Widows Authorised Corporate Director (ACD) funds. An ACD is a corporate body given powers and duties under FCA regulations to operate an open ended investment company. Scottish Widows operates two such bodies, Scottish Widows Unit Trust Managers Limited (SWUTM) and HBOS Investment Fund Managers Limited (HIFML).

Some customers may hold more than one pension or savings product and as such the number of individual customers will be lower.

The Pension Investment Approaches – with a value nearing £50.9bn – forms the base of our workplace pension offering and now amounts to over a third of our total customer assets.

In early 2022, Lloyds Banking Group acquired Embark – a digital retirement solutions provider. This report does not cover this part of our business as we are currently in the process of assessing how our Responsible Investment and Stewardship policies may apply to that business.



* Total Assets Under Management includes
Policyholder: unitised and with-profit fund assets held in life and pension funds of Scottish Widows Limited and Scottish Widows Europe; mutual funds managed by SWUTM and HIFML; and the workplace savings business of Scottish Widows Administration Services Limited. In scope assets include investment funds structured as insurance contracts. Assets under administration for customers of Schroders Personal Wealth and Halifax Share Dealing Limited are not included. Assets held under the Embark group are currently excluded from these calculations. Shareholder: assets held by Scottish Widows Limited and Scottish Widows Europe backing annuities and non-unitised liabilities. Investment balances in other Scottish Widows group companies including the General Insurance business. Policyholder and Shareholder investments are governed by the Responsible Investment and Stewardship Framework, Stewardship Policy and exclusions policy, while the direct lending part of Shareholder investments are also covered by Lloyds Banking Group External Sector Statements.

** Based on our front book platform business and amounts to c.£70bn of corporate pensions covering 3m policies and c.£15bn or individual pensions over 136 thousand policies. This does not include approximately £24bn of asset value of longstanding corporate and individual pensions business, which we will aim to include the profile of these books of business in forthcoming reports. Longstanding Pensions are our closed book of business

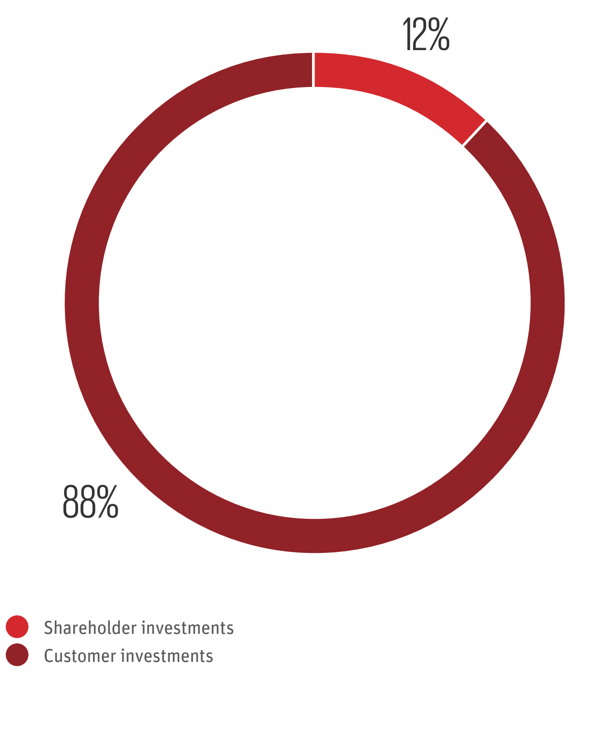
*** Due to auto-enrolment, we now have more customers who may have a 60+ year investment horizon. New, younger customers currently offset the aging of existing customers. For corporate pensions the average age has fallen from 42 since last year on a like-for-like basis and risen from 60 for Individual pensions.

1.2 BREAKDOWN OF OUR INVESTMENTS

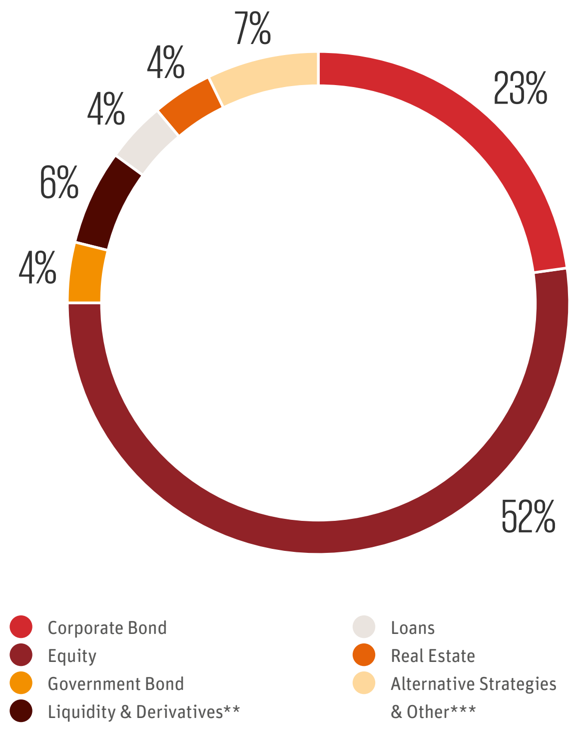
Our investment portfolio includes Scottish Widows' 'customer funds' which are primarily comprised of life and pensions products, retail savings and investments, and some institutional business. It also includes our 'shareholder investments' which is made up of our investments used to manage our liabilities, i.e. paying annuities*, and other surplus capital. Both our Customer and Shareholder investments are governed by our Responsible Investment and Stewardship framework, Stewardship Policy and Exclusions Policy, while the direct lending part of Shareholder investments is covered by Lloyds Banking Group External Sector Statements**.

Our total investment portfolio demonstrates diversification across regions and asset classes, factoring in the long-term needs of our customers. Our resulting portfolio asset class breakdown is the outcome of choices made by our customers for self-select funds and by employers for scheme default funds, as well as discretionary investment of multi-asset funds by Scottish Widows.

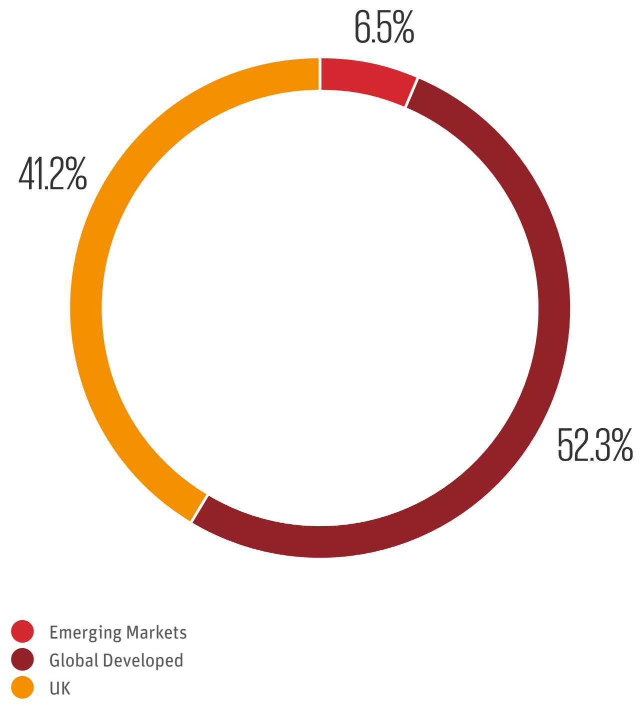
OUR CUSTOMERS AND SHAREHOLDER INVESTMENTS



SCOTTISH WIDOWS ASSET CLASS BREAKDOWN



REGIONAL SPLIT OF SCOTTISH WIDOWS ASSETS



* An annuity is a type of retirement income product that allows customers to exchange pension savings for a guaranteed and regular income for the rest of their life, with no investment risk for the customer. We invest the proceeds that we receive from our annuity customers by making long-term fixed income investments and loans. https://www.lloydsbankinggroup.com/who-we-are/responsible-business/downloads.html

** 'Liquidity' includes cash and other money market instruments.

*** 'Other' includes some externally managed multi asset vehicles and commodity funds.

1.3 OUR PENSION PORTFOLIO FUNDS

The Scottish Widows Pension Portfolio Funds are the underlying investments in our flagship workplace pension default strategy, Pension Investment Approaches (PIA), as well as providing multi-asset investment options to personal pension customers. These funds have a growing allocation to climate-aware or ESG-screened strategies.

Our Strategic Asset Allocation (SAA) Review for PIA

We adapt our Pension Portfolio Funds, which underpin our workplace default strategy, to help maintain an optimal and effective investment mix. We believe strategic asset allocation has the biggest impact on long-term performance. Pensions are long-term investments and our experience shows that there's the opportunity to ride out periods of shorter-term market volatility in markets, with assets returning to growth over the longer term.

We constantly monitor the portfolios and adapt them if there's a change to the market environment that leads to adjustments to our longer-term outlook, and as we see new investment opportunities emerge.

We also conduct our in-depth review – the Strategic Asset Allocation review – every 12-18 months. Changes will only be made if the new allocation proposals are expected to produce more efficient portfolios, i.e. to generate higher returns without increasing risk or to generate similar returns for a lower level of risk.

Given significant market volatility and uncertainty around the macroeconomic environment, with bonds losing their diversifying nature, we decided not to make any material strategic asset allocation changes in 2022. We reduced equities exposure by 1% using cashflow and allocating to cash-type assets. We introduced an allocation to the BlackRock ESG Insights Corporate Bond Fund using positive cashflow and changed the benchmark for our global property fund to track a green low carbon target index (further information on these funds can be found in Section 2.4).

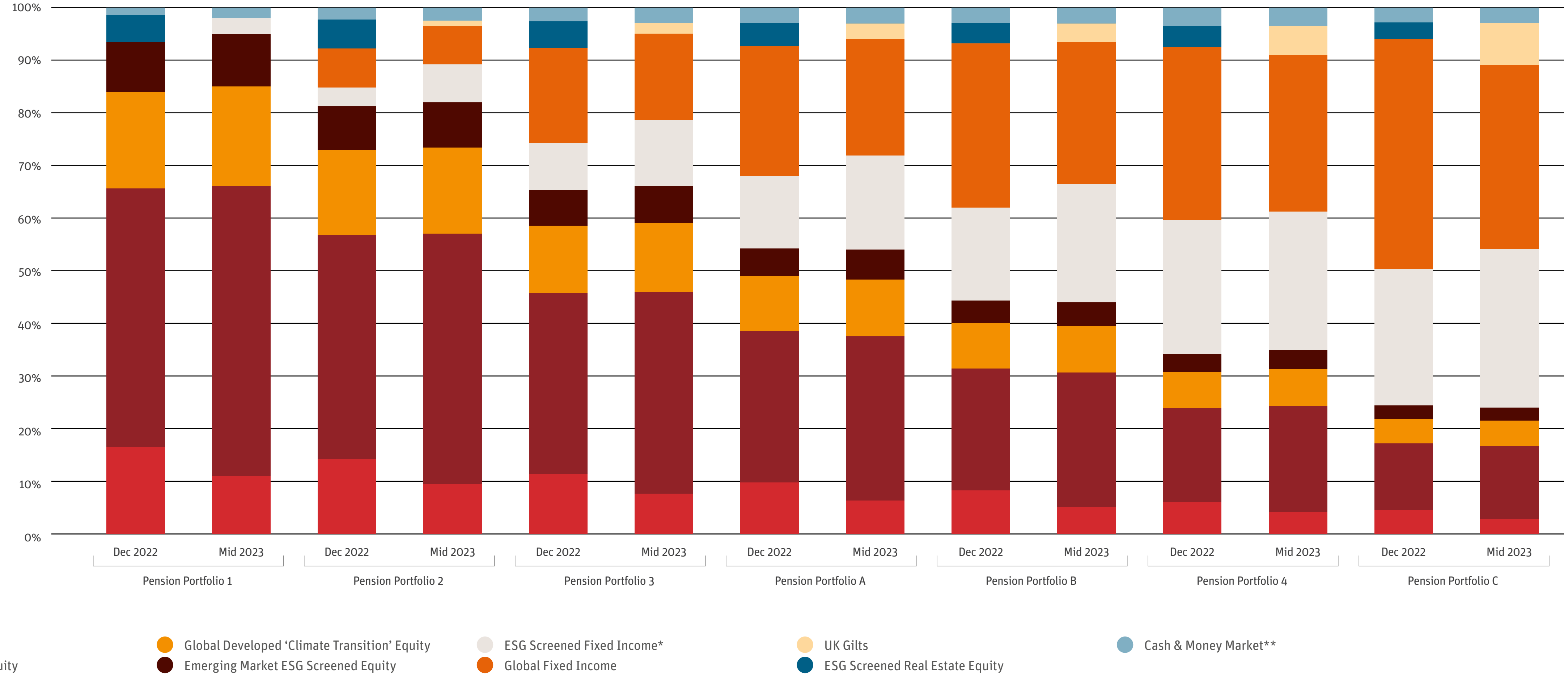
We are making a number of adjustments as a result of the in-depth asset-class modelling and optimisation process for the 2023 Strategic Asset Allocation review. This includes further reducing the UK equities bias in the regional equities mix. In line with peers, we have historically had a home bias reflecting the view that customers felt more comfortable investing domestically. We do not believe a systematic continual overweight to the UK relative to a global market-cap index can be justified on investment grounds. So over time, we have been reducing the UK equity weighting. In our workplace default, we are making a further reduction to UK from c.18.5% to c.12.5% of the total equity. Further reductions towards the UK's weighting within the global market will be driven by valuation differentials in the market.

We are diversifying the bond element of the portfolios by introducing allocations to a UK government bond fund. To date, we have preferred corporate bonds over government bonds, due to the prolonged low-yield environment in the wake of the Global Financial Crisis. In 2022, the bond market and global economic environment experienced some major shifts with bond yields rising. Our models show by adding gilts and reducing reliance on corporate bonds, the overall projected risk-adjusted returns improve. We will allocate between 1%-5% to 0-5-year gilts given the comparable yields available at the shorter end of the yield curve, and given their lower level of interest rate duration risk. The gilts allocation, in particular, diversifies the bond segment of the portfolio in the run-up to retirement.

Within property, we are slightly reducing the allocation to global real estate investment trusts (REITs). We believe the longer-term outlook for property markets is more challenging in an environment of higher interest rates and possibly more difficult credit conditions.

1.3 Our Pension Portfolio Funds continued

Pension Portfolio Funds: Strategic Asset Allocations***



* ESG transitioning in Sterling fixed income fund implemented in Q1 2022

** Cash & Money Market includes short duration bonds

*** At point of publishing the asset allocation changes labelled as 'Mid 2023' will be complete or well underway, following the most recent strategic asset allocation review commencing late in 2022

1.3 Our Pension Portfolio Funds continued

PENSION PORTFOLIO FUNDS INDUSTRY BREAKDOWN

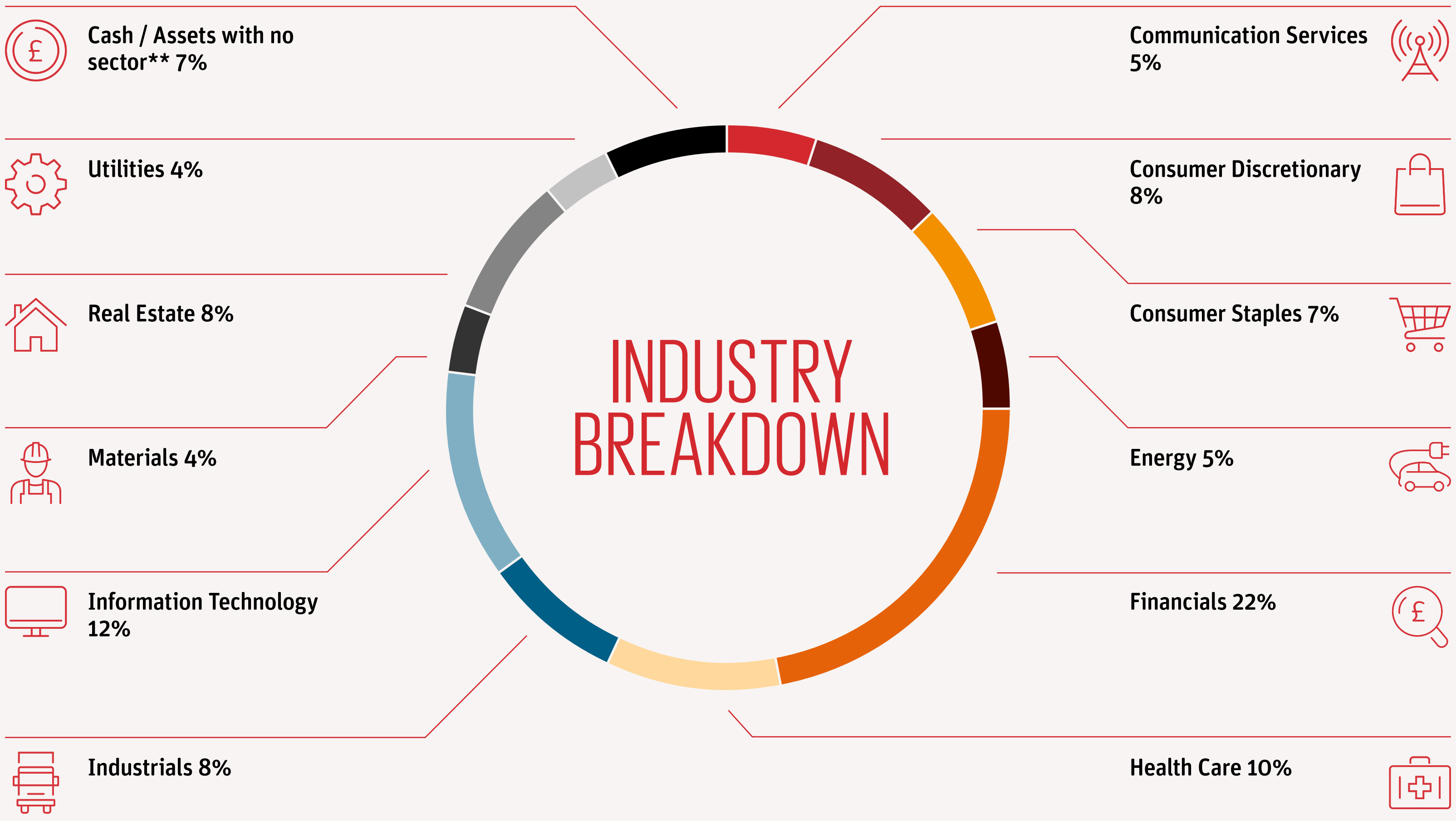
At the end of 2022, assets under management in these seven Pension Portfolio Funds were close to £51bn. Their aggregate sector exposure on a look-through basis, classified using the Global Industry Classification Standard (GICS)*, is illustrated opposite.

Broadly, the Pension Portfolio Funds are most heavily exposed to Financials and Information Technology, followed by Consumer Discretionary, totalling over 40% of the portfolio value across these funds. The four sectors considered most material to a low carbon transition are Energy, Industrials, Materials and Utilities. Looking across the Pension Portfolio Funds, the four sectors represent a little over a fifth of exposure.

It is critical that we invest into a diverse range of sectors and underlying industries as it allows us to spread investment risk and to play an active role in bringing about real world change through our stewardship initiatives with investee companies.

The sector analysis excludes Pension Portfolio 5, which is a money market fund.

Pension Portfolio Funds



* GICS® is an industry analysis framework that helps investors understand the key business activities for companies around the world. MSCI and S&P Dow Jones Indices developed this classification standard to provide investors with consistent and exhaustive industry definitions. www.msci.com/our-solutions/indexes/gics

** 'Assets with no sector' relates to sovereign debt, cash, index and currency derivatives, and an element of global fixed income assets, many of which securitised, that have not been assigned GICS sectors.

1.4 OUR INVESTMENT GOVERNANCE

OUR FUND MANAGEMENT TIERS

Being an asset owner means that we delegate most investment management activities to our appointed investment managers, but actively use stewardship tools to monitor our managers.

Tier 1: Scottish Widows mandated funds

Our Tier 1 appointed investment managers are responsible for the day-to-day fund management including the monitoring of investee companies on matters including strategy, performance and risk, capital structure, and environmental, social and governance (ESG) factors. This includes:

- Our regulated funds which are owned by Scottish Widows' Authorised Corporate Director (ACD)*
- Where Scottish Widows owns the investment strategy and sets the mandate

Across our range of mandated funds our investment managers use a range of internal and external specialist analysis, market data, third-party ESG assessments and other data sources to evaluate an investment's characteristics, including both its financial outlook and its status in terms of ESG risks and opportunities. We offer a wide range of investment strategies which integrate both financial and non-financial considerations in their design or asset selection process. Whilst these investments are managed on our behalf, we have control over voting and engagement activity. In addition, we have the right to instruct our own votes. We have direct control over investments made in Tier 1 which enables us to work in collaboration with our appointed investment managers, engage with holdings directly, and put forward shareholder resolutions.

We closely monitor the compliance with our Stewardship policy by Tier 1 managers. Should material concerns arise regarding their stewardship programmes, we will act, as allowed by our contractual relationships with these managers. Where we own shares in our appointed investment managers, we may also engage with them as we would with any other investee company, to address suboptimal performance on responsible investment issues.

Over the course of 2022, we have improved the engagement with our appointed investment managers and investee companies. This year, we have looked to enhance the expectations we set on behalf of our customers and better communicate these to Tier 1 managers.

In 2023, we will continue to use the Stewardship and Engagement options available to us in a bid to improve investment outcomes and ensure we are delivering value to our customers.

Our Stewardship and Engagement Options:

- Oversight and direction of the stewardship activity undertaken by delegated asset manager.
- Participating in collective shareholder resolutions
- Voting guidelines and instructions
- Collaboration with other investors
- Challenging delegated managers where differences in approach
- Our Stewardship and Exclusions policies are mandatory

Tier 2: Managed multi-asset pension funds

Our multi-asset pension funds invest in funds from multiple external investment managers. Whilst the choice of underlying funds is within our control, specific stewardship activity carried out by these investment managers is not. Therefore, we leverage our strong relationships to ensure we have regular dialogue to influence investment and stewardship activity. As a last resort, it is within our mandate to remove our investments from Tier 2 asset managers if we are not satisfied with their approach to stewardship.

Our Stewardship and Engagement Options:

- Oversight of the stewardship activity undertaken by investment manager.
- Regular governance meetings to review and challenge stewardship activity in line with our engagement priorities
- Our Stewardship and Exclusions policy are applied on a comply or explain basis
- Collaboration with other investors
- Apply voting options available

Tier 3: External fund links

Tier 3 refers to the external funds that Scottish Widows customers can select from, usually via a life or pension wrapper. We do not have the authority to mandate the managers of these funds in relation to investment and stewardship actions, but can remove their funds from our offering if they do not meet our expectations.

We also have an open dialogue with these investment managers to ensure they understand our expectations around our investment and stewardship themes. In our 2021 Responsible Investment and Stewardship report, we set a target for Tier 3 managers to become signatories of the UK Stewardship Code by 2024. We continue to engage with them to help them meet this target.

Our Stewardship and Engagement Options

- Informing managers of our Stewardship and Exclusions Policy to encourage them to comply
- Monitoring managers' ratings e.g. PRI**, ShareAction*** and Stewardship Code**** signatory status
- Requiring specific disclosures for trust-based schemes to support trustees' stewardship activities

Tier 4: Funds offered through technology platforms

Tier 4 are externally managed funds outside of the Scottish Widows fund range. They may be offered to customers by specific pension schemes or accessed via a fund supermarket. We do not have authority over client-directed investments or investment strategies in these funds. Therefore, Tier 4 funds are exempt from the expectations set out in our Stewardship and Exclusion policies.

* Authorised Corporate Director, a corporate body given powers and duties under the FCA regulations to operate an open ended investment company. Scottish Widows operates two such bodies, SWUTM and HIFML.

** PRI | Home (unpri.org)

*** ShareAction | Harness the power of investment

**** Investors I UK Stewardship Code I Financial Reporting Council (frc.org.uk)

1.4 Our investment governance continued

ADDITIONAL INFORMATION

Managers of Scottish Widows mandated customer funds are expected to comply with contractual and regulatory requirements of Investment Management Agreements (IMAs) and individual fund mandates. Scottish Widows designs a funds mandate in conjunction with the investment manager as part of a detailed selection process that considers a broad range of factors including a firm's structure and financial stability, management, investment personnel and strategy, its risk management approach and operational support abilities. Each mandate documents clear performance and investment risk constraints tailored for an individual fund's requirements from an asset class, investment strategy and management approach and the profile and duration of liabilities where appropriate.

We operate regular review processes with our appointed investment managers covering a wide range of factors such as long- and short-term performance, sustainability factors, stewardship outcomes and the evolution of portfolio characteristics against the market backdrop. Mandates are usually in place for a minimum of five years to allow a holistic review of managers' performance, including their ESG and stewardship activities and taking of action, if necessary, at certain intervals. Our Investment Management Agreements contain appropriate service-related provisions and termination rights-related to performance. Our specialist investment oversight teams have a diverse skill set and wide-ranging experience of investment managers, processes and market developments. An investment manager failing to meet performance objectives or constructing portfolios not aligned with our beliefs can be quickly identified. Our process of continual oversight enables engagement activity to commence quickly and options for improvement to be identified. Ultimately, we have the option of terminating a manager and seeking a replacement.

1.4 Our investment governance continued

PERFORMANCE REVIEW

We review Tier 1 and Tier 2 appointed investment managers' performance regularly, usually monthly but at least quarterly, to have a clear understanding of performance trends and patterns, so that potential issues are identified in a timely manner. Investment Leads, in our Investment Office, are responsible for the governance of all mandated and externally managed funds. They are supported by a broader team of investment experts. The Investment Leads specialise in different fund types or asset classes.

A recent enhancement to our governance process involves monitoring ten key factors, including ownership, process/style drift, liquidity and material fund AuM changes, with the aim of identifying potential issues or early warning of possible risks that may require investigation. This enables us to be more proactive and intervene at an earlier stage when concerns with any of our appointed investment managers are identified.

As part of the quarterly performance review process undertaken by the Investment Leads, we use metrics that show how each fund is performing on a range of ESG measures. Any issues we identify, such as consistent failure to meet performance targets, breaches of mandate parameters, or inconsistency between data metrics and the managers explanation of ESG integration in the investment process are document through this review and if unable to be resolved will be escalated. If one of our appointed managers consistently fails to meet their performance target, and engagement with them fails, we have the option of selecting a new manager.

Other external managers, classified as Tier 3, are monitored by our Fund Manager Assessment team, which produces regular qualitative reports for our investment committees. Quantitative performance monitoring is undertaken monthly and the output for all funds is reviewed to identify any underperforming funds that may require further scrutiny. During 2022 several funds that had not been performing as expected, and where we had concerns about the fund's suitability or ability to meet its stated objectives, were earmarked for closure.

When reviewing external fund managers, the extent to which ESG factors are embedded into the managers' investment process forms an important part of our overall assessment. Examples of questions that we ask and issues that are taken into account include:

- What is the manager's approach to ESG integration?
- To what extent is the manager active in voting and engaging on ESG matters?
- Does the fund's approach align with Scottish Widows' Exclusions Policy (see Section 3.3)?
- How are climate change risks and opportunities considered in the manager's investment decisions?
- Does the wider asset management business have any ambitions to achieve net zero carbon emissions?
- How do you establish cognitively diverse teams to support better problem-solving and decision-making? (Greater detail can be found in section 3.4. We will be adding additional Due Diligence Questionnaire over the course of 2023 for managers of our mandated funds).

STRATEGIC ASSET ALLOCATION AND INTEGRATING CLIMATE CONSIDERATIONS

As part of our long-term investment approach, we invest across a range of different types of funds from a variety of investment managers.

The Scottish Widows Asset Allocation team optimises our multi-asset funds using, as a starting point, projected asset returns over at least a 10-year time horizon. Alignment to long-term customer needs is achieved by modelling customer outcomes (in particular, for our workplace pension default strategies) and aligning to customer risk profiles and appropriate asset classes. Active funds have benchmarks with performance targets over and above that benchmark.

When setting the Strategic Asset Allocation (SAA) for our funds, we use long-term asset class forecasts from a variety of sources, including Moody's Analytics. Moody's provide year-on-year forecasts over 40 years and we also include 10 and 30 year forecasts from Tier 1 investment manager, Schroders, that incorporate the projected impact of climate change on a variety of asset classes.

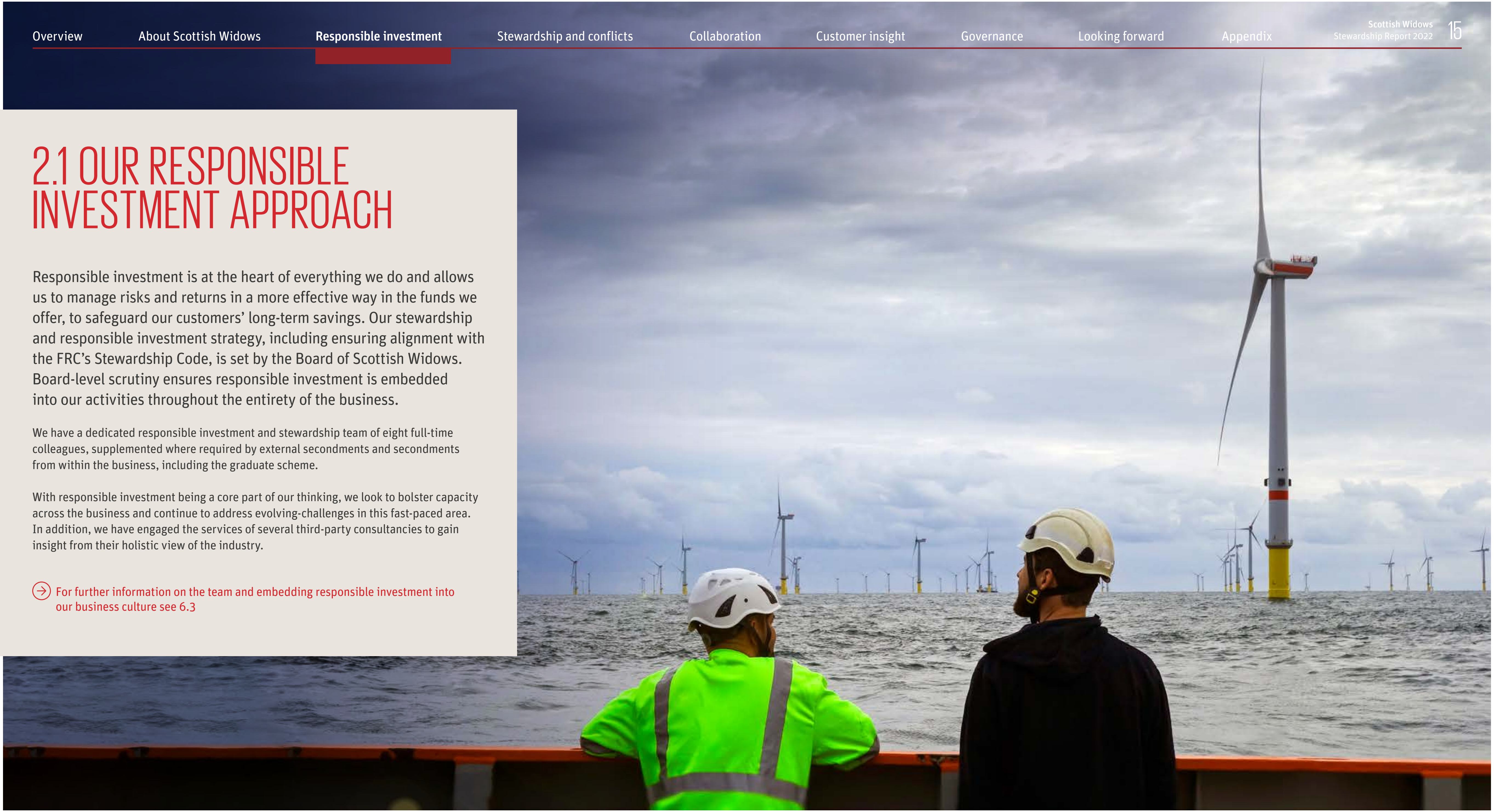
Whenever reviewing the SAA for the Scottish Widows multi-asset funds, we also analyse the underlying funds being used and the overall change on ESG factors and carbon footprint. We can employ a variety of strategies to achieve desired goals, including market capitalisation index funds with exclusions, quantitative funds that incorporate ESG signals, fundamentally-weighted index funds, fundamental research active funds as well as climate transition funds. As a result of work in this area we have launched both equity and bond funds with climate transition goals, applied a range of exclusions within market cap passive funds and, from 31 March 2023, a suite of Paris-Aligned Benchmark equity funds which can be used in our multi-asset funds.

Our annuity investments are in matching adjustment portfolios within our shareholder funds, which adhere to all matching adjustment regulation as required under Solvency II. These assets in the portfolios, including direct loan investments, are matched to long-term liabilities based on the profile of our annuity customers. For example, asset duration and returns are aligned while maintaining credit quality within suitable risk parameters.

We also receive carbon metrics from MSCI to enable us to understand changes to the carbon footprint of investments whenever an optimisation is undertaken. Presently, we are only undertaking this on the equity component of our funds but we will extend that to most asset classes over the course of 2023 when we have data that is of a suitable standard.

In March 2022 we adopted new custom screened benchmarks for our passive mandated equity funds to enable the application of the updated Scottish Widows Exclusions Policy, which contains a tobacco exclusion and features strengthened fossil fuel restrictions. In addition, we seeded a new Global Corporate ESG Insights Bond Fund, which BlackRock designed in consultation with Scottish Widows. The fund seeks to provide broad-based exposure to global investment-grade corporate bonds whilst also looking to achieve certain ESG-related aims, including a carbon emission intensity score that is less than 50% of the benchmark index. These have been discussed in Section 2.4 in greater detail.

RESPONSIBLE INVESTMENT



2.1 OUR RESPONSIBLE INVESTMENT APPROACH

Responsible investment is at the heart of everything we do and allows us to manage risks and returns in a more effective way in the funds we offer, to safeguard our customers' long-term savings. Our stewardship and responsible investment strategy, including ensuring alignment with the FRC's Stewardship Code, is set by the Board of Scottish Widows. Board-level scrutiny ensures responsible investment is embedded into our activities throughout the entirety of the business.

We have a dedicated responsible investment and stewardship team of eight full-time colleagues, supplemented where required by external secondments and secondments from within the business, including the graduate scheme.

With responsible investment being a core part of our thinking, we look to bolster capacity across the business and continue to address evolving-challenges in this fast-paced area. In addition, we have engaged the services of several third-party consultancies to gain insight from their holistic view of the industry.

For further information on the team and embedding responsible investment into our business culture see 6.3

2.2 OUR RESPONSIBLE INVESTMENT PROCESS AND PROGRESS

Our Responsible Investment and Stewardship Framework articulates our ambition, which includes six principles of Responsible Investment and our Stewardship Commitments. Our decisions on asset allocation, manager selection, fund research and engagement activity are guided by this framework and these principles are integrated into our overall investment policy.

In this section we provide details on the progress we have made on Responsible Investment, as well as providing an overview of our investments.

RESPONSIBLE INVESTMENT PRINCIPLES

2.2 Our responsible investment process and progress continued

1

We will be a responsible investor. We will strive to protect our investments from material ESG-related risks and seek to capitalise on ESG-related opportunities.

Our due diligence processes for third-party investment manager selection now includes the assessment of ESG credentials. New managers must be UN Principles of Responsible Investment (PRI)* signatories and signatories to the UK Stewardship Code 2020, with existing managers given until the end of 2024 at the very latest to become signatories to the Code, if applicable within their jurisdiction. Our core appointed managers, across Tier 1 and 2, are expected to already be signatories to the Code. In 2021, we signed up to the Asset Owner Diversity Charter and over the course of 2022 we have reviewed the diversity data disclosures from our core appointed managers and are integrating the findings into our manager review process.

We also continued to integrate sustainability within deliverables across our various investment functions and in areas like Finance, Risk, Operations, HR & Learning and Marketing. This enables us to pull in the same direction in how we embed sustainability into our business.

2

To help us manage downside risk, we will take a position on the companies we will not support and will implement exclusions throughout funds managed or mandated by us.

We believe divesting from certain companies has its place but we apply exclusions with caution. Well-considered exclusions can not only help protect our customers' savings from unrewarded investment risk, but also send a market signal about industries and activities incompatible with a responsible investment approach. The cumulative divestment we have made from companies that haven't met our ESG criteria since introducing our Exclusions Policy in November 2020 is c.£3bn. In our mandated funds (i.e. those where Scottish Widows is the investment manager), our policy is to not invest in controversial weapons manufacturers, UN Global Compact violators (apart from a handful of those where we are running a focused, three-year long engagement process), companies where 5% or more of their revenue is derived from thermal coal and tar sands extraction, and companies with more than 10% of value chain revenues from tobacco products. These exclusions are implemented across our mandated active funds. For our passive index trackers, we worked with FTSE Russell to create a range of custom ESG screened indices to implement our policy.

3

We will aim to reduce the carbon intensity of our whole portfolio to 50 per cent by 2030 and achieve net zero by 2050.

At the start of 2022 we launched our Climate Action Plan – a roadmap of how we aim to achieve our net zero emissions ambition across our investments. It lays out a target for investing £20-25bn in climate-aware investment strategies** by 2025, with at least £1bn in climate solutions***. We aim to achieve our 2025 target by integrating climate considerations across all our investments and through allocation to specialist funds. For example, at the end of 2022 we had invested over £10bn in a climate transition fund which we developed with BlackRock. In Q1 2023, we launched three self-decarbonising passive funds for use in our multi-asset funds, concluding work we undertook during 2022. Through these, and other planned actions, we aim to reduce the carbon intensity of our whole portfolio by 50% by 2030 and achieve net zero by 2050 or sooner. We conduct a full review and refresh of our Climate Action Plan every three years.

4

We will aim to offer an industry-leading fund range to our customers to help support causes that are close to their hearts while growing their savings for the future.

In addition to the integration of ESG and our Stewardship themes across our investments, we have developed a range of Scottish Widows funds that invest in companies that are decarbonising their business, or offering sustainability solutions. These funds are discussed in more detail in Sec 2.4.

We have also developed a Find Your Impact (FYI) tool, to show workplace pension savers how their investments score against select ESG metrics. As the roll out of this tool progresses to all workplace customers, this allows them to be able to better understand the link between their savings and the impact it is having. The development of the FYI tool was informed at each stage by customer research. More information on this has been detailed in Section 5.1.

5

We will seek to extend our responsible investment principles into all asset classes over time.

Our Responsible Investment & Stewardship Framework, Exclusions and Stewardship policies, Climate Action Plan, fund selection, management and allocation decisions cover all asset classes.

Our core appointed investment managers integrate ESG factors into their investment analysis and decision-making. For example, Schroders, our strategic appointed manager for active management, integrates ESG factors across asset classes in our active funds. For our passive funds and funds which invest in pooled investments, our appointed investment managers apply ESG screening and engage with investee companies as part of their active stewardship approach, which we oversee, influence and enhance with our own targeted activity. In Q1 2023, we have further enhanced this by converting three of our regional equity funds to track decarbonising benchmarks.

6

We will work with policymakers and industry participants to promote direct investment opportunities required to successfully transition to a lower carbon economy.

We continue to make direct loan investments in green infrastructure and social projects, currently lending around £7.5bn from our annuity assets to support social housing, education, sustainable energy and infrastructure projects needed for the low-carbon transition. In parallel, we continue to advocate for policy measures that would allow defined contribution pension funds to invest in private markets and other illiquid assets, an example being our response to Department of Works and Pensions (DWP) consultation on Enabling Investment in Productive Finance.

* PRI | Home (unpri.org)

** Climate-aware investment strategies: funds that have a bias towards investing in companies that are adapting their businesses to be less carbon-intensive and/or developing climate solutions.

*** To define climate solution investments, we look at company revenue associated with activities such as alternative energy, energy efficiency, green building, sustainable agriculture, sustainable water and pollution prevention. We use MSCI Environmental Impact Revenue data to help with this classification.

**** In the event that an existing holding exceeds a revenue threshold, a review will be carried out by our Investment team. If the review deems that this is likely to persist for the foreseeable future, we would look to exit the holding, taking into account market conditions and any other investment impact to the funds.

2.3 OUR CLIMATE ACTION PLAN

Our ambition is to align all our investments with achieving net zero carbon emissions, by 2050 at the latest. 'Net zero' refers to achieving a balance between the amount of greenhouse gases, such as carbon dioxide, emitted into the atmosphere and the amount removed from it. Emissions referred to are Scottish Widows' Scope 3 'financed emissions' which are calculated from the Scope 1 and 2 emissions generated from the companies in which we have invested and those to which we have lent.

This net zero ambition underpins our investment strategies across all asset classes. Execution of these strategies will support consistency between investment and the profile and duration of our liabilities while seeking performance over the medium to long-term.

See the following page for emissions definitions.

