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Global corporate governance and responsible investment policy

Intended for investment professionals only. Not to be distributed to consumers

Contents

Introduction

This document sets out what we consider to be responsible investment best practice. It explains our expectations with respect to topics we believe are essential for an efficient governance framework, and for building a sustainable business model.

We expect all companies in which we invest on a global scale to closely align with our principles, which set out the fundamentals of corporate governance. When developing our policies, we consider broader global guidelines and principles such as those provided by the United Nations Global Compact, OECD and ILO conventions and recommendations as well as local market regulatory expectations. The extent to which we apply these policies allows some leeway for those markets that are still developing their governance policies.

Although there is no 'one-size-fits-all' solution to building a sustainable business model, we look for the companies in which we invest to demonstrate that sustainability is effectively integrated into their long-term strategy and daily operations. Companies should aim to minimise any negative impact their businesses have on the environment, while innovating to find better solutions. Their strategies should include ways to make a positive impact on society, embrace the value of their workforce and supply chains, while delivering positive long-term returns to shareholders.

We have also developed other region-specific policies for the UK, North American and Japanese markets. They are publicly available on our website here.

We publicly disclose our voting decisions, including the rationale for votes against management. This data is accessible one day after the shareholder meeting here.

Company board

The board of directors is responsible for the management and long-term success of the company. In doing so, it should act as a steward of stakeholders' interests.

The board has the important task of setting strategy and direction, ensuring that the necessary resources are available to enable their implementation, and that appropriate risk management and internal controls are in place. The board is expected to take into account environmental, social and governance considerations, and to report on company performance in these areas. It is also responsible for ensuring the integrity of a company's accounting and reporting, and the effectiveness of internal control systems. Lastly, the board is ultimately accountable to investors and other stakeholders and should make sure its decisions are effectively communicated to them.

We acknowledge that the structure of the board may vary between companies and countries. However, we believe that the key elements of an effective board are universal.

Board leadership

We believe that having the right composition at the top of a company is an essential element of its success. We expect each director on the board to fully exercise their duties and promote the long-term success of the company.

We expect the board's decisions and actions to demonstrate leadership in managing the company's responsibilities to its stakeholders and to limit any negative impact of its operations on the environment.

As such, LGIM will usually hold the board chair accountable for failing to meet our minimum expectations under key policies to protect our planet and to safeguard society. For more information on key environmental and social focus areas please see below and our website.

Board chair and chief executive officer (CEO)

The responsibilities of the chair include leading the board, setting the agenda for board meetings, and ensuring directors receive accurate and timely meeting information. Under their direction, there should be a good flow of information between the board and its committees. The chair is also responsible for leading the appointment process of the CEO.

The chair should be able to challenge the executive directors and encourage the non-executive directors to actively participate in board discussions. It is the chair's role to regularly assess whether board members have the adequate skills, expertise and time commitment to make a positive contribution, and whether board composition is sufficiently diverse.

By contrast, the CEO has responsibility for executing the strategy agreed by the board and leading the business.

Given the importance of the role, we expect the chair to be independent.

We would therefore not expect a retiring CEO to take on the role of board chair, as these two roles involve different responsibilities and a different approach to board relationships and the company's strategy. Additionally, we recognise the challenge for those who previously had executive responsibilities to adequately distance themselves in a new role as the non-executive chair.

Where a company would find the presence of the former CEO on the board beneficial in times of transition, our preference is that the former CEO acts as a consultant, rather than as a formal board member. Their services should not be necessary for more than one year.

There are also instances where a company may, for a short period, be governed by an executive chair. This tends to be when the company is undergoing a shift in its structure or management or is under severe stress. In such circumstances, we expect companies to commit to separating the roles within a short, pre-set timetable. In addition, we expect that a deputy chair be appointed to ensure that no person has unfettered powers of decision-making.

For more details, please refer to our board guide on the nomination of the board chair, available here.

The case of the combined chair and CEO role

We believe that the roles of chair and CEO are substantially different and require distinctly different skills and experience. Therefore, we expect the two roles to be separated. This division of responsibilities ensures that a single individual does not have unfettered powers of decision-making at the head of the company, thereby securing a proper balance of authority and responsibility on the board.

If a company takes the decision to combine these roles, we believe that this decision should be put to a shareholder vote for approval, given that these are key board risk functions.

We expect companies that decide to maintain a combined role structure to appoint a strong senior or lead independent director, or deputy chair, as well as to provide a meaningful explanation and justification in their annual disclosures.

We believe that a separation of the board chair and CEO roles is positive for company culture, board discussions, remuneration policy and shareholder rights. Therefore, we will vote against the election or re-election of any individual holding such a combined role.

For more details, please refer to our board guide on the topic, available here.

Senior or lead independent director

We believe that the presence of a senior or lead independent director (LID) should not be limited to cases where there is a combined chair and CEO on the board.

The lead independent director plays an essential role on the board and should lead the succession process for the chair and appraise the chair's performance. Additionally, they should meet investors regularly to stay well informed of key concerns.

They can also be a key contact for investors, especially when the normal channels of the chair, CEO or chief financial officer have failed to address concerns or are not the appropriate avenues.

We expect the senior or lead independent director to be unquestionably independent. This is of particular importance for companies that have chosen to maintain a combined chair and CEO.

Our thought piece on the role of the lead independent director is available here.

Non-executive directors/outside directors

We expect non-executive directors to use their skills and experience to constructively contribute to board discussions and help develop proposals on strategy. They are expected to oversee management performance and provide constructive challenge at board meetings.

We encourage boards to appoint one non-executive director who may not have previous board experience, but has unique skills aligned with the strategy of the company. We hope this will support board discussions and help to develop the future pool of non-executive director talent.

Given the responsibility the role involves, non-executive directors must make sure they have sufficient time to perform their duties. We expect non-executive directors to take this into account when they take on any additional board roles. Please refer to our section on board mandates below.

Non-executive directors should continually update their skills and knowledge and agree on their specific training and developmental needs, which should include all aspects of social, environmental, and reputational risks faced by the business.

