

Marks and Spencer Pension Scheme - Responsible Ownership Policy Statement

GENERAL APPROACH

Marks & Spencer Pension Scheme ('M&S PS') believes that having engaged owners who are clear about their expectations will help companies produce sustainable value and that companies' long-term financial returns are connected to their strategic, environmental, social and governance performance.

M&S PS has appointed Hermes Equity Ownership Services ('EOS') to act as its agent in carrying out public policy, best practice and corporate engagement across all equity and corporate bond portfolios and voting for any / all segregated equity portfolios held within its defined benefit pension scheme at any point in time. M&S PS believes in the value of collaborative shareholder action and where applicable, will communicate and collaborate with other shareholders. Hermes EOS assists M&S PS in fulfilling its undertakings as a signatory to the UNPRI and as a signatory to the UK Stewardship Code.

Hermes EOS typically conducts engagement and voting related dialogues with companies in confidence and will not disclose M&S PS's involvement in such engagements, unless specifically agreed in advance. For companies identified by M&S PS as being of particular interest to M&S PS, Hermes EOS will revert to M&S PS for further instructions before abstaining, exercising a vote against management or in favour of a shareholder resolution and in advance of engaging with these companies. This consultative approach is also adopted by M&S PS with regard to the indexed equity fund managers who manage pooled equity vehicles on behalf of the Scheme.

In carrying out company monitoring, voting and engagement activities on behalf of M&S PS, Hermes EOS uses as a basis for its approach M&S PS's Responsible Ownership policy as described in this document and the Hermes Responsible Ownership Principles (http://www.hermes.co.uk/Portals/8/Hermes_Corporate_Ownership_Principles_non-US.pdf), and regional policies (<http://www.hermes.co.uk/eos/en-gb/literature/policydocuments.aspx>). With respect to the pooled equity funds within the defined benefit section, voting is undertaken by the relevant investment manager, while Hermes EOS may also engage with investee companies on behalf of M&S PS, as may the investment manager itself. In addition, all M&S PS engagement activities carried out are informed by social and environmental commitments made by Marks and Spencer – M&S PS's corporate sponsor – as described in its "Plan A".

PROXY VOTING

Proxy voting is an important investor right and responsibility. Through its agent, Hermes EOS (with regards to the segregated equity funds within the defined benefit section), M&S PS seeks wherever practicable to vote responsibly on every resolution at all meetings of companies in its portfolios. The voting rights attaching to the shares held by the pooled funds invested in by the defined benefit Scheme are voted by the relevant investment manager.

Voting is regarded as an important constituent of M&S PS's engagement programmes and the use of voting rights attached to shares held by M&S PS is appropriately aligned to the Scheme's overall responsible investment policies and objectives.

Voting recommendations are made based on the unique circumstances of each company, taking into account local best practice and regulation. Voting is undertaken pragmatically and in pursuit of positive change. The purpose of the vote is to achieve beneficial change in company behaviour, not simply to register dissatisfaction. Votes are executed in accordance with M&S PS's interests as a long-term owner.

Whenever possible, M&S PS, through Hermes EOS, seeks an open dialogue with portfolio companies in advance of casting a vote against management to explain M&S PS's rationale and to seek change to the company's position. Where a vote against management is cast, communication is continued with the

company to explain the voting action and to discuss possible solutions to avoid a recurrence. Whilst the responsibility for voting the securities held in the pooled funds in which the defined benefit Scheme invests is the responsibility of the relevant investment managers holding them, both Hermes EOS and the investment manager concerned may engage on behalf of M&S PS with regards to investee companies in these funds.

Specific Voting Policies

Board behaviours and composition

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

M&S PS encourages the development of appropriate board behaviour and expects open disclosure on individual directors' contributions to the board.

No individual director or small group of directors should be in a position to dominate the decision making process. M&S PS views independence as a mindset rather than as a box-ticking exercise.

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

In general, M&S PS supports the separation of the roles of Chair and Chief Executive to ensure that appropriate challenge is present at the top of the company.