To achieve our mission, we have set ourselves the following targets and milestones:

2025

Invest between £20bn – £25bn in climate-aware investment strategies*, with at least £1bn invested into climate solutions investments

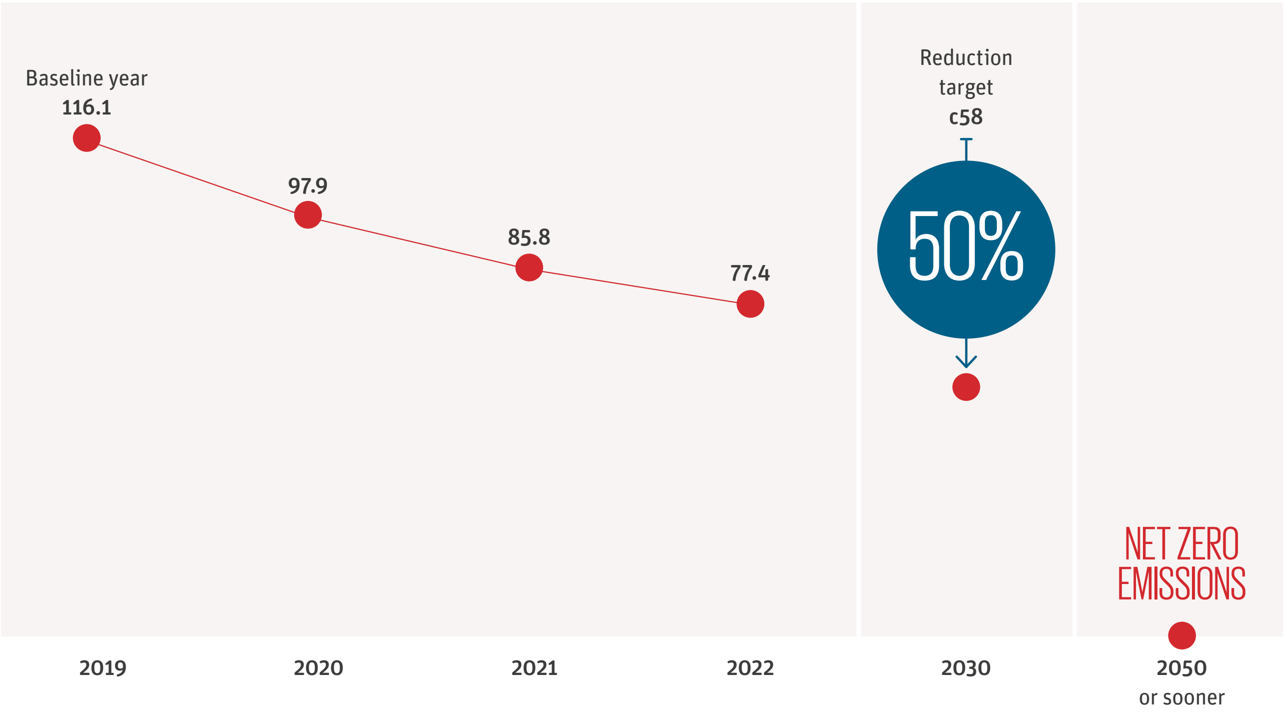
2030

Halve the carbon footprint** of our investment portfolios

2050

Net zero across the entirety of Scottish Widows' investments

Carbon emissions (tCO_2/£m)



* Climate-aware investment strategies: We're working closely with our strategic fund management partners BlackRock and Schroders to develop and refine a range of funds that have a bias towards investing in companies that are adapting their businesses to be less carbon-intensive and/or developing climate solutions. We will invest in climate solution investments either within these strategies or other funds. To define climate solution investments, we look at the proportion of company revenue associated with activities such as alternative energy, energy efficiency, green building, sustainable agriculture, sustainable water and pollution prevention. We use MSCI Environmental Impact Revenue data to help with this classification.

** Carbon footprint is a measure of carbon intensity calculated as absolute value of emissions applicable to an investment divided by the value of investment.

2.3 Our Climate Action Plan continued

ESTIMATED CARBON EMISSIONS

At the heart of the decarbonisation effort to combat climate change is the need to efficiently measure and track greenhouse gas (GHG) emissions. The success of emissions reduction strategies first requires an understanding of those emissions.

We've carried out detailed investigations to calculate the carbon footprint of our investments to serve as the baseline for our targets and against which we'll measure our progress. Data isn't universally available and doesn't have complete coverage, however we are continuously working to improve this.

2019 baseline

We've selected 2019 to be the baseline year in line with the science-based recommendations of the Intergovernmental Panel on Climate Change (IPCC) and guidance from the Institutional Investors Group on Climate Change (IIGCC)*.

To calculate a reduction of emissions produced by the companies in our investment portfolios, we've used the emerging industry standard for calculating financed emissions developed by the Partnership for Carbon Accounting Financials (PCAF). PCAF is an international industry-led initiative to measure and disclose the greenhouse gas emissions financed by loans and investments. It's currently the most widely adopted global standard for measuring financed emissions by the financial sector.

To establish emissions data for corporate bonds and equities, we matched our investments against the published emissions data available on those companies from S&P Global Trucost's data and analytics tool. Trucost provides carbon and environmental data and risk analysis for more than 15,000 companies. However, there is a lack of published emissions data on loan investments. Therefore, we adopted an alternative PCAF-aligned approach to calculate emissions using estimates from the Office for national Statistics and Department for Business, Energy and Industrial Strategy sector averages.

What emissions do we calculate?

Emissions are classified into three distinct 'scopes', as defined by the Greenhouse Gas Protocol Corporate Standard, which covers the different kinds of carbon emissions a company creates in its own operations and in its wider value chain.

Scope 1 and 2 emissions

Scope 1 and 2 emissions are a mandatory part of reporting for many organisations across the world and relate to emissions that a company makes directly, for example while running its boilers and vehicles, and those made indirectly, like when the electricity or energy it buys for heating and cooling buildings is being produced on its behalf.

Scope 3 emissions

Scope 3 emissions are those that are more external to a specific organisation, such as from buying products from its suppliers and from its products when customers use them. Scope 3 emissions include all other indirect GHG emissions (not included in Scope 2) that occur in the value chain of the reporting company.

Our baseline

Our baseline represents Scottish Widows' Scope 3 financed emissions which are calculated from the Scope 1 and 2 emissions generated from our investment or lending. When it comes to Scope 3 of the companies we invest in, at this time we do not feel the data is robust enough or has wide enough coverage for us to be able to set targets using it. We will continue to watch the developments in data quality and will consider extending our portfolio targets to cover Scope 3 of our underlying holdings when there is market consensus on the appropriateness of available data. As a first step, in our TCFD report**, in accordance with the PCAF guidance for financial institutions, we have reported Scope 3 emissions arising from our investment in the oil, gas and mining sectors from 2021 onward. Additional sectors will be added from 2024.

* The European membership body for investor collaboration on climate change. IIGCC works with business, policy makers and fellow investors to help define the investment practices, policies and corporate behaviours required to address climate change. IIGCC – The Institutional Investors Group on Climate Change

** TCFD Report 2022

2.3 **Our Climate Action Plan** continued

OVERVIEW OF FINANCED EMISSIONS

The decrease in Footprint from 2019 to 2020 relates to the fall in investee company emissions during 2020, in part due to reduced production and energy usage during the Covid-19 pandemic. During 2021 company market values increased in some sectors but the investee company emissions still reflected 2020 causing the Footprint to fall. The 2022 results include the change in market values of investee companies during 2022 but also the change in investee company emissions from 2020 to 2021. Market values and emissions have not moved consistently across different regions and sectors. The US and Emerging Market indices fell, but the UK was relatively flat. In terms of higher emitting sectors such as Oil & Gas, the emissions increased but the company market values increased by more, meaning the Oil & Gas Footprint has fallen.

Total financed emissions

		Total assets under management (AUM) £bn	AUM in scope according to PCAF methodology and for which emissions data is available £bn	In-scope AUM for which emissions data is available %	Estimated total $MtCO_2e$ (Scope 1 and 2 emissions, for investments where data is available)	Carbon Footprint (where data is available)* (tCO_2/£m invested)	PCAF data quality score	Weighted average carbon intensity (where data is available) (tCO_2/£m sales)
2022	Policyholder	145.7	115.1	79%	9.1	77.7	2.3	192.0
	Shareholder	20.7	12.7	61%	1.1	75.6	3.7	121.5
	Total	**166.4**	**127.8**	**77%**	**10.2**	**77.4**	**2.4**	**188.0**
2021	Policyholder	161.1	114.4	71%	9.7	86.7	2.2	192.8
	Shareholder	27.3	15.4	56%	1.1	78.8	3.6	125.6
	Total	**188.4**	**129.8**	**69%**	**10.8**	**85.8**	**2.3**	**188.3**

Scope 3 financed emissions for oil, gas and mining sectors

		2022			2021
		Total assets under management (AUM) £bn	Estimated total $MtCO_2e$ (Scope 3 emissions, for investments where data is available)	Data quality score	Estimated total $MtCO_2e$ (Scope 3 emissions, for investments where data is available)
Policyholder	Oil and gas	6.6	24.4	3.1	23.5
	Mining	3.4	8.4	3.4	12.2
	Total	**10.0**	**32.8**	**3.2**	**35.7**
Shareholder	Oil and gas	0.2	0.6	3.1	0.6
	Mining	0.1	0.3	3.0	0.4
	Total	**0.3**	**0.9**	**3.1**	**1.0**
Scottish Widows total	Oil and gas	6.8	25.0	3.1	24.1
	Mining	3.5	8.7	3.4	12.6
	Scottish Widows total	**10.3**	**33.7**	**3.2**	**36.7**

2.3 **Our Climate Action Plan** continued

INSTITUTIONAL INVESTORS GROUP ON CLIMATE CHANGE NET ZERO INVESTMENT FRAMEWORK ALIGNMENT

As one of the founding signatories to the Paris Aligned Investment Initiative (PAII), set up by the IIGCC, we have drawn on the PAII Net Zero Investment Framework to produce our Climate Action Plan and embed it in our investment processes. We also support the Taskforce on Climate-Related Financial Disclosures (TCFD) Framework, publishing our first TCFD report in 2022 and the second one in June 2023.

Action 1

Develop climate-aware investment strategies and climate solutions investments.

Read more on Page 22

Action 2

Integrate climate considerations into asset allocation optimisation.

Read more on Page 23

Action 3

Exclude high carbon investments that we believe present a high risk of becoming stranded assets.

Read more on Page 23

Action 4

Focus stewardship activity on companies failing to address climate change risk.

Read more on Page 24

2.3 Our Climate Action Plan continued

ACTION 1:
DEVELOP CLIMATE-AWARE INVESTMENT STRATEGIES AND CLIMATE SOLUTIONS INVESTMENTS

We estimate we'll make discretionary investment of £20 – 25 billion into climate-aware investment strategies by 2025, with at least £1 billion invested in climate solutions investments.

We're working closely with our core appointed strategic investment managers to develop and refine a range of funds that have a bias towards investing in companies that are adapting their businesses to be less carbon-intensive and/or developing climate solutions. As of the end of 2022, we have a collective investment totalling £17.5bn in climate-aware strategies, including the Scottish Widows UK Environmental Fund, Climate Transition World Equity Fund (BlackRock) and ESG Insights Bond Fund (BlackRock). To define climate solution investments, we look at company revenue associated with activities such as alternative energy, energy efficiency, green building, sustainable agriculture, sustainable water and pollution prevention. We use MSCI Environmental Impact Revenue data to help with this classification, focusing on revenues classified as 'climate change' and 'natural capital'. MSCI is a recognised provider of ESG data to the investment industry. Our investment in climate solutions, amounted to £1.3bn, already achieving our 2025 goal of £1bn.

We continue to seek out opportunities to invest in climate-aware solutions through our loan investment activity.

Our existing book contains a range of green infrastructure projects, including green energy solutions across wind and solar power generation, as well as smart metering.

In 2022 we invested £30m in Zenobe, the UK market leader in the provision of electric bus fleets.

£17.5bn

Our end of 2022 Investment In Climate-Aware Strategies

We are here ▼ £17.5bn | 2025 target ▼ £20 – 25bn

£1.3bn

Our end of 2022 Investment In Climate Solutions

2025 target ▼ £1bn | We are here ▼ £1.3bn

2.3 Our Climate Action Plan continued

Case study

We use different approaches to measure our 'climate aware' and 'climate solutions' Investments. However, for both, the key concept is that of intentionality. Page 13 of our CAP has the definitions we use. For 'climate aware', we use the AUM in specifically identified strategies/funds that meet this definition and do so with intent. For 'climate solutions', we use % 'green revenues' as a proxy for AUM (i.e. if 10% of a company's revenues are considered 'green' then 10% of our AUM in that company is considered towards our climate solutions target). We use MSCI Environmental Impact data to measure and monitor.

Our climate aware and climate solutions targets started with equity and fixed income investments, but we have since brought listed property into scope as well and looking to expand to other asset classes as opportunities become available. We are co-leading an IIGCC working group that is tasked with providing guidance to measure and aggregate to portfolio level for these asset classes as well as several others. Our approach pre-dates this guidance but is conceptually aligned despite being different in implementation.

By having 'intent' as a foundational concept we treat all 'solutions' equally, leaving it to market forces, companies, and our external managers to allocate capital efficiently. However, we have more flexibility in designing and/or seeking out climate aware strategies – here, we are focusing on how to include more explicit S & G elements alongside the E.

ACTION 2:

INTEGRATE CLIMATE CONSIDERATIONS INTO ASSET ALLOCATION OPTIMISATION

Our Responsible Investment & Stewardship Framework and policies extend to cover all of our asset classes in our portfolio influencing fund selection and asset allocation decisions across our portfolio to ensure that material ESG factors are embedded. Schroders, our strategic appointed manager for active fund management, integrates ESG risks and opportunities into their security analysis and portfolio management decisions to achieve long-term sustainable investment returns. As our appointed passive fund manager, we work with BlackRock to deliver tailored strategies that integrate ESG considerations. For example, the recent launch of the Global Corporate ESG Insights Bond Fund, which applies ESG-related tilts to achieve its aims.

In addition, we carry out optimisation modelling on our SAA, which are invested in a series of underlying Scottish Widows and third party single asset class fund, for our core multi-asset funds on an annual basis. As part of this SAA modelling work we'll look at economic scenarios which take into account the impact of climate risk on longer-term asset class projections and use this to help set the SAA for our multi-asset funds. Please refer to Section 1.4 for more details on our SAA and our SAA reviews.

ACTION 3:

EXCLUDE HIGH CARBON INVESTMENTS THAT WE BELIEVE PRESENT A HIGH RISK OF BECOMING STRANDED ASSETS

We aim to reduce long-term investment risk by excluding investment in companies which fail to meet minimum criteria and/or invest in activities that are outside our Responsible Investment and Stewardship Framework. We believe companies that fall into this category run the risk of becoming 'stranded assets'.

Stranded assets are defined as investments that have suffered from unanticipated or premature sell-offs or devaluation. The issue of stranded assets caused by environmental factors, such as climate change and society's attitudes towards it, has become increasingly high profile. Changes to the environment caused by climate change could potentially strand both individual companies and whole industries within a short timeframe, leading to direct and indirect impacts on investment strategies.

Thermal coal and oil extracted from tar sands are two of the most CO_2 intensive fossil fuels. Their use is a significant contributor to climate change. Reliance on fossil fuels needs to be significantly reduced in the coming decades to achieve the objective of limiting global warming to below 2°c, which was set out by the Paris Agreement in December 2015. As countries across the globe work towards meeting this target, we believe companies that fail to amend their business models to be less carbon-intensive will pose an investment risk. Our position as a large institutional investor allows us to lobby for positive change in the companies we invest in. As such, we don't seek to exclude all high CO_2-emitting sectors. Instead, we focus on excluding individual companies that we believe pose the most significant risks. The carbon, climate change, and social impact of companies involved in thermal coal and tar sands is not aligned with our long-term investment strategy. So, in our mandated funds our policy is not to invest in companies where 5% or more of their revenue is derived from thermal coal or tar sand extraction*.

* In the event that an existing holding exceeds a revenue threshold, a review will be carried out by our Investment team. If the review deems that this is likely to persist for the foreseeable future, we would look to exit the holding, taking into account market conditions and any other investment impact to the funds.

2.3 Our Climate Action Plan continued

ACTION 4:

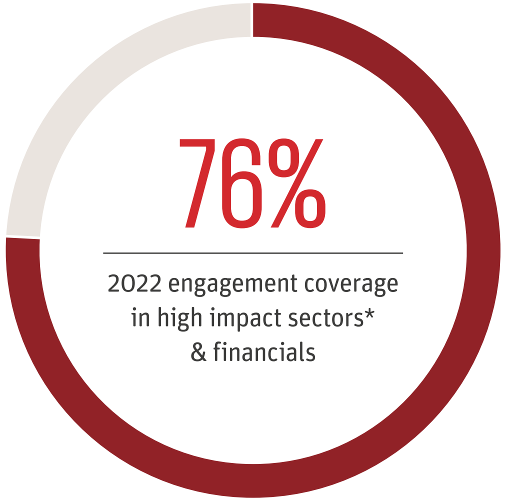
FOCUS OUR STEWARDSHIP ACTIVITY ON COMPANIES FAILING TO ADDRESS CLIMATE CHANGE RISKS

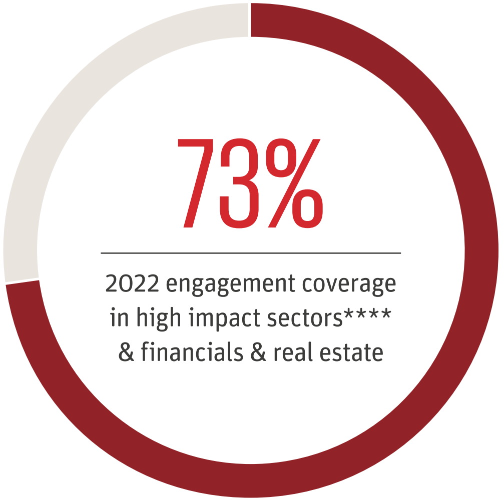
To support decarbonisation in line with our targets, a strong engagement programme is needed with investee companies. Our primary role is to monitor coverage with our appointed investment managers and engage with them to encourage the gradual extension of that coverage. In 2022, we strengthened our Voting Guidelines on climate by naming some of the high carbon sectors we expect Scope 3 reporting from. We also expanded the just transition section of the Voting Guidelines to encourage companies to incorporate the International Labour Organisation's (ILO) "Guidelines for a Just Transition" and to disclose metrics to measure progress on just transition goals and activities. We continued to engage directly with companies on climate through 2022. Stewardship and engagement activities are currently focused on our equity and bond holdings; they represent c.75%* of our investment book. We have also mapped how this would change, if we included Real Estate into our analysis. This would reduce coverage to c.73%.

In 2021, our appointed investment managers engaged with companies representing 79% of AUM within high impact sectors outlined by Transition Pathway Initiative (TPI)** including Banks and Insurers. This is mostly due to the fact that the most recent analysis, based on our YE 2022 equity and bond holdings, matched a wider base of assets to material sectors following the adoption a new ESG data platform***. We now also include the Real Estate Sector as high impact, and factoring in this wider definition, we engagement reached 73% on climate topics in 2022 including, but not limited to:

1. Climate risk and oversight
2. Climate mitigation
3. Climate adaptation
4. Climate transition plans

These are a mix of 'thematic' and 'focused' engagements, with the majority targeted towards companies with the potential to have the largest negative impact.





* Including equity and bonds owned in externally pooled funds at year-end 2022.

** A global, asset owner led initiative that assesses companies preparedness for the low-carbon transition. Home – Transition Pathway Initiative

*** With full coverage of our external pooled equity and bond exposure, going forward we expect to make this assessment year-on-year on a like-for-like basis.

**** High impact sectors are as per GICS classification presented in the NZIF Implementation Guide.

2.4 RESPONSIBLE INVESTMENT EXAMPLES

It is important that we continue ESG integration in our flagship workplace pension default strategy given what we know about our customers' attitudes. In terms of ESG specifically, our Green Pensions Report* found that 72% of respondents thought it was important for their employees to invest their pensions sustainably. We expect the customer benefit to be improved risk-adjusted returns with heightened ESG characteristics. During 2022, we focused on the fixed income and real estate elements, which we outline opposite.

BlackRock Global Corporate ESG Insights Bond Fund

In the last quarter of 2022, Scottish Widows co-developed and became the first investor in BlackRock's new ESG bond fund – BlackRock Global Corporate ESG Insights Bond Fund – with an initial backing of £500m. Through its exposure to global investment grade bonds, the Fund seeks to achieve a set of ESG-related aims, including achieving a carbon emissions intensity score that is 50% less than the index. With an investment of £942mn at the end of 2022, the Fund's strategy applies an exclusion overlay** before the remaining investible universe is assessed based on issuer ESG performance. Scottish Widows' investment marks the second collaboration with BlackRock, following the seeding of the Climate Transition World Equity Fund in 2020 with £2bn initial investment. Working with our appointed asset managers in the design of tailored ESG funds reflects the growing customer demand for climate-aware strategies as well as helping to drive innovation in ESG investing.

iShares Environment & Low Carbon Tilt Real Estate Index Fund

ESG screens set by the index provider seek to limit and/or exclude corporate issuers within the Parent Index which have exposure to, or other ties with, activities including but not limited to:

- Non-renewable energy (including extraction of oil sands, thermal coal and thermal coal power generation);
- Tobacco (including related to the manufacture, supply and distribution of tobacco);
- Weapons (including chemical and biological, cluster bombs and nuclear weapons); and
- Controversies (including human rights, labour, environmental and anti-corruption controversies).

The remaining constituent weights are then adjusted (tilted) based on improvements relative to the Parent Index across three sustainable investment considerations:

- Green building certification (the share of total net leasable area owned and/or managed by a company that is certified as part of an eligible green certification scheme, minimum 30% improvement);
- Energy usage (the average modelled energy consumption per square metre of net leasable area owned and/or managed by a company; minimum 10% improvement); and
- Carbon emissions intensity (which is the total operational emissions scaled by company value including cash; minimum 20% improvement).

Scottish Widows Global Environmental Solutions Fund

We have built a fund which provides targeted thematic exposure to global companies actively involved in providing solutions to the climate crisis or other areas of environmental challenges.

It provides access to a wide range of themes such as alternative energy, clean mobility, transport and infrastructure sustainability, forestry, sustainable agriculture, biodiversity and pollution prevention. It is actively managed with a concentrated portfolio of high conviction companies. It is expected to make a substantial contribution to our 'at least £1bn in climate solutions' target outlined in our Climate Action Plan for 2025.

Scottish Widows Self-decarbonising Funds***

We've converted three of our regional equities funds to track decarbonising benchmarks: Scottish Widows Emerging Markets Paris-aligned Index Equity Tracker Fund; Scottish Widows Developed World Paris-aligned Index Equity Tracker Fund; Scottish Widows UK Climate Index Equity Tracker Fund. We believe the use of these strategies provide several benefits for multi asset funds:

- They offer certainty of decarbonisation pathway through the index level objective to achieve immediate carbon intensity reductions and ongoing annual minimum decarbonisation levels.
- They provide exposure to climate solutions assets which are at the forefront of the transition to a low carbon economy.
- They add diversification to the range of climate-aware strategies available.

Furthermore, there is an immediate carbon benefit of tracking these three indices versus its standard parent; 50% for Developed and Emerging markets, and 30% for the UK. All three tracker funds also target a 7% annual carbon reduction, in line with achieving the net zero goals of the Paris Agreement. The back-tested history of such indices suggest they should provide improved volatility-adjusted returns. This is in line with our expectation the cost of capital will move in favour of companies lowering their carbon intensity. Lower-carbon portfolios should therefore deliver superior investment results over the longer term.

Ongoing investment in the BlackRock Climate Transition Fund

In 2020 we worked with BlackRock to launch the BlackRock ACS Climate Transition World Equity Fund, which is integrated into our Pension Portfolio Funds, which underpin our workplace default strategy. We started with a £2bn allocation, and at the end of 2021, we had invested over £5bn. This fund continues to be an integral component of the investments we make as part of our Climate Action Plan with around £9bn invested by end of 2022. While we have continued to increase investment into this fund from the workplace default, we also added it to our workplace customer fund range so that scheme members selecting their own investments can increase their exposure to the fund.

We've allocated 20% of the equities portion of our Pension Portfolio Funds, which underpin our workplace pension default solution, to this BlackRock ACS Climate Transition World Equity fund, which has a bias towards companies decreasing carbon emissions, more effectively managing water and waste and developing clean energy technologies.

* Green Pensions Report – 2022 (scottishwidows.co.uk)

** The Fund's exclusion policy removes companies with involvement in thermal coal and tar sands; tobacco; UN Global Compact violators; and controversial weapons including nuclear and civilian firearms.

*** ICISC Approval paper, Adoption of EU Climate Benchmarks, 2022-06-21, Author/Presenter: Iain

2.4 Responsible investment examples continued

DIRECT LOAN INVESTMENTS SOCIAL HOUSING

We currently lend around £7.5bn from our annuity fund to support social housing, and sustainable energy and infrastructure projects, supporting the transition to a low-carbon future and making a contribution to the Lloyds Banking Group ambition of Helping Britain Prosper.

In 2022, we continued to develop our support in this space, with a particular focus on the social housing sector. During the year we invested a total of £328m, supporting a range of housing associations around the UK and providing funding for a variety of initiatives, including the development of new affordable, energy efficient housing, as well as financing for the retrofitting of existing homes to improve energy efficiency.

Loan investments

£60m

40 year term loan

Funding to support the delivery of new affordable homes and the client's environmental strategy.

June 2022

£40m

40 year term loan

Funding energy efficiency improvements to existing homes and supporting delivery of 1,000 new homes over the next five years.

April 2022

£60m

40 year term loan

Part of funding package to support the development of over 500 new energy efficient homes.

April 2022

£70m

Fixed rate loan

September 2022

£100m

Fixed rate loan

August 2022

2.4 Responsible investment examples continued

Case studies

BRIGHTER PLACES

Based in the South West, Brighter Places is a housing association managing 3,300 homes in Bristol and the surrounding areas. Scottish Widows provided the association with a £40m investment to support its recently launched five-year strategy.

Aimed at improving the quality and energy efficiency across their existing estate, the funding will also support the association's ambitious growth plans which include the creation of a further 1,000 energy efficient homes across Bristol and South Gloucestershire.

As well as traditional housing stock, the association is planning to include 42 multi-generational homes in their plans to aid the development of increasingly supportive, inclusive communities, as well as developing critical facilities such as charging for electric vehicles.

IRWELL VALLEY

Irwell Valley is a traditional housing association based in Greater Manchester, with c.7,700 homes under management.

Scottish Widows provided Irwell Valley with a £60m 40-year term loan in June 2022. This funding will help support an ambitious development programme that will see the association build over 1,000 new homes for social and affordable rent over the next five years, together with a commitment to achieve net zero carbon emissions across all of its properties by 2038.

Scottish Widows annuity fund

How it works in three steps

1

Our customers pay us a premium using their pension pot and in return we guarantee them a regular income, called an annuity, for the rest of their life.

2

We invest the funds we receive from customers into long-term loans to commercial clients, such as housing associations and infrastructure projects.

3

The interest we receive on these loans helps us price our annuities as competitively as possible to give best value to our customers.

Bonds

In our 2021 Stewardship report we outlined changes in our Exclusions policy* so that we will no longer invest in companies with more than 10% of their revenues linked to tobacco products. With this in mind, in October 2022 Schroders completed the sale of our tobacco holdings in line with the updated policy. We completed the reinvestment of our final British American Tobacco holdings into alternative bonds in November 2022.

In January 2023, our asset manager for the bond portfolio, Schroders, alerted us to a potential spike in the thermal coal income of one of our holdings driven by increased coal prices, which could have taken it over the 5% revenue threshold set out in our exclusions policy. We queried this with our data provider, which identified its initial calculation did not allow for the disposal by the company of its stake in another business. When restated to factor in this disposal, the exposure to thermal coal remained within the 5% revenue threshold. We are pleased that our monitoring processes flagged this potential breach and are confident that any future increased in exposure would be identified through this mechanism**.

We continue to develop our capabilities for investing in new asset classes and in 2022 undertook a tendering process to appoint an asset manager for US private placements. This process incorporated an assessment of bidding firms' ESG credentials, including relative to Scottish Widows policies and requirements for its asset managers, such as the expectation that Tier 1 asset managers are signatories to the UK stewardship code. Our ESG requirements have also been factored into the mandate, which is currently in its final stages of completion.

* https://adviser.scottishwidows.co.uk/assets/literature/docs/60694.pdf

** In our mandated funds our policy is not to invest in companies where 5% or more of their revenue is derived from thermal coal extraction. In the event that an existing holding exceeds a revenue threshold, a review will be carried out by our Investment team. If the review deems that this is likely to persist for the foreseeable future, we would look to exit the holding, taking into account market conditions and any other investment impact to the funds.

2.5 OUR EXCLUSIONS POLICY

Our preference is to engage with the companies we invest in and our appointed investment managers to influence for positive change, however, this is not always possible. Since 2020, Scottish Widows has operated an exclusions policy*. We use this policy to help ensure that our investment approach is aligned with the interests of our customers.

In 2021, we reviewed our policy to include tobacco exclusions across the value chain and lowered thresholds on revenue generated from thermal coal and tar sands. This revised policy was formally launched in early 2022 and implemented through the course of the year.

* In early 2022, Lloyds Banking Group acquired Embark – a digital retirement solutions provider. This report does not cover this part of our business as we are currently in the process of assessing how our Responsible Investment and Stewardship policies may apply to that business.

Our exclusion policy is based upon three principles

How the policy is applied depends on whether an in-scope fund is active or passive, and can be summarised as:

1 ADHERENCE TO INTERNATIONAL STANDARDS AIMING TO MINIMISE HARM

We exclude companies involved in the manufacture of controversial weapons prohibited by international conventions (e.g. anti-personnel mines, cluster munition, chemical and biological weapons).

We may exclude companies which violate any of the 10 principles of the United Nations Global Compact.

We exclude companies that derive more than 10% of their value-chain revenue from tobacco products.

2 MITIGATING EXPOSURE TO CLIMATE RISK

To protect investments from material ESG risk, we exclude companies whose business models are unsustainable and represent a high risk of becoming 'stranded assets' in the medium term.

Exclusions apply to those companies deriving more than 5% of their revenue from extracting thermal coal and/or oil from tar sands**.

** In our mandated funds our policy is not to invest in companies where 5% or more of their revenue is derived from thermal coal extraction. In the event that an existing holding exceeds a revenue threshold, a review will be carried out by our Investment team. If the review deems that this is likely to persist for the foreseeable future, we would look to exit the holding, taking into account market conditions and any other investment impact to the funds.

3 SIZE-RELATED EXEMPTIONS

For UNGC violators, we intend to apply the following approach where possible due to the nature of our investment:

For active funds, where a company represents more than 0.5% of a relevant stock market index, it will be flagged as a priority engagement target. We'll use our scale to influence for change over a three-year period. If there's no change after that period, the company will no longer be exempt from our exclusions policy and we'll consider selling out of our investment.

For active funds, where a company represents less than 0.5% of a relevant stock market index, it is excluded. This is because the size of our investment in these companies is too small to enable us to influence them to change.

There are no exemptions for UNGC violators in our mandated passively-managed index-tracker funds; there is not the same scope for effective engagement as there is with active funds.

2.5 Our exclusions policy continued

Applying the exclusions

TIER 1 FUNDS	It's mandatory for the managers of our mandated funds to comply with this policy. Our mandated funds are those where we have specified how the investments are to be managed. Scottish Widows is responsible for defining these funds' aims and determining the strict parameters on how they should be run. The managers of these mandated funds screen the exclusions at least annually and apply them to all investments falling within this policy's remit. New mandated funds must comply with this Policy from launch. Existing actively-managed funds have three months to implement, whilst passively managed funds may be permitted a longer transition period. After this, failure by fund managers to meet this policy's requirements will be deemed non-compliant with their contractual obligations. Accordingly, this may result in financial consequences or termination of the contract*.
TIER 2 FUNDS	Managers of funds in which our multi-asset funds invest, where we're not responsible for how the investments are managed, are expected to adhere to this policy on a 'comply or explain' basis. We engage with these managers to encourage them to implement the same, or similar, exclusions for the benefit of all investors in these funds.
TIER 3 FUNDS	Managers of external fund links are informed of this policy.

* In the event that an existing holding exceeds a revenue threshold, a review will be carried out by our Investment team. If the review deems that this is likely to persist for the foreseeable future, we would look to exit the holding, taking into account market conditions and any other investment impact to the funds.

Policy implementation challenges and progress

The key challenges to implementing our Exclusions Policy consistently across all our products is our use of external funds (Tier 2 & 3 funds), notably index tracker funds. While Scottish Widows is a significant investor, the asset managers must also take into account the other institutional investors in these pooled funds. However, we continue to engage these managers to adopt our policy, as a minimum. In 2022 we have been successful in encouraging BlackRock and State Street to incorporate our exclusions criteria in the passive tracker funds that we use in our workplace default strategy. We have yet to achieve full alignment for all component funds, but will continue to exert our influence on our managers to align with our own policy.

We have evolved our Exclusion Policy since originally developed in 2020 with the addition of tobacco exclusions and lowering the threshold for maximum permitted revenues from extraction of thermal coal and tar sands. This addition of a tobacco exclusion now sees a proportion of our default pensions proposition no longer being fully consistent with our policy. Here again we are in active conversations with the fund manager regarding several possible solutions for these assets to retain alignment with the Scottish Widows exclusions policy.

STEWARDSHIP AND CONFLICTS OF INTEREST

3.1 OUR STEWARDSHIP POLICY

Our stewardship approach is central to our investment strategy. Our Stewardship Policy* applies to all investments other than a very small proportion, which is comprised of direct loans in our shareholder funds, where Lloyds Banking Group External Sector Statements are applied.

Our Stewardship Approach

We believe Stewardship is integral to our business and investment philosophy. As a large UK asset owner, we want to ensure we play our part, not only in the responsible oversight of our own assets, but in driving industry-wide transition for better long- term outcomes for our customers and clients, benefiting our economy as a whole.

We target our Stewardship initiatives across three core pillars – monitoring and oversight of our appointed investment managers, direct and collective engagement with material investee companies and contributing to industry-wide initiatives like those related to policy advocacy. We aim to underpin this activity through dialogue and engagement with our customers and members.

Overview of Stewardship Policy updates in 2022

We made several updates to our Stewardship Policy in 2022. We added human rights as a new social theme and extended our Climate and Carbon priority to include broader environmental factors like biodiversity and deforestation, renaming it to Climate and the Environment, and explicitly included the 'just' element of the low carbon transition. These are discussed in greater detail in the next section.

* 60209.pdf (scottishwidows.co.uk)

Our Voting Guidelines, which form a core component of our Stewardship Policy, have been updated to include clear parameters around all the above mentioned sub-themes. We also tightened our language on our asset manager expectations. As our Stewardship Policy has been live for a couple of years, we thought it was important to add timelines to our expectations of asset managers.

For Tier 1 managers ongoing compliance with the UK Stewardship Code, or an equivalent in a manager's own jurisdiction, is now mandatory, barring exceptional circumstances. For Tier 2 managers, ongoing compliance is also mandatory and for existing managers, we expect them to become Code signatories by end of 2024, as we do with Tier 3 managers. We expect managers to also be signatories to UN Principles for Responsible Investment.

We anticipate that our new policy language will strengthen expectations and ultimately help improve stewardship quality in the asset management industry.

Our internal Engagement and Voting framework, which forms part of our Stewardship Policy, has also been updated to improve efficiency and agility of our voting process, while ensuring the right people have oversight and can approve votes we wish to cast.

Further engagement and voting details are discussed in sections 3.3-3.6.

Our three core pillars

1 Engagement & Oversight of Investment Managers

Exercise regular governance, oversight and monitoring of managers on Stewardship and ESG activities. This relates to engagement, voting and ESG integration activities which are delegated to our managers. Our voting is delegated or directed, using the ISS Socially Responsible Investment policy for eligible pooled funds' investments.

2 Engagement with Companies

Engage with investee companies on our articulated engagement priorities, either directly or through relevant collective engagement opportunities. While voting is delegated to our asset managers, we reserve the right to direct voting on matters relating to our core priorities in our own mandated funds, and utilise a specialist third-party policy across investment types.

3 Engagement with Industry and Policy Makers

We take part in collaborations and investor coalitions, playing a significant role to influence policy, develop frameworks and contribute to industry research projects, in order to address systemic risks to the future of well-functioning markets.

Ongoing dialogue with our customers

3.2 OUR STEWARDSHIP THEMES

2022 Progress

In 2021 we had started thinking about expanding our climate and carbon theme to include the just transition and biodiversity. In addition, we wanted to expand our themes to ensure we had a specific social theme.

We adopted the new themes into our Stewardship Policy and Voting Guidelines in 2022. On our climate theme we decided to change the name to Climate and the Environment to represent the interconnected nature of our climate and environment. We decided to include human rights as a social theme due to it being material to most of companies we invest in, and the potential for engagement on the topic to have impact.

OUR AREAS OF FOCUS

Climate and Environment

Climate Page 33

Environment Page 34

Just Transition Page 33

Deforestation Page 35

Human Rights

Page 38

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Cognitive Diversity on Boards

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3.2 **Our stewardship themes** continued

CLIMATE AND ENVIRONMENT

Climate – ongoing theme

The rationale for keeping Climate as one of our core focus areas remains the same:

- A rapid and successful net zero transition will support better outcomes for our customers and broader society.
- Climate change risks and opportunities have the potential to materially impact the companies we invest in and we need to support them to manage both successfully.
- Our customers care about climate change and expect us to manage the financial risks appropriately. Our Green Pensions Report found that 83% of UK workers think climate change is an important issue*.

Taking action over this decade continues to be crucial to protect our planet and economy, guiding our ambition to reduce our carbon emissions, in line with the actions outlined in our Climate Action Plan, published in 2022 (with an update provided for the progress over 2022 in Section 2.3 of this report).

Just Transition – additional explicit integration of the social impact of the climate transition

Climate change is one of the biggest existential threats humanity has ever faced. We're already seeing the physical impacts through changes in weather patterns, severe fires, hurricanes, and sea level rises. Global political powers recognise the need to change how we do things. Moving from air polluting production methods to cleaner ones, changing the materials we use, and investing in renewable sources of energy to power countries.

The Paris Agreement – struck in 2015, recognised that the deep systemic changes required to achieve the goals could permanently harm society if not managed sympathetically. For example, the phasing out of fossil fuels is vital for the survival of our planet, but the adjustments needed will have major effects on workers, the economy, production methods and our way of life in general.

Social consequences, such as the impact on jobs and local communities, must be considered over the next few decades as we go through these monumental changes. Implementing the adjustments needed to combat climate change brings an opportunity to do things better than before. New products, skills and systems will be created.

Over the last year, as a responsible investment team we have increased our activity on the 'S' of ESG: developing our thinking and frameworks to incorporate greater consideration of social factors. The Just Transition is the framework and lens that marries together the 'E' and the 'S' – making it the perfect topic of focus for us.

Just Transition considerations feed into our Climate Action Plan and overall Responsible Investment and Stewardship Framework. Put simply, the Just Transition is transitioning to a low-carbon, environmentally sustainable economy, without leaving people behind. By engaging with investee companies, encouraging them to put the Just Transition at the heart of their ESG strategy, and using our voting power where necessary, we can help companies understand the importance of the Just Transition.

In 2022, we conducted in-depth research into the Just Transition, examining the makeup of the global economy and the impacts decarbonisation may have on various sectors and their employees. In our 'The Just Way' report** we advocate for a Just Transition as the world decarbonises. We also explain why this is important to the pensions industry, while detailing some of the tools available to help pension providers, schemes and policymakers take positive action. To inform our thinking, we spoke to a number of leading industry experts.

The purpose of the paper was to provide a holistic overview of the Just Transition, utilising public research and evidence provided by industry experts. The objectives can be summarised as below:

- Make clear exactly what the Just Transition is and why it is relevant to Scottish Widows and the wider pensions and investments industries.
- Review the different lenses through which the Just Transition can be inspected.
- Recommend investor and government actions for enabling a smooth and just transition.
- Provide a Scottish Widows specific view of how we will use the paper to inform our own approach.

We believe companies should connect their action on climate change with inclusive development pathways driving a 'just transition' for workers, communities and other stakeholders as the world's economy responds to climate change. This includes planning for an equitable transition and engaging with stakeholders and disclosing the key risks and measures being taken to minimise negative impacts. We believe that failure to adequately consider a just transition can expose companies to material social and environmental risks, which may deter and impact the pace of change required to decarbonise. In our Voting Guidelines, we encourage companies to incorporate the International Labour Organisation's "Guidelines for a Just Transition" and to disclose metrics to measure progress on just transition goals and activities.

Following publication of our Just Transition paper, we updated our core stewardship priorities, expanding 'Climate & Carbon' to 'Climate & the Environment', making specific reference to the Just Transition as an integral part of any engagement on climate-related issues, taking due consideration of the impact of the transition to a low carbon economy on people. (Public Stewardship Policy)

We will generally support voting against the Say on Climate, report & accounts, and/or re-election of directors or members of a relevant committee if there is no disclosure to indicate that the company considers the impacts on employees, communities and other stakeholders in its climate transition strategy and/or the company has not disclosed a just transition plan outlining how it aims to support stakeholders negatively affected by its climate transition strategy. (Voting Guidelines)

To translate what we had learnt about the Just Transition into actionable application for the investment industry, we became a founding participant of the Just Transition Finance Challenge. The challenge, launched by the Impact Investing Institute (and in partnership with the City of London Corporation) aims to mobilise investment that is inclusive and socially beneficial. We discuss the Just Transition Challenge further in section 4.1.