Structure and operation

Independence

A board's independence is essential in ensuring it exercises oversight and consistently acts in the best interests of the company and its stakeholders. Its importance to companies' performance has been shown in several academic studies. Therefore, as a minimum standard, we expect the board to include at least 30% independent directors. Well-governed companies should have boards with at least 50% independent directors; unless, employees comprise 50% of the board, in which case, we would expect the level of independence to be at least one third. In controlled companies (where at least 50% of the economic control is held by one person/entity or a group who are acting together), we also expect the level of independence to be at least one third.

We would consider a director to be non-independent if they:

- Have been an employee of the company or group within the past five years;
- Have, or had within the past three years, a material business relationship with the company either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the company;
- Have received or receives additional remuneration from the company, apart from a director's fee, such as the company's share option, performance-related pay or pension scheme;
- Have close family ties with any of the company's advisers, directors or senior employees;
- Hold cross-directorships or has significant links with other directors through involvement in other companies or bodies;
- Have served on the board for more than 12 years from the date of first election; or
- Represent a significant shareholder of the company.

Our separate regional policies take into consideration local best practice, and therefore may have stricter criteria. Please refer to these regional policies, available on our website, for more details.

We also recognise that non-independent, non-executive directors can offer significant skills and sector knowledge. In this instance, we expect the company to fully explain to its shareholders how the non-independent director provides valuable input to the business.

Diversity

We believe a diverse mix of skills, experience and perspectives is essential for a board to function and perform optimally. Several studies have demonstrated that a good level of diversity can improve business decision-making, minimise risks, improve the sustainability of profit growth and therefore maximise long-term returns for investors.

Please refer to our diversity policy for further information on the topic.

Developed markets

In France, Iceland, Norway and Sweden: we will vote against the re-election of the chair of companies where the underrepresented gender makes up less than 40% of the board. From 2026, we will expect all companies within the European Union to comply or explain.

In all other countries within developed markets: we will vote against the re-election of the chair of companies where less than a third of board members are women.

Global markets (markets not included above or in the specific regional policies)

We will vote against the re-election of the chair of all companies where there are no women on the board.

Board committees

Board committees ensure that specific directors are responsible for key board functions.

As a minimum, we expect all listed companies to put in place three separate board committees, responsible for the core functions of audit, nominations and remuneration.

Companies may choose to include other key committees such as a sustainability committee or advisory committee to assist the board in its discussions. A sustainability committee could be beneficial to a board by providing an increased focus on an issue that is directly linked to its long-term success or where the company operates in a high-risk sector where environmental and social risks represent a material part of the business model.

An advisory committee may be considered useful where a board needs direct access to independent external expertise from third parties or stakeholders. We are supportive of companies setting up advisory committees. We consider this a flexible option to obtain specific and relevant information to assist the board and management in their decision-making without having to affect the board's size and composition.

To enable investors to assess their effectiveness, we expect the role, composition, and activities of all board committees to be published in the annual disclosure documents.

Audit committee

The audit committee is responsible for:

- Monitoring the integrity of the company's financial statements;
- Appointing external auditors, monitoring their qualifications and independence as well their effectiveness and resource levels; and

- Oversight of the company's overall risk management to ensure that sound and robust internal controls are in place to appropriately manage the company's financial, operational and reputational risks.

As the audit committee plays a vital role in safeguarding investors' interests, we expect all companies to have an audit committee. Although the requirements in terms of the composition of the audit committee varies by country, LGIM would expect the audit committee to comprise only independent non-executive directors. The committee should have at least three members with sufficient financial experience to provide oversight and accountability. We expect the audit committee chair to have financial expertise. This requirement is a voting issue.

Non-independent directors may attend audit committee meetings by invitation, but we believe that they should not be members of the committee. LGIM's policy allows the board chair to be a member of the committee, if they are considered independent, but should not chair the committee. However, we note that in some countries the board chair is not permitted to be a member of the audit committee.

Members should have sufficient time to examine the company's financial statements and to liaise with both internal and external auditors. As a minimum, we expect the audit committee to formally meet at least three times per year. The chair of the audit committee should be available to answer investors' concerns on specific audit issues.

Nomination committee

The nomination and succession committee is responsible for overseeing all board and senior executive appointments, ensuring an orderly and successful board and executive succession process. The committee should ensure the board has the right composition, taking into account important governance considerations such as skillsets, diversity, tenure, and over-boarding.

The focus of the committee should not be restricted to the board and instead it must also seek to include alignment with the rest of the workforce in terms of human capital policies. The committee should work closely with the remuneration committee to ensure that appropriate service contracts are in place.

Given the key role of this committee in board composition matters, we expect a majority of its members to be independent non-executive directors.

The committee chair should be accountable to investors if it is felt that appropriate succession plans are not in place or where there are concerns over the composition of the board.

Remuneration committee

The remuneration committee is responsible for the setting the remuneration strategy for executive directors and senior executives. In doing so, the committee should be aware of the remuneration policy for all other employees below executive management level.

The chair of the remuneration committee should have appropriate knowledge of the business to align the remuneration policy with its strategy. For this reason, the remuneration committee chair should have ideally served as a member of the board for at least a year prior to their appointment as chair of the committee.

We expect the committee to consist exclusively of independent non-executive directors. We know that in some countries, the board chair is prohibited from serving on the remuneration committee. However, LGIM will support the board chair being a member of the committee but not as its chair. Non-independent directors may attend remuneration committee meetings by invitation, but should not be members of the committee.

Remuneration committees should:

- Seek independent advice. The committee should have the authority to appoint its own independent, external remuneration advisers to assist it. We recommend that information such as the use of such advice, and associated fees should be reported in public annual disclosures. The committee should exercise its own independent judgement when considering any advice provided by third parties. External advisers, consultants and internal employees advising the committee should be fully accountable to the committee.
- Consider carefully the company's pay and related policies and be able to demonstrate how they have reviewed these when setting pay for the executive team. The committee should also be able to demonstrate how executive pay is aligned with the company's culture.
- Challenge the management team if the company is paying less than the living wage to its employees and/or is not offering all employees the chance to work a minimum of 15 hours per week. This represents the minimum a company should be doing to reduce income inequality and poverty within its workforce.
- Consider the views of the company's shareholders. Many institutional investors' policies on executive pay are available on their website.