M&S PS encourages active and open dialogue between the board and shareholders. While the first point of contact in most cases will be the chairman, it advocates the appointment of a lead independent director to facilitate this process where a conversation with the chairman is not appropriate.

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

Remuneration

Remuneration structures should be designed to incentivise executives to promote the long-term, sustainable performance of the company. In some markets, shareholders are entitled to vote on compensation structures and M&S PS ensures that votes are submitted according to the following policies.

- Ø Compensation structures should directly link pay with performance, avoiding the possibility of reward for failure and incorporating risk management to ensure practices that promote sustainable performance.
- Ø Significant consideration should be given by the remuneration committee as to how performance criteria and hurdles accurately represent the long-term goals and ambitions of the company. In particular, performance metrics should include company-specific measures and assessments of operational and financial risk and other risk factors, such as environmental and social risks, which could affect the long term health of the company.
- Ø The interests of key executives should be aligned with those of shareholders through material direct company investment.
- Ø Clear disclosure of remuneration structures and their rationale should be made annually with board consultation with major shareholders on material changes.
- Ø Independent directors' pay should not be structured such that it could impair their independence.

Risk management and audit

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

Regular reports on the effectiveness of the risk management function should be made to the full board with the audit or risk committee taking ownership of its supervision.

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

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

To promote accountability, shareholders should be given a vote on the re-appointment of the company's auditors.

Promotion of equitable shareholder rights

M&S PS aims to ensure its rights are protected by voting against resolutions that are considered not to be in its interests as a shareholder, including excessive dilution through share issuances and the establishment or maintenance of inequitable shareholding practices such as double voting rights.

Shareholder Proposals

Where shareholder proposals are submitted at M&S PS's portfolio companies, a full analysis of the benefits of the proposals to the long-term value of the company is made. This takes into account M&S PS's aims as a good owner and supports shareholder objectives that are consistent with promoting long term sustainable shareholder value at investee companies. M&S PS supports shareholder proposals that require full and timely disclosure of all policies, practices and matters that materially affect shareholder value.

ENGAGEMENT

Hermes EOS has been appointed to undertake engagements on behalf of M&S PS with companies on issues which may impact the companies' long-term sustainable shareholder value. Proposals for engagement, whether generated by Hermes EOS or M&S PS directly, usually involve some breach of the financial, strategic, operational, legal, social, environmental, ethical or governance principles set out below, or a breach of the Hermes Responsible Ownership Principles or their regional policies.

Engagements may relate to longer-term strategic, environmental, social or governance issues, which may not have immediate stock-specific impacts, for example where the company's shares are already fully valued and the intent is to preserve that value. Hermes EOS will escalate its engagement according to the nature and severity of the concerns.

Company specific engagements are normally undertaken by where it is believed that:

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

In determining whether and how the engagement is taken forward, due regard is given to the level of the company's exposure to the issue at hand and the likelihood of engagement success and potential to bring about positive change. Such considerations are based around an assessment of the likely impact of the engagement and the ultimate benefit to the value of M&S PS's holding.

Engagements may involve:

- Ø Meetings with executive and non- executive directors
- Ø Meetings with other company representatives
- Ø Discussions with the other shareholders of the company
- Ø Participation in collaborative investor initiatives
- Ø Submission of shareholder resolutions at general meetings as appropriate

In addition to engagement with companies, Hermes EOS has a broad public policy engagement programme internationally which it carries out on behalf of M&S PS and the other investors it represents, engaging with governments and regulators to promote the interests of long-term institutional investors.

Specific Engagement Policies

Governance

M&S PS's engagement policies on board behaviours, remuneration, risk management and audit and shareholder rights are covered under "Specific Voting Policies" in the Voting section of this document.