The report was received well and got good press coverage:

"'Not only an environmental issue': Scottish Widows calls on pensions industry to steer a just transition to net zero" – Business Green

"Scottish Widows details recommendations for 'just transition' to green economy" – Pensions Age

"Scottish Widows sets criteria for 'just transition'" – Better Society Network

* Green Pensions Report – 2022 (scottishwidows.co.uk)
** 60644.pdf (scottishwidows.co.uk)

3.2 Our stewardship themes continued

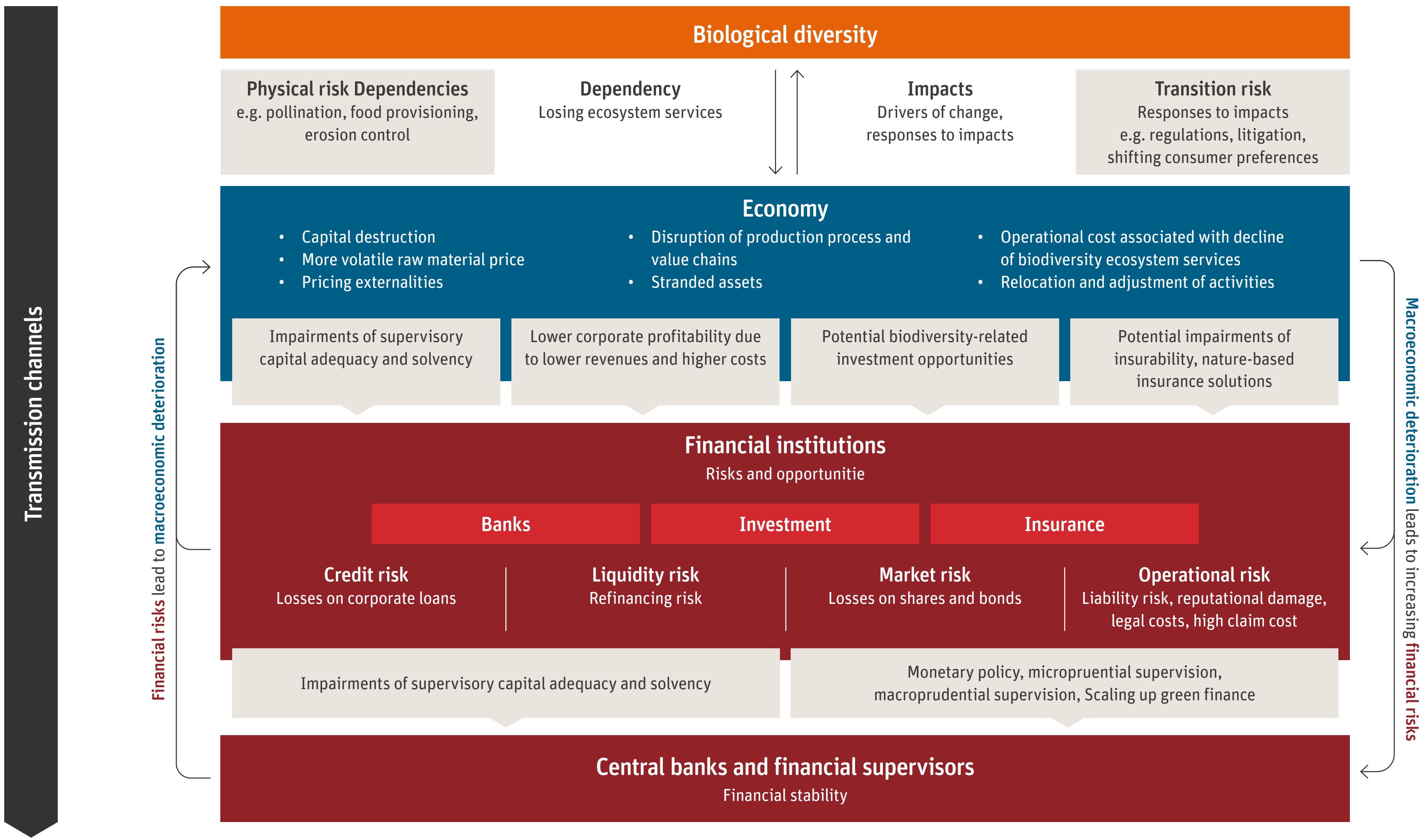
Environment (Nature and biodiversity): New theme

Nature degradation and biodiversity loss are among the biggest threats to the planet, society and the economy. Despite this, humans continue to drive an unprecedented and dangerous rate of biodiversity loss, subsequently presenting these threats in the form of non-linear physical, transition and systemic risks. Environmental risks – including climate change and the loss of biodiversity – now make up four of the top five global risks over a 10-year period as ranked by the World Economic Forum's Global Risk Perception Survey. Endangering financial stability, global sustainable development and economic prosperity, these risks also threaten business profitability and value, and in turn, investment value. We can see the implications for the economy and financial institutions in the figure to the right:

While there has rightly been much focus on climate change and the role pension providers can play in supporting the transition to net zero, much less attention has been paid to the loss of nature and biodiversity. Just as we are with climate-related risks and opportunities, here at Scottish Widows we are clear on the need to engage with both the companies we invest in and our appointed investment managers on nature-related risks and opportunities. We recognise the importance of an integrated approach in this respect – climate change and the loss of nature are inextricably interlinked and mutually reinforcing. Climate change can impact environmental processes such as soil moisture and water cycles, while biodiversity loss can exacerbate climate change. Interactions between climate and nature can amplify risks to business and financial portfolios – any focus on climate-related financial risks without due consideration of other environmental-related risks could lead to under-pricing of risk. It follows that both crises must be addressed in tandem.

Source: NGFS-INSPIRE, NGFS, Central banking and supervision in the biosphere, An agenda for action on biodiversity loss, financial risk and system stability, 2022.

Biodiversity, the economy and the financial system. Risk transmission channels



3.2 Our stewardship themes continued

Alongside the risks that degradation of nature and loss of biodiversity present, halting and reversing that offers potential opportunities at both a societal and economic level. As an asset owner, we need to ensure that the investments made on behalf of our customers are done so in a 'nature-smart' manner – risks must be considered while capitalising on the opportunity that the transformation to a nature-positive economy can offer. Over the course of 2022, our Biodiversity and Nature focus has been put into practice by engaging with our asset managers on nature and biodiversity related topics which we discuss further in section 3.4. In addition, we produced two papers on the theme of nature:
1. Nature and Biodiversity: The pensions imperative
2. Our approach to deforestation

Our industry advocacy paper, 'Nature and Biodiversity: The pensions imperative'*, discusses the nature crisis and associated risks in greater detail, and through a series of recommendations, offers up a call to action to galvanize government and our industry, and catalyse the necessary attention and action. We set out six actions in our call to action for the government, and four actions for the pensions industry:

Governments
1. Demonstrate leadership in protecting nature
2. Establishing incentivising policy
3. Incentivise capital flows into nature protection and restoration via regulation of the voluntary carbon market
4. Integrate nature-related risks and targets into all policy and regulatory matters
5. Deliver and implement clear governance and accountability
6. Optimise coordination, planning and engagement

* 60908.pdf (scottishwidows.co.uk)
** MSCI, 'Deforestation risks on the rise', Arne Philipp Klug, December 2022.
*** Deforestation report (scottishwidows.co.uk)

Pensions Industry
1. Increase awareness, build capacity – be 'nature smart'
2. Assess portfolio exposure
3. Support corporate engagement and transformative action
4. Carry out policy and regulatory advocacy

For more detail, see our publication.

Given the scope of nature and biodiversity as a theme can be all encompassing, in 2022 we decided to start tackling this by focusing on one key sub-strand – deforestation. Over this, the next sections and chapters, we have elaborated on the risk assessment, manager and company engagement and industry activities we have initiated and contributed to over the course of the year.

Deforestation

Deforestation is one of the key drivers of climate change as the clearance of forested land through burning releases vast amounts of GHG into the atmosphere. 12% of global GHG emissions are absorbed by forests**. Land use change – such as that brought about by deforestation – is the leading driving force behind loss of nature and biodiversity. As reflected in our paper, 'Our approach to deforestation'***, we understand the risk that deforestation presents to the planet, society, economies, businesses and investment portfolios.

As an asset owner, we have an opportunity to leverage our shareholder power to minimise the negative impact of the global economy on the world's forests and reduce deforestation. We have, therefore, begun to enhance our understanding of the impact that our funds have on the issue of deforestation. In collaboration with the Global Canopy and Make My Money Matter, we supported the development of 'deforestation-free pension funds' guidance that encourages the pensions industry to measure and disclose deforestation risk within portfolios and develop strategies to minimise contribution to deforestation (further details in Section 4).

The guidance is structured in six phases:
1. Mapping risk
2. Setting an effective policy
3. Monitoring and engagement
4. Disclosing
5. Eliminating deforestation, conversion, and associate human rights abuses
6. Nature and people positive financing

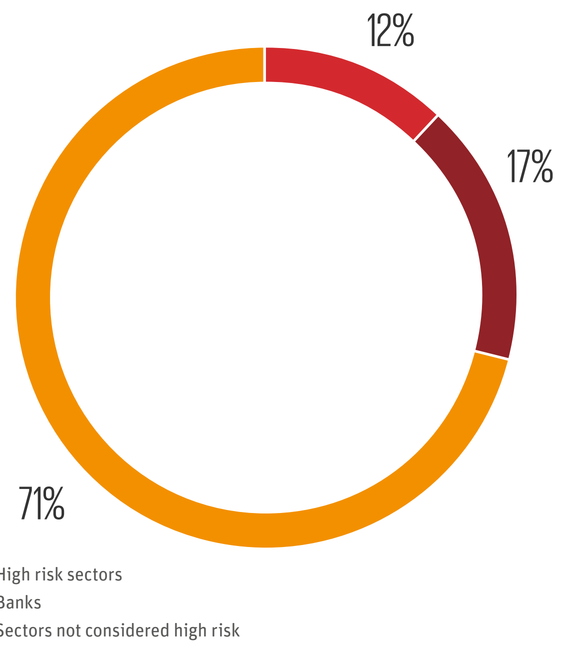
Following adoption of appropriate areas of this guidance, we initiated phase 1 of the guidance and conducted a risk mapping exercise across our investments. In terms of potential contribution towards deforestation, companies within sector groupings identified as 'high-risk****' amount to 12% of our corporate exposure, increasing to 28% when including the banking sector. £124bn of corporate exposure was analysed, including externally managed funds; in all representing almost all our total corporate exposure and 75% of our total assets under management.

In addition, we have mapped our holdings to Forest500***** and identified we hold 164 companies totalling £12bn out of the 350 corporates listed by Global Canopy as influential in forest-risk supply chains, focusing on palm oil, soy, cattle and timber products. We also hold 103 of the 150 banks included in the Forest 500, totalling £11bn.

On phase 2 of the guidance, we have integrated deforestation not only in our Stewardship Policy, but also included it under our Voting Guidelines, and will continue to explore if and when to enhance these further.

**** Sector and industry exposure to commodities associated with deforestation using the Global Industry Classification Standard (GICS®). These High Risk sectors are as set out in the Investor Guide to Deforestation and Climate Change published by Ceres, June 2020, and adopted by the Global Canopy guidance.
*****https://forest500.org/about

Deforestation: Our exposure to high risk sectors*



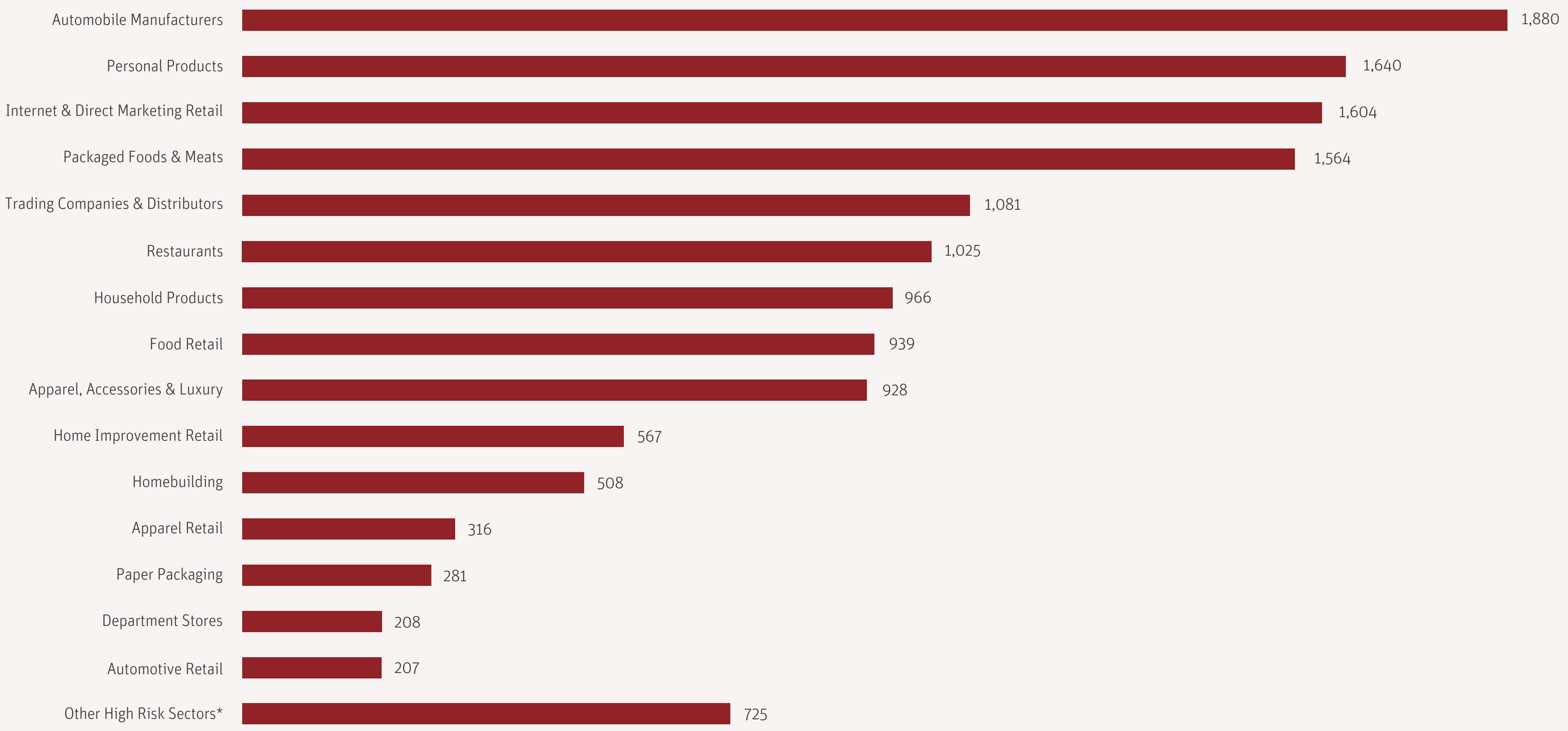
*Figures have been rounded to whole numbers.

We have identified over 1,750 companies totalling over £14bn sitting in sectors identified as at high risk of contributing towards deforestation. When including the financial sectors adds an additional 850 company names covering an extra £21bn of our assets.

3.2 Our stewardship themes continued

21 sectors have been identified as high risk by the guidance for pension funds and we have mapped this against total corporate exposure (bond and shares held in companies). In many cases exposure is concentrated in household names with significant value within our portfolio. This analysis not only includes our own fund mandates but holdings of almost every third-party managed fund where Scottish Widows is the asset owner.

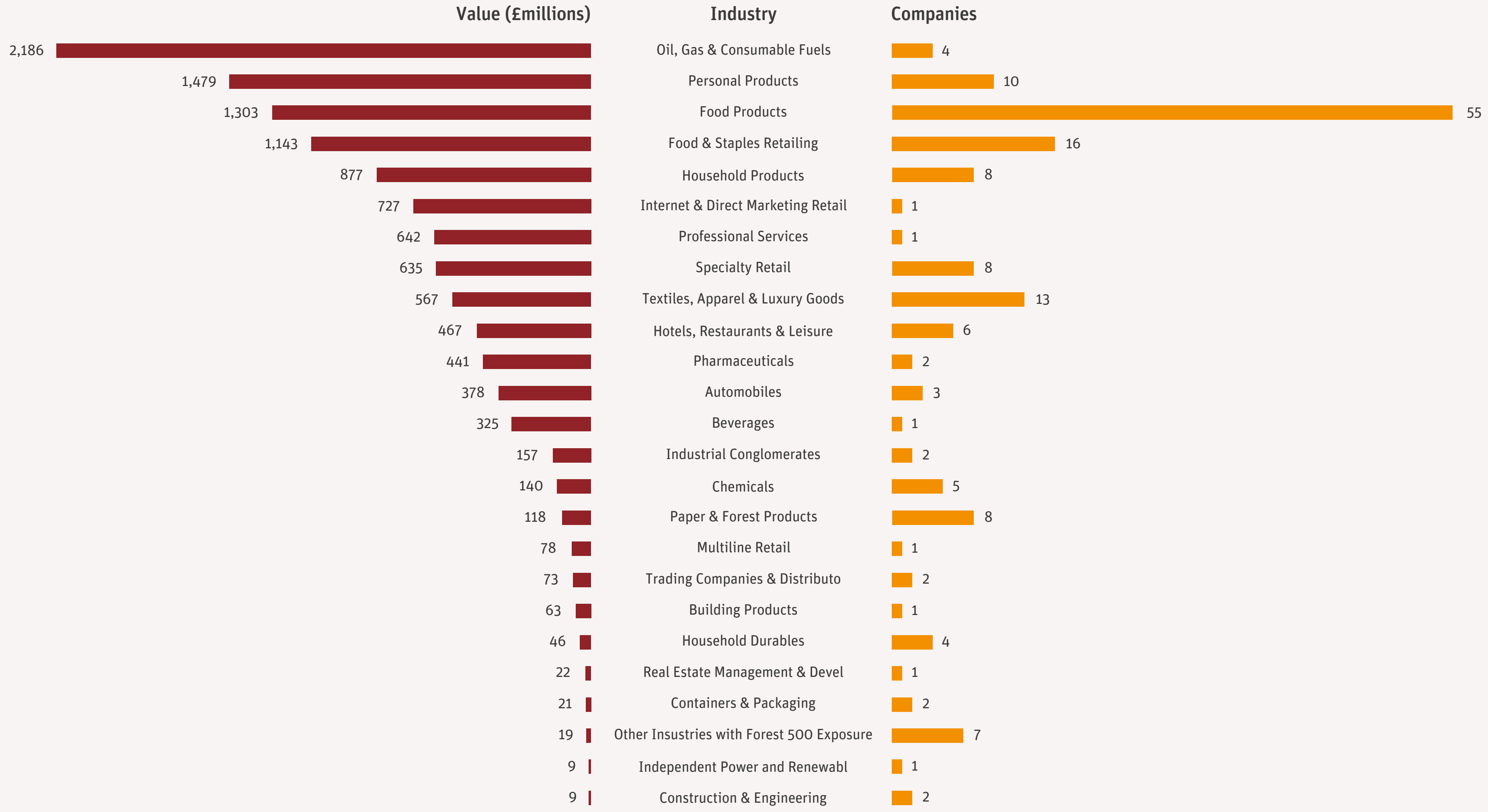
Deforestation: Exposure to high risk sectors excluding banking sector (per £m, rounded)



* Other sectors amounting to £725mn (409 companies) include Paper Products, Footwear, Agricultural Products, Renewable Electricity, Food Distributors, Home furnishing Retail, Coal & Consumable Fuels, Forest Products, Textiles, and Home Furnishings.

3.2 Our stewardship themes continued

Forest500 Company Exposures (excluding Financials)



In addition, we have also mapped the 350 corporates identified as significant in the fight towards deforestation by Global Canopy's Forest500. While there are fewer names compared to the wider sector mappings, these companies still amount to 10% of our total corporate exposure.

Over the course of 2023, we aim to further deepen our understanding of nature, biodiversity and deforestation. It is our ambition to complement deforestation exposure analysis with other nature-related indicators and build a more holistic view of our real impact and risk. Industry standardisation in risk management approaches, such as the Taskforce for Nature-related Financial Disclosures (TNFD)* risk management and disclosure framework, will support us in this ambition.

For more detail on deforestation risk, see our publication.

Companies and sectors viewed as significant in the fight against deforestation that score particularly poorly regarding policy and action help us identify key areas of focus for direct engagement and discussion with our appointed managers, with particular focus on companies falling within our largest individual exposures.

* TNFD – Taskforce on Nature-related Financial Disclosures

3.2 Our stewardship themes continued

HUMAN RIGHTS: NEW THEME

Human rights form the basis of good business practice and risk management. It is broadly accepted that companies have a responsibility to respect human rights, including in supply chains and business relationships, and this is articulated in international law. The Universal Declaration of Human Rights sets out: “a common standard of achievement for all peoples and all nations, to the end that every individual and every organ of society … shall strive … to secure their universal and effective recognition and observance”.

The UN Guiding Principles on Business and Human Rights (UNGPs) are the authoritative standard for corporate conduct. They are widely supported and adopted by states, regional institutions and multilateral organisations. In 2013 the UN Office of the High Commissioner for Human Rights (OHCHR) clarified that the UNGPs apply to institutional investors.

Human rights is a broad theme which relates to companies differently depending on their sector, geographical area and business model. Human rights can be broadly split into three areas which businesses have to consider:

- Due diligence – an ongoing risk management process that a company needs to follow to identify, prevent, mitigate and account for how it addresses its adverse human rights impacts. It includes four key steps: assessing actual and potential human rights impacts; integrating and acting on the findings; tracking responses; and communicating about how impacts are addressed.
- Working conditions ensures safe working environments, both physical and mental, but also encouraging a diverse workforce and enabling worker empowerment.
- Decent/fair/living wage ensures that workers are compensated fairly that allows for a minimum standard of living.

We began embedding the theme into our approach through engagement with our appointed investment managers, joining investor collaborations and conducting analysis on the materiality of human rights across our portfolio. Human rights is discussed further in later sections and chapters of our report.

COGNITIVE DIVERSITY ON BOARDS: ONGOING THEME

We believe cognitive diversity in leadership – in other words individuals who have different styles of problem solving and can offer unique perspectives because they think differently – leads to better long-term value creation for the companies we invest in and, hence, our customers. Cognitive diversity has grown out of the more established concept of ‘representation’. It is now well established in business and government that our institutions should make every effort to represent society, including but not limited to gender, ethnicity, social background. Having got to this point, we can now think deeper and broader about what being representative should mean. Our research* paper produced in partnership with the University of Bath discusses these linkages and their relevance to business in more detail.

We have provided greater depth on this theme in our 2020 and 2021 reports. The next section outlines our engagement activities undertaken in 2022 on this.

* Great Minds Don’t Think Alike. Cognitive Diversity in the Boardroom (scottishwidows.co.uk)

3.3 ENGAGING DIRECTLY WITH INVESTEE COMPANIES TO DRIVE POSITIVE CHANGE

CLIMATE AND ENVIRONMENT

We are continuing to engage with companies on their net zero transition plans, targeting companies based on specific criteria to ensure our activity is additional to other engagement by market participants. Of the 49 companies in our biggest 100 holdings which fall under the six most polluting sectors, as per the Global Industry Classification Standard (GICS)* classification 22 are already subject to extensive engagement activity by Climate Action 100+, of which we are members.

In 2021 we wrote to the remaining 27 companies which fell under the 6 most polluting sectors, as per the GICS classification. In 2022, for our next stage of engagement, we decided to concentrate our engagement on 15 of the 27 companies which were not covered by Climate Action 100+ engagement and were targets for improvement.

Our first letter in 2021 asked companies to commit to a net zero plan and outline a credible pathway to transition. For our second letter in 2022, we conducted research on their TCFD reporting, transition plans and approach to nature and biodiversity, as an integral part of our Climate and Environment sub theme, to engage on a company specific basis.

Our letters to these companies highlighted:

- Scope 3 emissions are often a company's largest set of emissions which require the most work to reduce. We encouraged companies to disclose and develop plans to reduce their Scope 3 emissions.
- Broader environmental impacts including biodiversity loss, waste and water management, pollution and land use and management.
- The Forest 500 ranking identifies companies with the greatest exposure to tropical deforestation risk and assesses them on the strength and implementation of their commitments. We included companies' places in the ranking and encouraged them to take action to reduce their deforestation risk.
- Our report on the Just Transition, to ensure companies are embedding the social aspect of the transition to a low carbon economy into their plans. We included a link to the report – The just way: the case for a just climate transition.

For example, in our letter to McDonalds we asked them about their approach to zero deforestation in the supply chain and how they were considering other biodiversity themes.

At the end of 2022, eight companies had responded to our letter, and we had met with three to discuss their approach in detail. Here are some case studies.

Case study

LARGE UK DEPARTMENT STORE

Our initial climate engagement began in 2020 and was based on a high-level GIC Level 1 classification to ensure we were taking an additionality approach to those companies already being engaged with via Climate Action 100+ (CA100+)**. Engaging with the consumer goods sector has been productive due to the broad range of ESG factors these companies are exposed to and the interrelated nature of these factors. We had a follow up call from our climate letter with a large UK department store which began with discussing some of the climate basics such as disclosure of Scope, 1, 2 and 3 emissions and becoming a member of initiatives such as RE100. The conversations were productive and we were able to dig deeper into understanding whether the company was working with its landlords on reducing energy consumption and increasing decarbonisation. In addition, we were able to discuss a range of biodiversity concerns related to the production of raw materials for products and packaging related to the transport and delivery of products.

While there is still a lot more for the company to do in the nature/biodiversity space, and we will engage with management again on this topic, it is taking necessary steps on climate with the focus now moving to non-UK markets within its supply chain. We will look to have follow up conversations with them on 'social' factors which we think are equally important.

* www.msci.com/our-solutions/indexes/gics

** An investor-led initiative established to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change. Climate Action 100+

3.3 Engaging directly with investee companies to drive positive change continued

Case study

AMAZON

We initiated contact with Amazon in 2021 and have received a response from them in 2022. Whilst the company is active on climate and has pockets of good practice, it is reluctant to tackle supply chain emissions and emissions from third parties.

We sympathise with the difficulties in sourcing data and influencing third-party operations. However, we feel strongly that for a large company to claim to be a leader on climate it needs to take steps to support its broader supply chain and stakeholders, especially when it has significant influence and resource. In our response, we have asked the company to go further across a range of climate and environmental metrics. These include publishing a detailed transition plan with medium term targets and interim milestones encompassing their supply chain, Scope 3 emissions disclosures to include third-party products, embedding sustainability into executive remuneration and objectives, setting targets on sustainable sourcing of packaging, and showing progress on mitigating commodity-related deforestation.

We have not heard back from the company even after reminding them. In the absence of a response, we believe the way forward for us is to i) participate in relevant collective engagement initiatives, ii) monitor engagement activities of our appointed investment managers, and iii) direct our votes to support relevant resolutions that will drive change and action.

Climate-specific engagement

In 2022, we decided to change our approach on direct climate engagement. As asset owners, for a well-defined and advanced theme like climate, we believe we should be spending most of our time contributing to collective engagement activities. As such, we joined IIGCC's Net Zero Engagement Initiative, which has a two-fold remit. First, to provide support and escalation routes to CA100+ engagement leads on select companies headquartered in Europe, and second, to extend engagement activities to material companies in the 'demand' side, in addition to the supply, beyond the focus list of CA100+. Further detail can be found in Section 4 of this report. We continue to assess our approach on climate engagement.

Broader environmental engagement

In 2022 we joined a collective stewardship initiative organized and fronted by the Farm Animal Investment Risk and Return (FAIRR)* initiative focusing on waste and pollution. We will be involved in engaging with Cranswick and Yara International. More details about this initiative can be found in Section 4. In 2023, for engagements related to Nature/Biodiversity and broader environmental factors, we will continue to engage with our appointed investment managers, participate in any relevant collective opportunities, but also outline a plan for direct engagement with companies on select sub-themes.

* The FAIRR Initiative is a collaborative investor network that raises awareness of the environmental, social and governance (ESG) risks and opportunities brought about by intensive animal agriculture. FAIRR Initiative | A Global Network of Investors Addressing ESG Issues in Protein Supply Chains

3.3 **Engaging directly with investee companies to drive positive change** continued

COGNITIVE DIVERSITY ON BOARDS

As outlined in Section 3.2, we published a report on cognitive diversity on boards in 2021. We used this report to engage our largest 50 company holdings and expressed our view that the outcomes of the Hampton-Alexander* and Parker** reviews on gender and ethnic diversity should be a minimum requirement, but they do not capture the full spectrum of diversity. We encouraged firms to read our report and consider cognitive diversity as an integral part of workplace diversity to enable them to work towards developing stronger boards and more effective senior leaders.

We received positive responses from 15 of the companies we wrote to, including a number of more detailed responses. We followed up with a roundtable for companies to discuss the topic in more detail, such as some of the complexities of cognitive diversity in the workplace and work through the challenges collaboratively. It was an open, honest and candid discussion with representatives from several UK and Global companies covering a range of sectors like consumer goods, telecoms, healthcare and financial services. The discussion points from the roundtable were shared with attendees to support them in taking cognitive diversity initiatives forward in their workplaces.

* FTSE women leaders: Hampton-Alexander review – GOV.UK (www.gov.uk)

** Ethnic diversity of UK boards: the Parker review – GOV.UK (www.gov.uk)

Roundtable – Summary of discussion

1. Leadership

Leadership is key to creating change in the workplace and we can set an example through the teams we manage by establishing work boundaries, as well as time for solitude and thinking. Key ideas and examples which were shared included:

- Leaders need to be open to feedback and a number of organisations are trying formal ways for colleagues to input and feed into strategy such as colleague panels, emerging leaders groups and shadow boards.
- Spending personal and informal time together is hugely helpful for building connections and provides opportunity for informal feedback. For example, board dinners offer space to chat through agenda items informally and spend the time to understand people's perspectives.
- During the pandemic we lost the opportunity for 'team away days' and other informal meet ups, the move to hybrid working will need to ensure we have time to get to know each other again.
- Organisations are also thinking about ensuring offices are set up with a suitable balance of collaborative and quiet spaces to cater for all personalities and working styles.
- Assigning time for 'thinking' is essential, this can be easily done through 'no meeting' days or teams can go further and encourage colleagues to volunteer and take up other interests in work time, as part of their personal development.

2. Representation

Work on diversity has often centred around fairness but we are increasingly acknowledging that in order to celebrate and encourage our differences we need to allow people to do things differently.

Organisations are starting to move past gender and consider a much broader range of characteristics and the value that those characteristics bring. Skills and strengths are attributes which support us in celebrating difference and can be used in recruitment, in addition to more traditional attributes such as experience and qualifications.

Our recruitment processes are a good place to start when thinking about encouraging more diverse candidates, job advert wording and the flexibility allowed in use of cameras in interviews are simple things which can make a big difference.

The reputation of certain sectors can influence how people feel about an organisation and the type of people that work there. It is important that organisations publicise the range of roles and people at their organisation and the steps they undertake to reach a wider audience. This first impression will influence whether someone will consider applying for a role.

While creating boards and teams that better reflect society is going to be a work-in-progress, we can make our workplaces kind and open, where people want to work – inclusivity is key.

3.3 Engaging directly with investee companies to drive positive change continued

3. Measurement

Measurement is important but it is important to measure the right things. Collecting data across a broad range of characteristics is only a small piece of the puzzle.

We need to ensure measurement highlights peoples' attributes and strengths and not just what defines them demographically or socially. Sometimes being neurodivergent can be classed as a disability but people may not class themselves as being disabled. Being a carer is also an option to disclose in some workplaces but situations vary and people may feel the word has implications.

We also need to ensure we are measuring how inclusive our organisations are, whether people can be themselves and feel comfortable sharing their views. Organisations already conduct colleague engagement surveys, they could be used more effectively to track authenticity and culture.

There is also a lot of measurement we can do without straying into legal barriers, teams can do insight questionnaires and measure characteristics such as introversion/extroversion. These can be used to learn and share rather than add to organisational wide statistics.

Leaders and laggards

The roundtable was aimed at companies who acknowledged diversity was important and wished to share ideas to advance the agenda. Unfortunately, not all companies in our portfolio have reached this stage of their diversity journey. Therefore, alongside the roundtable, later in the year, we decided to target companies who were laggards on diversity.

Further targeted engagement activity in 2022

We assessed our list of top 300 companies and wrote to those that had less than 25% of women on their board.

- For UK companies we set out targets from the Hampton-Alexander and Parker reviews and asked companies how they are considering diversity more broadly.
- For European and US companies we included the targets as best practice.
- For companies domiciled in emerging markets/China only gender targets were included. Ethnic diversity is a much less developed concept and requires a 'country-specific' nuance to be applied, which currently is out of scope.

In total 31 companies were contacted, and we requested a meeting with 10 of them. We were pleased that 18 companies responded to our engagement and provided additional information on their approach. We monitored companies' progress over 2022 and may take voting action if progress isn't made, or we there is not sufficient explanation of their action on this topic. Three companies we engaged with were committed to achieving 30% women on the board as soon as 2023. One company also stated they planned to have an all women shortlist for their next director position. Alongside monitoring we also had three meetings lined up for early 2023 to dig deeper into companies' approach to diversity and to understand some of the challenges of increasing diversity on the board.

We have been encouraged to see that companies' diversity efforts went further than the board and considered the pipeline of future leadership. Some of the companies we engaged with were in traditionally male-dominated industries, such as technology and energy, which reduced the pool of directors who would likely apply for board positions. To combat this long term, one company was ensuring inhouse training in coding was available which they hoped would lead to lateral moves between departments and promotions. A few companies were also committed to partnerships with universities, NGOs and grassroots organisations to increase diversity proactively.

3.3 Engaging directly with investee companies to drive positive change continued

HUMAN RIGHTS

In 2022, we analysed our investee companies to prioritise them for engagement. This included:

1. Identifying target industries
2. Identifying relevant third-party data sources
3. Mapping third-party data to our own portfolio
4. Applying normalised scoring framework to companies in target industries
5. Identifying concentrated list of worst scoring companies

1. Identifying target industries

We began with identifying the target industries adopted by the Business & Human Rights Resource Centre. We combined this with research from an asset manager and other organisations, as well as our own knowledge, to end up with 12 industries (based on GICS level 3*) that have the most human rights risk.

2. Identifying relevant third-party data sources

Once we had identified the target industries, we began researching data sources. We concentrated on sources that had the most coverage, were the most recognised, and had the most depth. Five data sources were identified:

Workforce Disclosure Initiative (WDI) company data for 2022
WDI data is provided by individual companies through a survey response. It is very extensive and covers both direct company operations and supply chains and questions are both quantitative and qualitative. For the purposes of this analysis, the five most relevant quantitative human rights related questions were selected.

KnowTheChain benchmarks: ICT (2022), Food & Beverage (2020), Apparel & Footwear (2021)
The KnowTheChain methodology assesses companies' efforts to address forced labour risks in their supply chains. It is based on the UN Guiding Principles on Business and Human Rights and covers policy commitments, due diligence, and remedy. The methodology uses the ILO's core labour standards (which cover the human rights that the ILO has declared to be fundamental rights at work: freedom of association, the right to collective bargaining, and the elimination of forced labour, child labour, and discrimination) as a baseline.

World Benchmarking Alliance: Corporate Human Rights Benchmark (2022)
The CHRB assesses 127 companies in the food and agricultural products, information and communications technology, and automotive manufacturing sectors on their human rights performance. The benchmark is composed of five measurement themes. Each theme contains a series of indicators focusing on different aspects of how a business seeks to respect human rights across its own operations and supply chain. Our indicators are grounded in the United Nations Guiding Principles on Business and Human Rights and other international human rights standards, with additional sector-specific requirements applied to some indicators.

World Benchmarking Alliance: Human rights sub-indicator of Social Transformation Baseline Assessment (2022)
The Social Transformation Baseline Assessment looks at what 1,000 of the world's most influential companies are doing to contribute to the social transformation of our global system, assessment scores these companies on 18 core social indicators. These indicators signpost high-level societal expectations of businesses. The 18 core social indicators are bucketed in to three pillars. We have chosen to take the aggregated score from the 'Respect Human Rights' pillar, which is made up from the first eight sub-indicators.

MSCI ESG Manager data
We extracted some simple data points from the MSCI ESG Manager data platform. This acts as a simple data baseline and fills in gaps where coverage from the other data points is low.

3. Mapping third-party data to our own portfolio

We mapped each third-party data point to our own portfolio, concentrating on our top 500 holdings based on AuM.

4. Applying normalised scoring framework to companies in target industries

Because each third-party had their own scoring methodology, and some sources were primary data whereas others were proprietary scores, it was important that we standardised scoring to easily compare across portfolio companies.

5. Identifying concentrated list of worst scoring companies

Once scoring was standardised, we were able to identify worst performing companies. We decided to avoid calculating an overall average because it would have resulted in bunching towards the mean and hiding outlying scores. Instead, we added a trigger for any company that was in the worst scoring 40% based on any of the third-party data sources i.e. if a company performed very well on one data source, but poorly on another, they would still be flagged.

Results and next steps

The final target list totalled 27 companies, representing £5.8bn AuM (based on 2022 end), with 10 companies on the target list sitting in Scottish Widows top 100 list. We are currently in the process of conducting further concentrated research on each of the 27 companies before developing an engagement plan to be initiated in 2023-24.

In 2022 we joined Advance, a PRI collective stewardship initiative on Human Rights and are supporting collaborative engagement with Anglo American. In addition, at the end of 2022, alongside two other investors, we joined the Collective Impact Coalition (CIC) organised by the World Benchmarking Alliance (WBA) to improve human rights data and voting provisions. More details about the Advance initiative and that carried under the WBA CIC can be found in Section 4.

* Oil, Gas & Consumable Fuels; Interactive Media & Services; Metals & Mining; Internet & Direct Marketing Retail; Food Products; Specialty Retail; Food & Staples Retailing; Hotels, Restaurants & Leisure; Textiles, Apparel & Luxury Goods; Diversified telecommunication services; Construction Materials; Building Products.

3.3 Engaging directly with investee companies to drive positive change continued

UNITED NATIONS GLOBAL COMPACT (UNGC)

Our Exclusions Policy states that we will not invest in companies which violate UNGC principles in our mandated passive funds. In our mandated active funds, where a company represents more than 0.5% of a relevant stock market index, it is flagged as a priority engagement target. We use our scale to influence for change over a three-year period. If there is no change after that period, the company will no longer be exempt from our policy, and we will consider selling out of our investment.

In 2020, we wrote letters to nine companies that had been flagged as UNGC violators by MSCI, asking them to take corrective action and keep us informed of their progress and engaged directly with Shell, Walmart and Volkswagen. By the end of 2021, only five companies we invest in remained flagged as violators (no new companies had been added to the list). Both Walmart and Volkswagen had their violator flags removed. We wrote to the five remaining companies with flags to understand their actions, monitor their progress and request follow-up conversations. We met with Shell again in early 2022 and were pleased to see that it too had subsequently been cleared from the violators list by MSCI.

However, towards end of 2022, new companies were added by MSCI as UNGC violators, including Volkswagen again, but this time under a different UNGC principle related to Human Rights violation. We contacted the 11 violators and heard back from Volkswagen and Glencore.

Timeline

END 2020

Wrote letters to nine companies highlighting concerns over its UNGC violation

2021

Further in depth engagement with three companies details have been covered in our previous reports

END 2021

Wrote letters to five companies highlighting concerns over its UNGC violation

2022

Further engagement with one large company, critical one for invest portfolio

END 2022

Wrote letters to eleven companies and heard back from two

2023

Met with representatives from one company, re-entered into the list but related to a new UNGC violation

Case study

VOLKSWAGEN

Having recently been removed from the UNGC violators list off the back of its emissions scandal, Volkswagen was re-added in 2022 in relation to operational activity in the Chinese Xinjang region by linkages in its supply chain. As a result of our engagement via a letter, we met with Volkswagen in Q1 2023 when the company assured us that risk management processes were in place and that it was engaging further with MSCI with regards to the allegations. We continue to monitor the situation and will further engage with Volkswagen where necessary.

Case study

BHP AND VALE

The two companies that have been on the violators list from the time our Exclusions Policy came into force are BHP and Vale. We have written to them every year since 2020, but have not had any response back from BHP, and heard back only once from Vale in 2021 with a response to our letter alongside their reparation report. We are keeping a close watch on both companies. **If they are unwilling to engage** and unable to clear their name from the UNGC violators list by the end of 2023, in keeping with our Exclusions Policy, we will consider divesting from them.

3.4 MONITORING AND OVERSIGHT OF OUR APPOINTED INVESTMENT MANAGERS

Monitoring and helping to improve our appointed investment managers' approach is one of the key tenets of our stewardship approach – perhaps the most important one as it enables us to scale our impact – alongside direct engagement with companies and contribution to industry-wide developments.

In 2022, we continued to monitor, review and challenge our core appointed investment managers Schroders, BlackRock, State Street and Hermes at regular check points through the year, in keeping with our procedures, as well as communicating with managers on an ongoing basis. As part of our reviews, we scrutinise managers' ESG reports and other publications, news articles and third-party/non-profit organisations' commentary such as relevant reports from ShareAction*, Principles for Responsible Investment**, and Reclaim Finance***. The reviews cover the full spectrum of ESG integration and engagement activities, any relevant reporting requirements, voting preferences and activity. Alongside regular stewardship items, we aim to get a detailed understanding of the managers' ESG integration capabilities, industry collaboration and policy advocacy activities and relevant consultation responses to government. We have found that working upfront to establish focused agendas and requesting the right people to attend the reviews results in us being able to concentrate on areas of discussion, support and challenge, contributing to improving market practices.

The focus of our reviews is dictated by materiality, level of exposure, and ESG themes which are shared areas of interest between us. We acknowledge that investment managers will approach thematic topics across their entire portfolios rather than specifically in relation to the funds we invest in. Therefore, we also undertake deep dive case studies to understand and challenge, if appropriate, the success of engagement and escalation strategies in relation to the specific companies held in our funds. In 2022, we found that we had effective ongoing communication with all core managers across the year on a variety of stewardship and ESG related topics, in addition to our formal checkpoints. We have found that this has helped reinforce the strategic nature of our relationships and resulted in a more joined up approach to how we conduct our activities.

* ShareAction | Harness the power of investment

** PRI | Home (unpri.org)

*** https://reclaimfinance.org/site/en/home/

As most of our mandated passive funds moved from Abrdn to BlackRock in March 2022, we prioritised time with BlackRock in 2022 where we had the largest exposures, to support the transition between asset managers. We engaged with Abrdn on the implementation of exclusions over 2022, but will resume our regular oversight activities with Abrdn for the residual funds managed by the company and for our investments in its pooled funds over 2023.