We will vote against the re-election of chair of the remuneration committee or individual board director's where we do not support the company's executive remuneration policy or its implementation for the second consecutive year or where there are particularly contentious issues.

Succession planning

Succession planning is a vital component of an effective board. It ensures continuity, provides individuals with the right sets of skills sit on the board and can help to avoid the dangers of 'group think'.

We expect companies to put in place a formal and transparent procedure for the appointment of new directors. The external board evaluation exercise should assist in this task. We expect the nomination committee, together with the board to consider setting short-, medium-, and long-term plans to ensure there is an orderly replacement of board members and senior executives. These plans should map out potential successors in the short term for unexpected departures, in the medium term to replace directors who reach their tenure limits, and in the longer term to take account of future skills and diversity requirements.

We encourage companies to publish as much of this information as possible in their annual disclosures. This includes the skills the company is looking for and why the selected individual is the right fit for the board.

In addition, we would expect to see a skills matrix linked to the company's strategy, and an explanation of how newly-appointed director's skills complement the matrix, and the minimum time commitment expected of each director.

Re-election of directors

To ensure the successful composition and functioning of the board, it is essential that shareholders exercise their voting rights by holding directors accountable.

We are opposed to the practice of bundled proposals that prevent shareholders from approving individual nominees to the board.

We acknowledge that the regulations that govern the frequency of director re-election vary greatly from one country to another. However, we encourage companies to allow shareholders to vote on directors' elections annually.

To allow investors to assess the profile of the board directors proposed for election or re-election and to make sufficiently informed voting decisions, we expect companies to disclose the name of the directors proposed for election or re-election and to provide a detailed biography of each proposed director. We would also encourage disclosure of the attributes and skills that the director brings to the board and how these fit with the combined skill set of other directors and the long-term strategic direction of the business. In addition, it would be useful to investors if companies provided information regarding the expected time commitment to the company, a record of attendance and an explanation if a director has missed a scheduled board meeting.

Board effectiveness

Culture

Companies should maintain the highest standards of conduct towards all stakeholders. The board should promote behaviour and values that demonstrate integrity and respect.

Boards should disclose information that helps investors understand their company culture. Investors need reassurance that the CEO and senior management are really driving the cultural message and setting the tone from the top, and that this is regularly discussed and challenged by the board, which should monitor how the cultural message is filtering down to the rest of the organisation.

We expect companies to disclose information in their annual disclosures including:

- How they measure culture and how that relates to the business strategy;
- How their mission statement values are communicated and reinforced; and
- Any key performance indicators (KPIs) that are linked to culture.

We may vote against the re-election of directors who we believe have not demonstrated good business conduct or have failed to avoid reputational risks caused by this, e.g., harassment, fraud.

For more details on our position, please refer to our publications on the topic, available here.

Board tenure

The regular refreshment of the board helps ensure that its non-executive members remain independent from executive management and third parties, that different perspectives feed into board discussions, and that skillsets remain relevant. A regularly refreshed board is more likely to be willing and able to question established practices, avoid group think, and exercise more efficient oversight over management to stay ahead of market changes.

Board tenure is assessed in two different ways:

- On an individual director basis: we consider the optimum tenure for a director to be between 6-12 years.
- On an average board tenure basis: average tenure across all board members should not exceed 9 years.

Although different regions have different best practice guidance on this issue, we expect all companies to put in place an individual director term limit of a maximum of 12 years. Please refer to our regional policies for more details on regional expectations on tenure.

Board mandates

We believe it is important for executive directors to seek an external board role at a different company as this will help broaden their skills and knowledge, enabling them to provide more input to board discussions. However, when taking up an external board appointment, they should be mindful of the time commitment required to exercise their duties on multiple boards.

In our view, as the number of boards on which a director serves increases, so does the risk that they may become less effective. This risk increases further, depending on the role and time commitment needed due to the company's size and complexity. A director has a duty of care to ensure they have sufficient time to fulfil each role effectively. We would encourage executive directors not to undertake more than one non-executive directorship of an unrelated listed public company.

We also encourage non-executive directors to limit the number of company boards they serve on to five. We consider an independent board chair role to count as two due to the extra complexity, oversight and time commitment that it involves.

Shareholders would benefit from an understanding of the time commitments required for each board mandate held by a director.

Board meetings and attendance

Regular board meetings are vital for the board to effectively perform its duties. We believe the chair should hold separate meetings with the non-executive directors to discuss the performance of the executives. In addition, the non-executives should have at least one meeting during the year without the chair present.

Director attendance at board meetings is a vital part of the role to ensure contributions to board decisions and fiduciary duties to investors are fulfilled. We therefore expect companies to allow investors to assess directors' attendance at board and committee meetings by disclosing attendance records in their annual disclosures. We expect directors to have attended at least 75% of board and committee meetings held during the year. Where a director does not attend a board or committee meeting, the company should provide investors with an explanation for the absence. We would not expect to see a trend of a director's non-attendance at meetings. Where a director's attendance is below 75%, and the board has not provided an explanation, LGIM may vote against the director's re-election.

Board size

LGIM believes a company should put in place a board that is appropriate for the size of the company and complexity of the business. It is essential that the size of the board does not compromise any exchange of thought, challenge and efficient decision-making. It should not be so large as to be unwieldy, which can reduce its effectiveness. In our view, the optimal size of a board is between 10 and 15 directors.

Board effectiveness reviews – internal and external

Board effectiveness reviews have become a more established practice globally as boards increasingly recognise their benefits. The board review can provide investors comfort that the functioning of the board is being regularly assessed to ensure it continues to operate effectively, and that the company is operating in a way that is consistent with its purpose and values.

External reviewers can also bring different perspectives on how the board is functioning, as well as experience of how other boards operate. We expect an external evaluation of the board to take place at least every three years. This should be performed by an independent third party to avoid conflicts of interest. The board as a whole should approve the appointment of the reviewer who should not be used for this role for more than two consecutive times. The board should agree the scope of the evaluation at the outset and receive the findings at the conclusion of the review.

To safeguard the independence of the external board evaluator, we discourage them being appointed to provide other professional services to the company. Where an external board reviewer is providing other services, we expect these to be disclosed, and a minimum cooling-off period to be adopted and disclosed.

