



**PENSION FUND COMMITTEE AND
PENSION BOARD
TO BE HELD ON THURSDAY,
14 SEPTEMBER, 2017**

**Please find attached the Appendices in respect of Items
No. 7 and No. 9 on the agenda for the above meeting**

7.	Voting Consultant - PIRC (Pages 1 - 16) Presentation by Head of Public Policy and Engagement Services Manager, PIRC. (Copy attached).	45 mins
8.	Baillie Gifford (Pages 17 - 24) Presentation by Andrew Cave, Baillie Gifford. (Copy attached)	45 mins

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Scottish Borders Council Pension Fund

The voice of responsible shareowners

Introduction

Presentation to: Scottish Borders Council Pension Fund

Presentation from:

Ian Jones, Head of Public Policy

Tessa Younger, Engagement Services Manager

Regulated by the Financial Conduct Authority

Introduction

Agenda

- About PIRC
- How we work, product description
- Research process, capacity and approach
- Governance philosophy and approach
- Unique selling points and products

About PIRC

Who we are and what we do

- **Focused on shareowners:** PIRC was set up by pension funds in 1986 to provide research and advice to them.
 - **A dedicated resource:** we operate a large team focused purely on corporate governance and responsible investment issues.
 - **Completely independent:** we are entirely owned by current and former directors of PIRC.
 - **No conflicts:** we only provide services to shareholders, not the companies we research.
 - **An influential voice:** we advise clients with assets of over £1.5trn our views are frequently sought by investors and companies.
 - **Global reach:** we cover any company that our clients hold, whatever the market, currently spanning 62 countries
 - **Company engagement:** we actively engage with companies and give them the opportunity to respond to our analysis.
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About PIRC

We believe good governance adds value



“The balance of academic evidence supports the thesis that good corporate governance adds value.... The benefits gained may be return-enhancing, but may equally be risk-reducing in nature.”

Remapping Our Investment World,

Towers Watson

“We believe that active ownership can help enhance long-term shareholder value and are therefore supportive of pension funds being more active.”

No action, no option,

Towers Watson

About PIRC

What they say about us

"PIRC is a firm with a well deserved reputation as a canary in the coalmine of corporate governance."



"The investor group which led the so-called Shareholder Spring."

The Daily Telegraph

"[PIRC's comments] on News Corp and BSkyB might have been condensed into just four words: 'We told you so'. For PIRC did indeed tell us so – it has been warning about governance issues at both companies for several years."



How we work

PIRC

How we work

Corporate Governance: Service description

- PIRC provides **global portfolio coverage** of client equity portfolios.
- For UK portfolios, PIRC provides a proxy report **incorporating environmental and social analysis** with its governance coverage and voting recommendations.
- Coverage in any market can be based on a **client's own corporate governance policy and voting guidelines**.
- PIRC delivers reports in a pdf format to a **unique client website**.
- Unique **capital strategies/stewardship** coverage
- Previous year's **proxy results** incorporated into reports
- **Engagement with company recorded** in the report.

How we work

Research process

- **Proprietary research:** All research is undertaken in-house, in line with a standardised process, drawing on various primary sources.
- **A flexible process:** An internal Policy Forum enables our research staff to decide how to approach new issues, or situations where fine judgment is required.
- **A structured approach:** Our shareholder voting guidelines underpin the analysis undertaken. We believe that our guidelines-informed approach helps prevent personal/cognitive biases affecting analysis and voting advice. Clients' custom guidelines are implemented by a dedicated client executive.
- **Going beyond the minimum:** Our guidelines also set out where our view goes beyond existing legal or regulatory requirements.
- **Company buy-in:** We actively seek company views on draft analysis and recommendations, and send copies of final reports.

How we work

A PIRC report



The front page of a typical proxy report provides an overview of our analysis and voting recommendations

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BP PLC

UK Governance Service

MEETING DATE	Wed, 17 May 2017 11:30 am	TYPE	AGM	ISSUE DATE	Wed, 30 Aug 2017
MEETING LOCATION	ExCeL London, One Western Gateway, Royal Victoria Dock, London				
CURRENT INDICES	FTSE 100, FTSE EuroFirst				
SECTOR	Integrated Oil & Gas				

COMPANY OVERVIEW

BP plc is the parent company of the BP group of companies and has its worldwide headquarters in London. The Company finds, develops and produces sources of energy, turns them into products, and buys and sells at each stage of the hydrocarbon value chain in three main businesses - fuels, lubricants and petrochemicals. In renewable energy, BP's activities are focused on biofuels and wind.