3.4 Monitoring and oversight of our appointed investment managers continued

Case study

VOTING PROCESS

In 2021, we worked with our appointed investment managers to enable us to be more involved in voting. One of the managers has been especially receptive to exploring how this could work in a more efficient way. Mid-way through the voting season we completed our onboarding of Minerva Analytics, a specialist voting intermediary, and gained access to its research portal to enable us to take a view on upcoming votes. Having not directed votes before, we had a steep learning curve to understand the practical considerations such as deadlines and the nuanced complexity of the votes. Over the course of 2022, this investment manager has been patient and supportive in enabling us to learn from its experience while setting up the process for us to override vote. As a result, we have established a good process with the manager to have forward-looking discussions on some significant upcoming votes.

We are also pleased to work collaboratively with another manager of our mandated passive funds to add an instruction to allow us to override votes on our passive tracker funds, much like on our active investments. This took a while to iron out, but in the end, the manager helped connect us with their own proxy-voting agency to create a seamless process, which will come into effect in 2023. This facility will allow us to direct votes on the same resolutions across most of our mandated funds.

Case study

REGULAR OVERSIGHT MEETINGS

Based on ongoing feedback over the course of 2021 with one of our appointed investment managers related to our investments in its pooled funds, we saw remarkable change in the preparation of the meeting agenda, providing supporting materials, inclusion of relevant specialists and the general quality of discussion and follow up actions. In addition, this manager, which had historically struggled with the quality of its reporting, has shown improvements both in quality and timeliness. The manager also went beyond expectations with proactively providing us with data before the request was made.

Case study

VOTING CHOICE IMPLEMENTATION

We were keen that voting on the companies in most of our passive tracker investments, either through mandates or through pooled funds, was carried out using the same ISS Socially Responsible Investment policy, which we consider most closely aligns with our Voting Guidelines. Having implemented this policy across our mandates and with one of the pooled fund managers, we engaged with the other significant pooled fund manager we work with to allow the same voting choice. Over the course of 2022, we shared with them our learnings from implementing the policy with some of our investments. At the end of 2022, we were delighted to see this manager enable this facility for some of their UK and US clients. Its implementation is well under way, and we hope to start using it in 2023.

3.4 Monitoring and oversight of our appointed investment managers continued

Case study

CLIMATE TRANSITION PLANS

In the run up to climate conference COP26, many companies from a range of sectors made net zero announcements, with medium-term targets of 2030 and net zero targets for 2050. Post COP26, 2022 was a year of ensuring these targets had supporting governance in place. For many investors the next step, kicking off in 2022, was to start considering and assessing how a company intends to transition to meet those targets. One of our appointed investment managers presented its approach to assessing companies' transition strategies as part of an escalation framework. We were able to constructively discuss and challenge the framework and followed up later in the year to understand the progress the manager had made. We are pleased with the proactiveness and openness of this manager. There are many companies in jurisdictions which do not support climate progress, and the manager is continuing to challenge these companies in a sensitive but focused way.

Case study

DIVERSITY

We are keen to ensure our stewardship activity builds on that of our appointed investment managers and that we pull in a similar direction when it comes to ESG topics. We have been encouraging managers to be honest and open about their company engagement. As an example, one manager has been moving past engaging just on gender issues with US and Latin American companies, and now also challenges on increasing ethnic diversity. They informed us that they have decided to take voting action against a particular American company which has been unresponsive to engagement.

Given the scarcity of diverse talent, we also discussed the risk that increasing diversity on boards can lead to 'over-boarding', where a person sits on an excessive number of boards resulting in an under-commitment of time and attention. The asset manager informed us that there has been many cases of over-boarding in Nordic countries, especially with demand for directors with sustainability and human rights backgrounds increasing. We shared our approach of focusing on cognitive diversity, encouraging boards to hire from wider pools of people to increase diversity and tap into a broader range of backgrounds and perspectives. The manager agreed with this approach but commented that the pool of candidates in the region has not increased that much yet.

Case study

FAIR PAY

Our voting approach enables us to override voting decisions on our largest investee companies by our appointed active investment manager. In 2022, we directed our vote in support of a special shareholder resolution for Sainsbury's to commit to paying all its workers the living wage, by July 2023, going against how our manager voted.

Overall, the resolution garnered c.17% support, which was encouraging given it is uncommon for supermarkets to be challenged on paying the living wage and the result was only just short of the 20% support customarily considered in the UK as enough support to warrant some management action.

We had extensive discussions with our appointed investment manager on the resolution and where our views differed. We are pleased that the resolution has been responsible for softening the ground on several further conversations and engagement activities on the topic. In addition, the resolution has helped raise the profile of the cost-of-living crisis and ever-increasing inequality gap between senior exec pay and median employee/national median average. In 2023, we will continue to raise these points and engage managers on Fair Pay and related voting activity.

More information on the Sainsbury's living wage resolution can be found in the voting section of the report.

3.4 Monitoring and oversight of our appointed investment managers continued

Case study

BIODIVERSITY

In 2022, we extended our climate theme to include broader environmental themes which extends to nature and biodiversity. To embed the theme into our stewardship and investment processes, we began by engaging with appointed investment managers to understand their approach to the theme, also exercising oversight of their activity and influencing them in the process. They recognised the importance of the theme and were considering it in different ways. Most managers had been considering the topic for some years and included it in engagement activity where the topic was material. However, managers have acknowledged that while there is a good understanding of the broader costs to society of biodiversity loss and environmental degradation, there is less analysis of the costs to individual companies. Therefore, managers have started exploring the topic with a view to better understanding and progressing the relationship between the environment and companies' business models and strategies. Our appointed investment managers are undertaking a range of activities in this area:

1

One manager has been heavily involved in the policy landscape on nature and arguing for better representation from the financial industry for the last few years. This has resulted in the launch of the Finance for Biodiversity Pledge which was showcased at the UN Biodiversity Conference (COP 15) and the manager co-chairs. The role of finance is a crucial part of activity on nature, and we were pleased to see an asset manager making a strong contribution to the topic.

2

Another asset manager has been heavily involved in the TNFD in the hope for better disclosures from companies on nature related risks. This information is key for investors to better assess and act on the topic.

3

The same asset manager has also been active in engaging companies on deforestation through an in-depth engagement exercise, to better understand best practice on palm oil and cocoa. The manager has also engaged with NGOs to build more nuanced knowledge and expertise on the topic. The plan is for this engagement to be scaled up once a better understanding of the issues and best practice is established.

4

Another asset manager has been focusing on plastics as part of their approach to better managing risks associated with environmental degradation. The engagement has been a learning experience to better understand the challenges companies face and the different stakeholders involved. This supports managers establish more meaningful objectives for companies and combine company engagement with policy advocacy.

5

Lastly, one of the asset managers has been trying to integrate land use and nature-based topics into their conversations about carbon emissions, as well as learning from other organisations. We have been pleased that managers have been collaborating closely with NGOs and research organisations on the topic. We feel this type of collaboration is essential to making progress on such a systemic and complicated topic. They shared an example of engaging with a company on deforestation with clear objectives for the company and subsequent outcomes which included:

- Implemented public grievance reporting
- Strengthened palm oil sourcing policy
- Advanced company conservation and restoration efforts and accelerated RSPO certification targets to 2021 from 2022

3.4 Monitoring and oversight of our appointed investment managers continued

Case study

HUMAN RIGHTS

Similarly to biodiversity, we have had deep dive sessions on human rights with our asset managers after adding the theme to our core priorities in our Stewardship Policy. All our appointed investment managers have been considering the theme and focusing on different sub-themes.

- One of our asset managers has been active in the space for some time. We focused on their research approach to the theme and covered some of their engagement activity. They split the theme into four areas – communities, customers & consumers, workers, regulations & government. We found this approach useful as it covered a broad range of sub-themes such as indigenous rights, ethical product use & interaction and workers' rights. The asset manager also shared their experience of engaging through the Find it, Fix it, Prevent it initiative where they were engaging with a company on a lack of transparency of their audits of workers' working conditions. We discussed the difficulties in improving transparency as companies were often concerned with the immediate repercussions of being honest about human rights breaches.
- Another manager had found human rights and governance concerns coming together. They were engaging heavily with a company on wages and health & safety following the striking of approximately 1,000 workers. The asset manager informed us that alarmingly the company board didn't consider the collective bargaining situation a risk to the company, despite the obvious impact of striking workers on the company's ability to operate. Furthermore, the company board's remuneration structure had reduced board members' objectives to ensure they were still paid despite poor performance. Consequently, the asset manager took strong voting action against the company, voting against two directors and the remuneration proposal in addition to supporting a shareholder resolution on governance. We were pleased that our asset manager took strong voting action and was able to link human rights concerns to the broader mismanagement of the company.

Case study

ASSER OWNER DIVERSITY CHARTER

Scottish Widows became signatories of the Asset Owner Diversity Charter in 2021. We follow the principles of the charter, which includes encouraging our appointed investment managers to complete the asset manager questionnaire on their firm's internal Diversity, Equity and Inclusion characteristics, programmes and targets. The questionnaire aims to standardise complex diversity metrics, beyond just gender, to improve on disclosures.

In addition to sending the questionnaire annually and reviewing responses, we have been working to include diversity as one of the areas we look at as part of our ongoing investment manager monitoring, focusing on our core investment managers first. Our Fund Manager Assessment Team and risk teams conduct an annual survey of our appointed investment managers as part of their ongoing due diligence. We have already incorporated ESG questions into the survey to capture updates to policies and practises and are in the process of adding diversity questions, including one on cognitive diversity of teams which we feel is essential for effective portfolio management. In addition, we have had some deep-dive discussions with investment managers to understand their approach to diversity. One manager has been proactive in their approach to increasing diversity and ensuring a culture of inclusion and equality. Senior managers have received hands-on training, programmes have been set up to increase diversity hiring through internships for underrepresented groups and colleagues from ethnic minorities have a safe space to discuss concerns.

3.4 Monitoring and oversight of our appointed investment managers continued

Case study

APPLYING EXCLUSIONS TO POOLED FUNDS

We continue to engage with our core appointed managers to more closely align their exclusions policies with ours. One manager is yet to implement thermal coal and tobacco screens, but has taken our feedback on board and is engaging with the index provider on that basis. The other manager has coal exclusions in place that go beyond our own, but is yet to take action on tobacco exclusions. We will continue to engage with them both over the course of 2023.

Non-core investment manager oversight

We have a different monitoring approach for non-core investment managers (who manage a substantially lower value of assets for us), depending on which tier they are in, as detailed in Section 1.4. For Tier 2 non-core managers we share our annually updated Stewardship Policy, along with our Voting Guidelines, as an expression of wish*. On an annual basis, we ask for evidence from the managers as proof of compliance with our Stewardship Policy, including, but not limited to, examples of engagement activity aligned to our stewardship themes, examples of collaborative activity, voting statistics, evidence of UK Stewardship Code signatory status, and latest UNPRI assessment scores. For Tier 3 managers, where we have little oversight of their fund operations, we share both our Stewardship Policy and Voting Guidelines, and ask for evidence of UK Stewardship Code signatory status, and their latest UNPRI assessment scores.

In addition, across all managers, we monitor their ratings/rankings on ESG and stewardship activities provided by third-parties like ShareAction.

We share the annual reviews across Scottish Widows teams, like the Fund Manager Assessment team, and other relevant investment operations and risk teams. This enables a more cohesive firm-wide view of investment managers we deal with and helps inform any future reviews or manager interactions.

* It is not a formal requirement written into contracts. It is a form of communication, similar to sharing a policy or client preference, which we would expect asset managers to consider. driving-change-through-the-voting-chain.pdf (publishing.service.gov.uk)

3.5 OVERVIEW OF ENGAGEMENT ACTIVITY BY APPOINTED INVESTMENT MANAGER*

In 2022, we have continued to engage our appointed investment managers through monitoring and oversight of their activity. To support this, we need to understand their overarching approach and have the data on their engagement activity. This guides our discussions with managers on actions and outcomes, and helps determine our ongoing engagement priorities.

The information in this section also includes specific analysis on our most material (Top 300) holdings across our stewardship priorities, and the breakdown of the specific themes under ESG categories. We ensure the scope of the fund managers' activities is across asset classes and geographies and discuss the relevant nuances during oversight and governance meetings as outlined in the previous section. Our activities are guided by our priority themes and focused on our most material holdings but we expect broader ESG engagement coverage from investment managers across different topics, geographies and asset classes.

For this report, we have provided an overview of the engagement activity undertaken by our core Tier 1 and Tier 2 investment managers, which supports our ongoing assessment of their stewardship performance.

Engagement Activities by our appointed investment manager

In addition to engaging directly with our top material holdings on our Stewardship themes, as explained in Section 3.3, our asset managers also conduct engagement activities with our investments i.e. delegated engagement. Our investment managers are expected to engage on our priority themes and across a range of other ESG themes.

This section covers 2022 engagement activity by:

- Our Tier 1 managers, Schroders, who manage most of our mandated active funds portfolio and BlackRock, who managed our mandated passive funds during this period; BlackRock. We have also included, as appropriate, activity by Hermes who manage our Ethical fund and by Abrdn, who managed two of our mandated passive fund that couldn't transition to BlackRock for operational reasons.
- Our Tier 2 managers, BlackRock, Abrdn and State Street Global Advisors (SSGA), who run the external funds** used in the Scottish Widows Pension Portfolio funds.

How we tier our managers has been described in Section 1.4. Each manager's exposure across the Scottish Widows book of business will depend on the type and number of funds they manage on our behalf or used within our funds. However, combined our investment managers will invest in a high proportion of all company names held in Scottish Widows customer and shareholder assets.

The type and number of funds that a manager manages will also have a direct bearing on the statistics highlighted in the analysis below, including on Scottish Widows top 300 company exposures, and therefore, these numbers should not be compared and in some instances, may appear small.

* All charts, graphs, case studies, top priorities, and related narrative have been paraphrased for Scottish Widows' stewardship reporting purposes, please visit each managers' own website for more insight.

** These 8 funds cover the majority of c.£50bn asset value held in the Pension Portfolio funds.

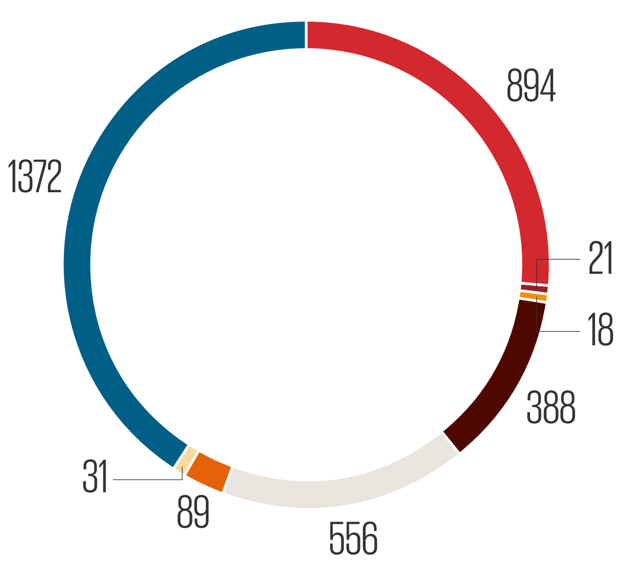
3.5 Overview of engagement activity by appointed investment manager continued

ENGAGEMENT ACTIVITY BY DELEGATED MANAGERS WITH SCOTTISH WIDOWS TOP 300 HOLDINGS

Our top 300 company exposures within our customer and shareholder assets, as at year-end 2022, amount to over a third of Scottish Widows total assets under administration. Due to this concentration of corporate exposures, and the potential influence these large companies will have in the global economy, we have an interest in monitoring how our underlying managers engage with these companies and what subjects are discussed. The top 300 calculation relates to all our direct holdings in companies held in Tier 1 funds in addition to those held within Tier 2 external pooled vehicles used in our Pension Portfolio funds.

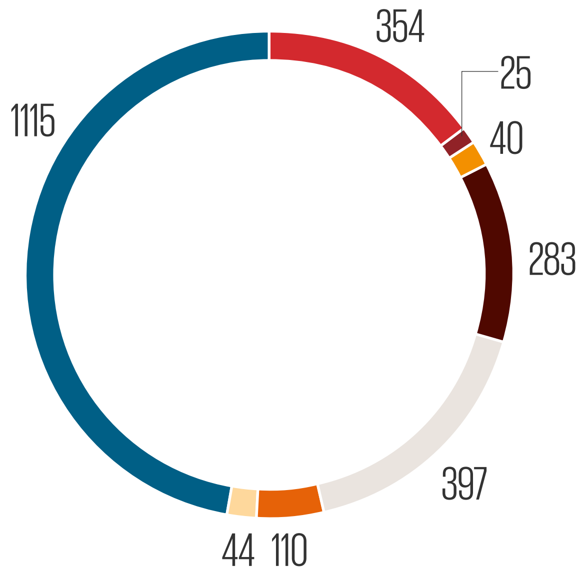
ESG Factors and Sub-themes engaged on by our Delegated Asset Managers in SW Top 300 – Tier 1

Environmental	1321
Social	645
Governance	1403
Total	**3369**



ESG Factors and Sub-themes engaged on by our Delegated Asset Managers in SW Top 300 – Tier 2

Environmental	702
Social	507
Governance	1159
Total	**2368**



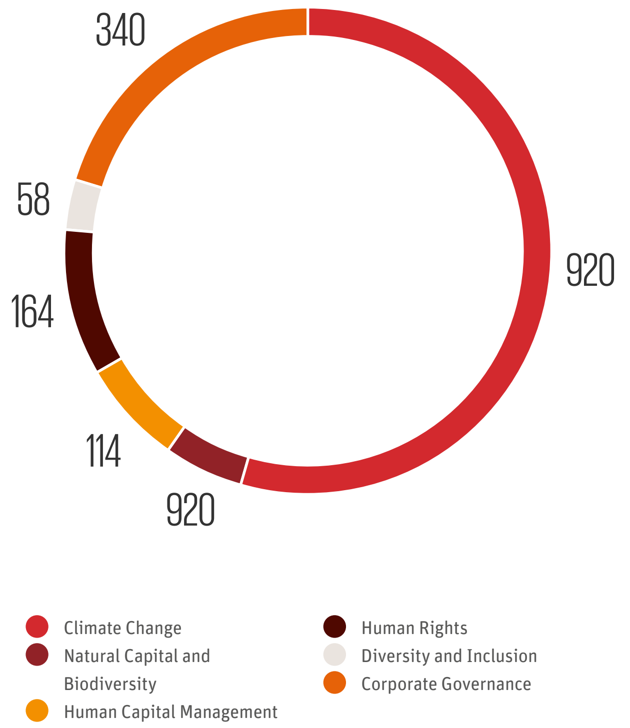
Climate & Carbon
Deforestation
Biodiversity
Other Environmental
Human Rights
Other Social
Board Diversity
Other Governance

3.5 Overview of engagement activity by appointed investment manager continued

ENGAGEMENT ACTIVITY WITH COMPANIES HELD IN SCOTTISH WIDOWS PORTFOLIO: CORE TIER 1 MANAGERS

Engagement Activity Breakdown by Theme by Manager

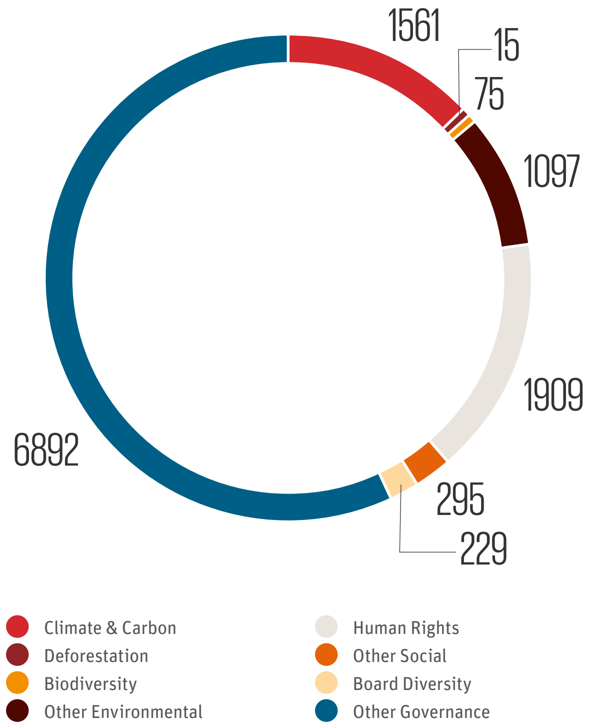
Schroders



Schroders Top 5 priority themes for 2022

- Climate Change
- Natural Capital and Biodiversity
- Human Rights
- Human Capital Management
- Corporate Governance

BlackRock



BlackRock Top 5 Engagement themes for 2022

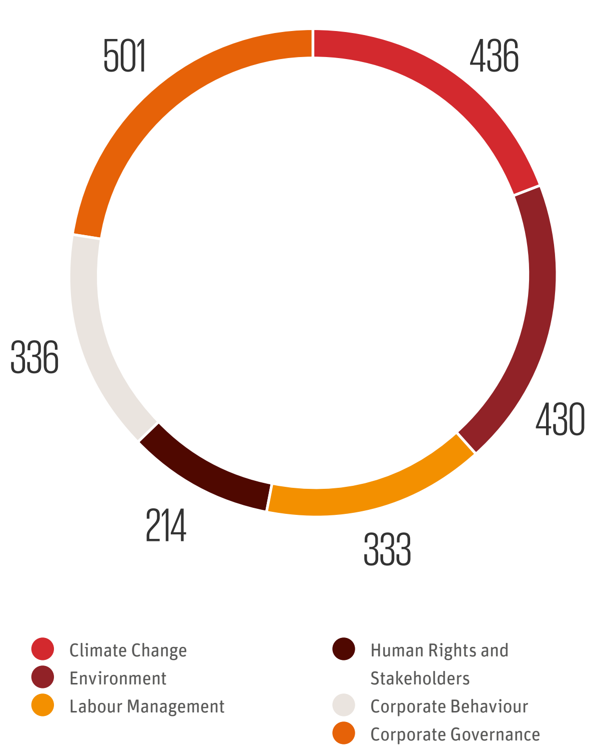
- Board Quality and Effectiveness
- Strategy, Purpose, and Financial Resilience
- Incentives Aligned with Value Creation
- Climate and Natural Capital
- Company Impacts on People

3.5 **Overview of engagement activity by appointed investment manager** continued

ENGAGEMENT ACTIVITY WITH COMPANIES HELD IN SCOTTISH WIDOWS PORTFOLIO: CORE TIER 1 MANAGERS CONTINUED

Engagement Activity Breakdown by Theme by Manager

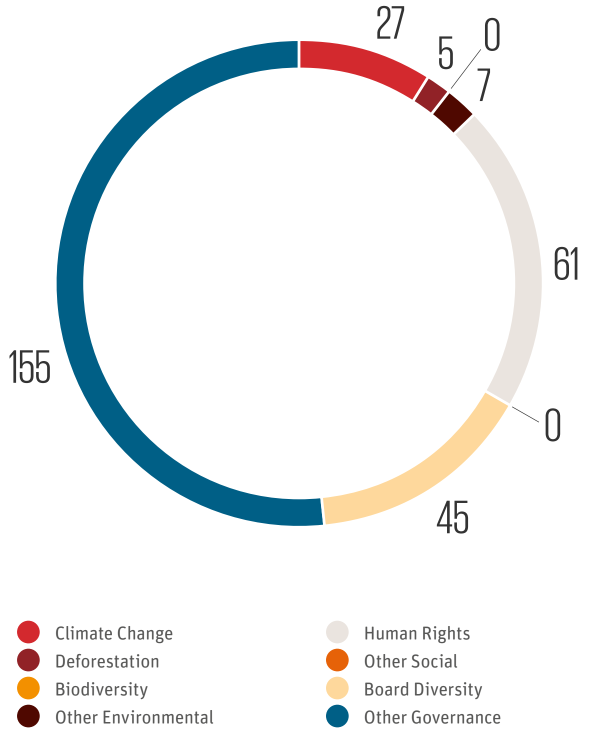
Abrdn



Abrdn Top 5 Engagement themes for 2022

- Corporate Governance
- Environment
- Climate
- Labour Management
- Corporate Behaviour

Hermes*



* Hermes only hold one singular fund for Scottish Widows with a smaller AUM than our other Asset Managers.

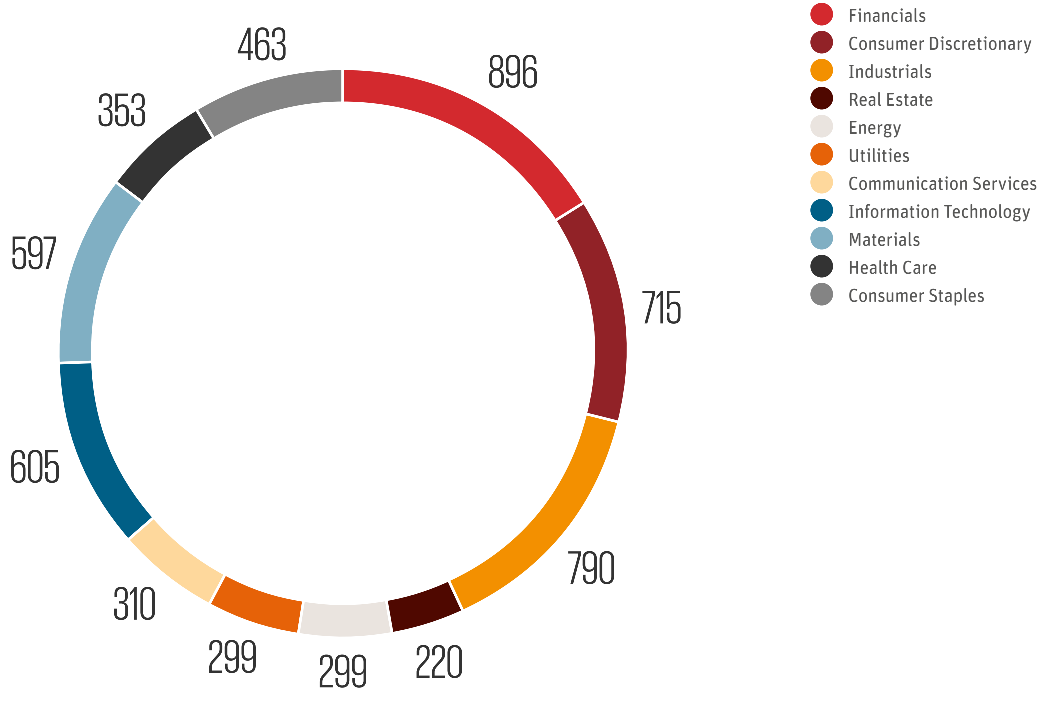
Hermes Top 5 Engagement themes for 2022

- Climate Change
- Executive Remuneration
- Board Diversity
- Human Rights
- Shareholder Protection and Rights

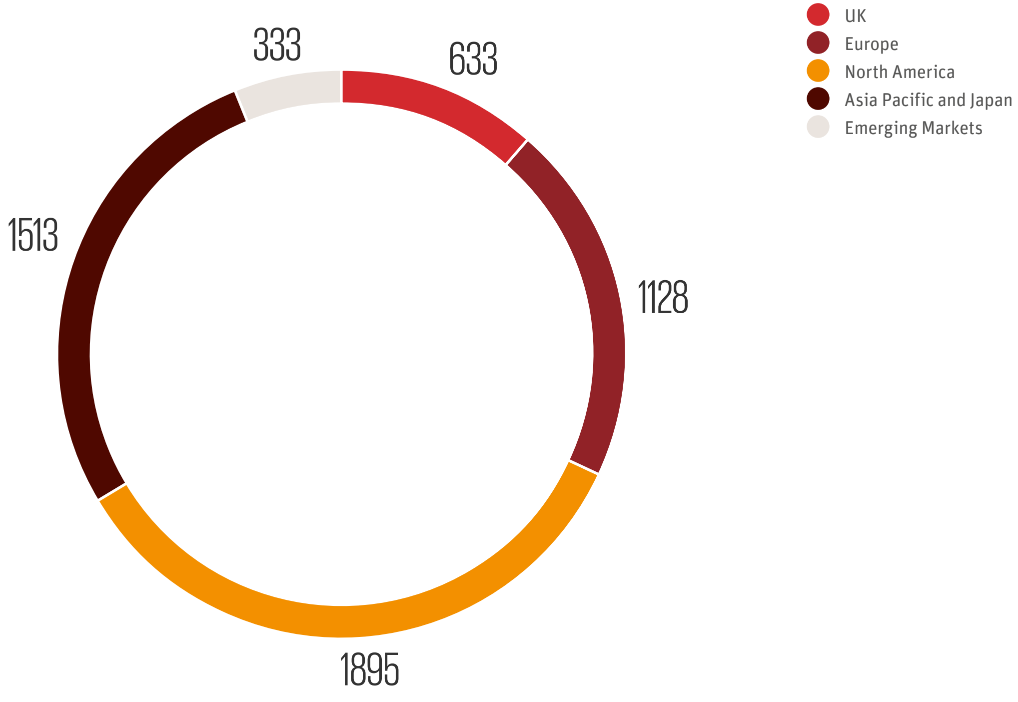
3.5 Overview of engagement activity by appointed investment manager continued

COMBINED TIER 1 MANAGERS BREAKDOWN OF ENGAGEMENT ACTIVITY BY REGION AND SECTOR*

Tier 1: Engagements by Sector (SW holdings)



Tier 1: Engagements by Region (SW holdings)



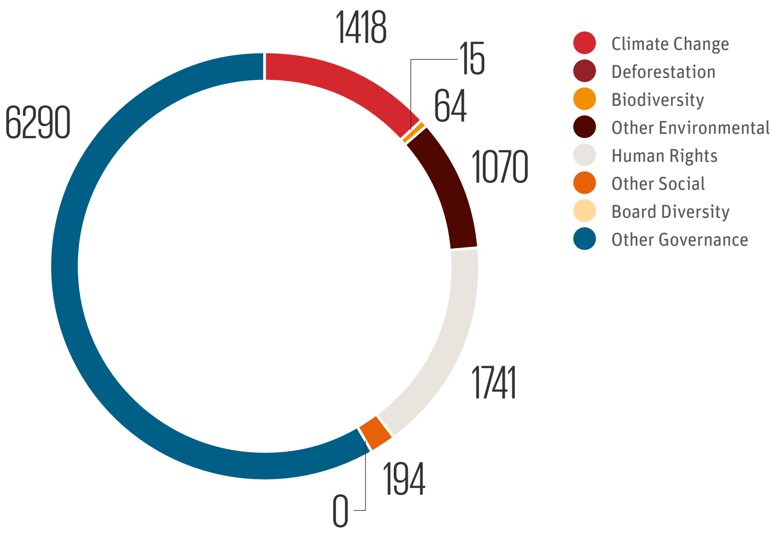
* These Regional and GICS Sector statistics relate to companies held in Scottish Widows portfolios managed by Abrdn and Schroders. Data is provided by the manager based on specific data request made by Scottish Widows on the funds covered in our regular Stewardship governance meetings. Some data presented may not be fully comparable owing to managers differing internal definitions, tagging and data management systems, but have been collated here, to the best possibility, to be fit for this reporting purposes.

3.5 **Overview of engagement activity by appointed investment manager** continued

ENGAGEMENT ACTIVITY WITH COMPANIES HELD IN SCOTTISH WIDOWS PORTFOLIO: CORE TIER 2 MANAGERS

Engagement Activity Breakdown by Theme by Manager

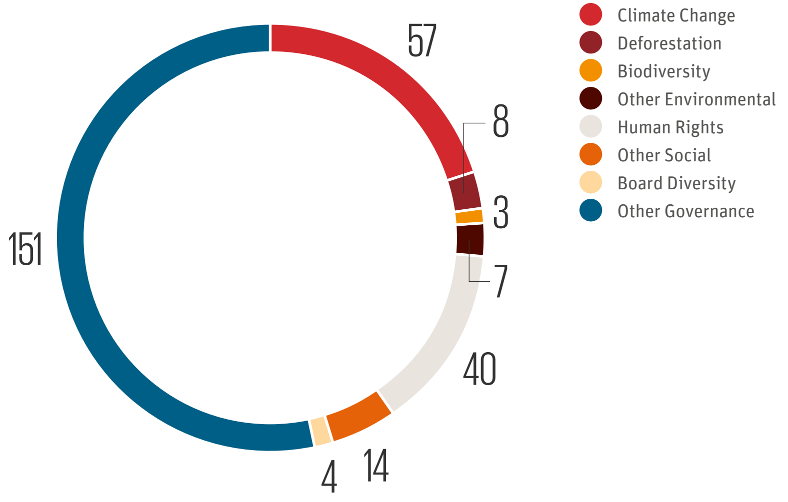
BlackRock



BlackRock Top 5 Engagement Themes

- Board Quality and Effectiveness
- Strategy, Purpose, and Financial Resilience
- Incentives Aligned with Value Creation
- Climate and Natural Capital
- Company Impacts on People

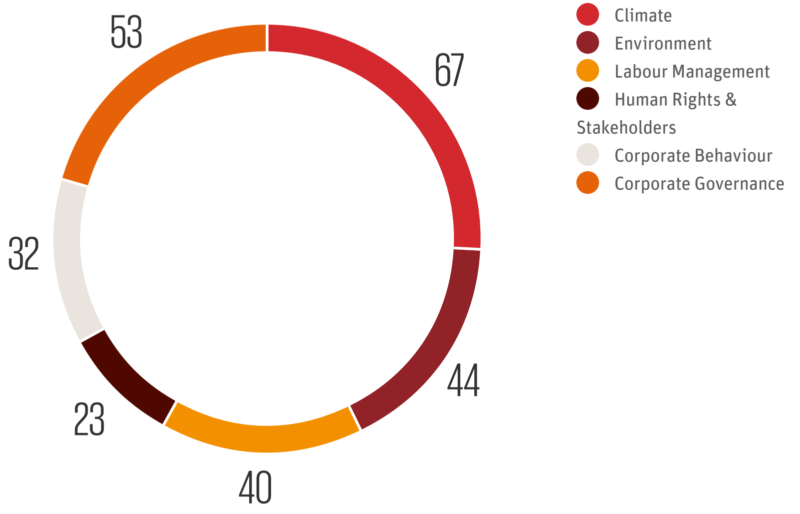
SSgA



SSgA Top 5 Engagement Themes

- Independent Board Leadership
- Climate Change
- Diversity
- Human Capital Management
- Executive Compensation

Abrdn



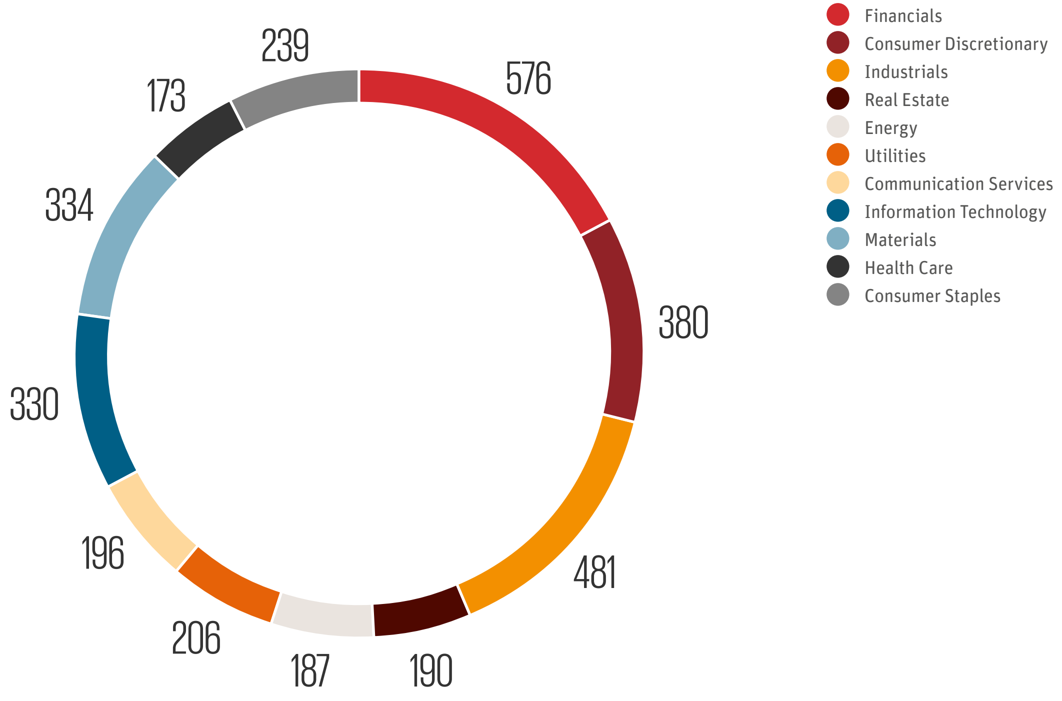
Abrdn Top 5 Engagement themes for 2022

- Corporate Governance
- Environment
- Climate
- Labour Management
- Corporate Behaviour

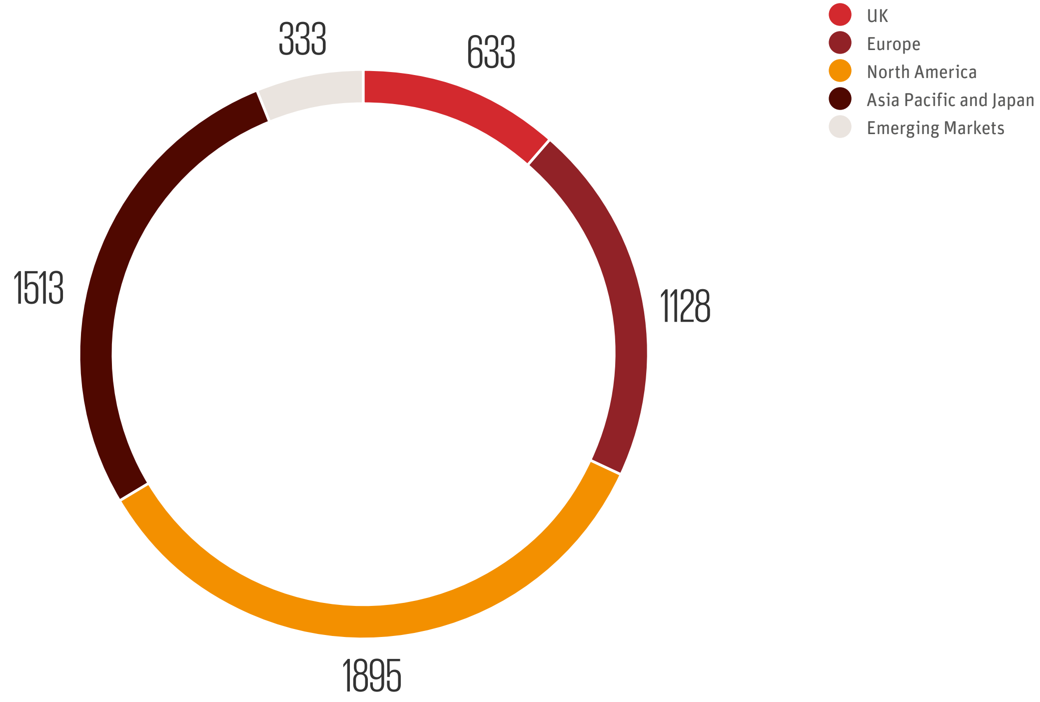
3.5 Overview of engagement activity by appointed investment manager continued

COMBINED TIER 2 MANAGERS BREAKDOWN OF ENGAGEMENT ACTIVITY BY REGION AND SECTOR*

Tier 2: Engagements by Sector (SW holdings)



Tier 2: Engagements by Region (SW holdings)



* These Regional and GICS Sector statistics relate to companies held in Scottish Widows portfolios managed by Schroders, BlackRock, and to a lesser extent Abrdn and Hermes. Data is provided by the manager based on specific data request made by Scottish Widows on the funds covered in our regular Stewardship governance meetings. Some data presented may not be fully comparable owing to managers differing internal definitions, tagging and data management systems, but have been collated here, to the best possibility, to be fit for this reporting purposes. The combination of manager data results in double count when the managers have engaged with the same company on identical themes.

3.5 Overview of engagement activity by appointed investment manager continued

CASE STUDIES OF ENGAGEMENT ACTIVITY BY OUR DELEGATED MANAGERS ENCOMPASSING EQUITY, FIXED INCOME AND PROPERTY*

Schroders

Case study

NORTH AMERICAN BANK – EMISSIONS TARGETS

Schroders supported an Institutional Investors Group on Climate Change (IIGCC) initiative asking all European CA100+ companies that had not yet committed to undertake and publish a review of their climate lobbying policies and activities to deliver on what is set out in the CA100+ benchmark**.

In 2022, Schroders wrote a letter to a North American bank, on behalf of collaborators in the initiative, as a follow up to discussion to the initial 2021 engagement setting out their net zero expectations. In 2021, it had urged the bank to develop interim science-based targets for its Scope 3 emissions relating to financing activities, and to strengthen its fossil fuel lending and underwriting policies. The 2022 letter was followed by a call with the bank where they gave an update on their progression in setting out Scope 3 financed emission targets. Despite their progress, Schroder's used the call to further urge for stronger fossil fuel policies and financed emission targets.

Ahead of the banks AGM, Schroders met with them once again to understand their progress which helped to inform a few upcoming votes. Off the back of the AGM, Schroders held a meeting with the bank to reflect on the AGM, the votes, and to discuss their progress providing European market practice examples.

As a result of the consistent engagement, the bank has made encouraging progress on net zero and Schroders will continue to urge the company for further action in the future.