In the interests of transparency, we expect the process and general outcomes of such evaluations to be published in the company's annual disclosures, as well as any progress made on the outcomes of previous board evaluations. For more details on our position on the topic, please refer to our thought piece on the topic, available on our website here.

Board responsiveness

Voting at company meetings is part of a shareholder's escalation strategy to signal concerns with aspects of the company's governance. Where 20% or more of votes have been cast against a board's recommended resolution, we expect the board to engage with shareholders to determine their reasons. The next annual report should provide information on the steps they have taken to address shareholder concerns.

A vote against a relevant director's re-election may be applied if the company has not provided information regarding the concerns expressed by shareholders that led to the high vote against, and any actions taken by the board to address shareholder concerns.

Non-executive director induction

The chair is also responsible for ensuring that incoming non-executive directors receive a comprehensive induction to the company on joining the board and that training is available on an ongoing basis. This will allow new directors to contribute to board meetings as soon as possible.

We support the view that companies' divisional directors should hold regular briefings or presentations to the board to ensure that members are kept informed on all aspects of the business. The corporate secretary can also be an important training resource for non-executive directors.

Directors should be encouraged by the chair to continually update their skills and knowledge and should agree on their specific training and developmental needs, including all relevant aspects of social, environmental, and reputational risks faced by the business. One way to remain up to date is to regularly meet with investors, along with other relevant board members, to gain knowledge and to hear various perspectives.

LGIM organises an annual seminar in the fourth quarter for board directors covering key governance and sustainability topics. We also regularly publish thought leadership pieces on relevant topics related to corporate governance, stewardship and responsible investment, which can be accessed through our website and the LGIM blog.

Stakeholder engagement

We believe companies should be managed to consider stakeholder interest on material issues. Therefore, regular dialogue with key stakeholders is encouraged to ensure a good understanding of any material concerns. We expect companies to report in their annual disclosures how engagement with key stakeholders has fed into board discussions.

Employee dialogue

We acknowledge that different countries, through regulation or best practice codes, may have different approaches to how boards should consider the views of their employees. We believe investors should be able to hold directors accountable for their consideration of employee views.

Where hard or soft law does not provide any guidance, we encourage companies to set up an appropriate structure. Companies may prefer to appoint employee representatives to the board or use forums or advisory panels.

We do not consider any single model superior to another. All companies should embrace their employees as valued assets and select the method that is most effective for their business model and current circumstances.

For more details on our position on the topic, please refer to our thought piece on this issue available here.

Investor dialogue

We believe that engagement is a vital risk-mitigation tool for the board. Engagement with investors should be a two-way discussion. Board directors should aim to use engagement meetings with investors as an opportunity to explain company decisions and to make sure they are well understood by the market. Such meetings should also be an opportunity to listen to investors, use their experience and act on their feedback.

LGIM's stewardship priorities include focusing on material issues that are not only important to our clients, but also pose a material risk to the long-term value of the assets we manage on their behalf, e.g., climate change, human rights, health, etc. As such, we are not always available to have general engagements with companies.

LGIM encourages companies to proactively request engagement with their investors at the earliest opportunity if the company is concerned that a specific governance issue might be subject to a negative vote, and for which the board wishes to provide additional context/information or to seek investors' opinions. Our position on board-investor dialogue is captured in our guide to board-investor dialogue.

Audit, risk and internal control

The board is responsible for determining and disclosing the company's approach to risk, its risk appetite, and monitoring the outcome and controls in place for effective risk management.

It is also responsible for presenting a true and fair view of the company's financial position, and should set out its future capital management plans and near-term financial prospects.

Processes and procedures should be established to ensure the independence and robustness of the internal and external audit functions.

The board is responsible for assessing the effectiveness of the internal and external audit functions, as well as the resources available to them. We expect the board's annual disclosures to investors to include its conclusions of this review along with bespoke narrative on the assessment and noted areas, along with actions taken to address any concerns.

Compliance with regulations

The audit committee should ensure that all applicable laws and regulations are complied with to avoid exposing the company to undue risk of fines, censorship and reputational damage. We will hold the audit committee chair responsible for failing to detect breaches in accounting practices.

External audit

An external audit provides independent assurance of a company's financial statements to its investors. The role of the auditor is to provide reasonable assurance that the financial statements give a true and fair view of the financial health of the company and that they have been prepared in accordance with appropriate accounting standards. Any significant audit matters raised by the auditor should be fully explained by the board, including how these have been addressed.

The external auditors are also responsible for producing the auditor's report, which is a formal opinion and evaluation of the financial statements. We support and encourage the use of the extended audit report to provide greater insight to investors of the auditor's assessment of the accounts.

The board is responsible for appointing the company's external auditor. The company is expected to clearly disclose the audit firm used, the audit partner who led the audit, the tenure of that firm, and why the board considers the auditor to be independent and how any potential conflicts are being mitigated. We believe the role of the external auditor should be put to tender on a regular basis – at least every 10 years – with the total tenure of the audit firm not exceeding 20 years. Within this timeframe, we expect the lead audit partner to be subject to refreshment at least every five years. We will vote against the election of the external auditor if they have served as external auditor for more than 20 years.

We also expect companies to include one audit firm that is not one of the global top four firms in the tender process. The way the tender process is carried out should be explained to investors in annual disclosures, covering whether it included a firm outside the global top four firms and why the successful firm was selected.

The fees for the external audit should be disclosed in the company's annual reporting. Where the external auditor provides additional non-audit services, these should be fully explained and disclosed in the appropriate annual disclosures. We expect any non-audit services provided to be incidental to the audit, with the primary purpose of improving the quality of the financial accounts. We do not expect excessive non-audit work to be conducted by the company's external auditors, as this will bring into question the independence of their judgement. We do not expect non-audit related services to exceed 50% of the value of the audit services in any given year. We expect companies to disclose audit and non-audit services fees as two separate amounts in their annual disclosures. LGIM will vote against the election of the auditor or the approval of their fees if this information is not provided.

We believe auditor liability is an important and proportional approach to supporting a high-quality audit. We are not supportive of a fixed auditor liability or restrictions on that liability.