MEETING SPECIFIC INFORMATION

Quorum requirements and voting majority

Resolutions under extraordinary business have special voting majority requirements. Resolutions 20 to 23 require three quarters of the votes validly cast in order to be approved.

PROPOSALS		ADVICE
1	Receive the Annual Report The Strategic Review is considered adequate. There are adequate environmental and employment policies in place. Quantified environmental data has been published. It is noted that the Company has not provided shareholders with an opportunity to approve dividends paid during the year. Given the lack of opportunity to approve the dividend, shareholders are recommended to oppose.	Oppose
2	Approve the Remuneration Report Overall disclosure is considered acceptable although targets attached to performance shares granted during the year are not clearly sated. The changes in CEO pay over the last five years are considered in line with the changes in the Company's TSR performance. However, the variable pay of the CEO is considered excessive at 400% of salary. Also, the ratio between CEO pay and average employee	Abstain

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How we work: Theme: Capital Stewardship

Looking at how shareholder funds are invested



- **Focusing on capital:** Over the past three years, we have developed our services to include a tighter focus on capital maintenance and the stewardship of capital, i.e. the real wealth of the company as distinct from market derived estimates of it.
- **Revised guidelines:** Our shareholder voting guidelines include detailed commentary on capital stewardship and accounting.
- **Policy work:** We have undertaken extensive research for clients unpicking unreliable accounting practices, and calculating the costs.
- **In our services:** Our proxy reports on companies in key markets now include a capital stewardship section:
- **Into practice:** Concerns about capital and related issues have a significant impact on voting recommendations (annual meetings and extraordinary general meetings), eg illegal dividends

Capital Stewardship

The black hole at Barclays



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governanceplus
BARCLAYS PLC

Meeting Date:	Wed, 27 Apr 2011 11:00	Proxy Deadline:	Mon, 25 Apr 2011	Type:	AGM	Issue date:	Tue, 12 Apr 2011
Meeting Location:	Royal Festival Hall, Southbank Centre, Belvedere Road, London SE1 8XX						
Current Indices:	FTSE 100	FTSE EuroFirst	MSCI Europe				
Sector:	Banks						

PROPOSALS	ADVICE
<p>1 Receive the Annual Report</p> <p>The company's Business Review meets ASB RS guidelines in our view. Adequate environmental and employment policies are in place and quantified environmental reporting is disclosed. Non-EU political donations made by group subsidiary in the year but recipients identified. Total dividend paid in the year of 5.5p (2.5p) comprises 3p interim and 2.5p final and is covered by earnings however no vote is provided in order that shareholders may approve the dividend distribution policy. It is the Group's policy to declare and pay dividends on a quarterly basis. We are further concerned at the linking of distribution policy to executive pay. The company has adopted clawback provisions which become executable if a dividend is not paid. Historically dividend has been decided without introducing the possibility that executives may have to return incentive awards and the new clawback arrangements change this situation.</p> <p>Given the impact on the economy of the global financial crisis and the pivotal role of banks in particular we consider that shareholders should focus on reporting by financial institutions and any misalignment with governance arrangements. In this context we are concerned at the company's statement that the "chief operating decision maker" - for applying IFRS 8 is the executive committee and not the board. The company's segmental reporting note (IFRS 8) states that the "chief operating decision maker" is the executive committee. Given that the objective of IFRS 8 is to segment the business according to how the major capital allocation decisions are taken and then reported, the company's disclosure appears at odds with the schedule of matters reserved for the board which includes approval of financial statements and any significant changes in accounting policies. The segmental reporting is contrary in our view to the intention of Section 393 Companies Act in which it is the directors who are responsible for ensuring that the accounts give a true and fair view. Under section 393 the directors of a company must not approve accounts unless they are satisfied that they give a true and fair view of the assets, liabilities, financial position and profit or loss of the consolidated group. The UK legal environment also provides complementary governance rights to shareholders. Shareholders have the right to dismiss board members and elect directors. Such rights do not extend to all executive committee members.</p>	<p>Oppose</p>

– PIRC, April 2012

– *Barclays has overvalued its assets by at least £6.7bn, and its capital is overstated by that amount.*

– The company persistently denied this including up to the 2013 AGM.