Case study

UK HOSPITALITY COMPANY – MODERN SLAVERY RISKS GOVERNANCE

In 2022, Schroders engaged with a UK hospitality company in March 2022 as part of an investor-led project to identify modern slavery risks in investee companies called 'Find It, Fix It, Prevent It'. The aim was to encourage the company to improve governance and policies to mitigate the risk, and report on modern slavery in line with best practice.

Schroders raised concerns that:
- The company does not disclose stakeholder engagement processes or outcomes in its modern slavery statement.
- There was a lack of outcome-focussed reporting.

Schroders provided recommendations as to how these policies could be improved. As a result, the company issued a 'slavery statement' in 2022 which incorporated a number of the suggestions. However, the engagement also highlighted additional social issues which encouraged escalated engagement beyond the scope of the 'Find It, Fix It, Prevent It' project.

Schroders followed up seeking clarifications around purchasing practices and why supply chain risk assessments have not been extended to German and Middle Eastern operations. As a result, the company provided a more detailed explanation of its modern slavery policies including a case study reflecting how it dealt with a forced labour incident in its supply chain.

The result of the engagement was the company's improved slavery statements and increased confidence that there is no modern slavery in the company's supply chain.

* Names of the companies have been disclosed where our Delegated Managers have disclosed them.

** The benchmark presents key measures of corporate progress on climate transition and the move to achieve net zero emissions by 2050 or sooner. Net Zero Company Benchmark | Climate Action 100+

3.5 Overview of engagement activity by appointed investment manager continued

CASE STUDIES OF ENGAGEMENT ACTIVITY BY OUR DELEGATED MANAGERS ENCOMPASSING EQUITY, FIXED INCOME AND PROPERTY

Schroders continued

Case study

PRI- SOVEREIGN CLIMATE CHANGE

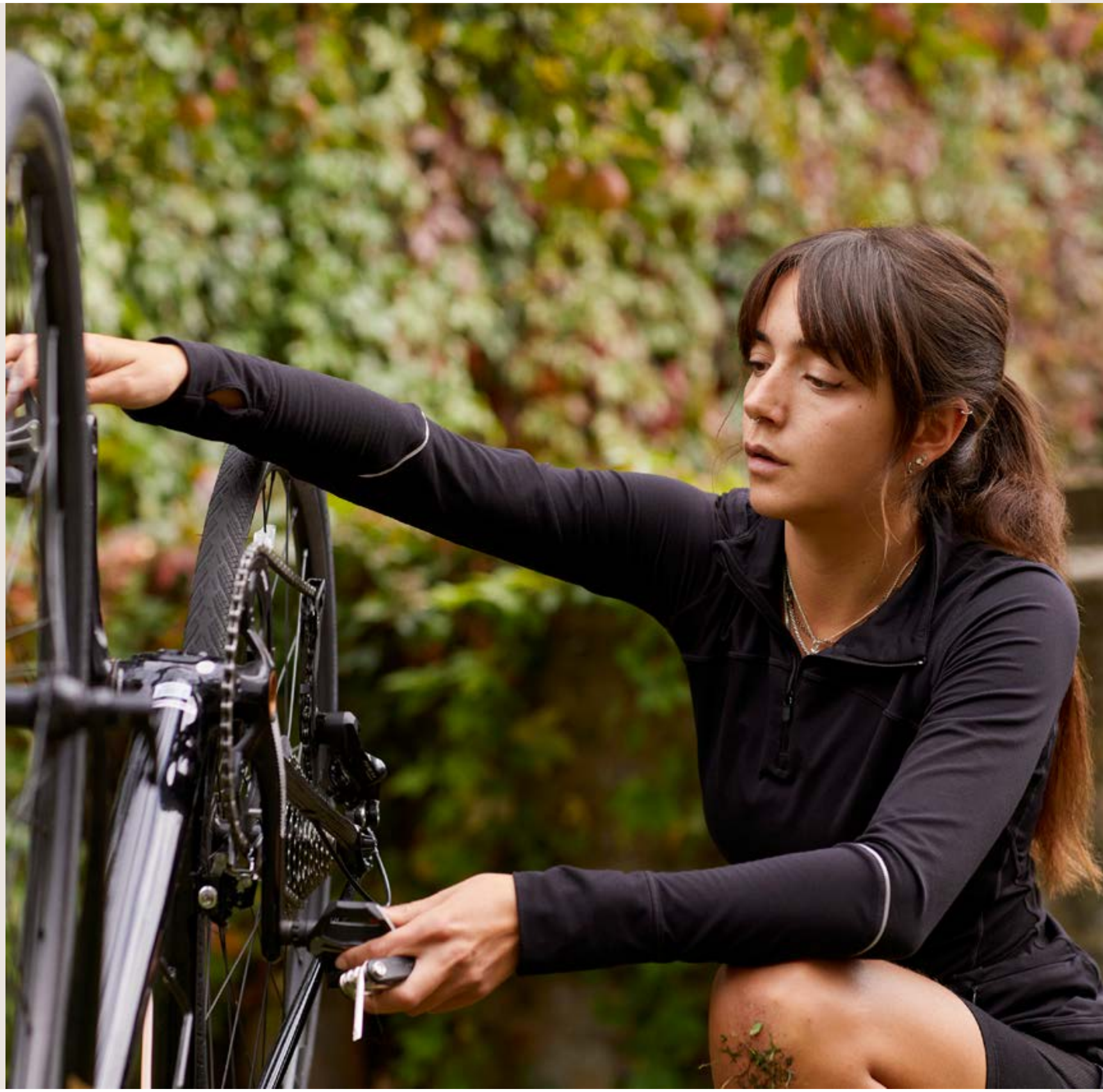
In 2022, Schroders joined the Principles for Responsible Investing (PRI) sovereign engagement programme. This programme aimed to focused on supporting governments' net zero transition plans. As part of this work, the programme engaged with the Australian government on climate policy action, following the introduction of the Climate Change Act. The engagement considered several official policies and documents, including:

- The Climate Change Act;
- 2022 Emission Projections; and
- The First Annual Climate Statement.

This engagement involved several initial engagements with the Australian Office of Financial Management and the Treasury in 2022, and plans to extend the engagement to other government agencies and departments in the future.
This includes:

- Department of Climate Change, Energy, the Environment and Water;
- Climate Change Authority; and
- Reserve Bank of Australia.

Schroders will continue as part of this collaborative engagement through the PRI working group, to encourage stronger policy action in Australia and in other countries going forward.



3.5 Overview of engagement activity by appointed investment manager continued

CASE STUDIES OF ENGAGEMENT ACTIVITY BY OUR DELEGATED MANAGERS ENCOMPASSING EQUITY, FIXED INCOME AND PROPERTY

BlackRock

Case study

IMPROVING NATURE-RELATED DISCLOSURES IN APAC

In 2022, BlackRock engaged with the Budweiser Brewing Company APAC off the back of extreme droughts in China. Due to Budweiser's highly water-intensive operations, BlackRock feared that these weather events could impact their production, and so looked to understand their approach to water-risk management, including the board oversight of material sustainability-related risks and opportunities.

At the time of BlackRock' initial engagement, Budweiser had produced disclosures on their water impact and dependencies, their incident prevention efforts arising from droughts, and their efforts to reduce the negative impacts to communities around their operations. Although it had not completely aligned their reporting to the TCFD framework, it had expressed an interest to do so.

As a result of the BlackRock engagement, Budweiser APAC's 2022 sustainability report was aligned with the TCFD framework. BlackRock was encouraged by Budweiser's' disclosures and will continue to monitor progress against the TCFD framework.

Case study

SIME DARBY PLANTATION – HUMAN RIGHTS

In 2020, Sime Darby Plantation (SDP), a Malaysian palm oil producer, received a Withhold Release Order (WRO) from the United States Customs and Border Protection (CBP) regarding allegations of forced labour in the supply chain. In January 2022, CBP investigations found sufficient information to support that SDP and its subsidiaries were using forced labour.

In the last two years, BlackRock conducted nine engagements with members of SDP's management team and Board on a range of issues in the company's Malaysian palm oil operations, including forced labour allegations. As a result, SDP has introduced several improvements:

- SDP has made constructive improvements to its worker policies, including placing a cap on overtime and consecutive days worked, establishing an annual budget allocated towards improving and maintaining worker housing, reimbursing recruitment fees that may have been paid by current and eligible former workers to secure employment, and enlisted the help of migrant worker rights specialists to enhance their Migrant Worker Responsible Recruitment Procedure. The company has also established a Social Welfare and Services (SWS) department responsible for overseeing the implementation of wellbeing and safety policies and procedures.

In addition, SDP submitted a comprehensive report to the CBP containing a detailed assessment of SDP's operations mapped against the International Labour Organisation's (ILO) forced labour indicators, containing in-depth descriptions of improved governance structures and systems with supporting evidence.

In early 2023, the CBP announced that the finding on SDP has been adjusted.

3.5 Overview of engagement activity by appointed investment manager continued

CASE STUDIES OF ENGAGEMENT ACTIVITY BY OUR DELEGATED CORE TIER 1 MANAGERS ENCOMPASSING EQUITY, FIXED INCOME AND PROPERTY

Abrdn

Case study

SIRIUS REAL ESTATE – CLIMATE TARGETS

In July 2022, Abrdn discussed with Sirius, a large property company investing in German and UK business parks, its net zero plans and targets, as the company was considered to be lagging its peers in certain aspects of decarbonisation. To support Sirius in setting targets, Abrdn shared industry examples of best practices for climate reporting and target setting. It encouraged Sirius to use the industry best practice as a guide when disclosing data and full-year results.

As a result of the engagement, Sirius showed progress with regards to benchmarking and setting net zero Scope 1 and 2 targets in 2022. However, due to the nature of its business park estate, reducing emissions across Scope 1 – 3 may be more challenging than other property landlords.

Going forward, Abrdn will continue to support Sirius in both setting new targets and monitoring performance in reducing emissions in line with these targets.

Case study

ENEL – NET ZERO DISCLOSURES

During 2022, Abrdn worked in collaboration with other institutional investors to lead two engagements with ENEL, an Italian multinational manufacturer and distributor of electricity and gas, as part of the Climate Action 100+ (CA100+) initiative. The key objective was to seek alignment of ENEL's disclosures to the Net Zero Benchmark, which was launched by CA100+ in March 2021. The Benchmark calls for robust and comparable information on how companies are realigning their business strategies and operations with the goals of the Paris Agreement. It acts as the foundation for investors engaging with companies through CA100+.

The investors first engaged ENEL in April 2022 when the company provided important updates on its climate strategy. This included its new long term targets related to Scope 1 emissions, new 2030 gas targets for Scope 3 emissions, its progress on disclosing how capital expenditure is aligned to the Paris Agreement and its work to improve disclosure on lobbying. The investors made follow up requests of the company, including points on climate governance on the board, climate lobbying disclosure, climate metrics within executive remuneration and disclosure related to progress in reducing Scope 3 emissions.

As a result of the collaborative engagement, in November 2022, ENEL became the first, and only, company to fully align its corporate disclosures with the CA100+ Net Zero Company Benchmark. Additionally, Enel has committed to decarbonising in line with a 1.5°C pathway and aims to reach net zero emissions by 2040.

Abrdn will continue to monitor progress against the requests that they made through their engagement.

Case study

TESCO PLC – LABOUR MANAGEMENT AND CLIMATE CHANGE

Abrdn engaged with Tesco, a leading British multinational groceries and general merchandise retailer, to understand how it is balancing employee rates of pay with the cost of living crisis and how that impacts customers and inflationary concerns. This was part of a wider British Retail Consortium (BRC) engagement programme with a number of large UK supermarkets to discuss efforts the sector was making to ensure employees were being paid the real living wage.

Abrdn held a call with Tesco, where they requested that Tesco increase their London hourly wage in line with the London real living wage and encouraged the firm to extend the base pay to subsidiaries and agency workers.

As a result of Abrdn's engagement, Tesco increased its London hourly rate only a month after their call to the real living wage.

3.5 Overview of engagement activity by appointed investment manager continued

CASE STUDIES OF ENGAGEMENT ACTIVITY BY OUR DELEGATED MANAGERS ENCOMPASSING EQUITY, FIXED INCOME AND PROPERTY

State Street

Case study

ROLLS-ROYCE – CLIMATE TRANSITION DISCLOSURE

With other CA100+ members, State Street engaged with Rolls-Royce Holdings, which specialises in the design and manufacture of engines for the aeronautics, marine, and energy sectors, throughout 2021 and 2022. This initially focused on the need for more disclosure of the company's approach to climate transition strategy which resulted in, Rolls-Royce releasing a report which included:

- Defining a science-based target to reduce by 35% the lifetime emissions of newly sold products by 2030,
- Re-assigning 75% of research and development (R&D) expenditure to lower carbon technologies by 2025, and making all commercial aero engines compatible with 100% sustainable aviation fuels by 2023.

In 2022, investors, including State Street, requested that Rolls-Royce undertook gap analysis exercises to identify whether there were any conflicts in its position on climate-related areas with the positions and activities of its industry groups.

State Street continues to engage with the company on aligning its position on climate change with the industry group.

Case study

CONOCOPHILLIPS – GHG EMISSIONS

In Q2 2021, State Street engaged with ConocoPhillips, a US multinational corporation which develops and produces crude oil and natural gas globally, on its approach to managing GHG emissions, including Scope 3 and methane emissions. This was part of a series of targeted engagements with investee companies in the oil and gas industry on methane usage as it represents one of the largest contributors to global methane emissions.
Discussions with ConocoPhillips included:

- Opportunities to enhance methane data quality; and
- Measurement-based reporting, including joining the Oil and Gas Methane Partnership (OGMP) 2.0, a multi-stakeholder initiative launched by United Nations Environment Programme (UNEP) and the Climate and Clean Air Coalition.

OGMP 2.0 provides a comprehensive reporting framework to improve the transparency and quality of methane emissions disclosure in the oil and gas industry. In Q3 2022, State Street conducted a follow-up engagement to discuss ConocoPhillips' methane detection, monitoring and reduction efforts in further detail.

As a result, the company formally joined OGMP 2.0 and committed to reporting methane emissions from both operated and non-operated assets and incorporated source-level and site-level measurements in line with the OGMP's guidance.
The company also set a new medium-term target to achieve a near-zero methane emissions intensity by 2030. State Street will continue to engage with the company on its methane emissions management and reporting efforts.

3.5 **Overview of engagement activity by appointed investment manager** continued

CASE STUDIES OF ENGAGEMENT ACTIVITY BY OUR DELEGATED MANAGERS WITH INDUSTRY WIDE INITIATIVES AND PUBLIC POLICY

Case study

Schroders

Nature, Biodiversity and Deforestation

Task Force on Nature-related Financial Disclosures (TNFD)

Nature, biodiversity and deforestation are gaining ever increasing focus in Financial Services. Global cooperative action to stop and reverse ecosystem destruction needs to be scaled immediately. As a global investment manager, Schroders has a responsibility to mitigate the risks in the portfolios it manages on behalf of clients. In November 2022, Schroders released its Group Nature and Biodiversity Position Statement, which sets out the group's position on nature and biodiversity covering both its investments and operations. As part of Schroder's commitment to Nature, biodiversity and deforestation, they have engaged with various market and policy initiatives.

The TNFD is developing a risk management and disclosure framework that helps organisations to assess, report and act on their nature-related risks. This aims to support a shift in global financial flows away from negative nature impact and toward nature-positive outcomes. The finalised TNFD guidance is set to launch in late 2023 and as a member of the TNFD Forum*, Schroder's had the opportunity to support a pilot.

In 2022, Global Canopy kicked-off a TNFD supported pilot on Palm Oil in Singapore. The main aim of the pilot was to gather early insights into current practices used in the assessment, measurement and disclosure of nature-related risks and opportunities related to palm oil, as well as common barriers and challenges experienced during the process. Schroders were actively involved in this pilot and contributed through workshops, proposal reviews, and sharing learned insights.

Deforestation

Additionally, Schroders is engaging with other market initiatives on nature and biodiversity and has made numerous commitments in line with its memberships:

Finance for Biodiversity Pledge

In line with the Finance for Biodiversity Pledge, Schroder's have committed to collaborate and share knowledge across the industry on nature and biodiversity, engaging with companies to encourage best practice in order to reduce the impact on nature. They aim to assess the impact that their financing activities have on nature using and set targets to reduce their impact, including decarbonisation and deforestation. In addition, they ensure transparency by reporting on their impact and management of nature risks in line with emerging disclosure guidance.

Natural Capital Investment Alliance (NCIA)

Schroders have committed to develop investment strategies to support greater investment in natural capital protection and regeneration.

United Nations Framework Convention on Climate Change (UNFCCC)

Schroders have committed to using best efforts to eliminate forest-risk agricultural commodity-driven deforestation activities at the companies in our investment portfolios and in their financing activities by 2025.

* A global multi-disciplinary consultative group of institutional supporters

3.5 Overview of engagement activity by appointed investment manager continued

CASE STUDIES OF ENGAGEMENT ACTIVITY BY OUR DELEGATED MANAGERS WITH INDUSTRY WIDE INITIATIVES AND PUBLIC POLICY CONTINUED

Case study

BlackRock

Recommendations to the US Securities and Exchange Commission (SEC) on proposed rule on climate-related disclosures

In June 2022, BlackRock supported the SEC's goal of implementing a framework for public companies to provide investors with more comparable and consistent climate-related disclosures. This was part of the Commission's proposed rule of climate-related disclosures. BlackRock also noted its concern that certain elements of the proposal, which go beyond or differ from the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD), will undermine the effectiveness of the Commission's overarching goal of ensuring companies provide reliable, comparable, and consistent climate-related information to investors.

In offering support for the Commission's initial efforts to mandate climate-related disclosures for investors and to offer much-needed guidance to companies, BlackRock submitted recommendations which allow the final rules to address these concerns.

Furthermore, BlackRock urged the Commission to consider ways to encourage greater transparency on climate-related considerations from US private companies. With the changes it outlined, BlackRock believes the SEC's proposal would create a robust framework for climate-related disclosures and help set a global benchmark for efficient, informed capital markets.

Case study

State Street

Sustainable Markets Initiative (SMI) – Asset Manager and Asset Owner Task Force

As governments across the globe increasingly identify, there is urgent need to scale up private sector investments in developing and emerging markets in order to reach the investment and capacity needed to meet the Paris climate goals and the UN Sustainable Development Goals. As such, State Street Global Advisors focuses policy contribution through established international fora.

For example, State Street's CEO leads the Asset Owner and Asset Manager Task Force under the Sustainable Markets Initiative (SMI) and is supported by their senior State Street Global Advisors representation. The Task Force was launched at the World Economic Forum in January 2020 by HRH King Charles III and is aimed at facilitating the flow of private capital needed to finance the net-zero transition through two levers:

- Capital already invested in companies; and
- Fresh capital investments directed at climate mitigation and adaptation projects.

In this capacity, State Street have attended COP26 and COP27 as well as a number of high-level business receptions with global leaders in order to advance common sustainability goals. In addition, State Street's Global Head of ESG has been working with multi-development banks under the auspices of the SMI to consider blended finance i.e. where private and public capital is co-invested – a means of helping to accelerate the net zero transition. The work of the SMI is complementary to other global initiatives that State Street Global Advisors contributes, including the Net Zero Investment Management Alliance.

3.6 VOTING AND VOTING RECORDS

Voting is an essential part of being active owners of our investments. It can be used as an escalation of engagement activity, to express support for an ongoing strategy and to ensure suitable governance is in place to deliver on ESG factors.

Through 2021 we worked on developing our own Voting Guidelines which were published at the start of 2022. Our voting activity is largely delegated to our appointed investment managers. We have been working on striking a balance between oversight of these managers' voting activity and playing a more significant role ourselves. It has been a journey, both developing our own guidelines and working to implement them, alongside the proxy voting policy we have established for pooled funds we invest in, with a range of asset managers across our investment types.

Voting approach

Our appointed investment managers use our shareholding to cast votes on company resolutions. We use our Voting Guidelines as an 'expression of wish' with asset managers to inform them of our preferences in a bid to influence their voting behaviour. But we are not instructing them to vote in a specific way. This was one of the recommendations by the Taskforce on Pension Scheme Voting Implementation, of which we were members and whose work has now concluded.

Other than directing certain significant votes, Scottish Widows' intention is to use these Guidelines to monitor and, where appropriate, challenge our key appointed managers' voting policies and practices to influence and encourage them to make their own in-house policies more progressive. This should benefit the investment industry and wider market.

We meet regularly with our core appointed investment managers to discuss upcoming votes and how we would like our votes to be cast. We also review their voting records on a regular basis. Additionally, we try to influence managers to join shareholder resolutions where they are aligned to our stewardship objectives.

Having a bigger role on voting

During our journey we have increasingly felt that oversight alone is not enough. We often hold shares in companies that feature in the investment portfolios of several funds managed by various investment managers. So a key consideration for us is that we do not cancel out our votes as a result of investment managers voting in opposing directions. In 2022, we began work to establish processes to enable us to direct votes and better oversee the voting of our appointed investment managers. The approach continues to evolve as market expectations change and different managers adapt to asset owners taking a bigger role.

We have now established a processes for asset owners to direct votes in pooled funds, using a policy closest to our own expectations, without extensive inhouse resource.

With our appointed active investment manager, we have been trialling the ability to override votes. We are working with the proxy advice company Minerva Analytics to which we provide our top 300 holdings. Minerva Analytics then provides all upcoming AGM information and research for those companies. Throughout the AGM season, we review upcoming ESG-related votes. If the vote topic is covered by our Voting Guidelines, and we feel we have suitable expertise in-house, we can decide to send an override instruction to the manager to ensure the vote gets cast how we wish. We initiated this process with Minerva Analytics in early 2022 and put our process into practice at the end of April 2022.

3.6 Voting and voting records continued

Case study

SAINSBURYS SHAREHOLDER RESOLUTION ON REAL LIVING WAGE ACCREDITATION

We directed our vote in support of a shareholder resolution for J Sainsbury Plc (Sainsbury's) to become a Living Wage accredited employer via Schroders at the 2022. The resolution filed at Sainsbury's represented the first time a UK publicly-listed company was formally requested via a shareholder proposal to become a Living Wage accredited employer.

In this particular case, though Sainsbury had increased wages for its outer London employees to cross the Living Wage (LW), it still excluded a small percentage (~2%) of its workforce comprising of contractual workers, the ones most vulnerable and lowest paid. Getting the accreditation would mean that all workers would earn enough to meet the cost of living in the future, per the updates made to the Living Wage. The accreditation would allow Sainsburys around three years to implement changes to wages in accordance with the real Living Wage.

We supported the resolution under our priority stewardship theme of Human Rights, that particularly articulates Fair/ Decent/ Living Wage and aligns with our Voting Guidelines. We expect companies to consider societal concerns about income inequality, particularly when setting executive pay levels, and are supportive of the adoption of a living wage to employees. Furthermore, addressing 'inequality' via paying a real living wage is critical for investors who are focused on long-term value creation, not only managing system-level risk, but also the company level risk. We believe it is imperative that 'inequality' is put on an equal footing with 'climate risk', where organisations sign up to external accreditations and validations to maintain and demonstrate progress. The Living Wage is an attainable benchmark for employers committed to ensuring their workforce earns a wage that meets the real cost of essential goods and services, overseen by a group including employers, trade unions, civil society, and independent experts. There is research to show that those who have become accredited have received a general boost in reputation and employee productivity, reduced staff turnover and associated costs, which supports the organisations' future sustainability and better financial performance. Living Wage-accreditation would give Sainsbury's reputational and competitive benefits by taking a leadership role in this area. We would also expect other major retailers to follow either voluntarily or as a result of shareholder engagement.

2022 was a year where we were testing the process and beginning to build our internal capabilities, within the constraints of being an asset owner, in actively taking voting decisions. Where we researched votes but decided not to take any action, this was for a range of reasons, such as our lack of detailed knowledge of the company, capacity at the time of researching the vote to further engage, ramifications of some of the geo-political disruptions, or if a vote was not directly related to one of our stated stewardship priorities.

As this was a developing process, sometimes we were able to have a conversation with our appointed investment manager before the vote but other times the timeline was too short so we caught up afterwards. We were pleased that the manager was able to share what its voting intention was before the vote, which gave us confidence in the process. In some cases, the research process resulted in a clear view from the team, and we went straight to 'directing' the vote. In most circumstances, we were satisfied with the rationale provided by the manager when enquiring on vote decisions. While we will never bring full scale voting in-house, we are envisaging directing more votes during the 2023 season as we build our internal capability and experience.

Below is a list of votes which were highlighted to us by our proxy advice agency, Minerva Analytics, as related to our material holdings and our priority themes. We also selected votes which we wanted to learn and understand more. All votes were 'researched' by us, looking at Minerva's guidance and other relevant materials such as news articles of the company's reporting. In addition, we discussed some votes with our asset managers, 'enquire' and 'directed' some votes.

3.6 Voting and voting records continued

Voting Record

Company	AGM date	Action	Topic	Resolution number	Resolution Detail
Bank of America	4/26/2022	Enquire	Climate	6	To request that the Board adopt a policy to cease financing new fossil fuel supplies
Glencore	4/28/2022	Research	Climate	13	To approve the Company's 2021 Climate Progress Report
Credit Suisse	4/29/2022	Enquire	Climate	9	To request that the Articles be amended regarding climate change strategy and disclosures
Standard Chartered	5/4/2022	Enquire	Climate	31	To approve the Company's net zero by 2050 pathway
Standard Chartered	5/4/2022	Enquire	Climate	32	To request the Board to implement a revised net-zero strategy and mandate with annually reporting
Barclays	5/4/2022	Enquire	Climate	26	To approve the company's Climate Strategy, Targets and Progress for 2022
UPS	5/5/2022	Enquire	Climate	7	To request the Board to require adoption of independently verified science-based greenhouse gas emissions reduction targets
UPS	5/5/2022	Enquire	Climate	8	To request the Board to prepare a report on balancing climate measures and financial returns
JPMorgan	5/17/2022	Enquire	Climate	9	To request the Board to prepare a report on setting absolute contraction targets for the greenhouse gas emissions
Home Depot	5/19/2022	Directed – For	Diversity	8	To request that the Board prepare a report on steps taken towards greater racial and gender equity on the board
Home Depot	5/19/2022	Directed – For	Diversity	9	To request that the Board prepare a Racial Equity Audit to shareholders
Shell	5/24/2022	Enquire	Climate	20	To approve the progress of the company's Energy Transition Progress
Shell	5/24/2022	Enquire	Climate	21	To request that the Company report to shareholders on the strategy and policies for reaching greenhouse gas emission targets
Total Energies	5/25/2022	Research	Climate	16	To approve the Sustainability and Climate progress report
Morgan Stanley	5/25/2022	Research	Climate	4	Shareholder proposal requesting adoption of a policy to cease financing new fossil fuel development
Amazon	5/25/2022	Research	Climate	5	To request the Board to report to shareholders on retirement plan options
Amazon	5/25/2022	Directed – For	Diversity	6	To request the Board to report to shareholders on gender/racial pay
Amazon	5/25/2022	Enquire	Biodiversity	8	To request the Board to report to shareholders on packaging materials
Amazon	5/25/2022	Enquire	Human rights	9	To request the Board to report to shareholders on warehouse working conditions

3.6 Voting and voting records continued

Voting Record continued

Company	AGM date	Action	Topic	Resolution number	Resolution Detail
Exxon Mobil	5/25/2022	Research	Climate	6	To request that the Board reduce emissions and hydrocarbon sales
Exxon Mobil	5/25/2022	Research	Climate	7	To request that the Board report to shareholders on low carbon business planning
Exxon Mobil	5/25/2022	Research	Climate	8	To request that the Board report on scenario analysis
Exxon Mobil	5/25/2022	Research	Biodiversity	9	To request that the Board report to shareholders on plastic production
Exxon Mobil	5/25/2022	Directed – For	Climate	10	To request the Board to prepare a report to shareholders on the Company's political donations
Wells Fargo	5/26/2022	Enquire	Diversity	7	To request that the Board reports to shareholders on Racial and Gender Board Diversity
Wells Fargo	5/26/2022	Enquire	Climate	9	To request the Board to adopt policies regarding Climate Change
Citigroup	5/26/2022	Enquire	Climate	8	To request the Board to adopt a policy to end new fossil fuel financing
Walmart	6/1/2022	Research	Human rights	5	To request the Board to Create a Pandemic Workforce Advisory Council
Walmart	6/1/2022	Enquire	Human rights	6	To request the Board to Report on Impacts of Reproductive Healthcare Legislation
Walmart	6/1/2022	Directed – For	Diversity	7	To request the Board to Report on Alignment of Racial Justice Goals and Starting Wages
Walmart	6/1/2022	Enquire	Diversity	8	To request the Board to Civil Rights and Non-Discrimination Audit
Walmart	6/1/2022	Enquire	Business ethics	10	To request the Board to prepare a report to shareholders on lobbying
Comcast	6/1/2022	Enquire	Diversity	5	To request the Board to perform independent racial equity audit
UnitedHealth Group Inc	6/6/2022	Enquire	Business ethics	5	To request the Board to prepare a report to shareholders on the Company's political donations
General Motors	6/13/2022	Directed – For	Governance	5	To request that the Board establish a policy of separating the roles of Chairperson and Chief Executive Officer
General Motors	6/13/2022	Enquire	Human rights	6	To request that the Board report on use of child labour in connection with electric vehicles
Sumitomo Mitsui Financial Group Inc	6/29/2022	Research	Climate	4	To amend the Articles of Incorporation in connection with greenhouse gas emission reduction targets
Sumitomo Mitsui Financial Group Inc	6/29/2022	Research	Climate	5	To amend the Articles of Incorporation in connection with financing consistent with the IEA's Net Zero Emissions Scenario

3.6 Voting and voting records continued

Voting Record continued

Company	AGM date	Action	Topic	Resolution number	Resolution Detail
J Sainsbury	7/7/2022	Override – For	Human rights	21	Proposal regarding the payment of the real Living Wage
National Grid plc	7/11/2022	Research	Climate	19	To adopt the Climate Transition Plan
SSE plc	7/21/2022	Research	Climate	21	To approve the report on the SSE's Net Zero Transition Report for the year ended 31 March 2022
United Utilities Group plc	7/22/2022	Research	Climate	16	The company's climate-related financial disclosures for 2022 be approved
JD Sports Fashion plc	7/22/2022	Enquire	Governance	2	To approve the report on the implementation of the remuneration policy for the year ended 29 January 2022
Linde plc	7/25/2022	Research	Governance	6	To request that the Board take steps to adopt a simple majority vote policy
Tesla Inc	8/4/2022	Enquire	Human rights	7	To request the Board to prepare a report to shareholders on Anti-Harassment and discrimination efforts
Tesla Inc	8/4/2022	Enquire	Diversity	8	To request the Board to prepare a report to shareholders on Board Diversity
Tesla Inc	8/4/2022	Enquire	Human rights	9	To request the Board to prepare a report to shareholders on Employee Arbitration
Tesla Inc	8/4/2022	Enquire	Governance	10	To request the Board to prepare a report to shareholders on lobbying
Tesla Inc	8/4/2022	Enquire	Human rights	11	Adoption of a freedom of association and collective bargaining policy
Tesla Inc	8/4/2022	Enquire	Human rights	12	To request the Board to prepare Additional reporting on child labour
Tesla Inc	8/4/2022	Enquire	Biodiversity	13	To request the Board to prepare Additional Reporting on water risk
Nike	9/9/2022	Enquire	Governance	3	Ratify PricewaterhouseCoopers LLP as Auditors
Nike	9/9/2022	Enquire	Human rights	5	Adopt a Policy on China Sourcing
Auto Trader Group plc	9/15/2022	Enquire	Governance	1	To adopt the report & accounts for the year ended 31 March 2022
Auto Trader Group plc	9/15/2022	Enquire	Governance	2	To approve the report on the implementation of the remuneration policy for the year ended 31 March 2022
Auto Trader Group plc	9/15/2022	Enquire	Governance	4	To re-elect as a director, Ed Williams
Auto Trader Group plc	9/15/2022	Enquire	Governance	13	To re-appoint as auditors, KPMG LLP

3.6 Voting and voting records continued

Voting Record continued

Company	AGM date	Action	Topic	Resolution number	Resolution Detail
FedEx Corp	9/19/2022	Enquire	Governance	1k	To re-elect as a director, Frederick Smith
FedEx Corp	9/19/2022	Enquire	Governance	1o	To re-elect as a director, Paul Walsh
FedEx Corp	9/19/2022	Enquire	Governance	3	To ratify the appointment of Ernst & Young LLP as auditors
FedEx Corp	9/19/2022	Enquire	Governance	4	To adopt the 2019 Omnibus Stock Incentive plan
FedEx Corp	9/19/2022	Enquire	Diversity	8	To request that the Board assess inclusion in the workplace
Games Workshop Group plc	9/21/2022	Enquire	Governance	1	To adopt the report & accounts for the year ended 29 May 2022
Games Workshop Group plc	9/21/2022	Enquire	Governance	4	To re-elect as a director, E O'Donnell
Games Workshop Group plc	9/21/2022	Enquire	Governance	8	To re-appoint as auditors, KPMG LLP
IG Group Holdings plc	9/21/2022	Enquire	Governance	1	To adopt the report & accounts for the year ended 31 May 2022
IG Group Holdings plc	9/21/2022	Enquire	Governance	2	To approve the remuneration report for the year ended 31 May 2022
IG Group Holdings plc	9/21/2022	Enquire	Governance	16	To re-appoint as auditors, PricewaterhouseCoopers LLP
Alibaba Group Holding Ltd	9/30/2022	Enquire	Governance	1.02	To elect as a director, Jerry Yang
Alibaba Group Holding Ltd	9/30/2022	Enquire	Governance	2	Ratify the appointment of PricewaterhouseCoopers as the independent registered public accounting firm of the Company
Diageo plc	10/6/2022	Enquire	Governance	17	To authorise the Company to make political donations to political parties and political organisations and to incur political expenditure
Cisco	12/8/2022	Research	Governance	1a	To re-elect as a director, Michele Burns
Cisco	12/8/2022	Research	Governance	1c	To re-elect as a director, Michael Capellas
Cisco	12/8/2022	Research	Governance	1d	To re-elect as a director, Mark Garrett
Cisco	12/8/2022	Research	Governance	1g	To re-elect as a director, Roderick McGeary

3.6 Voting and voting records continued

Voting Record continued

Company	AGM date	Action	Topic	Resolution number	Resolution Detail
Cisco	12/8/2022	Research	Governance	1i	To re-elect as a director, Charles Robbins
Cisco	12/8/2022	Research	Governance	2	To approve an advisory vote on the remuneration of the Company's named executive officers
Cisco	12/8/2022	Research	Governance	3	To ratify the appointment of PricewaterhouseCoopers LLP as auditors
Microsoft Corp	12/13/2022	Enquire	Board	1.02	To re-elect as a director, Hugh Johnston
Microsoft Corp	12/13/2022	Enquire	Board	1.04	To re-elect as a director, Satya Nadella
Microsoft Corp	12/13/2022	Enquire	Governance	2	To approve an advisory vote on the remuneration of the Company's named executive officers
Microsoft Corp	12/13/2022	Enquire	Governance	3	To ratify the appointment of Deloitte & Touche LLP as auditors
Microsoft Corp	12/13/2022	Enquire	Human rights	5	To request that the Board report to shareholders regarding hiring people with arrest or incarceration records
Microsoft Corp	12/13/2022	Enquire	Climate	6	To request that the Board report to shareholders regarding 401(k) retirement funds connection with climate change
Microsoft Corp	12/13/2022	Directed – For	Human rights	7	To request that the Board commission an independent report to assess whether governmental customer use of products can contribute to violations of privacy
Microsoft Corp	12/13/2022	Enquire	Human rights	8	To request that the Board issue an independent report regarding risks for being identified as a company involved in the development of weapons used by military
Microsoft Corp	12/13/2022	Enquire	Governance	9	To request that the Board issue a tax transparency report

3.6 Voting and voting records continued

Pooled fund voting

At the end of 2021, BlackRock announced it would enable pooled fund clients to vote their own shares through the adoption of a choice of ISS voting policies. This announcement was an industry first, as the asset manager industry has largely been reluctant to allow asset owners influence and control over voting. For detailed background and our role in helping to make this happen, please refer to our RI and Stewardship Report 2021*.

In 2021, we chose the ISS Socially Responsible Investment Policy**, which we felt was most closely aligned with our approach to voting and is progressive across a range of ESG factors, in addition to climate change. This policy was implemented for our passive mandated funds managed by BlackRock in April 2022 and for our eligible investments in BlackRock pooled funds in Sept 2022. At the end of 2022, after a close engagement with us over the year, State Street Global Advisors also announced a similar approach to BlackRock which we will be implementing through 2023. The announcement means we can have a significant proportion of our investment in pooled funds under the same ISS Socially Responsible Investment Policy and voted in a consistent manner.

The report monitoring the voting activity of our core managers, and covering our Top 300 holdings, is covered in detail later in the report. They highlighted that our own Voting Guidelines supporting most sustainability resolutions and the differences between our managers voting records. We were especially pleased to see the ISS SRI policy align closely with our Guidelines which evidence that it was the right choice for us from the off-the-shelf policies made available to us.

* 60694.pdf (scottishwidows.co.uk)

** In voting their shares, socially responsible institutional shareholders are concerned not only with sustainable economic returns to shareholders and good corporate governance but also with the ethical behaviour of corporations and the social and environmental impact of their actions.

As we get better our voting process, juggling the various policy options, directing votes and monitoring manager voting practices, we expect to understand the greater nuances and impacts of voting decisions made. We are mindful of the fact that by choosing a voting policy different from our managers this may risk delineating their engagement outcomes with the voting activities, but at this point it was more important to us that we voted consistently across a large portion of our investments and as closely aligned to our own Voting Guidelines as possible. Managers have a range of escalation strategies to choose from, if need be, and our voting choice will only help in improving outcomes from a company. We review our voting policy choice annually ahead of every AGM season, and should we feel that managers' in-house policies have progressed enough to be closer to our own expectations, we will consider reverting back to using their policies.

Oversight of our appointed investment managers voting activity

Manager Vote Monitoring Highlights

The period covered by this commentary is 1 January 2022 to 30 June 2022. We monitor Schroders, BlackRock and State Street Global Advisors voting activity in relation to the top 300 companies (the "monitored companies") we invest in which gives us a clear picture of how the managers are making use of voting rights and any challenges they face. The analysis examines meetings held by the monitored companies during the review period. In addition, we monitor the ISS SRI voting against BlackRock's in-house voting policy.

Our annual report assesses progress in terms of companies' ESG standards in relation to Scottish Widows' Voting Policy and investment managers' use of votes to highlight their ESG policy preferences to companies.

Vote monitoring is about understanding investment risk management and oversight of stewardship activities, not enforcing compliance with a policy. It allows for a comparison of fund managers, general shareholder voting behaviour, and governance expectations.

The analysis shows that:

- Our appointed investment managers in aggregate were more likely to oppose management by supporting a shareholder resolution than by opposing a management resolution. Fund managers voted against management recommendation on 43.81% of shareholder proposals and voted against management recommendation on 9.58% of resolutions proposed by management.
- ISS SRI, applied to our eligible BlackRock funds, and Schroders' voting polices were more supportive of shareholder proposals than BlackRock's and State Street's policies; with ISS SRI voting 'For' on 80.48% of shareholder proposals, Schroders 67.74%, State Street19.45% and BlackRock 11.37%. Most shareholder proposals concerned ESG factors, but also covered topics such as shareholder rights.
- ISS SRI voted against management recommendations on a higher proportion of corporate actions, board, political activity, and sustainability-related resolutions than the fund managers; opposing 29.55% of board-related resolutions compared to the to 5.09% (BlackRock), 6.20% (Schroders) and 8.80% (SSgA) Schroders voted against management recommendations on a higher proportion of audit & reporting, charitable activity, and remuneration-related resolutions than the other fund managers. Schroders opposed 10.32% of audit & reporting-related resolutions compared to the 0.20%(BlackRock), 0.81% (ISS SRI) and 0.41% ((SSgA) SSgA voted against management recommendations on a higher proportion of capital and shareholder rights-related resolutions than the other fund managers; opposing 37.07% of shareholder rights-related resolutions compared to the 2.39% (BlackRock), 14.90% (ISS SRI) and 13.61% (Schroders). BlackRock did not vote against management recommendations more often than the other fund managers in any resolution category and recorded the lowest level of overall dissent; of 4.67% compared to 22.08% (ISS SRI), 10.94% (Schroders) and 9.05% (SSgA).

BlackRock has informed us that its escalation strategy is more geared towards voting against directors where it has concerns about material ESG issues rather than supporting shareholder resolutions, which it claims can sometimes be overly prescriptive. The data from Minerva does not seem to evidence this approach and so we will continue to engage and challenge BlackRock to provide evidence of this approach working in practice.

The table below shows how often our appointed investment managers voted with management for director elections, so 'for' the resolution. All our managers opposed management on director elections more often than shareholders in general, but BlackRock supported directors more than the other asset managers.

Fund manager	Resolutions	Voted with mgt
BlackRock	2,202	95.58%
ISS SRI	2,190	68.99%
Schroders	1,680	94.14%
State Street	2,155	92.83%

This analysis is essential to back up our engagement with our asset managers. The support for shareholder resolutions demonstrates clear differences between the voting activity of the different managers and also the ISS SRI Policy. While we have found that BlackRock and State Street's engagement activity has improved, we believe they can still better use their voting to ensure measurable and timely positive outcomes from companies. This level of monitoring helps us make a clear case for continued improvements. We also anticipate highlighting the difference between the votes will encourage future voting in relation to the managers' pooled funds to be more in line with our own guidelines.

3.6 Voting and voting records continued

Sustainability-related Shareholder Proposals

The majority (89.47%) of sustainability resolutions were shareholder proposals, which generally asked companies to either improve their reporting of, or performance on, specified sustainability issues. Meaningful routine categorisation of these issues is challenging because the specific ask is defined by the proponent and could be about anything, from asking the company to close specific operations to requesting a one-off report on employee conditions. The large number of shareholder proposals, of varying quality, explains the high level of fund manager and general shareholder (including Scottish Widows) dissent in the category.

