Universities Superannuation Scheme Global Stewardship Principles

Engagement and Voting in Listed Equities, 2022

Our approach to engagement

Unique pension fund perspective

The majority of the Scheme's investments are managed internally by USS Investment Management Ltd, the wholly-owned fund management subsidiary of USS. Our investment process and approach to stewardship is tailored to the Scheme's long-term investment requirements and we are able to avoid many of the agency issues and conflicts that can exist between asset owners and fund managers. We are therefore able to provide a unique perspective to our investee companies compared to many other institutional investors.

Advanced and interactive communication

USS welcomes proactive communications from companies, particularly where we hold an active investment position, and will respond when we can. We expect companies to advise us when there are material changes and issues which impact long-term shareholders, such as strategy, capital structure, sustainability, and governance. We specifically encourage companies to engage on issues beyond remuneration. We would, in particular, welcome communications on board appointments and the nomination process, and environmental and social strategy, neglected areas of focus but ones on which we place considerable importance.

We strongly encourage companies to inform USS early on in the decision-making process regarding changes to their governance structures. An early approach during the busy proxy season, for example, gives us the best opportunity of giving prospective governance changes the consideration they deserve. Earlier communication can play a vital role in resolving issues ahead of the AGM season.

There may be occasions when we would be prepared to be taken 'inside' for a limited period of time, however we would require advanced notice. There will also be occasions when USS may be prepared to publicly support a company's course of action, for example to galvanise broader shareholder support.

Integrated engagement

USS aims to engage with companies in an informed, constructive and confidential manner. USS will aim to ensure that the right individuals are involved in any interaction with companies. This may often include individuals from both the Responsible Investment (RI) and portfolio management (where we have an active holding) teams. If this is not possible, the individuals representing USS will be suitably apprised of USS' position on operational, financial and strategic issues as well as environmental, social or governance (ESG) matters. We can provide assurance that discussions will be undertaken on a confidential basis. Reciprocally, we would expect a similar integrated and confidential approach to be adopted by investee companies.

Building trust and confidence

USS' default position is to be supportive of the board and management. We assume discretionary changes will be applied to board and executive arrangements when necessary on the basis that the rationale will be disclosed to investors. When appropriate and where we have concerns, we may put forward proposals to companies for the board's consideration.

In order to establish, develop and maintain relationships there should be a regular and consistent process of engagement between companies and investors. Companies should hold periodic earnings calls and investor days and also establish an annual strategic meeting for key intrinsic and long-term investors. This meeting would provide an opportunity for the chairman and chairs of the various sub- committees to explain how corporate governance and the management of environmental and social issues are appropriate for the needs of the business.

Support for market-based solutions

USS is not typically supportive of regulatory or prescriptive measures to govern the ways in which companies and investors engage. Our preference is to seek and formulate joint market-based solutions developed by companies and investors to the challenges that present themselves. We will however support regulatory intervention where market practices need to adapt at a faster rate that is occurring.

Collaboration with peers

USS welcomes joint meetings (and other collaborative fora) with other investors and our representative bodies in different markets[1], and recognises the potential benefits to companies and ourselves that accrues from this approach. However, we reserve the right to request an individual meeting with a company.

Our approach to voting

Active and responsible ownership

USS is an asset owner signatory to the UN backed Principles for Responsible Investment and a supporter of the UK Stewardship Code. We also welcome the development of other stewardship codes around the world. As part of the Scheme's commitment to being a long-term, active and responsible shareowner, USS intends to vote its shares in all the markets in which it invests and views voting as a valuable tool for engaging with companies to encourage better standards of corporate governance and management of ESG issues.

[1] 1 For examples USS participates in the following initiatives: ACGA (Asian Corporate Governance Association), ASCSI (Australian Council for Superannuation Investors) CGF (Corporate Governance Forum), CII (Council of Institutional Investors), Eumedion, GIGN (Global Investors Governance Network), ICGN (International Corporate Governance Network), ICPM (International Centre for Pension Management), IIGCC (Institutional Investors Group on Climate Change), JEC (Japan Engagement Consortium), PLSA (Pensions and Lifetime Savings Association), Tomorrow's Company, UN PRI (United Nations Principles for Responsible Investment).

Pragmatic approach

The Scheme's voting principles have been developed in-house and outline the Scheme's expectations from investee companies, reflecting international best practice - including the UK Corporate Governance Code. Outside the UK and for companies quoted off the main UK market, we seek to take into account local market standards and best practice.