The audit committee should explain how it has assessed the quality of the external audit and recommendations arising from the external audit, and this should be reported to investors when considered material by the board or the audit partner.

Internal audit

Companies should have an effective and sufficiently resourced internal audit system in place that is designed to take account of new and emerging risks that may affect business objectives and identify the level of risk taken. The process and procedures in place to manage such risks should be embedded in the company's risk-based control system and summarised in the annual reporting to investors. The audit committee should have responsibility and oversight of the internal audit function.

Whistleblowing

We expect companies to establish a whistleblowing policy that is integrated into its code of conduct. The policy should be publicly disclosed and open to all employees including those within the supply chain. The whistleblowing reporting channels should be easily identified and channelled through an independent third-party with a direct line to the audit committee to allow for appropriate oversight and independent escalation where necessary. Companies should ensure their policy safeguards the identity of any whistle-blower and that they are protected from internal harassment. Companies should also report how the risks associated with bribery and other illegal behaviour are being monitored and addressed.

Cybersecurity

The vulnerability of a company's IT systems can lead to a material financial impact and reputational damage. Therefore, we expect a risk-based approach to be taken to address the issue of cybersecurity and data protection. It should be integrated into the business's control functions and overseen from a strategic perspective by the board. It is the board's role to understand the infrastructure needed in the business to protect valuable information assets, key intellectual property, and customer's confidential data. Therefore, accountability should not be delegated. Cybersecurity should be a regular board agenda item. Any data breach incident should be disclosed to customers and the market in a timely manner.

For more information, please refer to our guide on the topic, available here.

Climate risks

We expect companies for whom climate change is a material financial risk to appropriately reflect these risks in the scenarios, assumptions and estimates used to prepare their financial accounts. Companies should ensure, through transparent disclosure, that there is consistency between their narrative on climate change and their accounting determinations. In addition to our ongoing targeted engagements relating to climate accounting topics, we will develop our work further in this area. This may lead to applying voting sanctions on companies that fall short of minimum expectations from 2024.

Remuneration

We are increasingly concerned about the misalignment of the total opportunity of executive pay versus company performance, and the current social sensitivities around income inequality.

To address the issue of income inequality, LGIM expects remuneration committees to be mindful of the pay and benefits offered throughout their organisation. LGIM's minimum expectations on employee pay and wellbeing can be found below.

As a long-term and engaged investor, we entrust the board to ensure executive directors' pay is fair, balanced and aligned with the strategy and long-term growth and performance of the business.

Although we appreciate it is not yet standard practice in many countries globally to disclose all details of executive remuneration in their annual disclosures, we believe it is important for investors to understand how executive directors (internal directors) are being remunerated and whether the remuneration is aligned to the delivery of sustainable performance.

In several markets around the world, shareholders are given a 'say on pay' vote which we consider to be important to hold the remuneration committee members to account for the decisions taken in relation to executive pay policy or its implementation. In some markets, these are advisory votes, while in others they are binding votes. The amendments made in 2017 to the Shareholder Rights Directive meant that companies within the European Union are required to put their remuneration policy and their remuneration report to a shareholder vote at least every four years. In Australia, their binding vote means that if a company receives a 25% vote against their pay resolutions in two consecutive years, it triggers a 'spill vote' which allows shareholders a vote to decide whether board members should stand for re-election.

LGIM encourages more countries globally to mandate a 'say on pay' vote and for all companies to disclose their executive remuneration structure, including the total opportunity under each element of pay together with a description of the metrics and targets used under incentive plans, where applicable if they are not considered commercially sensitive.

Although we are cognisant of the variations in executive pay practices globally, we expect companies to consider our principles when setting pay policies for their executive board.

Key principles

We apply a set of simple pay principles when looking at remuneration structures:

- The structure of remuneration and the payments awarded should be fair, balanced and understandable. This means fair in terms of what the company has achieved; balanced in terms of total pay opportunity to the executive, versus employees and investors; and understandable for the recipient, the board and investors.
- Awards should incentivise management to focus on the long-term and be aligned with and support achieving the business's strategy and objectives.

- Executives should have meaningful direct equity holdings while employed and thereafter; buying shares is one of the best ways of aligning the interests of management and investors.
- Boards should retain the ultimate flexibility to apply discretion and 'sense-check' the final payments to ensure that they are aligned with the underlying long-term performance of the business.
- Companies should be transparent on why rewards have transferred to the executive, setting out targets, their relevance to meeting long-term goals, which targets were met and justifying all adjustments made to accounting measures for remuneration purposes.

Fixed remuneration

We expect executives' base salary to be commensurate with the size and complexity of the company. Although salary levels at peer companies may be considered, these should not set a definite benchmark.

Salary increases should not be automatic each year. Any increase to salary levels should not exceed what is offered to the general workforce, and its impact on total remuneration should be assessed before approval.

Addressing the cost-of-living crisis – the remuneration committee of companies that have decided to give employees on lower salaries a significant pay increase to help them navigate the current crisis should exercise caution if they plan to use the average workforce salary increase rate when setting executive salaries. Consideration should be given to the impact of a similar increase on the total pay for an executive given the inclusion of incentives that are based on a percentage of base pay.

Incentive arrangements

Annual incentive

Companies may choose to award annual incentives to executive directors. We believe that any annual incentive should be geared towards delivering the business's strategy. A majority of the annual incentive should be linked to the delivery of financial performance. In addition, achieving a threshold level of financial performance should be a pre-requisite for payment of any bonus that is based on personal or strategic objectives.

Companies exposed to high levels of environmental, social or governance risks should include relevant and clearly measurable targets that focus management on mitigating these risks. These metrics should be meaningful, measurable, aligned to the company's strategy and subject to third-party verification.

For companies in high-risk sectors, where the health and safety of employees is key, we would expect a health and safety modifier to be introduced to the annual incentive to ensure that board members are held accountable for any loss of life within the workplace. Where a company is held responsible for any fatality within the workplace, we expect the remuneration committee to apply downward discretion on any performance-based pay earned. Although we expect any reduction to be material, if it is less than 20%, LGIM will vote against the company's remuneration report.