'Dissent', is the result of having added up all votes not supporting a management recommendation as a percentage of all votes cast ('Against' plus 'Abstain' votes where management recommended a 'For' vote and 'For' and 'Abstain' votes where management recommended 'Against').

Sustainability Resolution Sub-Categories

Resolution Sub-Category	Total Resolutions	SW Voting Guidelines Dissent	BlackRock in-house Voting Policy Dissent	ISS SRI Voting (applied in eligible BlackRock funds) Dissent	Schroders in-house Voting Policy Dissent	State Street Voting Policy Dissent	Average Dissent
Human Rights & Workforce	273	70.33%	23.29%	83.33%	74.55%	42.47%	26.88%
Environmental Practices	227	88.89%	10.00%	86.44%	67.35%	35.59%	22.11%
Ethical Business Practices	70	82.86%	0.00%	82.35%	58.82%	11.11%	11.48%
Other ESG	49	100.00%	0.00%	100.00%	90.00%	0.00%	23.00%
Sustainability Reporting	11	27.27%	0.00%	0.00%	0.00%	0.00%	0.64%

Additional thematic examples

The table right, further demonstrates the differences between our Voting Guidelines and Schroders voting versus that of our appointed passive investment managers, through specific company examples.

For the resolutions on political donations, both the ISS SRI and Schroders policies noted that it was helpful for investors to have further details on companies' political donations. Political donations are an important indicator of the relationship between political affiliations and company transparency and independence, which could pertain to ESG related factors, in addition to other issues. Transparent and consistent information about political donations is a core area of good governance and one of a host of minimum governance standards.

On climate lobbying and reporting on net zero, the ISS SRI policy and Schroders outline that while the current reporting from companies was welcome, additional reporting was needed given the importance of these topics. Net zero planning, and climate lobbying are both material activities for energy producers, utilities and logistic companies.

For all resolutions BlackRock and State Street commented that following their engagements they felt the companies were doing enough on the areas the proposals covered. We shared our concerns that we, along with other investors, felt more was needed. In addition, we fed back that supporting a resolution can be a signal that investors support the direction of travel and a need for improved transparency. We will continue to monitor similar resolutions.

This differential also demonstrates the importance of ensuring our votes are cast in line with our Voting Guidelines through the ISS SRI policy. If this had not been the case, our vote would have been split with Schroders supporting and State Street and BlackRock voting against.

Voting Resolutions

Company	Resolution	Dissent	State Street	BlackRock	Schroders	ISS SRI
Chevron Corp	6. To request the Board to report to shareholders on impacts of Net Zero 2050 Scenario	39.40%	Against	Against	For	For
Honeywell International Inc	5. Shareholders To request the Board to prepare a report to shareholders on climate lobbying	40.05%	Against	Against	For	For
Abbvie Inc	8. Shareholders To request the Board to prepare a report to shareholders on the Company's political donations	39.87%	Against	Against	For	For
UnitedHealth Group Inc	5. To request the Board to prepare a report to shareholders on the Company's political donations	40.65%	Abstain	Against	For	For
Home Depot Inc	7. To request the Board to prepare a report to shareholders on the Company's political donations	42.86%	Against	Against	For	For

3.6 Voting and voting records continued

SCOTTISH WIDOWS PORTFOLIO AND MANAGER'S FIRMWIDE VOTING OVERVIEW

We have monitored how our managers have voted on our behalf, as discussed in the section above. We have also engaged with them to understand how they each have chosen to define 'significant votes'.

The following tables indicate both firm wide voting statistics and the total for all company shares in Scottish Widows portfolios. Consistent with engagement activities above, the voting on Scottish Widows shares relate to mandates managed by Tier 1 managers and holdings of Tier 2 funds held in the pension portfolios.

As the regions and sectors will differ between managers, albeit often containing the same company meetings, these tables are not directly comparable.

* The difference between percentage voted with/against management differs between our funds with Schroders and Schroders as a firm due to the differing geographical make-up of the wider portfolio. Scottish Widows funds managed by Schroders have a greater UK allocation overall; a region where votes are, on the whole, more likely to be with management than some other regions.

** This data includes Scottish Widows votes cast in line with the ISS SRI Policy, which was put in place in April 2022.

Tier 1 Managers – Voting Analysis

Schroders

	SW portfolio Statistics	Schroders firm wide statistics
Meeting eligible to vote at	1,471	7,443
Proposals were you eligible to vote on	18,873	77,855
% Resolutions voted upon if eligible	98.55%	96.61%
% Voted With/Against Management+	90.63% / 9.39%*	87% / 13%

Significant Votes:

Schroder's believe that all resolutions when we vote against the board's recommendations should be classified as a significant vote, for example, votes against the re-election of directors, on executive remuneration, on material changes to the business (such as capital structure or M&A), on climate matters and on other environmental or social issues may all be more or less significant to different client stakeholders.

BlackRock

	SW portfolio Statistics	BlackRock firm wide statistics
Meeting eligible to vote at	2,317	18,272
Proposals were you eligible to vote on	31,561	173,326
% Resolutions voted upon if eligible	99%	98.3%
% Voted With/Against Management+	81.41% / 18.59%**	87.36% / 12.64%

Significant Votes:

BlackRock take a more bespoke view, guided by their Engagement priorities and Global principles, and publish vote bulletins after the shareholder meeting to provide transparency for clients and other stakeholders on their approach to the votes they consider to be most significant and thus require more detailed explanation.

BlackRock publish details of other significant votes (including vote rationales, where applicable) quarterly on the BlackRock website.

Abrdn

	SW portfolio Statistics	ABRDN firm wide statistics
Meeting eligible to vote at	2,601	7,316
Proposals were you eligible to vote on	30,778	76,255
% Resolutions voted upon if eligible	88.3%	99.3%
% Voted With/Against Management+	82.5% / 14.6%	84.8% / 13.3%

Significant Votes:

In line with the requirements of the Pension and Lifetime Savings Association (PLSA), Abrdn have established a process for identifying and recording what we deem to be the most significant votes (SV) instructed on behalf of their clients. These are defined under five separate categories:

1. SV1: High Profile Votes – Focus on votes which received public interest, reflect significant governance concerns, or are proposed by Abrdn.
2. SV2: Shareholder and Environmental & Social (E&S) Resolutions – Votes on shareholder or management-presented E&S proposals where we have engaged with the proponent or company on the resolution, and ii) Shareholder proposals where Abrdn have voted contrary to management.
3. SV3: Engagement – Resolutions where Abrdn engaged with the company on a resolution or voted contrary to their custom policy.
4. SV4: Corporate Transactions – Votes which have a financial impact on the investment (with focus on acquisitions).
5. SV5: Votes contrary to custom policy – Large active holdings where Abrdn voted contrary to custom policy following analysis.

Hermes

	SW portfolio Statistics	Hermes firm wide statistics
Meeting eligible to vote at	99	766
Proposals were you eligible to vote on	1,420	8,431
% Resolutions voted upon if eligible	97%	97.78%
% Voted With/Against Management+	85% / 14%	85.26% / 14.74%

Significant Votes:

All votes against Management.

3.6 Voting and voting records continued

Tier 2 Managers – Voting Analysis

BlackRock

	SW portfolio Statistics	BlackRock firm wide statistics
Meeting eligible to vote at	1,307	18,272
Proposals were you eligible to vote on	22,816	173,326
% Resolutions voted upon if eligible	98.66%	98.3%
% Voted With/Against Management+	77.57% / 22.43%*	87.36% / 12.64%

Significant Votes:

BlackRock take a more bespoke view, guided by their Engagement priorities and Global principles, and publish vote bulletins after the shareholder meeting to provide transparency for clients and other stakeholders on their approach to the votes they consider to be most significant and thus require more detailed explanation.

BlackRock publish details of other significant votes (including vote rationales, where applicable) quarterly on the BlackRock website.

State Street

	SW portfolio Statistics	SSgA firm wide statistics
Meeting eligible to vote at	4,845	21,922
Proposals were you eligible to vote on	45,247	199,985
% Resolutions voted upon if eligible	93.63%	98.63%
% Voted With/Against Management+	83.28% / 16.72%	84.98% / 15.20%

Significant Votes

SSGA identifies “significant votes” for the purposes of Shareholder Rights Directive II as follows:

1. All votes on environmental-related shareholder proposals.
2. All votes on compensation proposals where they voted against the management’s recommendation.
3. All against votes on the re-election of board members due to poor ESG performance of their companies (as measured by their R-Factor ESG score**).
   All against votes on the re-election of board members due to poor compliance with the local corporate governance score of their companies (as measured by their R-Factor CorpGov score***).
4. All against votes on the re-election of board members due to a lack of gender diversity on the board.

* This data includes Scottish Widows votes cast in line with the ISS SRI Policy, which was put in place in September 2022.

** In 2019, State Street created an engagement and voting screen that leverages R-Factor, our proprietary scoring system. R-Factor measures the performance of a company’s business operations and governance as it relates to financially material and industry-specific ESG risk factors, as defined by the Sustainability Accounting Standards Board (SASB). Since the 2020 proxy season, we started taking action against board members at companies in the S&P 500, FTSE 350, ASX 100, TOPIX 100, and STOXX 600 indices that are laggards based on their R-Factor scores and that cannot articulate how they plan to improve their score.

*** In 2020, State Street implemented a proactive screen to identify portfolio companies in their key markets that do not comply with their country-specific governance codes. The screen’s methodology centers around the R-Factor Corporate Governance score component (CorpGov), leveraging our proprietary framework to develop insights and drive our engagements with companies identified as laggards based on their low-ranking scores relative to their domestic and global peers. Laggard companies score in the bottom 10% relative to their local peers, and belong to one of the major indices where we applied the screen. Since most governance codes are implemented on a comply-or-explain basis, we engaged with these companies to understand their reasons for the laggard score status. In the event companies were unable to provide effective explanations for their noncompliance or have not made evident progress to improve their practices, we held them accountable by taking voting action against the independent leader of the board standing for election.

3.6 Voting and voting records continued

CASE STUDIES ON VOTING ACTIVITY BY OUR DELEGATED ASSET MANAGERS

Schroders

Case study

META (OWNER OF FACEBOOK) / ALPHABET – DIGITAL RIGHTS

In 2021, Facebook faced a whistleblowing complaint when a former employee revealed documents showing that Facebook was aware of the damaging effects of the content posted on its platform. Schroders wrote to Meta, which owns Facebook, to clarify Meta's definition of success in its bid to effectively moderate content. In addition, Schroders' participated in a group investor call, followed by a subsequent email. Although the company said that it uses prevalence of objectionable content as a metric to track progress, it is still unclear on its longer-term moderation objectives.

Schroders also convened a client Sustainability Forum to hear views on 'Responsible Technology' from external parties such as ShareAction and Friends Provident Foundation. Clients have been increasingly aware of the negative impacts of these big technology companies and were particularly concerned about how content on the platforms could contribute to misinformation, particularly regarding climate change.

To ensure its broader investments were in line with client beliefs, Schroders wrote to Google parent company Alphabet in August 2021 to gain clarity on how it moderates misinformation around climate change content. Alphabet has since said that climate misinformation will be covered by its content policy. However, engagement with Alphabet beyond this has remained difficult.

In 2022, Schroders became a member of the Investor Alliance for Human Rights which includes supporting the collaborative engagement on digital rights with Google parent company Alphabet and Meta.

Schroders have voted for eight shareholder resolutions at the Meta and Alphabet AGMs relating to digital rights i.e. the enforcement of community standards, online child sexual exploitation, and data privacy and security. The resolutions aim to improve business practices in a number of fields. Human rights is one of Schroders' six priority engagements. Digital rights sits within this category.

3.6 Voting and voting records continued

CASE STUDIES ON VOTING ACTIVITY BY OUR DELEGATED ASSET MANAGERS

Schroders continued

Case study

AMAZON – WORKERS RIGHTS AND IMPROVING DISCLOSURES

Amazon has come under intense scrutiny for the way it treats employees and the conditions under which they work. Schroders has urged Amazon to increase transparency around its contractors and specifically requested that it:

1. Increase its analysis of the root causes of safety issues; and
2. Increase disclosure defining the differences between part-time, seasonal and contracted workers.

Ahead of the 2022 AGM, Schroders pre-declared their voting intensions on Amazon workforce issues in order to drive change at the company. This resulted in Schroders supporting three shareholder proposals relating to Amazon workers.

Schroders believes it is important to support these proposals, which align with its own engagement activity. Workers' rights is one of six priority themes in Schroders' engagement blueprint, which sets out its approach to active management. Schroders will continue to engage with Amazon on workforce safety and transparency.

Case study

CHEVRON, EXXONMOBIL AND SHELL – CLIMATE TRANSITION

In 2022, Schroders pre-declared its voting intentions for three oil & gas majors – Chevron, ExxonMobil and Shell – to help drive a faster shift towards net zero. This comes off the back of Schroders having already supported similar shareholder resolutions at BP, ConocoPhillips, Occidental Petroleum and Phillips 66 earlier in 2022.

Schroders voted in favour of the shareholder resolutions at Chevron, ConocoPhillips, ExxonMobil and Phillips 66 as Schroders believe they should be more transparent and increase their ambition in transitioning to net zero. Whilst they acknowledge that these companies may already have net zero targets ambitions for 2050, they are lagging in comparison to peers regarding Scope 3 targets.

For BP, Shell and Occidental Petroleum – Schroders' voted in support of these shareholder resolutions as they encourage the companies to continue their efforts in reaching net zero. All three have an ambition to achieve net zero GHG emissions by 2050 or sooner across Scope 1, 2 and 3 emissions and are making progress in setting interim climate targets.

3.6 Voting and voting records continued

CASE STUDIES ON VOTING ACTIVITY BY OUR DELEGATED ASSET MANAGERS

BlackRock

Case study

AMAZON – PLASTIC USAGE

BlackRock engages with companies in certain sectors on their approach to plastic packaging. Amazon.com, Inc (Amazon), a multinational technology company, which engages in the provision of online retail shopping services, had a shareholder proposal on the agenda for its May 2022 AGM that asked the board to issue a report describing how the company could reduce its plastics use.

While BlackRock believed that Amazon's goals in relation to plastic recycling were clear, at the time of the AGM, the company did not explicitly disclose the total amount of plastic used, making it difficult for investors to determine how effectively it was managing this material risk and what progress it was making year on year. As a result, BlackRock supported this shareholder proposal, as having a better understanding, from enhanced disclosures, of how Amazon was addressing this material long-term business risk was aligned with investors' financial interests.

As a result of the vote, Amazon published an update to its packaging reduction strategy, detailing efforts to reduce and replace plastic packaging, among other initiatives, in December 2022. BlackRock will continue to engage with Amazon to discuss these issues and will monitor progress against stated plans.

Case study

ALPHABET (GOOGLE PARENT COMPANY) – NATURAL CAPITAL

Engaging on water risks is an increasingly important topic and BlackRock believes that water management is a material risk for Alphabet, a global technology group and the holding company of Google, given the significant volumes of water used to cool data centres. The company recently enhanced its water metrics disclosure to include total water withdrawal, consumption, and discharge, in line with industry standards.

In addition, Alphabet aims to replace more water than the company consumes by 2030 and is focusing water stewardship efforts in three main areas:

1. Improving stewardship of water resources across Google office campuses and data centres;
2. Replenishing 120% of the average amount of water they consume across their offices and data centres, and improving watershed health and ecosystems in water-stressed communities; and,
3. Sharing technology and tools that help everyone predict, prevent, and recover from water stress.

However, the Alphabet does not disclose annual water use or other risk metrics by location. For this reason, it is difficult for stakeholders to determine the company's regional approach, water stress risks, as well as annual progress.

BlackRock supported a shareholder proposal in 2022 which requested that Google annually report, at reasonable cost, quantitative water-related metrics by location, including data centres, and for each location, practices implemented to reduce climate-related water risk. It believes it is in the best financial interests of its clients for Alphabet to enhance its disclosure on this material long-term business risk.

3.6 **Voting and voting records** continued

CASE STUDIES ON VOTING ACTIVITY BY OUR DELEGATED ASSET MANAGERS

BlackRock continued

Case study

EXXONMOBIL – CLIMATE CHANGE

BlackRock voted against a shareholder proposal in 2022 which requested that international oil and gas company ExxonMobil issue a report describing how the company could alter its business model to yield profits within the limits of a 1.5°C global temperature rise by substantially reducing its dependence on fossil fuels.

BlackRock found the proposal overly prescriptive and straying into micromanagement of the business. In particular, the proposal asks ExxonMobil to report on how it can alter its business model specifically within the limits of a 1.5°C temperature rise scenario.

BlackRock does not believe it is the position of shareholders to tell companies what their corporate strategies should entail, including whether changes to the business model are warranted. Rather, based on a company's disclosures, BlackRock assesses the robustness of the company's climate action plan, board oversight, and capital allocation plan in addressing the risks and opportunities presented by the global energy transition.

BlackRock believes ExxonMobil is making encouraging strides to improve its disclosure to provide shareholders with insight into its strategic business planning around the energy transition. ExxonMobil has a goal to achieve net zero emissions from its operated assets by 2050 with interim 2030 targets and has increased planned investments to $15 billion from 2022 through 2027.

Through their engagement, BlackRock has fed back and discussed disclosures that could be enhanced, including continued detail on progress and the oversight of these low carbon plans and a more detailed breakdown of capital expenditures in support of stated goals.

Abrdn

Case study

RIO TINTO – HUMAN RIGHTS / GOVERNANCE

Abrdn has had ongoing engagement with Rio Tinto on a number of ESG issues over a number of years. This has included several meetings with the group following allegations of sexual discrimination and harassment at its fly in fly out sites*, and a subsequent inquiry by a Western Australian parliamentary committee on the same issue. In 2022, Abrdn met with the group's Investor Relations team to discuss the outcomes and recommendations of this inquiry.

The parliamentary inquiry found significant issues and encouraged the company to carry out a full review. Rio Tinto launched an independent review led by former Australian Sex Discrimination Commissioner Elizabeth Broderick which was made public and included 26 recommendations. Abrdn engaged with Rio Tinto and discussed the outcomes of the recommendations and the steps that the company was going to put in place.

As a result, Rio Tinto put together a plan to address the outcomes of the parliamentary review, committed to implement all 26 recommendations, and publicly report on its progress against them. While Abrdn was supportive of the steps that the company was taking, it abstained on the approval of the company's annual report & accounts at the 2022 AGM.

* A method of transportation where companies working in remote regions, fly their staff to and from worksites.

3.6 **Voting and voting records** continued

CASE STUDIES ON VOTING ACTIVITY BY OUR DELEGATED ASSET MANAGERS

State Street

Case study

APPLE – RACIAL EQUALITY

During the 2022 proxy season*, Apple had shareholder proposals asking management to undertake independent, third-party civil rights or racial equity audits.

In advance of the company's 2022 AGM, State Street engaged with Apple on a number of occasions on its approach to managing risks and opportunities related to racial equity. These discussions included the potential for greater insights into how the company was managing the potential adverse impact of its products and services on underrepresented racial and/or ethnic communities. As a result, State Street supported the relevant shareholder proposal.

After the proposal was passed, Apple publicly committed to undertaking a racial equity audit.

Case study

MITSUBISHI CORPORATION – GHG EMISSIONS REDUCTION

Mitsubishi Corporation faced a shareholder resolution in 2022 requesting disclosure of a business plan with short and mid-term GHG emission reduction targets. It requested that capital expenditure disclosures including annual reporting around assumptions, costs, estimates and valuations in the development of new upstream, midstream and downstream oil and gas assets.

State Street reviews climate-related shareholder proposals on a case-by-case basis. Leading up to the company's AGM, State Street examined the company's disclosures on ESG issues most relevant to this year's proxy.

In June 2022, State Street engaged with Mitsubishi Corp regarding the climate-related shareholder proposals. Through their engagement, State Street highlighted opportunities to enhance certain areas of disclosure to bring them in line with peers in the global market. This included adopting short-term GHG emission reduction targets, strengthening disclosure on current and planned capital investments to achieve interim and long-term climate goals, and providing more detail on the integration of climate risk assessment into transaction due diligence.

State Street voted for the first proposal as Mitsubishi Corp currently does not meet its disclosure expectations and it believes supporting the proposal will help encourage the company to continue to advance its efforts in this area. In regards to Scope 3 emissions, State Street believes Mitsubishi Corp can provide enhanced disclosure of opportunities for incremental Scope 3 reductions in line with State Street guidance.

* The time of year where shareholders are given the opportunity to vote on issues affecting the companies they own.

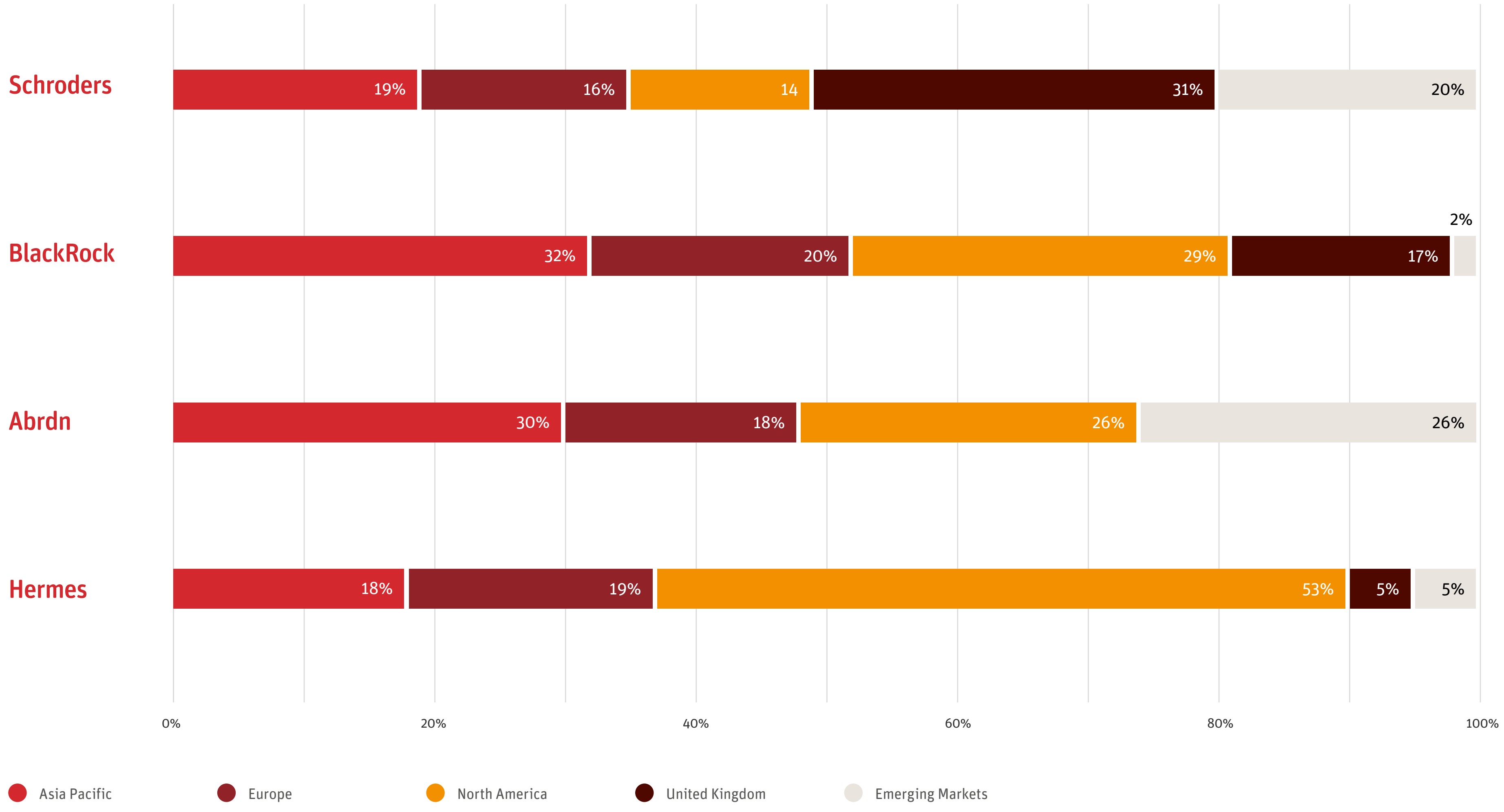
3.6 Voting and voting records continued

OVERVIEW OF VOTING ACTIVITY BY DELEGATED ASSET MANAGERS

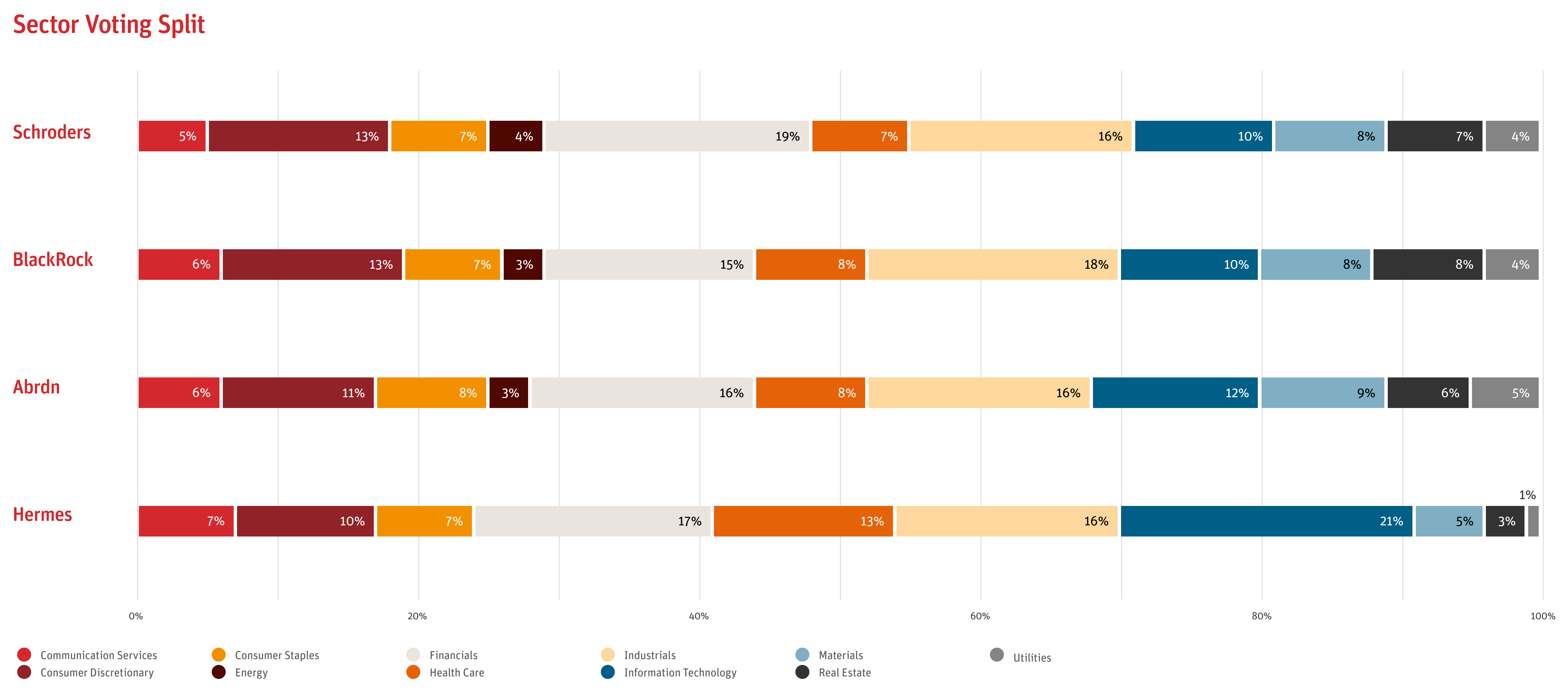
Regional & Sector Voting Activity by our Core Tier 1 Delegated Asset Managers

As our assets are invested in companies globally and across sectors, it is important that our delegated asset manager's voting activity reflects this. Therefore, we monitor this as shown in the charts to the right.

Region Voting Split



3.6 Voting and voting records continued



3.7 CONFLICTS OF INTEREST

Lloyds Banking Group, including Scottish Widows Group as a wholly owned subsidiary, has established and implemented a group-wide Conflicts of Interest policy which governs how conflicts are identified, managed, mitigated and monitored. A conflict of interest under this policy includes:

- An actual Conflict of Interest – where a Conflict of Interest has arisen;
- A potential Conflict of Interest – where a Conflict of Interest may arise given particular facts and circumstances; and
- A perceived Conflict of Interest – where there is a situation which may give rise to the perception of a Conflict of Interest, even where a Conflict of Interest may not in fact exist.

Such conflicts of interest may arise out of our day-to-day business activities, therefore we have implemented system and control procedures that are designed to promptly identify, manage, mitigate and monitor them. The procedures adopted by the firm include:

- Mandatory staff training and awareness requirements;
- Ongoing identification, recording and management of all actual, potential and perceived conflicts to which the business area is susceptible; and
- Appointment of business area specific Conflict of Interest Officers.

The specific nature and circumstances of any conflict of interest identified will determine the specific action(s) or controls required to manage and mitigate the conflict. In any instances where such controls would not be enough to eliminate the potential risk of damage to clients from specific conflicts, we will disclose to the client the general nature and/or source of those conflicts of interest and the steps taken to mitigate the potential risk.

Carrying out stewardship and other responsible investment activities creates a distinct array of conflicts, which we assess and manage on a stewardship-specific basis. Our stewardship-related conflicts, appended to our Stewardship Policy, fall into two categories: those related to being part of Lloyds Banking Group, and those related to being a pension provider. Many of these conflicts have two aspects: first, the risk that we allow commercial interests to affect stewardship decisions; second, the risk of our stewardship decisions resulting in loss of business or unintended consequences for our clients.

Categories of Stewardship conflicts

(I) Conflicts arising from being part of Lloyds Banking Group

- **Engaging with Lloyds Banking Group and its peers**- Lloyds Banking Group is one of our largest holdings and, as such, is in scope for stewardship activity. It is at the same time our parent company: we cannot demand less of Lloyds Banking Group than we would of its peers and competitors. To mitigate this risk we engage with Lloyds Banking Group as we would any other investee company of its size and type. An example of this from our 2021 stewardship activity is explained below.
- **Engaging with clients (and potential clients) of the Commercial Bank**- There is the risk of a conflict of interest between Scottish Widows in the carrying out of stewardship activity and our colleagues in the Commercial Bank acting in the interests of their clients. The mitigation for this risk is similar to that discussed below regarding Scottish Widows' own workplace pension clients: we inform client managers of the activity we are carrying out, in order that they can manage their relationships, but do not allow the commercial interests of other parts of the Group (or their clients) to influence our stewardship activity.
- **Responding to regulators' consultations**- As part of Scottish Widows' stewardship and responsible investment activity we submit responses to regulatory consultations separately to the wider Group as considered appropriate given our status as a separate legal entity and where our focus as an asset owner may be different. Where Scottish Widows' response is not consistent with that of the wider Group we ensure Group are appropriately engaged and any points of difference are highlighted to the regulator. This allows us to manage the sometimes-conflicting interests of the Group (a large retail and commercial bank) and of Scottish Widows (an institutional investor and insurer).

(II) Conflicts arising from being a pension provider

- **Engaging with an investee company that is also a client or a potential client** – We may engage with a company which is a pension scheme client or a potential client; this could damage our commercial relationship with this company. We do not include client relationship management and sales colleagues in decisions around stewardship activity but do alert them to this activity so that they can manage any consequences. Decisions about whether to work with a company as workplace pension provider are entirely separate from investment and stewardship decisions.

In 2022, our direct and collective engagement activities, across a range of sub-themes, increased considerably compared to previous years. This meant we had to follow our conflicts of interest governance process specific to the type of activity conducted, more often and sometimes a first of its kind, requiring governance sign offs, specific to the activity. The conflicts of interest guidance embedded in our Stewardship Policy has been vital in directing how we progressed with these decisions and processes and is an important element in how we steward our investments on behalf of our customers and beneficiaries, distinct from the wider business and its divisions.

Similarly, the Scottish Widows Responsible Investment team is an active participant in policy and regulatory advocacy, supporting enhancement of the regulatory environment by contributing to collaborative consultation positions and responses from several industry bodies, and providing individual contributions direct to regulatory bodies (detailed in Section 4). While some of these bodies are focused on a specific sector, for example the Association of British Insurers (ABI), others can represent a much broader range of financial activity, and thus many different lines of businesses, for example the UK Sustainable Investment and Finance Association (UKSIF). In the case of UKSIF, it is important for us to consider conflicts of interest between our internal view and that of UKSIF which is based on an industry-wide effort. Robust determination of internal view and rigorous consideration of any inconsistencies between that view and industry positions are the means through which we identify and manage any such conflicts. On occasion, policy and regulatory consultations may impact both Lloyds Banking Group and Scottish Widows, and due to the differing lines of business and activity undertaken, differing views may arise. Close collaboration between teams representing each entity allows us to identify and manage any such conflicts.

Some considerations also play out with respect to our investment activities. For example, implementing the new tobacco exclusion according to our policy had different impacts on our Customer funds and our Shareholder funds, asset classes (equity vs bonds) and how they are accounted for. Working closely with our appointed investment manager on this, we managed to implement this exclusion across all our investments, reinvesting the money in sectors with similar characteristics and mitigating risks.

Across the board, we aim to carry out our stewardship activity in a way that is positive, constructive, and consultative, rather than aggressive or censuring. This, itself, mitigates some of the risks from conflicts.

COLLABORATION

4.1 DRIVING PROGRESS THROUGH COLLABORATION

In 2021, the global community and investment world began to work together on environmental and social issues in new ways. 2022 was no different – only more focussed and joined up, despite the geo-political headwinds. In keeping with this spirit, and an even greater resolve to keep progressing across a range of sustainability factors, we have continued to collaborate with the rest of the industry to drive positive change.

Our active participation in partnerships and collaborations fits with our goal to support and encourage greening across the real economy in a just and fair way that bridges the inequality gap.

We recognise that we can be most effective through collaboration, and we continue to work with external bodies, organisations and initiatives to promote responsible investment, climate considerations, and social-related policy or advocacy initiatives.

Some of our material collaborations are outlined opposite.

Occupational Pensions Stewardship Council (OPSC)

The Asset Management Taskforce brought together government, senior representatives from asset management, regulators and key stakeholders. Based on the recommendations of the Taskforce, the Occupational Pensions Stewardship Council* was set up by DWP. The aim of the Council is to provide pension schemes, big and small, across the Defined Benefit and Defined Contribution spectrum with a forum for sharing experiences, best practice, research and practical support. In 2021, we became an inaugural member. As a large asset owner with a specialist team, we were keen to contribute and support smaller pension schemes.

From mid-2021 to mid-2022 we led the service provider engagement activity, one of the four focus areas for the year, which aimed to improve stewardship standards with service providers, develop common questions and collaborative engagement projects with asset managers.

a. Guidance for productive meetings with asset managers on stewardship – a meeting guide for asset owners

We produced a guide for OPSC members on the format and agenda of meetings with asset managers and what would help have the most to ensure they were productive and helped assess, support and challenge their stewardship activities, including those related the wider industry and economy, like policy advocacy and consultation responses. We were conscious that other asset owners in the group had much less facetime with their managers they worked with so wanted the guide to be flexible.

b. Driving change through the voting chain

Following our participation in the Taskforce for Pension Scheme Voting Implementation (TPSVI) to remove barriers to trustee-directed voting and create better alignment between asset owners and asset managers on voting matters, we collaborated with other council members on an engagement campaign with asset managers. It kicked off at the end of 2021 and was directly supported by the then, Minister for Pensions and Financial Inclusion, Guy Opperman. In December 2021, we wrote to 44 asset managers asking a range of questions – from enabling clients to share their bespoke voting policies as an ‘expression of wish’ as a minimum, to having forward-looking conversations and providing greater transparency on areas of voting misalignment and to facilitating client-led voting in pooled funds and overriding of specific votes.

We were pleased that 37 asset managers responded and we worked with the Council’s secretariat to analyse the responses. The analysis was summarised in an OPSC report published in 2022 Driving change through the voting chain, which received good media and industry attention. The findings of this report were aimed to help asset owners have more robust evidence-based negotiations with asset managers on voting and to ultimately lead to better alignment of manager voting with their clients’ wishes. For our revised voting arrangements, either implemented or initiated in 2022, outlined in Chapter 3, this initiative has been instrumental.

For 2022-23, we continue to contribute to the Council’s overall strategic direction, and are participating in the climate change and member engagement streams, while also being part of the Engagement Group which helps set direction for the Council.

UNPRI Advance

Following the formal inclusion of human rights as a priority theme of our Stewardship Policy in 2022, we wanted to build on our engagement approach and join collaborative engagements on the topic.

We have been accepted on to Advance which is a new stewardship initiative from the UNPRI modelled on Climate Action 100+ where institutional investors work together to take action on human rights and social issues.

The following expectations are set for investee companies:

- Fully implement the United Nations Guiding Principles on Business and Human Rights (UNGPs) – the guardrail of corporate conduct on human rights;
- align their political engagement with their responsibility to respect human rights; and
- deepen progress on the most severe human rights issues in their operations and across their value chains.

We are ‘collaborating investors’ for engagement with Anglo American on its human rights performance. We look forward to getting more involved in the Advance initiative through 2023.

* Occupational Pensions Stewardship Council – GOV.UK (www.gov.uk)

4.1 Driving progress through collaboration continued

Institutional Investors Group on Climate Change (IIGCC)

The IIGCC* is the European membership body for investor collaboration on climate issues, representing investors with more than €50tn of assets. Our IIGCC membership has been one of the most important elements of our Responsible Investment initiatives. In the past we have contributed to the development of the Net Zero Investment Framework among other initiatives, as outlined in our 2020 and 2021 reports. Over the course of 2022, we have participated in two further key initiatives:

Climate Solutions Working Group

During 2022, and continuing into 2023, one of our key contributions has been to co-lead the Climate Solutions Working Group. This group has produced guidance documents for asset owners and managers to measure, monitor, and disclose their relevant investments across different asset classes. This is particularly important as many more asset owners and asset managers have made, or are looking to make, specific commitments to invest in climate solutions as part of being a signatory of the Paris Aligned Investment Initiative. We have contributed, reviewed and communicated the guidance, as well as overseeing its creation through encouraging collaboration with other IIGCC members.

Net Zero Engagement Initiative (NZEI)**

This Initiative was set up to scale and accelerate climate-related corporate engagement, to support investors in aligning more of their investment portfolio with the Paris Agreement and accelerate real world impact. Whilst the CA100+*** initiative focuses solely on the biggest high emitting companies, the NZEI has expanded the universe of companies beyond the CA100+ focus list, to help investors more broadly align their portfolios with net zero initiatives. In 2022, the IIGCC launched a new Net Zero Engagement Platform, creating a central hub for corporate collaborative engagement workstreams, to accelerate progress against goals.

Along with a group of five other investors, we are participating in the Engagement Sub-Group, to provide close support for accelerating engagement and escalation with specific CA100+ target companies and in engaging with a greater number of real economy companies beyond the existing list. The aim is to make progress across both the supply and demand side of high-CO_2 emitting sectors.

In 2023, we continue our collaboration with the IIGCC across the two workstreams, contributing to the planned engagement activities with the target companies. Schroders, one of our core appointed investment managers, is already a core participant of this initiative. Engagement activities by our appointed investment managers is outlined in Sections 3.5.

UK Sustainable Investment and Finance Association (UKSIF)

In 2021, we joined the UK Sustainable Investment and Finance Association****, a body that seeks to influence policy for positive change for a sustainable future. Since joining, we have contributed to industry best practice and to advancing the regulatory and policy agenda for creating well-functioning markets, embracing and embedding a sustainable, long-term outlook.

In 2022, a number of our responsible investment team spoke at UKSIF virtual and in-person conferences. Our Head of Responsible Investments and Stewardship Maria Nazarova-Doyle was also elected to the UKSIF Board and Policy Committee.

Net Zero Investment Plan

In 2022, we contributed to a letter to the UK Government co-signed by UKSIF, IIGCC and E3G***** requesting it publish a Net Zero Investment Plan encompassing:

i. A Net Zero Delivery Tracker to assess the financial flows in support of our climate and nature goals.
ii. Assessment of investment needs for decarbonisation is different economic sectors.
iii. As assessment of the low carbon investment gap for these sectors and how these will be bridged. This was accompanied by a request to give an independent unit, like the Office for Budget Responsibility, to conduct this tracking analysis on an ongoing basis.

Over the course of 2023, we will continue this collaboration to engage with the UK Government and monitor its progress in producing the Net Zero Investment Plan.

Just Transition Finance Challenge

Following on from the publication of our paper****** on the Just Transition, we became one of the founding members of the Just Transition Finance Challenge*******. It is an initiative launched by the Impact Investing Institute and aims to encourage public and private investments to support a Just Transition to Net Zero, bringing together mitigation of climate change and the associated negative social consequences, whilst also leveraging the opportunities for job creation.

Together with other founding partners, the initiative is developing a new label for investment products that deliver the three critical elements of a Just Transition:

1. Actions must advance Climate and Environmental Action, and
2. Improve Socio-Economic Distribution and Equity, and
3. Increase Community Voice

We have engaged with the initiative across 2022, responding to consultations and participating in workshops to refine and finalise the underlying criteria for the product label, which opened for industry consultation in early 2023.

Deforestation Guidance

In 2022, Global Canopy, Make My Money Matter (MMMM), and SYSTEMIQ launched a guide for pension schemes called 'Cutting Deforestation from Our Pensions'********. The guide was informed and shaped by a working group of 12 pension funds, including Scottish Widows.