USS Investment Management Ltd uses a number of proxy advisory firms to provide a summary of the proxy information released to the market. We use this information alongside a number of other sources to reach a final voting decision. Individual vote decisions for priority holdings are reviewed and confirmed by the in-house RI team, working closely with USS Investment Management Ltd.'s portfolio managers. Stocks held in our Quant funds, our externally managed funds with retained voting rights, or which are lower priority are voted by a dedicated voting analyst at our main proxy research provider in accordance with the USS voting policy[2].

Fundamental voting principles are set out below and will be applied in the majority of cases. However, USS aims to take an informed and pragmatic approach to voting, treating every case on its own merits, giving due consideration to the specific circumstances and facts available to each investor before voting.

Communication

Where we have voted against management or abstained on a resolution and hold an active position, we will usually write to the company providing it with the reasons for our voting decision or let the company know where our voting decisions can be found on our website. In addition, our voting records are disclosed retrospectively on our website and, where relevant, include a brief comment to explain why we have not supported management.

Stock lending

USS has an active stock lending programme. To ensure that the Scheme is able to vote all its shares at important meetings or where USS is a significant shareholder, USS has worked with service providers to establish procedures to restrict lending for certain stocks and recall shares in advance of shareholder votes. Where we hold 3% or more of the issued share capital of a company, stock is recalled systematically. In other circumstances we monitor the meetings and proportion of stock on loan and will restrict and/or recall lent stock on a case by case basis, e.g. in the event of a contentious vote or in relation to engagement activities, further to discussion with the portfolio manager.

Our ten principles of stewardship

The principles below underpin the voting decisions that are taken in markets in which USS invests.

1. Long-term value creation

As a pension fund with liabilities extending into the future, it is in USS' interest to encourage the companies and markets in which it invests to focus on delivering durable shareholder value. We believe this means

[2]https://www.uss.co.uk/how-we-invest/responsible-investment/how-we-vote

management must consider long-term risks to performance, including environmental, social and governance (ESG) factors. Boards and management should have a long-term strategic vision to support this objective.

2. Environmental and social issues

Companies should manage environmental and social factors (such as climate change, pollution, and human capital) that could impact their business, both directly and via reputational damage, and seek to minimise negative externalities. USS has set an ambition to be Net Zero by 2050 and expects the companies in which it invests to have their own plans to achieve this target. Companies should comply with regulation and adopt voluntary best practices to promote sustainable business practices including the UN Sustainable Development Goals[3] and the UN Global Compact. We expect companies to demonstrate in their reporting how they manage ESG related risks or opportunities. USS may vote against management or relevant board members where such reporting is absent or we have concerns about a company's management quality score, as assessed by the Transition Pathway Initiative (TPI).

3. Capital governance

Companies should have developed policies in respect of capital management and disclose how chosen capital management disciplines are expected to contribute to long-term value creation. We believe such disclosure should extend (where relevant) to discussions of the role that mergers, acquisitions and asset disposals are expected to play in such value creation; how this aspect of capital management supports strategy, and the processes and core capabilities that underpin the company's approach to these.

We believe companies should also disclose the thinking behind their chosen capital structure and how this pertains to risk management; their approach to capital retention and the return of capital to shareholders (in the form of dividends and share repurchases, for example); the basis on which they make trade-off decisions between the uses of capital that are available to them, and the basis on which they measure performance in respect of capital allocation.

4. Shareholder rights

USS expects companies to enable their shareholders to exercise full shareholder rights. Shareholders should have the opportunity to vote at general meetings on material transactions including new share issues, dividends, share buy-backs, mergers and acquisitions, and related party transactions. In case of new share issuance, pre-emption rights should be given to the existing shareholders.

5. Equal treatment of shareholders

USS supports the principle of 'one share, one vote' and parity of voting power and economic interest. The board of directors should consider the interests of all shareholders in their decision making and seek to protect the interests of minority shareholders.

6. Accountability to shareholders

USS firmly believes that a company's directors should be accountable primarily to its shareholders as they are the owners of the company and the providers of its risk capital who reasonably expect the board to pursue business strategies to optimise long-term value. Shareholders should be given the opportunity to nominate

[3] https://www.un.org/sustainabledevelopment/sustainable-development-goals/

and vote on directors on an individual basis. USS encourages companies to adopt a majority voting system We also expect companies in which we invest to recognise the interests of other stakeholders as we believe this is consistent with long term value creation.

7. Effective leadership and oversight

The board is responsible for determining the company's strategy, and for supporting and overseeing its implementation. The board's effectiveness, integrity and objectivity is therefore critical to the long- term success of the company. The board should also ensure that the governance structure, the corporate culture and the remuneration policies are adequately designed to achieve the company's objectives. The board should strive for adequate skills, expertise and diversity in order to perform its role.