We ask companies to pay a portion (at least one-third) of the annual incentive in shares deferred for at least two years. Additionally, the annual incentive should be set as an appropriate proportion of base salary.

We expect companies to disclose the maximum level of annual incentive that may be awarded together with the performance conditions that will determine whether an award is justified.

For those companies aiming to follow best practice and highlight the integrity of the target-setting process, we expect the disclosure of weightings for each performance condition and the target ranges, at the very least on a retrospective basis. Targets that are commercially sensitive to the business should be disclosed within a year of payment; if this is not possible, an explanation of why the target continues to be commercially sensitive is expected.

Our expectation is that companies will use financial metrics that are reported in annual disclosures to determine performance. If these are adjusted in any way for example by excluding exceptional items, we expect the company to report how the calculation differs from the reported numbers and why it is considered appropriate to make the adjustment.

Long-term incentives plan (LTIP)
We believe that a company should motivate and reward executives by granting long-term equity incentives that will align their interests with those of long-term investors. Incentives should be structured to motivate management to build a sustainable business that will generate positive returns to investors over the longer term. Therefore, we encourage the adoption of a long-term incentive plan that will deliver the reward in the form of shares. We generally do not support cash-based long-term incentive plans.

In the interest of simplicity, LGIM advocates the adoption of one long-term plan. We discourage the adoption of any additional incentive plans that would complicate the remuneration structure, e.g., matching schemes, or that would reward executive directors for motives that should already be addressed by the LTIP, e.g. retention plans or transaction-bonus-type schemes.

LTIP awards:

We believe LTIP awards should be capped either as a percentage of salary or a fixed number of shares. Where a fixed number of shares is used, we would expect the level of award being offered to be reviewed every three years to ensure it is at a level commensurate to when the plan was first adopted. Any increase to levels of reward should be subject to shareholder approval.

Where a company has experienced a significant fall in the value of its shares, resulting in a greater number of shares being awarded under incentive plans for the year, companies are expected to reduce the size of the award to ensure there is no prospect of reward for failure. Where this has not happened, the remuneration committee should provide an undertaking to reduce awards when they vest. At the point of vesting, LGIM will expect a detailed explanation of how the committee has applied discretion to ensure appropriate adjustments were made to avoid windfall gains. LGIM will vote against a company’s remuneration report where we believe that the remuneration committee has not been thorough in its decision making and/or not provided sufficient information to explain its final decision.

LTIP performance conditions:

The board should determine the right metrics to deliver the strategy and ensure that the level of stretch in the target is appropriate to deliver the right outcomes for all stakeholders. Metrics should be linked to long-term strategy and should be challenging, but achievable, without encouraging undue risk-taking.

We do not recommend the use of more than four performance conditions as each additional measure will dilute the importance of the performance that it intends to reward, as well as increase the complexity of the incentive plan. We expect at least one measure to be linked to shareholder returns. Other measures should be linked to the business's strategy, such as key performance indicators (KPIs) that are selected by the board and reflect the company's ESG risks as well as target opportunities. Absolute share price measures used in isolation are considered insufficient justification for award vesting.

We support the use of relative total shareholder returns (TSR) subject to an appropriate benchmark group being used. However, we expect median performance to be the minimum performance that may trigger a reward. If used as a performance modifier, we would expect performance below median to trigger a reduction in the financial reward.

We would expect the full award to be subject to performance conditions and measured over at least three years. However, in markets where governance structures are still being developed, we have set a minimum standard of 65% of the award to be performance-based. These should still be assessed over a minimum of three years. We may vote against companies that fail to provide sufficient transparency of their target-setting policy to assure investors that robust performance targets are being set. We expect companies to prospectively disclose all performance conditions and as many individual targets as possible. In addition, except during periods of structural change, we would expect targets set to be higher than the actual performance achieved in the previous year.

We expect the remuneration committee to maintain sufficient authority to exercise discretion when there is not a clear link to performance.

We do not support retrospective changes to performance conditions that have been pre-set.

Use of ESG metrics

Companies in sectors that can have a significant effect on climate change should link part of their pay to delivering on their climate mitigation goals. The performance targets should be linked to SBTi approved/or equivalent transition plans aimed to achieve net zero by 2050 or sooner. Targets should also be set to create new opportunities that not only improve revenue, but also have a positive impact on climate.

By 2025, companies will have only five years to reach their 2030 climate change transition goals. By this time, we expect a majority of companies will have a clear idea of what must be done to hit these crucial targets. Therefore, from 2025, LGIM will escalate its policy on climate change. From January 2025, we will only support new remuneration policies being put to shareholders if there are climate targets within performance-based pay and ideally within the long-term plan. These targets should be in line with stated transition goals to reach net zero and across the full value chain (scope 1-3). Ideally, they should be SBTi approved.

This will apply to companies in the following sectors: autos, apparel, aviation, aluminium, banks, cement, chemicals, food, forestry, glass, insurance, logistics, mining, oil and gas, REITs, shipping, steel, technology, telecoms, and multi-utilities.

The weighting for climate targets should be meaningful and if used within an LTIP, it should represent at least 20% of the overall LTIP award at these companies. For companies that have adopted a restricted share plan, one of the underpins should be specific to achieving set transitional carbon reduction targets.

The use of diversity targets would be relevant for sectors that struggle to recruit women.

LGIM discourages the use of employee engagement targets, as we believe well-governed companies should have an inclusive culture in place. Financial incentives should not be necessary to drive such a programme. In our view, a better metric for companies, especially for those that have a high level of staff turnover, would be to set targets around employee retention to gauge whether their internal strategies to improve retention are working.

For oil and gas companies, remuneration should prioritise financial value over fossil fuel production volumes. The use of measures that directly encourage volume growth (such as reserve replacement ratios or production targets) risks incentivising overinvestment at a time when growth in demand seems increasingly uncertain and should therefore be avoided. LGIM prefers financial measures (relating to total shareholder return, balance sheet strength) or other strategic metrics. The use of volume growth targets may result in a negative vote.

Holding periods

We encourage the use of a two-year post-vesting holding period because we find this helps in aligning the remuneration structure with long-term performance. These holding periods should continue to apply even after a director has ceased employment with the company.