– Prudential Regulatory Authority (PRA), June 2013

– *Barclays needs to raise new capital [the Rights issue is pending] due to overvaluing assets by £8.6bn.*

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Capital Stewardship Protium



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PIRC, 2011 Barclays used an off balance sheet vehicle Protium in which to place toxic assets. This seems to have protected Barcap earnings from mark-down-to-market impairment of the assets transferred to Protium. Whilst it appears that the regulator had adjusted for this in terms of group balance sheet risk, the Barcap balance sheet for performance measurement is based on a measure of economic capital ... that does not necessarily correlate with that of the regulator. It would appear that the management of economic profit and the structure of Protium serves the purpose of artificially enhancing the performance of Barcap for remuneration purposes.

Financial Service Authority (FSA) to Barclays in 2012 (revealed by Treasury Select Committee) The development of the Protium structure in 2009 which, although not delivering Barclays any regulatory capital advantage and while within accounting rules, was perceived by many external commentators as a convoluted attempt to portray a favourable accounting result.

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Scottish Borders Council Pension Fund

Governance philosophy and approach

PIRC's Governance philosophy

- **PIRC's ability to spot emerging issues.** PIRC raises the profile of issues before many in the marketplace have recognised their significance. PIRC has been a market leader on executive remuneration. Our first report on pay, published in 1992, called for a shareholder vote on remuneration.
- **PIRC's independent and critical edge.** PIRC has no corporate conflicts and is unafraid to raise the difficult issues with companies that other investors often shy away from.
- **High quality research:** PIRC's analysis and research is well respected in the market place and provides the fundamental underpin to its policy approaches and voting recommendations.

PIRC's Governance philosophy (2)

-
- **Market influence:** Many of the elements of corporate governance best practice that are now taken for granted at public companies were reforms that PIRC had proposed much earlier.

For example, PIRC called for a shareholder vote on audit committee reports in 2009, this was proposed by the Competition Commission in 2013.

For example: PIRC called for a shareholder vote on executive pay in 1992 and this finally came to pass in the advisory vote and later the binding vote on pay policy in 2013.

PIRC launched the Environmental Investor Code in 1992, now all companies report on their environmental impacts.

- **Unique insights:** Our work on capital stewardship and accounting issues is market-leading.

REDEFINING CORPORATE GOVERNANCE

September 2017



*This document provides a short overview
of how we think about and approach corporate
governance and stewardship at Baillie Gifford.*

*Further information is available at
www.bailliegifford.com , or by contacting
CorporateGovernance@bailliegifford.com*



WHAT DO WE MEAN BY CORPORATE GOVERNANCE?

Corporate governance is the combination of a number of different aspects relating to the control, oversight and management of a company. Despite extensive regulation and the creation of a number of national-level corporate governance codes, companies still have broad discretion over how they choose to be incorporated, governed and operated. As long-term investors we pay close attention to these variables, taking particular interest in the following areas of a company's business:

- The capital structure, articles of incorporation, and the country or countries of incorporation and listing
- The treatment and protection of minority shareholders
- The alignment of interests between management, strategic shareholders and other investors
- The make up and effectiveness of the board of directors, the quality and performance of management, and the remuneration of key employees
- The corporate culture and approach to sustainable business, and the management of relationships with customers, employees, suppliers, regulators and the wider community

We focus on corporate governance not because of an interest in shareholder rights *per se*, but because we believe that governance really matters with respect to long-term investment performance. Our ongoing assessment of corporate governance issues may change our view on buying, selling or resizing our clients' holdings. It also determines how we choose to vote at company meetings and how we engage with management, the two principal levers we have for influencing change.

This combination of ongoing company monitoring and research, and 'active ownership' through voting and engagement, is what we think of as stewardship.

WHAT DO WE CONSIDER TO BE ‘BEST PRACTICE’ IN CORPORATE GOVERNANCE?

Just as there is no universally ‘right’ way to invest in the stock market, or to manage a pension fund, there is no ‘one-size-fits-all’ approach to corporate governance that should always be followed. We are open minded about the different ways to govern and manage a company, and we are pragmatic about the significant differences in both expectations and actions that exist across different countries. For example, we don’t have a fixed view with regards to the composition of a company’s board of directors. Effective boards can and do take many forms, and some of the least effective boards conform to the full range of widely accepted corporate governance ‘norms’.