8. Alignment of interests

Remuneration is seen as an essential tool to align the interests of executives, the company and its shareholders. Remuneration committees should expect executive management to make a material long-term investment in shares of the businesses they manage. USS considers that pay should be aligned to long-term success and the desired corporate culture throughout the organisation. Pay schemes should be clear, understandable for both investors and executives, and ensure that executive rewards reflect long-term returns to shareholders. Remuneration committees should use the discretion afforded to them by shareholders to ensure that awards properly reflect business performance.

9. Checks and balances

It is especially important that the audit committee acts independently from the executives, to ensure that the interests of shareholders are properly protected in relation to financial reporting and internal control. USS considers that the audit committee should comprise solely demonstrably independent directors. Also, to safeguard shareholders' long-term interests, the audit committee should rotate the external audit firm at least every 20 years and seek to maintain non-audit work to a minimum.

10. Transparency

USS expects companies to disclose clear, consistent and timely information on key material issues to the market and shareholders to enable investors to make informed investment and voting decisions. To ensure that appropriate information is available to our portfolio managers, we would expect material environmental, social and governance data to be integrated into the formal corporate reporting process including annual reports. For example, we would expect disclosure of key material indicators such as climate change (as per the TCFD[4]), carbon exposure, health and safety data and human capital information including staff turnover.

Appendix - Application of the principles

The below policy describes how we apply our Stewardship Principles and outlines our expectations in all markets in which USS invests, although individual company circumstances and local market practices are also taken into account. USS may escalate the vote by voting against additional relevant resolutions or individual directors if concerns raised in previous years have not been addressed in the current year.

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[4] https://www.fsb-tcfd.org/

Boards of directors

- The composition of the board of directors should be publicly disclosed.
- A majority of the board should be composed of independent non-executive directors.
- USS expects boards to demonstrate diversity, including gender diversity, and ensure this within the companies they represent.
- The audit committee should comprise solely of independent non-executive directors.
- The remuneration committee should comprise solely of independent non-executive directors.
- The Chairman and the CEO have two different roles which require different skills. Therefore, they should be separated.
- The Chairman should be independent on appointment.
- All directors should be able to allocate sufficient time to the company to discharge their duties alongside their other commitments. Whilst we review this on a case-by-case basis, we will further review cases where a director holds more than four mandates (where a Chairman's role is generally considered as counting for two). The number of meetings attended by each director should be disclosed in the annual report. Instances of poor attendance should be explained. Unless we receive an appropriate explanation from the company, USS will be minded to vote against a director who failed to attend at least 75% of board and committee meetings or who has considerable work commitments that might prevent him/her from devoting sufficient time to the role at the company.
- USS does not support the appointment of substitute directors or corporates to the board.

Independence of directors

USS will generally consider that a director is assumed not to be independent if he or she:

- Is currently or has been an employee of the company within the past five years;
- Has or has had within the last three years a material business relationship with the company;
- Received or has received remuneration from the company other than director's fees;
- Participates in the company's share option or performance-related pay schemes;
- Has close family ties with any of the company's advisers, directors or senior employees;
- Holds cross-directorships;
- Represents a significant shareholder; or
- Has served on the board for more than 12 years.

Election of directors

- The election term of directors should not be longer than three years.
- Full biographical details, including other directorships and/or chairmanships, should be disclosed.
- USS does not support plurality voting standards and encourages companies to adopt majority voting standards.
- Shareholders should be able to nominate directors.

Non-executive remuneration

- Fees for non-executives should always be fixed in advance. Non-executive directors should not receive any variable compensation, or payments that could be considered as linked to performance.
- USS has a preference for cash payment for non-executive directors' fees.
- USS will scrutinise fee increases and will not support excessive increases.

Executive remuneration

- There should be a separate vote on executive remuneration.

USS commonly expects to find the following characteristics within executives' remuneration structures:

- Long-term incentive arrangements should be subject to performance conditions being measured over at least a three-year period.
- Full and transparent disclosure of remuneration policy and performance targets should be reported by the company.
- Disclosure should be sufficient to allow shareholders to calculate total awarded and received (taken home) remuneration and understand the rationale for the payment.
- Performance targets should be challenging and long-term in nature and clearly aligned with business strategy and objectives linked to long-term value creation. Companies should use more than one performance criterion and include a link to financially material environmental and social metrics in their incentive schemes. USS expects companies to disclose their ESG-related targets and performance against these targets.
- Companies should avoid making additional payments outside the remuneration policy.
- USS encourages companies to introduce clawback and malus provisions in all variable compensation elements of remuneration.
- Service contracts should be limited to 12 months of fixed compensation upon termination.
- Companies are encouraged to adopt long-term share ownership requirements for executives.