Dividends

Accrued dividends on share awards should only be paid on those shares that ultimately vest. LGIM will vote against any share-based incentive plan’s operation if it permits the payment of dividends on unvested awards.

Malus and clawback

Employment contracts should be designed to enable the application of malus and clawback, which should apply to all elements of variable remuneration.

To provide clarity for all stakeholders, remuneration committees should set out the circumstances under which malus and clawback will be applied. These circumstances should not be too narrowly defined.

Equity dilution

We believe that strict guidelines should be adhered to in relation to the issuance of shares for incentive schemes to limit the potential dilution to shareholders. As a general rule, we expect no more than 10% of a company’s equity to be used for all share schemes over a 10-year period and no more than

5% in 10 years for discretionary schemes. The annual run rate or burn rate should also be reasonable; or about 1%.

These limits may vary in certain regions and any variance will be highlighted in the relevant regional policy. Treasury shares should be included within these limits. Such restrictions should apply to all newly-issued shares. We encourage companies to provide transparent explanations regarding the issuance of shares.

Shareholding guidelines

We expect companies to encourage their directors and senior executives to build up and retain a meaningful interest in the shares of the company they manage. This is an essential part of aligning directors' interests with those of investors. The level of shareholding should be linked to the size of the company and the level of reward that the director receives under the long-term incentive. Ideally, these shares should continue to be ring-fenced by the company in a trust.

Shares held within an unvested incentive award, including those held in retention periods, should not be included in the calculation of shareholding guidelines.

Pensions

Generally, pension contributions are not only a significant cost and risk for a company, but are also an element of remuneration that is not linked to performance. Therefore, the cost of providing a pension should be considered when evaluating a remuneration package. We will not support pension-enhancement payments at retirement or when a contract is terminated early. Additionally, we will not accept an individual being compensated for changes in tax. Companies should aim to reduce their pension fund liabilities and costs when recruiting new executives.

Pension provisions should be disclosed in full in the report and accounts and any changes to pension benefits should be fully explained.

We expect companies to work towards aligning pension benefits for their executives with what is offered to the general workforce.

Service contracts and termination payments

Executive contracts should provide for a maximum notice of 12 months. We do not support provisions within service contracts that enhance contractual terms for loss of office following a change in control.

Contracts of key people should provide the company with the authority to clawback unvested and vested awards.

New joiners

When setting the remuneration package for a new executive who lacks experience in the company and/or the role, we would encourage the remuneration committee to consider placing the individual on a lower salary than their predecessor, with a view to increasing their pay over an extended time, subject to continued good personal and corporate performance. We encourage the committee to set out its intention to increase their pay over a set period at the time of appointment and in subsequent disclosures to remind investors of this intention. Where possible, the existing remuneration arrangements should be used to incentivise new appointees.

New recruits should be encouraged to purchase shares in the company. Additional benefits in relation to the appointment, such as assistance to relocate, should be time limited and mirror the policies available to employees.

We do not support the use of ‘golden hello’ payments. Where a buy-out of existing awards from a previous employer is necessary, it should only cover the expected loss of value, and be awarded predominately in shares and be subject to performance.

Departing directors

We expect companies to ensure that there have been no rewards for failure. Therefore, the remuneration committee should take into account poor performance or any exceptional events and consider whether ‘good leaver’ or ‘bad leaver’ provisions should apply when determining whether a director should be paid a bonus for the period worked.

With the exception of dismissal for cause and/or poor performance where incentive awards should lapse, any outstanding share-based awards of leavers should be time pro-rated and allowed to run their course, subject to the same vesting conditions that applied at grant.

To promote long-term strategic decisions and shareholder alignment, directors should continue to hold a meaningful number of shares in the company even after their departure.

Although post-exit shareholding requirements are not typical in most markets, we believe there is value in requiring an executive director to maintain a percentage of their shareholder for a guideline period of two years from the time of departure. Although there are arguments that the director can no longer influence company performance after they leave, we believe this measure will ensure that directors continue to perform until their departure.

LGIM considers a significant post-exit holding to be no less than 80% of the in-post requirement. As a guide, vested shares, deferred bonus shares and shares subject to a holding period can count towards meeting shareholding guidelines. Any shares purchased by a director with personal funds are excluded from the post-exit shareholding requirement.

Benchmarking

We discourage over-reliance on frequent benchmarking and would not expect pay to be increased automatically each year. Benchmarking should not be used to justify a substantial increase to pay levels.

When using benchmark data, the remuneration committee should take into consideration several factors: size of the company, its geographic spread and performance relative to the benchmark peers. The peer group should not be too large or too small as both extremes could produce misleading results. Companies should ensure they disclose meaningful information on the benchmarking data used and why it has selected the benchmark group. Directors at underperforming companies should not expect to be remunerated as highly as directors of companies with outstanding performance.

Discretion

Companies can build trust with investors if they can demonstrate restraint, consistency, and alignment with the shareholder experience. In exceptional circumstances, discretion applied to any earned award by executives is one way to demonstrate this alignment. We define discretion as anything that alters the monetary outcome of total remuneration.

We expect the company to state:

- The main reasons that might give rise to the application of discretion
- Whether their discretion policy applies to revising pay upwards as well as downwards
- The elements of pay to which discretion may be applied
- The effect that the application of discretion has had on the director’s final pay outcome

Non-executive directors' fees

Non-executive directors’ fees should reflect the level of responsibility and time commitment of the role. The use of share options or other performance related pay is not supported, but a proportion of the fees may be paid in equity shares.

Shareholder and bondholder rights

The provision of shareholder and bondholder rights is a basic entitlement for investors. We expect companies to acknowledge and respect the rights of investors by adhering to the highest market standards. This includes providing high-quality disclosures and equal treatment of shareholders. Below, we have outlined guidance on the topical issues that concern us as an investor:

Voting rights and share class structures

We support the 'one share one vote' philosophy and favour share structures where all shares have equal voting rights and those rights are commensurate to the economic value held. We do not support the issue of shares with enhanced or impaired voting rights. In some markets, however, differential voting rights are a long-standing structure, and where this exists the structure should be transparently disclosed. In the case of controlled companies, we will review the issuance of shares with enhanced voting rights to understand why these would be necessary. In general, we encourage companies to eliminate differential voting rights over time.