For this reason, we are sceptical of the usefulness of rigid policies and checklists when analysing, engaging and voting on corporate governance issues. Just as our investment research is bottom-up, we prefer to take a case-by-case view on governance, focusing on what works in practice:

- Are we respected as minority holders?
- Are we consulted by management?
- Is executive compensation consistent with performance?

Ultimately, we want to be in a position where we can trust management to take a long-term view and to look after our clients’ interests as minority shareholders.

HOW DO WE EMBED CORPORATE GOVERNANCE CONSIDERATIONS IN OUR INVESTMENT PROCESS?

Our long-only, active approach to investment is based on identifying and holding high quality growth businesses that enjoy sustainable competitive advantages in their marketplace. To do this we look beyond current financial performance, undertaking proprietary research to build up an in-depth knowledge of an individual company and a view on their long-term prospects. This focus on bottom-up research also applies to our work on corporate governance and stewardship.

As a firm we are also very comfortable with our various investment strategies taking different approaches to reach the same goal of properly assessing and weighing up corporate governance considerations in the investment process. The general principles which follow are, however, valid across all of our investment teams.

RESEARCH & ENGAGEMENT

Corporate governance is not a separate side issue, it is central to our investment process. All of our investment staff share the responsibility for identifying, analysing and monitoring corporate governance issues with our current and potential holdings. Our investment staff spend a very significant amount of time assessing the quality, integrity, motivation and culture of management teams, and then acting on their convictions. The work of our Corporate Governance Team supports this, and is therefore complimentary to the work undertaken by our investment teams rather than separate.

Our investors and the Corporate Governance Team have regular meetings with management and board members to monitor performance, and to identify and understand issues. If we have reservations about a company's approach, we prefer to encourage change privately through engagement with management rather than divestment.

We will always review the merits of proposals on a case-by-case basis rather than following restrictive checklists.

VOTING

Thoughtful voting of our clients' holdings is an integral part of our commitment to stewardship. How we vote is an important part of the long-term investment process, and for this reason we always strongly prefer to be given this responsibility by our clients. Unlike many of our peers, we do not outsource the responsibility for voting to third-party suppliers. Our dedicated Corporate Governance Team oversees our voting analysis and execution in conjunction with our investment managers.

We will always review the merits of proposals on a case-by-case basis rather than following restrictive checklists. Checklists, often by necessity, revert to focusing on rights and inputs rather than outcomes. For example, it is easier to draw up a rule dictating how many other company boards a director can be on than to determine whether their performance as an independent director is effective. A formulaic approach to governance can often lead to recommendations that just don't make sense in an investment context – attempting to vote a successful founder CEO off the board because they are also company chairman for example.

WHAT IS ESG, AND IS IT THE SAME AS CORPORATE GOVERNANCE?

ESG stands for ‘Environmental, Social and Governance’. It has emerged as an industry shorthand for a very broad range of issues relating to how a company is governed and its impact on society. Whilst it is now a widely accepted term, we prefer to focus on corporate governance and stewardship as all-embracing concepts which already factor in a company’s performance on environmental and social issues – a business with an unacceptable environmental record, for example, is a poorly governed one that should be a priority for engagement, and if necessary, voting action.

WHAT ABOUT FIXED INCOME INVESTMENTS?

Corporate governance is also highly relevant to our fixed income investments. When investing in corporate bonds, for example, it is particularly important to undertake pre-buy research on material governance and sustainability issues, given the limited engagement levers for debt investors. We assess the risks to a company’s creditworthiness by considering governance matters such as the effectiveness of the board, and its approach to risk management.

STEWARDSHIP

Our commitment to responsible stewardship of our clients’ holdings is as old as our firm. Our clients trust us to oversee and manage their investments, and stewardship of their holdings is a core part of this commitment. As long term investors, we believe that our approach to voting and engagement supports investment performance. When the aim is to invest in a company for many years, ongoing oversight of the business is just as important as the initial investment decision.

But we also believe that we have a wider stewardship role to play in encouraging responsible, long-term capitalism. A company’s approach to governance issues can have a very material impact on society, and we should be using our influence to encourage sustainable practices. More broadly, our business is based on our ability to invest in stable and functional public markets. It is therefore ultimately in our own interests to ensure that the business sector enjoys ongoing public support and political, legal and regulatory backing in the key economies around the world. This will only happen if companies are seen to be operating with integrity and in a way that respects the interests of stakeholders.

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CURIOUS ABOUT THE WORLD