External auditors

- The external auditor must be 'independent' and free from major conflicts with the company, the Chairman and the audit committee members.
- The external audit firm should be rotated at least every 20 years and the contract retendered at least every ten years.
- Companies should disclose clearly in their annual report and accounts a breakdown of audit and non-audit related fees paid to their external auditors during the year.
- Non-audit fees must not exceed 70% of the audit fees of the average of group statutory audit fees over the previous three years.

Annual report and accounts

- Annual report and accounts, including the external auditor's opinion, should be disclosed sufficiently ahead of the annual general meeting to enable shareholders to vote in an informed manner.
- A separate resolution proposing the adoption or reception of the annual report and accounts should be tabled at all annual general meetings.

Capital authorities

- Capital authorities requested should be valid for no longer than three years.
- Where companies request multiple authorities, they should clearly disclose the aggregate amount of the authorities.
- USS considers pre-emption to be a basic shareholder right that should not be eroded.
- Where companies wish to request a general authority to issue shares without pre-emption rights, they should limit the authority to no more than 10% of share capital.

Transition Pathway Initiative (TPI)

The Scheme’s voting principles integrate data from the Transition Pathway Initiative (TPI), at transitionpathwayinitiative.org, and the readiness for a transition to a low carbon economy, into voting decisions. USS may vote against the resolution to receive the report and accounts where it has concerns about a company’s management quality score, as assessed by the TPI. This would equate to a score of zero, one or two. We may vote against management or relevant board members in case there is no resolution to receive the accounts.

Environmental & social reporting

USS considers the disclosure of a company's environmental and social policies, strategies and performance permits investors to build a more complete picture of the quality of a company's board and management and, sustainability of the business. The reliability, comparability, materiality and relevance of the environmental and social information disclosed by companies is fundamental to this process. USS promotes high quality disclosure and performance management of environmental and social issues through engagement with companies and the Scheme’s voting activities. USS expects all companies to disclose information on their exposure to and management of key environmental and social risks (such as climate change, pollution, and human capital). USS may vote against on the resolution to receive the report and accounts (or equivalent) or other resolutions where:

- The environmental and social disclosure provided is insufficient.
- The company’s environmental or social performance falls short of standards expected by USS.

USS may vote against management or relevant board members in case there is no resolution to receive the accounts.

Shareholder resolutions

Shareholder proposals, including those which relate to environmental and social issues such as climate change, human rights, labour relations and other ethical matters, will be considered on their individual merits. We will support those resolutions considered in the long-term interests of shareholders. However, if we consider the resolution as overly burdensome or better addressed through another route, we will not support it. USS tends to support shareholder resolutions which encourage good corporate governance, environmental and social practice.

Dividends

Companies are encouraged to put the final dividend to a shareholder vote at the annual general meeting. Where USS has concerns regarding the capital allocation decisions, or dividend policies of a company, it may be appropriate to register concerns when voting this resolution.

Donations

USS discourages companies from making political donations out of corporate funds. USS considers all distributions from company profits (or losses) should be transparent and accountable to shareholders, including charitable donations.

Voting at shareholders' meetings

Proxy voting: Shareholders voting by proxy should have the same voting rights as shareholders voting in person at the meeting.

Virtual meetings: Companies should not impede physical shareholder attendance at general meetings. A "virtual" (online) AGM should not be held without offering a physical AGM where the company's Board, executives and shareholders attend in person. However, we recognise that in exceptional circumstances, a physical AGM may not always be possible and in such circumstances, we may accept a virtual AGM as a temporary solution.

Disclosure: Meetings materials (notice of meeting, proxy card and annual report) should be published sufficiently ahead of the meeting to enable shareholders to vote in an informed manner. USS will vote against where there is insufficient information available to make an informed voting decision.

Poll voting: General meetings should be conducted using poll voting on all agenda items. The poll should be fully disclosed as soon as possible after the meeting on the company's website and announced to the market.

Bundled resolutions: Bundling of matters for consideration that should be put to separate shareholder votes is strongly discouraged.

About USS

Universities Superannuation Scheme was established in 1974 as the principal occupational pension scheme for universities and other higher education institutions in the UK.

USS has more than 470,000 scheme members across over 330 institutions and is one of the largest pension schemes in the UK, with total fund assets of £82.2 billion.

The scheme's trustee is Universities Superannuation Scheme Ltd, a corporate trustee which provides scheme management and trusteeship.

USS Investment Management Ltd (a wholly-owned subsidiary of Universities Superannuation Scheme Ltd) is the principal investment manager and advisor to the scheme.

USS Investment Management Ltd is authorised and regulated by the Financial Conduct Authority and based at USS Investment Management Ltd, 6th Floor, 60 Threadneedle Street, London EC2R 8HP, UK.