The guide details how pension schemes can integrate deforestation-free requirements into agreements with asset managers, as well as how to work with asset managers on engaging with investee companies. It also provides guidance on how pension funds, which directly finance companies, can identify, assess, and eliminate deforestation, conversion, and associated human rights abuses from their portfolios.

The guide is split into six phases, from identifying where deforestation risks can be found in portfolios to implementation and engaging to ensure funds are deforestation-free. We have already put he introductory phases of this guide into use, as detailed in Section 3.2 and 3.3.

* The European membership body for investor collaboration on climate change. IIGCC works with business, policy makers and fellow investors to help define the investment practices, policies and corporate behaviours required to address climate change. IIGCC – The Institutional Investors Group on Climate Change
** Net Zero Engagement Initiative – IIGCC
*** An investor-led initiative established to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change. Climate Action 100+
**** UKSIF – UK Sustainable Investment and Finance Association
***** An independent climate change think tank aiming to steer the global transformation, translating climate politics, economics and policies into action. E3G – A safe climate for all
****** 60644.pdf (scottishwidows.co.uk)
******* Just Transition Finance Challenge – Impact Investing Institute
******** Cutting-Deforestation-from-our-Pensions-final-report.pdf (makemymoneymatter.co.uk)

4.1 Driving progress through collaboration continued

FTSE 100 Pension Emissions Report*

Businesses do not report on emissions generated by their pension funds. To highlight the 'unreported' emissions financed by pensions, during 2022 Make My Money Matter commissioned consultancy Route2 to produce a report looking into the comparison of FTSE 100 companies reported operational emissions and the financed emissions of their employees' pension investments. We collaborated on the report and our responsible investment team played a crucial role with the research, offering advice, and providing data. The report assesses the emissions from companies in which corporate pensions invest – and compares it to the Scopes 1 and 2 operational emissions from the employers, allowing us to see for the first time side-by-side the carbon footprint of UK pensions versus corporate emissions.

We found that:

- The carbon emissions financed by typical FTSE 100 company pensions are 7 times higher than the reported Scopes 1-2 operational emissions of those companies; and
- the total carbon emissions financed by FTSE 100 company pensions is estimated to be 131 million tonnes, equivalent to roughly one third of the UK's annual carbon emissions.

The report was published in September 2022 and received widespread national press coverage, including a feature in the Financial Times.

DWP Taskforce on Social Factors

Following the Department for Work and Pensions' (DWP) consultation on consideration of social risks and opportunities by occupational pension schemes, the Taskforce on Social Factors was established. To help trustees of UK pension funds ensure financially material social considerations are getting as much focus as climate change. We were invited to participate in the Taskforce as chair of a sub-group focussing on making the case for social factors and developing a trustee framework for addressing these factors.

The key objectives for the Taskforce as defined by DWP are to:

1. Identify reliable data sources and other resources, which could be used by pension schemes to identify, assess and manage financially material social risks and opportunities;
2. monitor and report on developments relating to the International Sustainability Standards Board (ISSB) and other international standards; and
3. develop thinking around how trustees can identify, assess and manage the financial risks posed by modern slavery and supply chain issues.

The Taskforce includes representatives from pensions schemes, asset managers, data providers, cross-industry collaboration groups and civil society. Government departments and regulators are observers on this Taskforce, while DWP provides the secretariat support.

The Taskforce will operate for one year and deliver guidance and recommendations to the pensions and investment industry. In addition, its work will contribute to further development of wider social factor principles, international standards, and metrics.

Association British Insurers (ABI)

The ABI established a Board sub-group on Climate Change in 2021 to help the Insurance and Long-Term Savings sector join the leading pack on climate action and we are active participants. This sub-group, which reports to the ABI Board, is made up of CEOs from 10 leading firms from across the sector, along with their sustainability experts, provides practical insights and evidence to ensure the ABI's approach on climate change is consistent with the global climate change goals.

The group oversaw the development of the ABI Climate Change Roadmap, which set sector-wide commitments against 2025, 2030 and 2050 milestones. Over 2022, we have also joined ABI's newly established Stewardship Working Group to galvanise the insurance and long-term savings sector's stewardship efforts and have also begun work on developing a Nature and Biodiversity roadmap for the industry, fashioned on the roadmap we developed for climate change.

Farm Animal Investment Risk and Return (FAIRR)

We became members of the FAIRR Initiative** in 2022. The initiative provides detailed ESG insight into animal agriculture and global food companies. The initiative is a great resource for our climate, biodiversity and human rights stewardship themes in the food sector, providing in-depth company research and company engagement opportunities.

During the second half of 2022, FAIRR commenced a biodiversity engagement series, which we are involved in, focusing on waste and pollution, land management and resource use, and land/sea use change. These were identified as three key pathways to biodiversity loss.

The first in the series, waste and pollution, had an investor representation of $23 trillion AUM. During Q4, the engagement programme targeted 10 protein producers and two agro-chemical companies by letter with detailed questions and expectations for limiting biodiversity risk in their operations and supply chains. Meetings have been put in the diary for Q1 / Q2 2023. We are involved in the engagement activities with two of the companies (additional details in Section 3.4).

The Workforce Disclosure Initiative (WDI)

The Workforce Disclosure Initiative*** is the only investor-backed platform for disclosure of company workforce management data covering both direct operations and supply chains. It is unique in terms of its scope and ambition, covering areas such as governance, risk assessment, contractual status and remuneration, gender diversity, stability, training, wellbeing and rights issues. The WDI survey applies to all corporate sectors and covers all geographical regions. In 2021, 173 global companies took part in the initiative, demonstrating their commitment to transparency. We joined WDI in 2022 and are using the data to analyse our investee companies to understand how many are making disclosures to WDI and their performance on workforce metrics. We intend to use these insights in our engagements with companies over the course of 2023.

* FTSE100-hidden-emissions-–-September-2022.pdf (makemymoneymatter.co.uk)

** The FAIRR Initiative is a collaborative investor network that raises awareness of the environmental, social and governance (ESG) risks and opportunities brought about by intensive animal agriculture. FAIRR Initiative | A Global Network of Investors Addressing ESG Issues in Protein Supply Chains

*** ShareAction | Workforce Disclosure Initiative

4.1 Driving progress through collaboration continued

Other continuing collaborations

World Benchmarking Alliance (WBA)

The World Benchmarking Alliance* (WBA) is a not-for-profit organisation established to assess and rank companies based on their contribution to the Sustainable Development Goals (SDGs). In 2021, we became members of the WBA to strengthen our direct and collective engagement efforts, and heighten knowledge of emerging ESG themes (e.g. biodiversity, human rights, Just Transition). Over the course of 2022, we have integrated the WBA benchmarks in our direct engagement activities and are leveraging them to influence the market and enable action on human rights due diligence. We are participants in the Collective Impact Coalition (CIC) on Human Rights Investor Strategy and Actions sub-group, working on an industry-wide initiative that aims to improve the quality and consistency of human rights due diligence disclosures by companies and on voting policies, highlighted in Section 3.3.

In 2023, we will continue to collaborate with the WBA and other members to collectively engage on developing ESG themes.

* Home | World Benchmarking Alliance
** Asset Owner Diversity Charter – Diversity Project
*** Climate Action 100+
**** Home – Transition Pathway Initiative

Asset Owner Diversity Charter

The Asset Owner Diversity Charter** was set up to encourage asset owners to signal the importance of diversity and inclusion (D&I) to the asset managers they work with, and improve the transparency and standardisation of D&I data. The initiative aims to improve diversity, equity and inclusion through recruitment, retention and progression. We became signatories of the Charter in 2021 and over the course of 2022, have continued to engage with managers in our Tier 1 and 2 categories. We have created an implementation plan for our stakeholders that incorporates the integration of DE&I criteria into how we assess new and existing asset managers. For more detail on the Asset Owner Diversity Charter, see Section 3.4.

Climate Action 100+ (CA100+)

As Asset Owners, we are not required under the CA100+*** membership to participate directly in engagements with focus companies. However, over the course of 2022 we have continued to publicly support the goals of the initiatives and have used the Net Zero benchmarks in our own engagement activity. In addition, through our involvement with the IIGCC Net Zero Engagement Initiative, we have begun to participate in some investor meetings focused on targeted CA100+ companies.

Transition Pathway Initiative (TPI)

Our target of achieving net zero by 2050 will require significant action from Scottish Widows, our appointed investment managers, and the companies we invest in. In 2022, we leveraged the TPI data**** to improve our engagement activity with our investee companies.

4.2 RESPONDING INDEPENDENTLY TO INDUSTRY AND REGULATORY CONSULTATIONS

We believe engaging with industry bodies and regulators, and taking part in industry consultations can be the driving force behind combatting market-wide issues. We strive to participate in as many relevant industry consultations as possible.

We believe that we can leverage our expertise to offer insight to enable regulation to consider all stakeholders, including our customers. We want to remain at the forefront of industry development and continue to build relationships that contribute towards our overarching policy advocacy strategy and initiatives – responding to industry consultations helps us to do that.

Over the course of 2022, we engaged with a number of industry bodies and responded to numerous consultations. These include, but are not limited to, the following:

FCA Consultation Paper 22/20: Sustainability Disclosure Requirements (SDR) and investment labels

Following publication by the FCA in October, 2022, Scottish Widows responded to this consultation directly – and indirectly through collective industry bodies – in January, 2023.

There are concerns that firms across the economy, including those in the financial services sector, can make exaggerated or misleading sustainability-related claims about their products – otherwise known as 'greenwashing'. This can lead to consumer harm and impact the level of trust that customers' place in their chosen brands. In this particular case, proposals in this consultation were made in support of the Government's Roadmap to Sustainable Investing, which outlined plans to ensure that investors thoroughly understand product sustainability credentials and are not misled.

Through a package of measures, the FCA proposed a regulatory framework consisting of labels for specific funds, disclosure requirements and restrictions on the use of certain language in product naming and marketing. Here at Scottish Widows we fundamentally have no tolerance for consumer harm and believe strongly in the need for customers to be able to trust our products, and we therefore fully engaged with this consultation in support of better standards across our industry and, ultimately, better customer outcomes. In our engagement with this consultation process, we provided feedback where we believed clarification or consideration of an alternative approach would result in a more efficient and informative framework. Feedback covered several topics, including the following:

Fund labels

To build transparency and trust, the FCA proposed that labels be introduced for funds to help consumers navigate the market for sustainable investment products. Upon meeting certain criteria, funds would be classified and assigned specific labels to help consumers distinguish between different types of product on the basis of their sustainability characteristics, themes and outcomes. In our feedback we noted support for the classification and labelling of funds, while noting a challenge to implementation where funds could straddle two or more classifications, e.g., multi-asset funds. To help address this challenge – and drive clear classification for better understanding – we requested the FCA provide clarity on best practice for such situation.

Product disclosures

The FCA proposed that asset managers disclose a summary of what they would expect consumers to find as surprising holdings in a fund – so called 'unexpected investments'. Our feedback noted that this may lead to arbitrary – and thus unhelpful – measures determining what constitutes a sustainable investment. In the absence of a universally applicable definition of what a typical sustainable investment looks like, we recognised that our wide consumer base is likely to have vastly differing opinions, consequently making it impractical for asset managers to impose such measures without it causing confusion amongst some consumers. We requested that this requirement be removed from final regulation.

The FCA also proposed that new product- and entity-level disclosures be introduced for consumers. The idea is that better information through such disclosures supports better consumer understanding and allows for more informed decisions. In our feedback we noted our support for disclosures to summarise a product's key sustainability-related features and serve to hold providers to account over their sustainability claims. We identified a potential issue in the proposal which called for disclosures across all funds, irrespective of whether they are labelled as sustainable – the issue being confusion. It was our view that if a fund is not classified as sustainable under the labelling regime, yet a consumer received a disclosure titled as the 'sustainability-related features' of the fund, this may be cause for confusion.

Naming and marketing of funds

To prevent products which are not eligible to be labelled as sustainable being marketed in a way that may suggest they are sustainable, the FCA proposed restrictions on language in product naming and marketing. As part of our commitment to ensuring our consumers receive fair, clear and not misleading information, we noted a need for the FCA to reconsider these proposals. Having identified that such restriction may prevent accurate and appropriate description of strategies which have non-qualifying sustainability-related facets such as an active engagement programme, we raised this concern for the benefit of ensuring consumers receive the information they need.

Also under the topic of naming and marketing, the FCA proposed introduction of a general anti-greenwashing rule which would reaffirm that existing regulatory requirements concerning disclosure also apply in the context of sustainability-related claims. With consumer interests in mind, we noted support of the intent while highlighting an opportunity for the FCA to leverage the existing regulatory framework.

Following provision of this feedback, we had expected finalisation of the rules by the end of Q2, however the volume of feedback received by the FCA and identification of specific challenges has led to an extension of the required time – a policy statement will instead be published in Q3. In the interim we are pleased to hear that the FCA has recognised the same challenges which we had raised, including those for disclosures, marketing and the treatment of multi-asset funds. As the FCA continues to finalise this regulation, we will, through collaborative industry initiatives, continue to provide constructive feedback that supports creation of an effective regime.

4.2 Responding independently to industry and regulatory consultations continued

United Kingdom Sustainable Investment and Finance Association (UKSIF): Net Zero Inquiry*

At climate conference COP26 in 2021, the UK declared it would become the first 'net zero financial centre' in the world. This included obligations for companies and financial institutions to produce decarbonisation plans in line with the transition to a low-carbon economy. In direct response to these announcements, the UK Sustainable Investment and Finance Association (UKSIF) produced a report, together with its member institutions, highlighting key actions that governments, regulators and financial institutions will need to take to achieve this goal.

As an UKSIF member, we worked with the association in Q1 2022, alongside our peers across the industry, to develop industry-supported recommendations that the Government and regulators should adopt to move the financial sector towards net zero at the necessary pace and scale. Through this work, we contributed to debate and provided thought leadership on matters including how to transform the real economy**, strengthening the role of investor stewardship, and the creation of a world-leading disclosures regime and green taxonomy.

FCA: Vote Reporting Group (VRG)

In 2022, in response to the recommendations from the Taskforce on Pensions Scheme Voting Implementation, the FCA created the Vote Reporting Group*** (VRG), an industry working group which we are members of, which has a mandate to improve approaches to voting in the industry. The group is tasked with designing a comprehensive vote reporting framework and template and developing recommendations on minimum vote reporting requirements for asset managers, ownership of the vote disclosure framework, and the storage and dissemination of vote reporting data.

DWP: Addressing the Challenge of Deferred Small Pots****

Small pot proliferation has been an issue since the introduction of automatic enrolment. As people switch employers, new pension pots are created and previous pots are often not consolidated. This fragmentation of pension saving makes it harder for individuals to manage the retirement plans, can be disengaging and reduces market efficiency as costs are duplicated across multiple pots.

We have been engaging with the Department for Work and Pensions (DWP) on Small Pots for a number of years, promoting the idea of automatic consolidation of small deferred pots, with appropriate safeguards. We have been supportive of, and contributed to, the Small Pots Cross Industry Coordination Group, which reported in June 2022. It found that while a number of consolidation models deserve consideration, new legislation will be required to enable scheme-initiated consolidation. In the most recent DWP call for evidence, we set out our support for a pot-follows-member solution, which we think better complements the existing automatic enrolment framework than other proposals for automatic consolidation.

FCA/The Pensions Regulator: Pensions Consumer Journey*****

This joint call for input from the regulators sought feedback on what else can be done to improve engagement and to help customers make better decisions and achieve better outcomes. We believe it is important for the industry and policymakers to take a holistic approach to long-term saving. In our feedback, we discussed, as we have for number of years, how the pensions consumer journey sits in the broader context of saving for later life, with other savings vehicles, inheritance, housing assets also playing a significant role in retirement outcomes. We also raised the issue that certain direct marketing rules can present a challenge for pension schemes wanting to engage members. It is important to be able to educate customers about their options and keep them up to date with their pension. But, much like the advice and guidance boundary, there is a line between direct marketing to customers, which requires permissions, and sending more general information to help with understanding and ensuring they have effective plans in place. The rules are particularly challenging in relation to customers who have been auto-enrolled as their joining journey does not usually include requesting marketing permissions.

FCA: Improving outcomes in non-workplace pensions******

The FCA was proposing to require firms to offer a default investment option for non-advised customers entering non-workplace pensions. We responded to this consultation and were supportive of these proposals throughout the process and welcome the changes which will now come into effect in December 2023. This will help customers who do not want, or are not well equipped, to make investment decisions. It will also aid some comparability between different non-workplace pensions and, crucially, between workplace and non-workplace. This should help make it easier for individuals to make informed decisions about where to consolidate savings and where to get best value for money.

DWP: Helping savers understand their pension choices*******

In 2022, the Department for Work and Pensions (DWP) released a call for evidence to gather insight on the support that members of occupational pension schemes need when making retirement decisions. We inputted to this consultation, in particular focusing on the current gap in regulation for trust-based schemes, where the FCA's investment pathways do not apply and we think a similar regime should apply, to help customers choose suitable investments when entering non-advised drawdown.

Other industry consultation participation

DWP, FCA, TPR: Assessing value for money in Defined Contribution schemes
Increasing and aligning disclosures across all types of defined contribution scheme so that employers can make better assessment for value for money.

DWP: Collective Defined Contribution
Broadening Collective Defined Contribution (CDC) provision beyond single or connected employer schemes to accommodate multi-employer schemes.

FCA: Core Investment Advice
Providing an advice regime that makes it easier for firms to provide financial advice for consumers at a lower cost.

DWP: Pensions Dashboard
Improving the awareness and understanding of individuals' savings, re-connecting them with any lost pension pots and changing how they plan for retirement.

FCA: Competition impacts of Big Tech on financial services industry
Understanding the competition impact that 'Big Tech' could have on the various areas of the financial services industry.

* Delivering a Net-Zero Financial Centre – UKSIF
** Refers to the production, purchase and movement of goods and services with an economy.
*** Vote Reporting Group | FCA
**** Addressing the challenge of deferred small pots: a call for evidence – GOV.UK (www.gov.uk)
***** FS22/3: Pensions consumer journey | FCA
****** PS22/15: Improving outcomes in non-workplace pensions | FCA
******* Helping savers understand their pension choices – GOV.UK (www.gov.uk)

CUSTOMER INSIGHT

5.1 MEETING CUSTOMER NEEDS

We have two core responsibilities in how we relate to our customers:

- Investing on customers' behalf and helping them plan for their long-term prosperity.
- Empowering our customers to see their pension investments as a central part of their financial planning, and to understand the control they can have over their money.

We receive a growing number of questions from our customers and the wider public regarding responsible investment issues. We leverage these insights to help drive customer engagement with their pension investments. It is also crucial that we find out what our customers think about their pensions and the investments they hold, so that we can help them fill any knowledge gaps and increase the likelihood of them having better long-term financial outcomes.

Understanding customer needs

We regularly carry out customer research to help inform our investment approach and better understand customers' views and priorities on ESG matters.

Find Your Impact (FYI) Tool

We also regularly conduct polls via the **Find Your Impact tool on the Scottish Widows App*** into workplace pension savers' views on ESG issues. The 'Have your Say' polling function allows us to learn from members about the issues that matter to them.

Transparency is a crucial part of ensuring we bring members with us on our journey to net zero and the FYI tool helps members understand how their pension investments impact the world around them. FYI enables members to view the impact of their pension savings in three areas (Carbon emissions, Waste, and Board Diversity), but also provides a breakdown by funds they invest in, as well as the companies in which they invest the most (aggregated across their total savings). Each has a traffic-light rating and numeric score. Towards the end of 2022, we published a pilot report looking at early learnings from the limited number of pension scheme members who had access to the tool in the first year since launch. Average sample size for poll questions was relatively small for 2022. As the tool is rolled out to all pension schemes we look after, we expect more statistically-viable results in future reports as the tool matures and usage increases. The 'Have Your Say' function is designed for members to regularly see new questions, allowing them to share their thoughts on key ESG issues, emerging themes, or company-specific developments, as well as a few summary of their previous poll responses. Below are a few highlights from the pilot report:

THE 'HAVE YOUR SAY' FUNCTION RESULTS SHOW:

96%

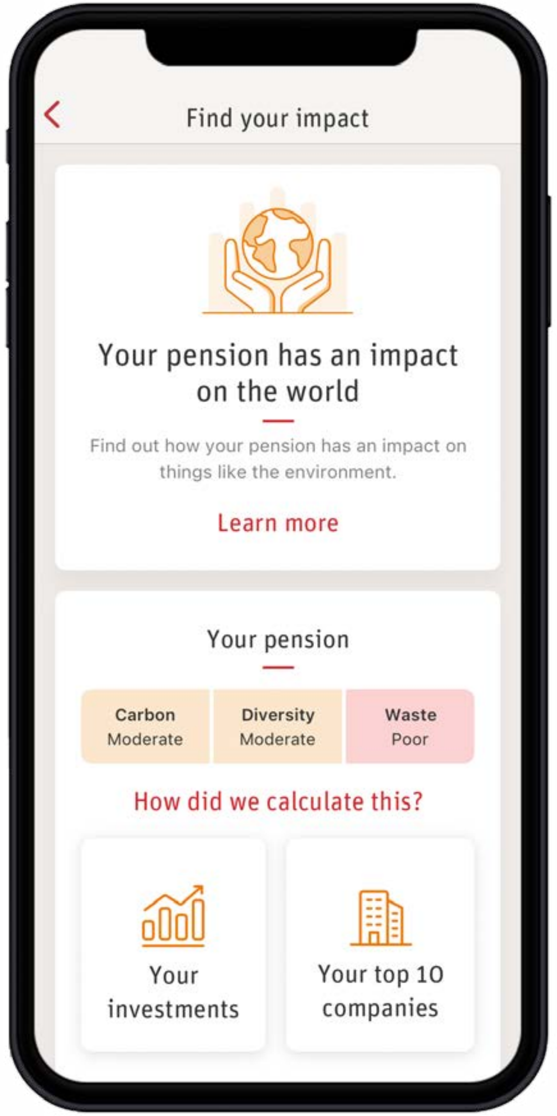
of respondents are keen for companies to disclose more about their environmental impact

62%

of respondents said that companies that have good levels of board diversity are more attractive investments

95%

of respondents agreed that companies should consider, measure, and report on their impact on nature loss and biodiversity degradation



* Why we invest responsibly (scottishwidows.co.uk)

5.1 Meeting customer needs continued

Voting guidelines – client input

Before we published our Voting Guidelines*, we surveyed our corporate clients and hosted a workshop to check our approach was in line with our clients' expectations. We repeated the survey with refreshed questions in 2022. While we received a smaller number of responses compared to when we initially launched the guidelines, they were unanimous in agreeing on the importance of engaging with companies and exercising voting rights on key ESG issues. Encouragingly, there was also blanket support for where we have enhanced our guidelines such as biodiversity, human rights and living wage. All respondents also agreed that there should be voting action when a company has no commitment to mitigating nature-related impacts when it is material to their business.

Green Pensions Report

The research we carried out for our first **green pension report****, which uncovers the changing priorities of employees and employers when it comes to their future finances, found that 83% of UK employees see climate change as an important issue. It found a clear contrast between employers and employees when it comes to their understanding of green pensions and the huge impact they could have on the environment. Many employees are simply not aware of how their pension may be delaying any progress in working towards a sustainable future – even though today's workforce expects its employers to take an active stance on social and environmental issues. There are clear differences when it comes to large and small businesses, as well as workers earning different wages.

The statistics in the picture below highlight a massive expectations gap. While so many employees think climate is an important issue and think that it is important pensions are invested sustainably, only 28% of large business and 8% of small and micro businesses have sustainable funds as their pensions default fund.

After years of slow real wage growth, the UK has seen multi-decade high inflation that has pushed up the cost of necessities and eroded households' capacity to prepare for retirement. The rapid inflation means a declining median real wage since February 2022. Collated with the economic fallout from the war in Ukraine, inflation is not expected to return to the Bank of England's target of 2% for at least another few years.

* 60631.pdf (scottishwidows.co.uk)
** Green Pensions Report – 2022 (scottishwidows.co.uk)

GREEN PENSIONS REPORT REVEALS EXPECTATIONS GAP

Today's workforce expects employers to take an active stance on environmental issues

95%

of employers across sectors are concerned about climate change

72%

place importance on their employer investing their pensions sustainably

But few employers currently offer sustainable options in their pensions

8%

only 8% of micro and small businesses offer green pensions as standard

28%

only 28% of large businesses offer green pensions as standard

5.1 Meeting customer needs continued

Retirement Report*

Scottish Widows published its retirement report in 2022 which examined the cost of living crisis, the effects of rising costs on spending and savings, and the impact and it has on different groups.

Effects on Spending and Savings

Increasing inflation on top of the 'lost' wage growth has left households facing the prospect of having to cut back on spending and potentially on their pension contributions. Groups of all ages have reported being concerned about the rising costs of living, with 76% of respondents having cut back on leisure, holiday spending, food, and even pension contributions in order to cope.

Impacts on Different Groups

Although rising living costs may impact everyone, research suggests that the impacts differ between different socio-economic and ethnic groups. Our research suggests that all minority ethnic groups are more concerned about rising living costs compared to those who are in the White British ethnic group. Pakistani (53%) and black (48%) ethnic groups stand out in terms of being the most concerned. As a result, those in minority ethnic groups are more likely to minimise their pension contributions.

Women and Retirement Report

Scottish Widows published its annual Women & Retirement Report** in 2022 which identifies that women continue to earn far less than men, especially as they get older, and they tend to take on more part-time work and face a divergence from men in their career prospects.

These differences are a main driver of the gender pension gap in retirement and compound the challenges women face in funding typically longer lives with greater social care needs. Our research suggests that the cost of living crisis is having a disproportionately worse impact on women than society at large. Women are more likely to be concerned than men, with particular groups being worse off, and more likely to be cutting back on essentials such as food. These pressures risk exacerbating existing gender gaps in financial situation and retirement preparations.

There are big and well-known differences in all forms of wealth, including pensions, between men and women. These are currently smaller for younger generations who are still in the early stages of building their wealth, but remain persistent in both expectations and preparation for retirement.

* 2022 Retirement Report (scottishwidows.co.uk)

** 2022 WOMEN & RETIREMENT REPORT (scottishwidows.co.uk)

5.2 COMMUNICATION AND ENGAGEMENT

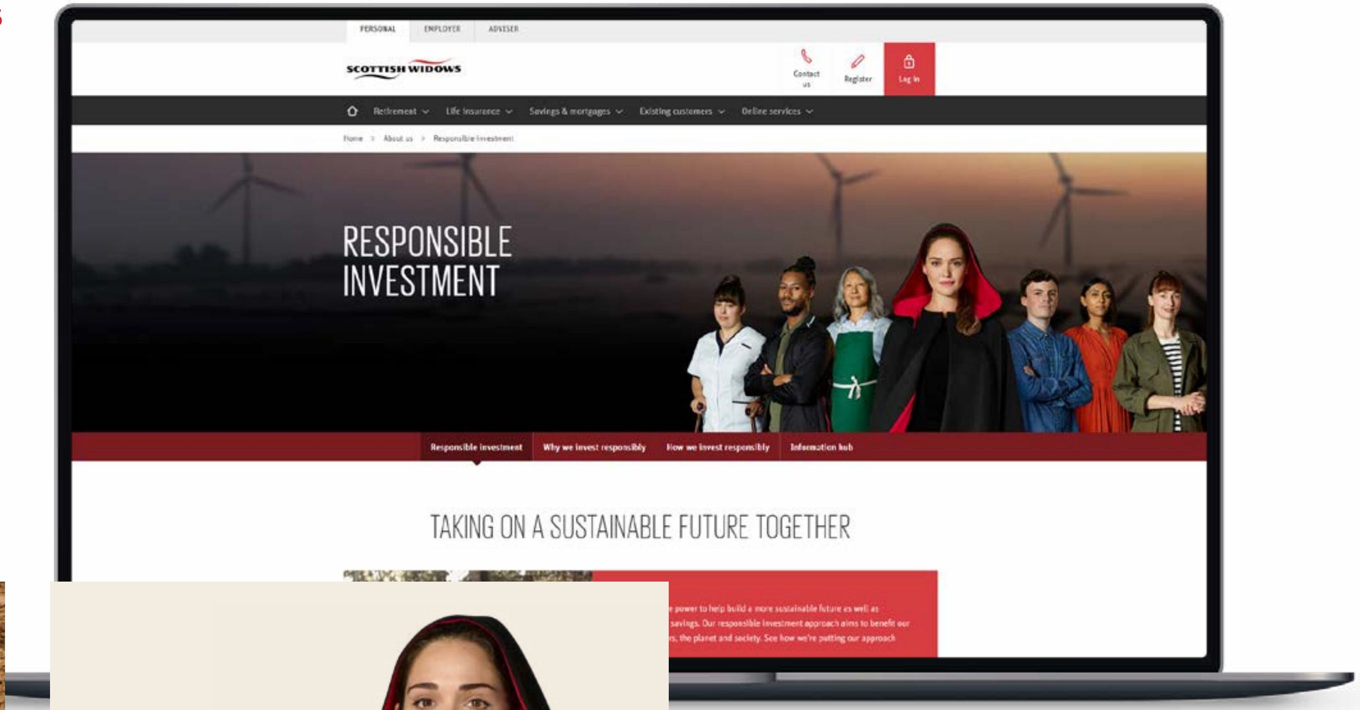
We believe it is important to bring customers on a journey with us as we undertake stewardship and responsible investment activity on their behalf.

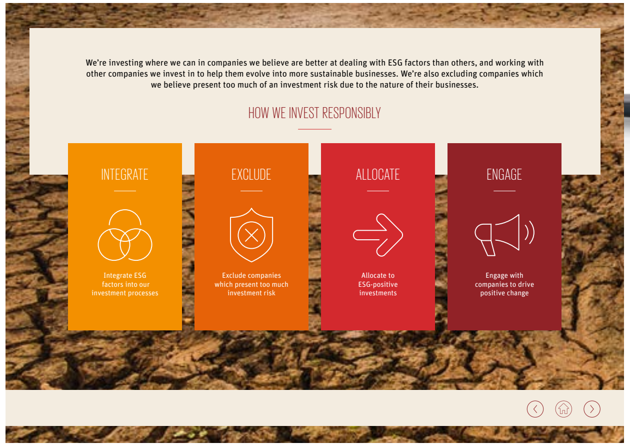
From our research, we know there remains a lack of knowledge and understanding not only of this topic, but generally around investing too. So we focus on helping our customers understand how their pension is invested and how and why we've evolved our investment approach to fully embrace responsible investment practices to allow us to manage risks, returns, and ESG factors in a more effective way in our pension funds to safeguard customers' long-term savings.

Engaging customers in their pension investments

We understand how important it is for customers to understand how we invest their pension savings to encourage better engagement. To that end, we produce **easy-to-understand guides** to help them understand our approach, such as our brochures on how we integrate ESG factors into our workplace pension default solution and our personal pension options.

We overhauled our Responsible Investment website* in 2022, to create a better, more engaging narrative and user journey and, to keep our customers up-to-date with new developments.

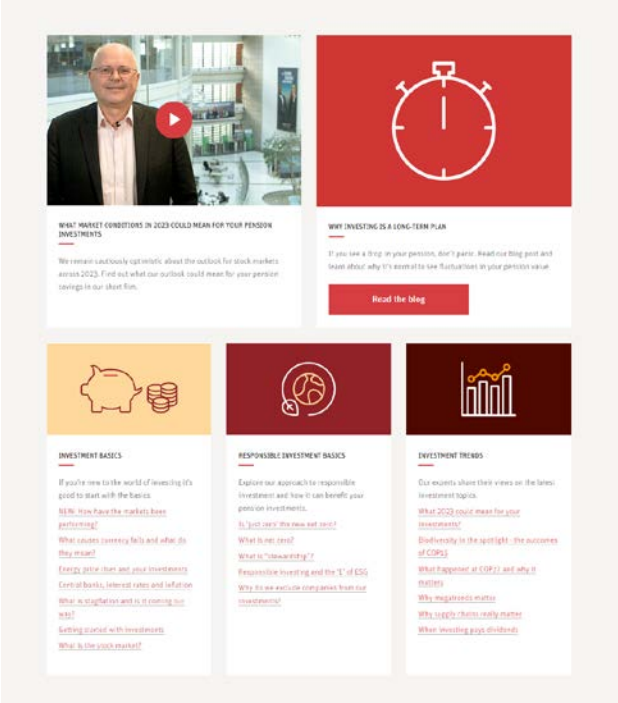




* Responsible Investment | Media Centre | Scottish Widows

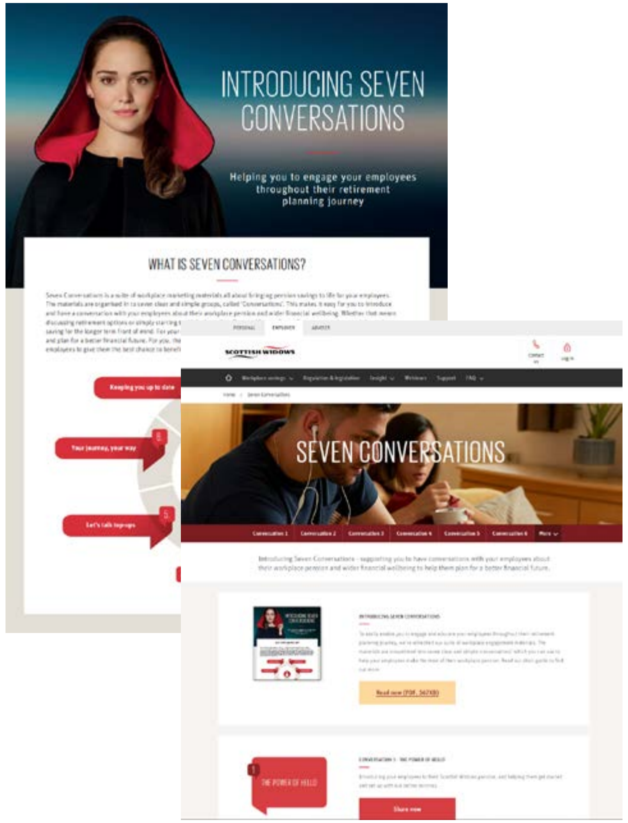
5.2 Communication and engagement continued

Alongside this initiative, we've introduced **Investment Essentials*** for our customers which delivers regular educational and topical investment thought leadership content in the form of blogs and videos, with a focus on responsible investing.

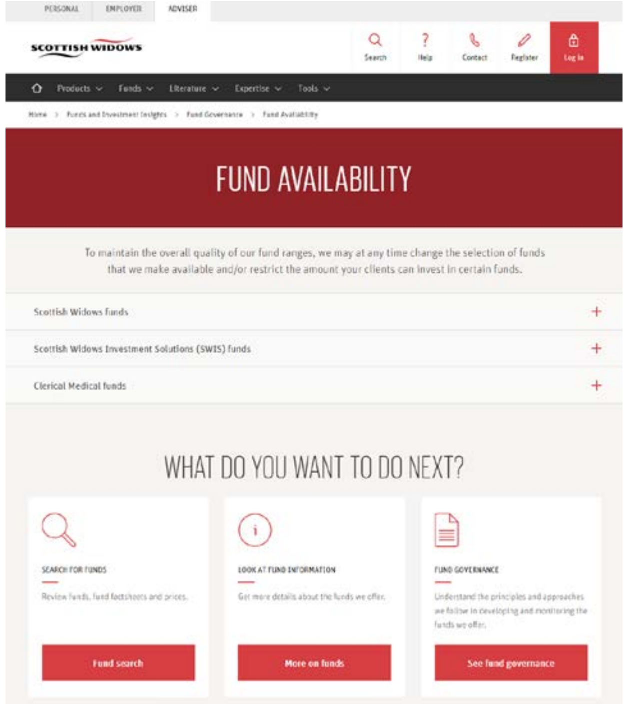


We also promote our in-depth research** to help customers better understand key topics, like what a 'just transition' is in relation to the transition to a sustainable future. And, most importantly, why these focus areas are important in how we manage investments in their pensions.

Our workplace pension **customer engagement programme**, 'Seven Conversations'***, is a suite of workplace marketing materials all about bringing pension savings to life for members of our workplace pensions. It is shared with employers to help make it easier to introduce and have a conversation about not only their pension, but their wider financial wellbeing. One of these 'conversations' focuses on understanding pension investments and understanding the ESG impact. We have dedicated resources on responsible investment and sustainability, helping employees engage with their retirement savings and understand how they can impact the world around us.



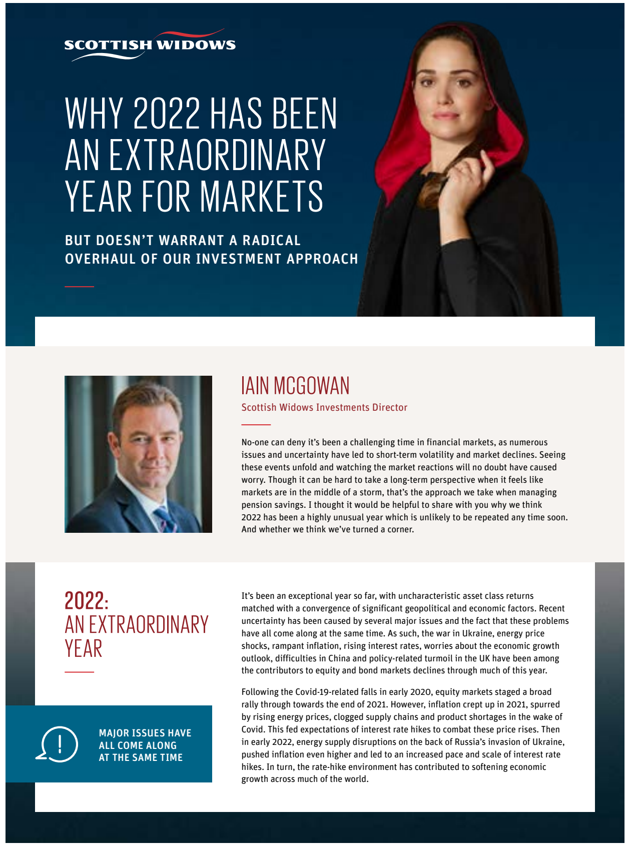
As well as providing customers with information on our **Fund Changes Hub******, we regularly communicate with employers and advisers on responsible investment, policy and proposition developments and milestones and encourage them to share these with their clients or employees. Examples include our Climate Action Plan, the extension of our exclusions policy and why we're divesting from tobacco companies and propositional enhancements such as our introduction of a new global environmental fund and changes to existing funds, like our property fund, to integrate ESG elements.



* Investments Expertise Hub | Pensions | Scottish Widows
** Information hub | Scottish Widows
*** Seven Conversations | Employer Hub | Scottish Widows
**** Fund Changes | Global | Scottish Widows

5.2 Communication and engagement continued

Market volatility can be unsettling for customers, and 2022 saw a lot of uncertainty leading to sudden falls in pension values. We responded with a campaign to reassure customers with written and video content explaining what was going and encouraging people to take a longer-term view.



Pensions Engagement Season (PES)

In September 2022, the UK government, ABI, and PSLA launched Pensions Engagement Season (PES)*, a new industry initiative which brought together leading voices in the retirement space to empower customers to engage with their retirement planning. However, the UK was entering a cost of living crisis meaning pension contributions were not going to be a priority for people. As reducing pension contributions could be detrimental to people's retirement, it was crucial for us to create a campaign in line with PES, that helped build awareness of the things that could be done immediately to save money.

Our campaign question, 'Can you do more with your pension right now?', asked people to consider their pensions, whether they could be doing more with it, besides increasing contribution, and encouraged them to take action now. We gave our customers clear signposts to engage with their pensions by taking three actions:

1. Check – what pensions you have by tracking down forgotten pension pots.
2. Manage – what you've got by looking at options to combine your pensions in one place.
3. Control – stay in control of your pension admin.

We ran an integrated campaign to amplify the PES initiative with our workplace employees too. To do this, we armed advisers and employers with content and tools to share with their clients and employees. We also set up virtual experiential events to directly engage with employees in their workplace, making it easy for them to take the next steps.

* Take control of your pension | Scottish Widows

OUR CAMPAIGN RESULTED IN:

1st

we were ranked 1st on customer awareness against our competitors

75%

of workplace employees reported being more inclined to engage with their pensions

88%

of customers said they would take action after seeing our campaign

62%

understood their pensions better

GOVERNANCE

6.1 COMMITTEE STRUCTURES

In recognition of our strategic priority to be a responsible business, the Insurance Board*, approves our responsible investment and stewardship strategy, including alignment to the Stewardship Code's expectation that our purpose, beliefs, strategy and culture enable effective stewardship, and strategic developments on responsible investments. The Responsible Investment team produces regular updates to the Board, its sub-committees and executive committees, on our progress in developing Scottish Widows' stewardship approach and progress towards embedding responsible investment principles.