Culture

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

Strategy

We believe that companies should have coherent strategies for each business unit and the corporation as a whole. It should ensure that it is the 'best parent' of each of the businesses it runs. Engagement is undertaken with companies to ensure that capital is allocated appropriately to business units and investments whether organically or through acquisition. These allocations should be based on an assessment of where the deployment of capital will deliver the maximum, sustainable risk adjusted return. We encourage companies to give sufficient management focus to core businesses and the opportunities to exploit the company's core capabilities for growth and enhanced economic returns. Engagement is also carried out to challenge companies to employ an appropriate capital structure taking into account the cyclicity of the industries in which they operate and the growth opportunities available.

Environmental

Climate change

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

- Energy use / CO2 emissions

We encourage companies to take steps to manage and minimise energy use for financial and environmental reasons. Key sectors are all major CO2 users including extractives, utilities, heavy industry and transport.

- Carbon capture & storage

Where appropriate, companies are encouraged to develop this technology as we believe this will put them at a competitive advantage. The key industry is power generation.

- Extractives

Companies in the oil and gas and mining sectors are among the heaviest users of energy and generator of carbon emissions. There continues to be significant focus on issues such as the carbon-intensity of the process of extracting oil from Canadian oil sands and in other Extractives activities, air pollution and land reclamation. In addition, stranded assets have become an issue for the industry when long term investments are initiated but become obsolete before their completion. Engagement is carried out with those companies most exposed to this area to ensure that they are effectively managing the risks involved.

Water stress

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

Biodiversity

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

Forest Sustainability

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

Social & Ethical

People

- Labour relations

Engagement is carried out with companies that do not grant or recognise their workers important rights such as the entitlement to collective representation. Workers have a basic right to organise themselves and where such activity is barred they are likely to become disaffected, and so less inclined to work to their full potential or to continue their employment with the company. Target companies for engagement include those in the retail and hotel sectors and any industry employing large numbers of blue collar workers. In addition, company engagement also addresses whether the value of human capital more generally can be unlocked through progressive initiatives.

- Community relations

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

- Health & safety

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

- Compensation

Compensation is a key mechanism by which company executives' interests can be aligned with those of shareholders. Engagement is carried out with companies where this does not appear to be the case on an ongoing basis. Examples include investment banks which we encourage to pursue compensation practices that discourage excessive short-term risk-taking.

Ethics

- Supply chain / ethical sourcing

M&S PS believes that world class companies should manage effectively the reputational and business risks in their supply chains. Benefiting financially from poor labour practices in the short-term will drive misleading and unsustainable levels of profit, potentially skewing investment decisions. One particular issue in this area is child or forced labour. Some of the key sectors for these engagements are textile companies, the iron and steel sector, food manufacturing and agriculture. We note that there is a significant difference between seasonal child labour at small (particularly family) agricultural operations and more long-term systematic use of child or forced labour.

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

- Presence in troubled regions

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

- Bribery & Corruption

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

Sector specific issues

- Production of cluster munitions / landmines (defence)

We believe that the production of cluster munitions and landmines is unsustainable given the high level of international opposition to these weapons and their illegality in some jurisdictions. Engagement is undertaken with companies involved in the manufacture of such weapons, or components of such weapons, to encourage them either to cease production or, where this is not practicable, to disclose their position to shareholders

- Banking

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

- Access to medicine (pharmaceuticals)

We believe that pharmaceutical companies are at risk of reputational damage if they seek to limit the availability of drugs in developing countries by rigidly enforcing patents. At the same time, we recognise that such companies need to invest in research and make good returns for shareholders. Engagement is carried out with companies in this sector to encourage them to find appropriate solutions that meet both of these requirements. Other areas of engagement in this sector include the shift of clinical trials to less developed markets, regulatory and political risk, and animal testing.

- Licence to operate (tobacco, alcoholic beverage and food manufacturers)

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

EVALUATION AND REPORTING

Hermes EOS reports in detail on a quarterly basis to M&S PS on voting and engagement activity undertaken on the Scheme's behalf and prepares annually a detailed evaluation of the progress and impact of engagements on companies in M&S PS' portfolios.