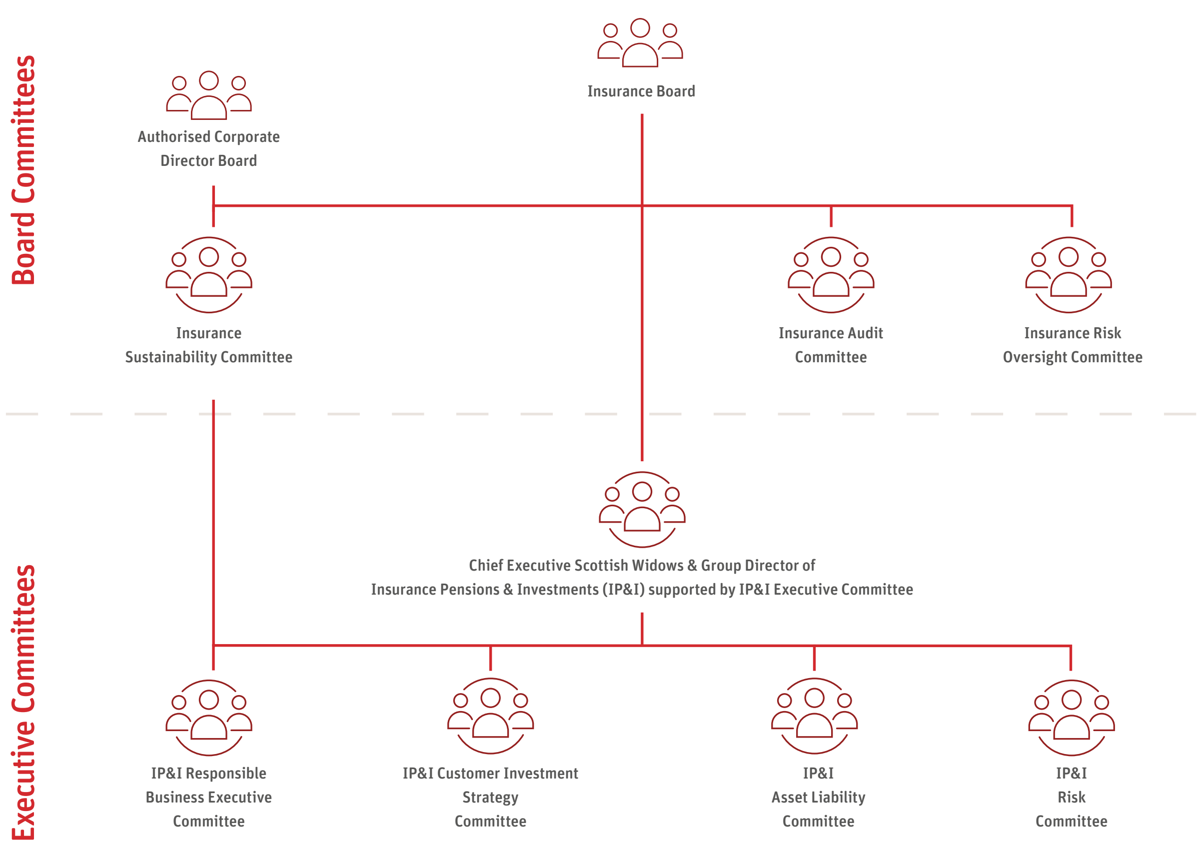
The Board of Directors as a whole is responsible for sustainability. In 2021, the Board of Directors established an Insurance Sustainability Committee ("ISCO") during a period when we were developing a new approach to sustainability which required specific focus and challenge. This was a committee comprised of members of the Insurance Board and the Authorised Corporate Director** (ACD) Board.

Our approach to sustainability and responsible investment has developed significantly since then and sustainability is now embedded as a core part of our committee governance as outlined below. The Board delegates the day-to-day governance of related operational activities to the appropriate committees within Scottish Widows.

Authorised Corporate Director Board

The ACD Board chaired by an Independent Non-Executive Director, has collective responsibility to promote and assess the long-term sustainable success of Authorised Fund Managers, Scottish Widows Unit Trust Managers Limited and HBOS Investment Fund Managers Limited ("ACD Companies").

OUR GOVERNANCE STRUCTURE (AS AT 31 DECEMBER 2022)



* The entities which comprise the Insurance Board are Scottish Widows Group Limited, Lloyds Bank General Insurance Holdings Limited, Scottish Widows Financial Services Holdings, St Andrew's Insurance plc, Scottish Widows Limited, Lloyds Bank General Insurance Limited, Scottish Widows Administration Services Limited and Scottish Widows Administration Services (Nominees) Limited.

** The entities which comprise the ACD Board are Scottish Widows Unit Trust Managers Limited and HBOS Investment Managers Limited.

6.1 Committee structures continued

Insurance Sustainability Committee

The Board of Directors as a whole was responsible for sustainability and, throughout 2022, had oversight via the Insurance Sustainability Committee chaired by an Independent Non-Executive Director. The Insurance Sustainability Committee was responsible for overseeing the development, delivery and embedding of the Insurance Group's ESG Strategy and its management of climate risk. The Insurance Sustainability Committee met six times in 2022.

IP&I Responsible Business Executive Committee

The IP&I Responsible Business Executive Committee is chaired by an executive director, Lloyds Banking Group General Insurance, Protection and Investments Director (responsible for our pensions and investments business). It is responsible for recommendation and delivery of the ESG strategy for the Insurance Group (including stewardship activities across Scottish Widows' investment book and other sustainability goals such as operational decarbonisation). The IP&I Responsible Business Executive Committee provides direction for the ESG Strategy and recommends this to the Insurance Board.

IP&I Customer Investment Strategy Committee

The IP&I Customer Investment Strategy Committee chaired by an executive director, is responsible for the formulation, review, recommendation and implementation of Investment Strategy; oversight of the execution of strategic investment decisions; oversight and challenge of fund performance across all customer funds within Insurance and review & approval of Strategic Asset Allocation Investment positioning (within Board limits).
This includes approval of all ESG investments-related activities e.g, Exclusions Policy, launch of passive screened indices and the UK ESG Bond fund.

Ongoing Monthly Oversight

Scottish Widows' runs a monthly ESG forum that monitors our core deliverables closely, giving the team an opportunity to escalate any risks or issues well in advance.

During 2023, we will continue to review and refine our committee governance to ensure ESG is fully embedded across the committee structure and into all BAU considerations.

Additional Independent Oversight

The Independent Governance Committee ("IGC"), operates independently of Scottish Widows. The majority of members and the Chair are independent as required by the rules set out by the Financial Conduct Authority (FCA). The IGC represents the interests of customers of Scottish Widows workplace pensions and investment pathway products. It has a duty to consider and report on the adequacy and quality of Scottish Widows' policies on ESG financial considerations, non-financial matters and stewardship. The IGC Chair provides a regular report to the Insurance Board.

The Scottish Widows Responsible Investment Team present to the IGC on ESG and stewardship matters at their regular meetings, to help them assess customers' exposure to ESG risks and understand how we take account of ESG opportunities, while being active and responsible stewards of our customers' pension savings. This provides an additional layer of governance of our sustainability strategy and activity. Each year, the IGC is required to assess the value for money customers receive within the products they oversee and publish their findings in a report. This assessment includes how well the funds in which these policies are invested are managed and whether they're delivering what they are supposed to. Feedback from the IGC is very valuable to us and we work hard to ensure we incorporate any recommendations that improve the value for money we offer our customers.

Trustees of the Scottish Widows Master Trust (SWMT), with a fully independent board and chair also have independent oversight of our responsible investment and stewardship activities insofar that they relate to the SWMT's investments. Across 2022, the IGC and SWMT have continued to provide feedback across a range of our key deliverables on RI and ESG matters.

Review and monitoring of our policies

It is critical that our Stewardship and Exclusions Policies are subject to robust review and monitoring, as they drive our activity in this area. Prior to being adopted, our policies go through a rigorous review process by various functions, including Risk, Legal, Responsible Investment and others, including several of the governance committees mentioned above. For example, during the process of developing our Stewardship Policy we took an early draft to our Policy Forum for its input, and developed subsequent drafts through an iterative process of collaboration.

For continued effectiveness, all relevant new policies and existing policies at annual reviews, are approved by the accountable Executive Owner and the approval noted at the relevant Executive Committees. Our Risk teams regularly provide their input and expertise to our responsible investment and stewardship activities, including policy updates and reporting, to ensure that we follow all the necessary internal processes, are in line with the regulatory requirements and act appropriately to achieve the best outcomes for our customers. This close working relationship with our risk teams has allowed us to develop more robust control frameworks for all of our deliverables, including the production of our Stewardship Report and the annual review of our relevant policies.

Case study

In 2022, we embedded and followed new processes and made enhancements following advice from an internal audit of our responsible investment and stewardship activities.

This includes further development of this Stewardship Report, which has also had an additional layer of scrutiny from our first line risk teams in relation to any greenwashing risk using their assessment framework, in additional to the regulatory risk oversight. Our second line risk teams also closely monitor if we have followed the necessary process in developing the report, have all the related evidence and the necessary sign offs on the disclosures and statements made. Based on their review, the report is then taken to two executive and Board level committees, IP&I Responsible Business Executive Committee for endorsement, which reviews it twice, and then the Insurance Sustainability Committee for a secondary review and noting, and then finally to the IP&I Board for approval and sign off.

6.1 **Committee structures** continued

OUR APPOINTED INVESTMENT MANAGERS

We expect the activity of our core appointed investment managers to be independently assessed by the UN PRI and ask them to share a copy of their Assessment Reports with us. We also have very clear expectations for them to become signatories to the Stewardship Code, as outlined in Section 3.

Over 2022, we engaged with Schroders, BlackRock, State Street and Hermes to ensure that their stewardship activities were being carried out in line with our expectations. We had over 30 review meetings with these managers and we continue to collaborate regularly with them to strive for better stewardship of our invested assets.

Regulators and industry bodies

We have regular dialogue with the Financial Reporting Council, Financial Conduct Authority, Department for Work and Pensions, other government departments, regulatory bodies and organisations responsible for setting industry standards for products and customers, to understand how we are performing against regulatory standards and market best practice. This dialogue also enables us to collect feedback to improve our policies, activities and reporting.

We also regularly contribute to working groups with industry bodies such as IIGCC*, UK Sustainable Investment and Finance Association (UKSIF), and Occupational Pensions Stewardship Council (OPSC), among others. We have detailed these industry collaborations in Section 4.

Case study

As of Dec 2022, all Tier 1 and 2 managers were signatories to the UK Stewardship Code 2020, and of Tier 3 only two of the 35 managers, are not yet signatories. We are currently engaging with them to understand how best to resolve this. These seem to be managers which are non-UK domiciled with limited operations in the UK.

* The European membership body for investor collaboration on climate change. IIGCC works with business, policy makers and fellow investors to help define the investment practices, policies and corporate behaviours required to address climate change. IIGCC – The Institutional Investors Group on Climate Change

6.2 OUR RISK MANAGEMENT APPROACH

OVERVIEW OF OUR RISK MANAGEMENT FRAMEWORK

The Insurance Group operates an Enterprise Risk Management Framework (RMF), designed to ensure a robust and consistent approach for managing risk, structured around six components.

Role of the Board and Senior Management

Key responsibilities of the Board and senior management include: setting Insurance Group's strategic aims; setting risk appetite and risk policies; cascade of delegated authority and effective oversight in accordance with the agreed risk appetite.

Risk Culture and the Customer

Supporting the formal frameworks of the RMF is the underlying culture, or shared behaviours and values, including tone from the top, clear accountabilities, effective communication and challenge and an appropriately aligned performance incentive and structure.

Risk Appetite Overview

We define Risk Appetite as "the amount and type of risk that we either prefer, accept or wish to avoid" and this aligns to the overall business strategy: In 2022 we further developed Climate Risk appetite statements.

Risk and Control Self-Assessment

An enterprise-wide framework for the identification, measurement, management, monitoring and reporting of risk is in place and covers the full spectrum of risks that we are exposed to including Climate Risk.

Risk Governance

Monthly reporting of risk exposures and the control environment enables monitoring of performance against Risk Appetite, and summarises key changes to the RMF profile. Insurance also operates an Insurance Policy framework, which defines mandatory requirements for risk management and control and is aligned to the agreed risk appetite.

Three Lines of Defence model

The RMF is implemented through a 'Three Lines of Defence' model distinguishes between risk management, risk oversight and risk assurance. It defines clear responsibilities and accountabilities and ensures effective independent oversight and assurance activities take place.

6.2 Our risk management approach continued

EMBEDDING CLIMATE RISK IN OUR RISK MANAGEMENT FRAMEWORK

We have adopted a comprehensive approach to embedding climate risk in our Enterprise Risk Management Framework through:

- Consideration of climate risk as its own principal risk, to drive dedicated focus and a consistent approach, while enhancing Board-level insight; and
- Integration of climate risk into our other principal risks, to ensure comprehensive consideration across all aspects of our business activity.

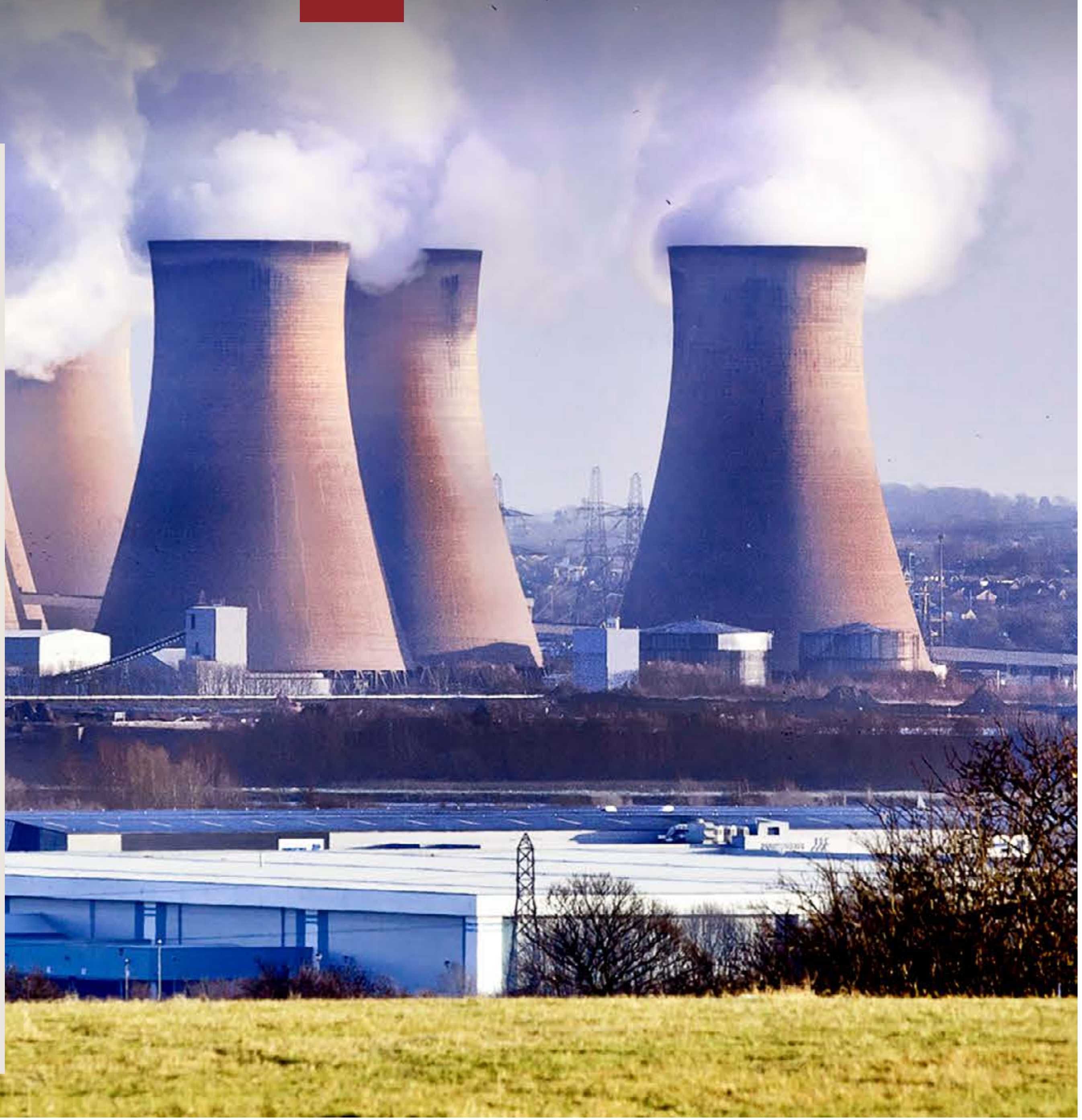
As its own principal risk, climate risk captures the risk that we, or our customers, experience losses as a result of climate change.

The Group Climate Risk Policy is structured around eight principles, with corresponding requirements designed to support achievement of these principles. It also supports our ambitions relating to limiting climate change and the relevant regulatory requirements, including the TCFD recommendations. We have also developed Insurance Climate Risk Procedures to better reflect local practices and processes. During 2022, we enhanced our control environment and created new risks around Climate Disclosure / Model risk; Greenwashing risk; Risk of failing to meet Net Zero, as well as enhancing existing risks around physical and transition risk, and regulatory compliance. Further information on our eight principle can be found on our Information Hub https://www.scottishwidows.co.uk/about-us/responsibleinvestment/information-hub.html

Risk identification process

To effectively identify all climate-related risks, several different approaches are used.

- **Emerging risk process:** Our approach to risk identification includes consideration of environmental factors, including climate change, among the external sources of risk to be proactively identified.
- **Horizon scanning:** Scottish Widows performs horizon scanning activities across several areas. Examples of the horizon scanning performed include:
  - **Weather and physical impacts;**
  - **Demographic developments;**
  - **Regulatory developments;** and
  - **Legal risks.**
- **Scenario analysis:** We have undertaken climate stress testing the medium-term business plan and projections of financed emissions. We continue to develop our scenario analysis capability in recognition of the external environment and are working with external experts to develop a model for projecting the impacts of climate risk.
- **Medium-term planning:** Over 2022, we have continued to develop our understanding of the risk and opportunities arising from climate risk and how they may impact on our medium-term business plans (1–5 years). This has included the following considerations:
  - Risk of increased weather events and the potential impact on our business
  - The impact of our strategy under different climate scenarios
  - Opportunities for improved customer outcomes from investments with positive ESG credentials; and
  - Consideration of required investment in business processes, data and tools to aid monitoring and reporting of key climate metrics.



6.2 Our risk management approach continued

RISK APPETITE

The Risk Appetite Framework has been extended to include specific Climate Risk Appetite Strategy, preferences and metrics. The Insurance Board approved a Climate Risk Strategy Statement and statements expressing our preference to avoid risks arising from climate risk:

"Climate risk is the risk that the Group experiences losses and/or reputational damage, either from the impacts of climate change and the transition to net zero ('inbound') or as a result of the Group's response to tackling climate change ('outbound'). We have no appetite to fail to proactively manage the risks and opportunities for our business as a result of Climate risk. We will take action to support the Group and our customer transition to net zero, and maintain our resilience against the risks relating to climate change."

Existing Risk preference statements have been updated to explicitly reflect the physical aspects of climate risk in underwriting risks and new statements have been added formalising our intent to:

- Avoid exposure to physical risk, or where this is not possible, appropriately allow for the risk.
- Minimise exposure to transition risk, while recognising that the ability to meet our targets is dependent on changes in the wider economy.
- Avoid litigation risk through failing to meet customer expectations.

Board and committee responsibilities

ESG and climate change-related risks, opportunities and stewardship are business matters which are, for the purposes of decision-making, governed via the existing structure of legal entity boards, board committees and executive management/committees.

Please see Section 6.1 for more information on our governance structure.

Risk in customer funds

We use a variety of sources for reviewing and overseeing market-wide and systemic risks for our customer funds. Any major issues or risks are reported to our Insurance Customer Investment Strategy Committee (ICISC). As part of the ongoing strategic asset allocation review process, market forecasts and risks are assessed and discussed on a quarterly basis with our core external investment managers and more frequently if market-wide issues emerge.

Our role relates primarily to strategic asset allocation and fund selection in multi-asset funds; and to setting mandates for single asset-class funds. With multi-asset funds, our discretion has historically related to traditional asset allocation, but has more recently extended to the integration of ESG considerations, initially through the allocation to low-carbon equity investments.

On single asset class funds, we outsource stock selection (within mandated parameters) for actively managed funds. It is, therefore, the responsibility of the investment manager to consider risks in relation to specific stocks, but within the context of overall risk budget limits. The constraints are set out for customers in a fund's Prospectus and/or other regulated documents and reflected through a fund's mandates and related documents.

Regular Investment Implementation and Industry Update papers, reviewed at ICISC, draw from research carried out in our Investments team and also by our core external managers. Over 2022, these focussed on our response to market conditions, liquidity management, inclusion of ESG in fund value assessments, responsible investment and net zero, reflecting both our engagement internally and with stakeholders such as industry bodies, regulators and trustees.

Risk in shareholder funds

In our shareholder investments we primarily identify and respond to market-wide and systemic risk by investing in geographies, sectors and structures that we have extensive experience of, making use of the wider knowledge and expertise of our strategic appointed investment manager Schroders to identify potential systemic risks. We review our shareholder investment strategy annually, considering changes in investment drivers, risks and regulations and it is subject to full internal governance.

We manage climate-related risks, which we consider to be a systemic risk, in our shareholder funds in two main ways:

- Market-traded assets managed on our behalf by our appointed investment managers operate in accordance with our mandates (including adherence to our Stewardship and Exclusions Policies) as well as being subject to the manager's internal ESG assessment. We continue to work with managers to develop a suite of ESG-related metrics which will enhance our existing oversight processes.
- With regards to our illiquid loan investments book, we continue to develop data coverage and quality as developing better quality emissions data for these loans will assist in both managing the current portfolio as well as informing strategic decisions for future investments in due course. Our loan investments are also aligned to the Group's published sector statements*.

Effectiveness of our risk management approach

The Risk Management Framework provides a robust and consistent approach to risk management across the organisation with mechanisms for developing and embedding risk policies and risk management strategies, which are aligned to the risks faced by the business. This in turn drives the risk profile of the business in line with risk appetite and through good risk-reward decision making.

Our approach to ESG risk management is continually developing to best meet the needs of our customers and the business, recognising that external expectations, and understanding of the impacts of climate risk are continually evolving. We expect to use continuous risk management which is integral to our RMF, to be able to reflect and adapt to new and emerging risks in this space.

* LBG External Sector Statements (lloydsbankinggroup.com) – updated link

6.3 ENABLING OUR COLLEAGUES TO DELIVER EFFECTIVE STEWARDSHIP

We have a dedicated Responsible Investment team of eight full-time colleagues, grown by a full-time colleague in 2022, and supplemented where required by secondments from within the business and externally. The team is led by our Head of Responsible Investments and Stewardship, with dedicated Investment and Stewardship and Responsible Investment leads. While the dedicated team continues to have oversight of our responsible investment and stewardship activities, we have embedded this thinking across our whole Investment division and other business functions like Risk, Legal and Finance, so that it is now a consideration for all aspects of our business, supplementing this with additional hires where needed, including the Investment Office.

2022 also saw the creation of a new Head of ESG position, in addition to a full time role, to support our Executive Leadership team in implementing our own business sustainability strategy across the division. We will grow the team further over the course of 2023.

Embedding sustainability into our culture through colleague engagement and training

Colleague Advisory Panel

As a business we want to test if we can ensure our propositions, decisions and cultural initiatives aren't too heavily influenced by groups of individuals who think in the same way. Based on this principle, in July 2022 we launched our Investment and Insurance Colleague Advisory Panel. As a business we believe it's important that a wide and balanced range of views form our thinking on important topics. We want to make sure that our decisions reflect the variety of viewpoints and experiences that make up our colleague and customer base, as well as the wider society we serve. By creating the Colleague Advisory Panel, it's our aim to encourage positive discussion, debate and challenge that harnesses a diverse range of perspectives.

The panel consists of 10 colleagues from across our Investment and Insurance business who meet monthly to review a variety of content to provide a cognitively diverse view and challenge whether the presumed approach on any content taken to them is the right one. Colleagues were selected for the panel using an anonymised recruitment process, which focussed more on colleagues' way of thinking, rather than a traditional view of CVs and experience. This was conducted through a questionnaire, which asked colleagues why they thought the panel was important and what topics they thought should be considered. The result of this is a panel which is 50% male/female, 20% Black, Asian and Minority Ethic spanning a variety of levels of seniority and dispersed across our Investment and Insurance business.

To date the panel has engaged in a variety of content including Motor Insurance strategy, ESG voting guidelines, Consumer Duty and Cost of Living and will continue to review items of strategic and cultural importance. The panel's input to date has provided additional thoughts for consideration for those presenting as well as validating existing thinking.

Colleague Training

We remain committed to embedding our sustainability values at all levels of the business as a key component of Scottish Widows' beliefs, strategy and culture to ensure it is considered in day-to-day decisions made across a wide range of business functions.

To achieve this, the Responsible Investment team delivers regular training sessions, and communications, across business functions to support colleagues to better understand customer needs and market expectations with regards to responsible investment and ensure they are aware of our strategic plans and developments.

We have also provide external training opportunities for colleagues. For example, a number of colleagues from Investments, Finance, Audit, Risk, Compliance and Sustainability took part in intensive, in-depth training by Zoological Society of London (ZSL) at the start of 2023 covering commodities-related deforestation and nature risks and their link to financial services and investments. This training helped to start building our understanding of nature and biodiversity-related risks and opportunities – a broad and nuanced area which is fairly new to the financial services industry. We also support colleagues who have an interest in taking their sustainability studies further by funding them to take the CFA Certificate in ESG Investing and Certificate in Climate and Investing.

To ensure all Scottish Widows employees have a basic grasp of sustainability, there is a Group training module which is updated annually for all colleagues to complete covering climate risk and its link to our business strategy. To complete the programme and encourage colleagues to embed the learning they are required to complete a 'Feeling Inspired' survey to develop a personal action plan to live and work more sustainably. Employees also have access to tools like a 'Carbon Calculator' to help them assess their carbon footprint, and have the opportunity to make personal choices via our Colleague Sustainable Car Scheme and variable employee benefits focused around sustainability, called 'Conscious Choices'.

We are also building a detailed training plan to support our business unit in building sustainability capability. This will include a review of colleagues that require sustainability learning and development to successfully deliver in their roles and colleagues who will require sustainability capability in the next 12-24 months to address changes in business requirements. This will support us in creating robust and structured development plans as we make the transition to a low carbon economy.

6.3 Enabling our colleagues to deliver effective stewardship continued

Embedding diversity into recruitment

As we have outlined, Board Diversity is one of our key priorities for the companies we invest in. We believe better decisions are made when there is a range of perspectives around the table. We are dedicated to delivering this at Scottish Widows too, and it goes broader than the Board room and across the organisation. Our Responsible Investment team has a 50-50 female-to-male gender split and has representatives from different backgrounds covering culture, nationality, socio-economic background, age, religion etc. To ensure we continue to recruit diverse talent we have carried out research into unconscious bias, the results of which have been applied to our recruitment process to ensure inclusivity.

As mentioned in last year's report, in June 2021, the Scottish Widows Board published its standards on board diversity. This was re-confirmed in April 2023. On gender diversity, female directors accounted for 33% of the Board which is in line with the Board's stated objective and the Hampton-Alexander objective*. The Board has also met the objectives of the Parker review** for at least one black, Asian or minority ethnic Board member.

The Board also places emphasis on ensuring diversity in senior management roles at Scottish Widows and supports Lloyds Banking Group's (LBG) objective of achieving 50 % of senior roles held by women and 13 % of senior roles held by black, asian and minority ethnic colleagues by the end of 2025. Scottish Widows contributes to the broader Insurance, Pensions & Investments (IP&I) divisional targets that supports the LBG target.

For 2022, the core IP&I divisional contribution was 39.1 % (an in-year increase of 3.5 %) for senior roles held by women, and was 5.2 % (an in-year increase of 1.4 %) for senior roles held by black, asian and minority ethnic colleagues. For 2023, the core divisional goal is 41.0 % for senior women, 7.2 % for senior black, asian and minority ethnic colleagues.

We support our colleagues through a wealth of policies, practices and learning for continual personal growth in an organisation that embraces diversity of talent, creativity, skills and thinking amongst our teams. Progress on this objective is monitored by the Insurance People Committee and built into the assessment of executive performance as part of their balanced scorecard.

For recruitment at senior manager level and above, we insist on gender diversity and have an expectation for hiring managers to actively encourage ethnic diversity in shortlists. Final recruitment decisions are made purely on merit but introducing the requirement for diversity in recruitment processes ensures that we are giving equal opportunity for individuals to demonstrate t he value they could bring to our organisation.

Furthermore, after successfully running our 'Growth Through Diversity' development mentorship programme aimed at black, asian and ethnic minority Scottish Widows employees in 2022, we will be continuing with it for 2023.

Embedding sustainability into performance reviews

As well as our commitment to upskilling our workforce, we had introduced sustainability-related objectives in our performance review process for colleagues in the Investment functions in 2021. Given the diverse nature of job roles, colleague objectives include an obligation to ensure ESG factors are considered in decision making and that an ESG lens is applied to investment decisions. To incentivise adoption and sense of ownership, colleagues are not given set objectives to follow but rather are encouraged to work with their line managers to decide what kind of sustainability-related objective makes the most sense in their line of work. These objectives are now becoming a business-as-usual component for many of our colleagues within the investment and risk teams. We will review these in due course to further develop our approach to performance assessments and incentives.

In addition, in 2022 our executive compensation continued to be linked to achieving our carbon reduction targets, both reducing our operational emissions and the growth in our sustainable financing and investments, with scorecard allocation of 5% each towards the two key performance indicators (KPIs). In 2023, we will be enhancing these further.

* A review to ensure that talented women at the top of business are recognised. FTSE women leaders: Hampton-Alexander review (publishing.service.gov.uk)

** A review that considers how to improve the ethnic and cultural diversity of UK boards. The Parker Review – Encouraging greater diversity of UK boards

LOOKING FORWARD

7.1 LOOKING FORWARD

2022 was marked by our accelerated learning across a number of ESG areas and approaches in our ongoing mission to advance and enhance our responsible investment and stewardship approach.

We have applied our learnings to help the development of our investment propositions, our stewardship activities, communicate better with our customers, exert influence in industry-wide initiatives and build more robust internal processes. We are proud of the progress we have made and the hard work of our colleagues to deliver on our ambition.

A focus on human rights and nature

Over the course of 2023, we will continue to focus our efforts on key initiatives we began in 2022, including those across the themes of climate and the environment and human rights, and will lay the groundwork for some new initiatives. Our direct engagement activities will continue on Board Diversity and with companies flagged as UNGC violators, an we will take action if necessary.

We'll use the risk analysis we conducted on our investments related to deforestation and human rights to initiate initial direct engagement activity. As we continue to better understand our exposure, we can target our engagement even better to those companies with the biggest impact, leveraging our existing industry memberships and collaborations. Our reports on Biodiversity and Deforestation were just the beginning of our nature journey. With the Taskforce on Nature-related Financial Disclosures due to launch their framework in September 2023, we will pre-emptively look to expand our assessment beyond deforestation risk across our holdings to other nature and biodiversity metrics like water and waste management.

Playing a bigger role in voting

2023 will also be the year when we will be implementing the ISS SRI Policy across most of the pooled funds we invest in to ensure that we vote our shares in companies as consistently as possible to optimise our impact. We will play an even bigger role as active owners by directing a larger number of votes across our key priority themes, including through the use of routine votes in our mandated funds. This is an important step towards not only helping the companies we invest in to take necessary action to improve their long-term economic performance while minimising any negative impacts they may have on society and the planet, but also in holding them to account.

We will also seek to further enhance our fund range, integrating more ESG factors across more asset classes and across all our investments.

Meeting our net zero ambition

As the key milestone dates for our net zero ambition – 2025 and 2030 – get ever closer, we will be assessing all viable options to mitigate climate risks and invest in climate-aware opportunities.

The power of collaboration

Our involvement in various policy initiatives has allowed us to contribute to improving responsible investment practices across our industry and shaping the future direction. 2023 will see us building on the work that kicked off last year, such as the development of Sustainable Disclosure Regime – a significant regulatory initiative to build consumer trust – and responding to FCA's consultation paper, 'Finance for positive sustainable change: governance, incentives and competence in regulated firms' aiming to narrow down good, evolving practices so that finance can deliver on its potential to drive positive sustainable change.

To sum up

With our peers and policymakers, we need to accelerate further improvements in the financial services sector to meet the challenges we face as a society on issues such as the environment, equality and inclusion. Looking back at 2022, we feel our efforts made a significant contribution to this aim but there is still more to be done. We hope to take learnings from the challenges we faced and improvements we made to take further steps to improve customer outcomes and bring about real world positive change.

Chirantan Barua
CEO, Scottish Widows

APPENDIX:

MEETING THE REPORTING REQUIREMENTS OF THE STEWARDSHIP CODE

The UK Stewardship Code 2020 (the Code) sets high stewardship standards for asset owners and asset managers, and for service providers that support them. The Code comprises a set of 12 'apply and explain' Principles for asset managers and asset owners, and a separate set of Principles for service providers. It defines Stewardship as the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.

Scottish Widows applies to the Code as Asset Owners.

Principle	Type	Expectation	Main Section(s) Reference
1	Context 1	Signatories should explain the purpose of the organisation and an outline of its culture, values, business model and strategy	CEO Letter and Key Highlights, 1, referenced throughout report
1	Context 2	Signatories should explain their investment beliefs, i.e. what factors they consider important for desired investment outcomes and why	2
1	Activity 1	Signatories should explain what actions they have taken to ensure their investment beliefs, strategy and culture enable effective stewardship	2.1, 2.2, 3.1, 3.2, 6.3
1	Outcome 1	Signatories should disclose how their purpose and investment beliefs have guided their stewardship, investment strategy, and decision-making	2, 3
1	Outcome 2	Signatories should disclose an assessment of how effective they have been in serving the best interests of clients and beneficiaries	1.4, 2.4, 3.1, 3.2, 3.3
2	Activity 1	Signatories should explain how their governance structures and processes have enabled oversight and accountability for effective stewardship within their organisation and the rationale for their chosen approach	1.4,2.1,3.1,6.1
2	Activity 2	Signatories should explain how they have appropriately resourced stewardship activities, including: • Their chosen organisational and workforce structures • Their seniority, experience, qualifications, training, and diversity • Their investment in systems, processes, research and analysis • The extent to which service providers were used and the services they provided	3.2,6.1,6.3
2	Activity 3	Signatories should explain how performance management or reward programmes have incentivised the workforce to integrate stewardship and investment decision-making	6.3
2	Outcome 1	Signatories should disclose how effective their chosen governance structures and processes have been in supporting stewardship	6.1, 6.2
2	Outcome 2	Signatories should disclose how they (their chosen governance structures and processes) may be improved	6.1, 6.3
3	Context 1	Signatories should disclose their conflicts policy and how this has been applied to stewardship	3.7
3	Activity 1	Signatories should explain how they have identified and managed any instances of actual or potential conflicts related to stewardship	3.7
3	Outcome 1	Signatories should disclose examples of how they have addressed actual or potential conflicts	3.7
4	Activity 1	Signatories should explain how they have identified and responded to market-wide and systemic risks, as appropriate	2.1-2.3, 6.2

Principle	Type	Expectation	Main Section(s) Reference
4	Activity 2	Signatories should explain how they have worked with other stakeholders to promote continued improvement of the functioning of financial markets	4
4	Activity 3	Signatories should explain the role they played in any relevant industry initiatives in which they have participated, the extent of their contribution and an assessment of their effectiveness, with examples	4
4	Activity 4	Signatories should explain how they have aligned their investments accordingly	1.4, 2.1, 2.3, 2.5, 3.1, 3.2
4	Outcome 1	Signatories should disclose an assessment of their effectiveness in identifying and responding to market-wide and systemic risks and promoting well-functioning financial markets	6.2
5	Activity 1	Signatories should explain how they have reviewed their policies to ensure they enable effective stewardship	3.1, 3.2, 6.1, 6.3
5	Activity 2	Signatories should explain what internal or external assurance they have received in relation to stewardship (undertaken directly or on their behalf) and the rationale for their chosen approach	6.1, 6.2
5	Activity 3	Stewardship reporting is fair, balanced and understandable	6.1
5	Outcome 1	Signatories should explain how their review and assurance has led to the continuous improvement of stewardship policies and processes	6.1
6	Context 1	Signatories should disclose the approximate breakdown of the scheme(s)' structure, for example whether it is a master trust, occupational pension fund, defined benefit or defined contribution, etc; and the size and profile of their membership, including number of members in the scheme and the average age of members OR their client base, for example, institutional versus retail and geographic distribution; assets under management across asset classes and geographies	1.1, 1.2
6	Context 2	Signatories should disclose the length of the investment time horizon they have considered appropriate to deliver to the needs of clients and/or beneficiaries and why	1.1, 1.4
6	Activity 1	Signatories should explain how they have sought beneficiaries' views (where they have done so) and the reason for their chosen approach	3.1, 3.2, 5.1
6	Activity 2	Signatories should explain how the needs of beneficiaries have been reflected in stewardship and investment aligned with an appropriate investment time horizon	1.1, 3.1, 3.2
6	Activity 3	Signatories should explain what they have communicated to beneficiaries about their stewardship and investment activities and outcomes to meet beneficiary needs, including the type of information provided, methods and frequency of communication	5.1, 5.2
6	Outcome 1	Signatories should explain how they have taken account of the views of beneficiaries where sought, and what actions they have taken as a result	5.1, 5.2
6	Outcome 2	Signatories should explain how they have taken account of the views of beneficiaries where sought, and what actions they have taken as a result	3.2, 5.1, 5.2

Principle	Type	Expectation	Main Section(s) Reference
6	Outcome 3	Signatories should explain where their managers have not followed their stewardship and investment policies, and the reason for this	1.4, 3.2, 3.4, 3.5
7	Context 1	Signatories should disclose the issues they have prioritised for assessing investments, prior to holding, monitoring through holding and exiting. This should include the ESG issues of importance to them	2, 3.2
7	Activity 1	Signatories should explain how integration of stewardship and investment has differed for funds, asset classes and geographies	2.2, 2.4, 3.2
7	Activity 2	Signatories should explain how they have ensured: • Tenders have included a requirement to integrate stewardship and investment, including material ESG issues • The design and award of mandates include requirements to integrate stewardship and investment to align with the investment time horizons of clients and beneficiaries	1.4, 2.1, 3.1, 3.4, 6.3
7	Outcome 1	Signatories should explain how information gathered through stewardship has informed acquisition, monitoring and exit decisions, either directly or on their behalf, and with reference to how they have best served clients and/or beneficiaries	3.3, 3.4
8	Activity 1	Signatories should explain how they have monitored service providers to ensure services have been delivered to meet their needs	1.4, 3.4
8	Outcome 1	Signatories should explain how the services have been delivered to meet their needs OR the action they have taken where signatories' expectations of their managers have not been met	3.1, 3.3, 3.4-3.7
9	Activity 1	Signatories should explain the expectations they have set for others that engage on their behalf and how OR how they have selected and prioritised engagement (for example, key issues and/or size of holding)	1.4, 3.1 – 3.6
9	Activity 2	Signatories should explain how they have developed well-informed and precise objectives for engagement with examples	3.2, 3.3
9	Activity 3	Signatories should explain what methods of engagement and the extent to which they have been used	3.3, 3.5
9	Activity 4	Signatories should explain the reasons for their chosen approach, with reference to their disclosure under Context for Principle 1 and 6 (purpose of organisation and approx. breakdown of schemes)	2.1, 2.2, 3.1, 3.2
9	Activity 5	Signatories should explain how engagement has differed for funds, assets, or geographies.	3.3, 3.5, 3.6
9	Outcome 1	Signatories should describe the outcomes of engagement that is ongoing or has concluded in the preceding 12 months, undertaken directly or by others on their behalf. E.g. • How engagement has been used to monitor the company • Any action or change(s) made by the issuer(s) • How outcomes of engagement have informed investment decisions • How outcomes of engagement have informed escalation Examples should be balanced and include instances where the desired outcome has not been achieved or is yet to be achieved	3.3, 3.5

Principle	Type	Expectation	Main Section(s) Reference
10	Activity 1	Signatories should disclose what collaborative engagement they have participated in and why, including those undertaken directly or by others on their behalf. E.g. • Collaborating with other investors to engage an issuer to achieve a specific change • Working as part of a coalition of wider stakeholders to engage on a thematic issue Signatories should provide examples, including the issue(s) covered, the method or forum, and their role and contribution	3.3, 4
10	Outcome 1	Signatories should describe the outcomes of collaborative engagement	4.1, 4.2
11	Activity 1	Signatories should explain the expectations they have set for asset managers that escalate stewardship activities on their behalf, OR how they have selected and prioritised issues, and developed well-informed objectives for escalation	1.4, 3.2 -3.4
11	Activity 2	Signatories should explain when they have chosen to escalate their engagement, including the issue(s) and the reasons for their chosen approach, using examples	3.3, 3.5
11	Activity 3	Signatories should explain how escalation has differed for funds, assets or geographies	3.3, 3.5
11	Outcome 1	Signatories should describe the outcomes of escalation either undertaken directly or by others on their behalf (as with principle 9)	3.3, 3.5
12	Context 1	Signatories should state the expectations they have set for asset managers that exercise rights and responsibilities on their behalf, OR explain how they exercise their rights and responsibilities, and how their approach has differed for funds, assets, or geographies	1.4, 3.4, 3.5
12	Context 2	For listed equity assets, signatories should: • Disclose their voting policy, including any house policies and the extent to which funds set their own policies • State the extent to which they use default recommendations of proxy advisors • Report the extent to which clients may override a house policy • Disclose their policy on allowing clients to direct voting in segregated and pooled accounts • State what approach they have taken to stock lending, recalling lent stock for voting, and how they seek to mitigate 'empty voting'	3.6
12	Activity 1-4	For listed equity assets, signatories should: • Disclose the proportion of shares that were voted in the past year and why • Provide a link to their voting records, including votes withheld if applicable • Explain their rationale for some or all voting decisions, particularly where: there was a vote against the board, there were votes against shareholder resolutions, a vote was withheld, or the vote was not in line with voting policy • explain the extent to which voting decisions were executed by another entity, and how they have monitored any voting on their behalf	3.6
12	Outcome 1	For listed equity assets, signatories should provide examples of the outcomes of resolutions they have voted on over the past 12 months.	3.3, 3.5, 3.6

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Registered office in the United Kingdom at 25 Gresham Street, London EC2V 7HN.

Authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority
and the Prudential Regulation Authority. Financial Services Register number 181655.

61027 07/23

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