Amendments to the company's constitution

It is common to see requests from companies seeking approval to update/amend the company's Constitution, specifically their Articles of Association.

We expect these changes to be clearly outlined and disclosed in the notice of meeting. We do not support changes to a company's constitution that are introduced to curtail or reduce shareholder rights.

We would expect substantially different changes to a company's constitution to be proposed under separate resolutions and not to be bundled into a single amendment to the constitution. Where such a bundled resolution includes one or more changes that are not deemed supportable, this will lead to a vote against the entire proposal under the resolution.

Executive forum provision

We believe that exclusive forum bylaw provisions limiting a shareholder's choice of legal venue are not in the best interests of shareholders. Such clauses may effectively discourage the use of shareholder derivative claims by increasing their associated costs and making them more difficult to pursue. We do not encourage limitations on shareholders' legal recourse including limiting themselves to a single jurisdiction without compelling evidence that it will be of benefit to shareholders and expect companies to provide a compelling argument on why the provision would directly benefit shareholders.

Virtual/electronic general meetings

We believe that a company’s general shareholder meetings are fundamentally important to the exercise of shareholder rights and integral to a good corporate governance system. Furthermore, we view physical shareholder meetings as providing an important mechanism by which a board is held publicly accountable to all their shareholders, both institutional and retail.

Shareholder meetings provide an invaluable opportunity to raise concerns with a board in a public forum and investors can use this mechanism as part of their stewardship activities. For example, they could be utilised as an escalation tool that enables shareholders to make statements and ask questions to the whole board.

We are cognisant that companies are keen to make sure that their shareholder communications keep pace with developing technology and virtual shareholder meetings is an area of focus. We also agree that using technology, such as webcasts, to complement the physical shareholder meeting could be beneficial and could increase investor participation.

However, we believe that such technology should be used in parallel with the in-person meeting and should not lead to companies adopting a virtual-only approach. The shareholder meeting is the only time that the whole board must be publicly accountable to its shareholders. The attendance of the board at such meetings demonstrates its commitment to hearing and understanding the views of shareholders.

Virtual-only shareholder meetings remove this accountability due to the remoteness of participants. The public nature of AGMs and full attendance of the board are also important to allow investors to bring matters to the board’s attention. Removing this tool impairs a shareholder’s ability to hold boards to account.

In certain countries, e.g., Germany, the law allows a company to amend its articles to hold virtual-only AGMs if this change is supported by its shareholders. This change in the law has resulted in the AGMs of many German companies being held on the same day, e.g., on 17 May 2023 there were approximately 35 shareholder meetings held. This impacts a shareholder’s ability to attend the meeting in person or virtually, which removes one of the important fundamental shareholder rights. This is particularly an issue for retail investors who do not have access to the board of directors during the year.

Therefore, despite changes in local laws that now permit virtual shareholder meetings, LGIM will not support the move towards fully virtual-only shareholder meetings. Any amendments to a company’s constitution in relation to electronic meetings should confirm that a physical meeting will continue to be held unless it is prohibited by law to hold a physical meeting.

Capital management

The board has a key responsibility to ensure the company has sufficient capital; overseeing the capital management of the company; ensuring efficient capital allocation; and, when additional capital is required, and facilitating its raising in an appropriate way.

Balancing the long-term investment needs of the company with shorter-term returns to investors is a critical role of the board.

Therefore, we support the right of shareholders to have a separate vote on the tools and authorities provided to the board in managing its capital structures. Such rights protect shareholder interests while balancing the need for board flexibility.

Share issuance

We support a company's ability to issue shares to raise capital. However, such issuances should be limited to what is necessary to maintain business operations and should not expose minority shareholders to excessive dilution of their holdings in the company's shares. In general, we would not support an authority to issue more than 100% of the issued share capital.

The existence of pre-emption rights is fundamental in protecting shareholders from excessive dilution. It gives the right conveyed to shareholders to be offered any new shares, pro-rata to their existing holdings, ahead of these being offered to non-shareholders. Our thresholds for approval of share issuance authorities are generally in line with established best practice in each market. In general, we would only support an authority to issues shares on a non pre-emptive basis if the authority sought is for 10% to 20% of the issued share capital. More information on specific guidance on limits can be found in our regional policies which consider the different local business practices and laws.

We expect companies to be transparent on whether any new authority sought will cancel any outstanding authority or whether any unused portion of the current authority will continue to be valid. If the authorities will be amalgamated, we expect companies to set a cap on the maximum potential issuances with and without pre-emption rights that applies across current and proposed authorities. Companies should provide a clear strategic rationale for any share issuance authority.

Share repurchases

Share repurchases can be a flexible way to return cash to shareholders. We expect the board to be transparent in how the share buyback authority will be used in relation to other potential uses of capital (such as dividends, internal investment or externally for mergers and acquisitions).

However, the benefits of using this approach depend on factors including the price at which shares are bought back, the company's individual financial circumstances and wider market conditions at the time. When utilising this authority, we expect companies to consider the impact on these and other issues. For example, on remuneration, performance conditions governing incentive schemes may be affected by the exercise of a share buyback authority. Furthermore, given the reduction in the number of shares in the market, the holdings of large shareholders will also increase, giving them more control.

Some markets may have an annual limit on the number of shares that can be bought back in any year, which is discussed in our regional policies. We would expect a detailed rationale for any buyback authority that is greater than 10% of the issued share capital.

Debt issuance

Good transparency and disclosure by the company on bond issuances is important for debt investors. In its reporting, we expect a company to include:

- The timely release of publicly-available prospectuses both before the new issue and while the bonds remain outstanding;
- Its commitment to provide public access to ongoing financials and disclosures; and
- Five-year financial history of the company.

Mergers and acquisitions (M&A)

We support proposals that create value for investors over the long term.

To make an informed assessment, we expect the board to be transparent on the terms of the transaction and its financial and cultural integration implications on the long-term business strategy. We also expect all companies to explain how the transaction is expected to yield significant long-term benefits for the company and its stakeholders, including investors.

We encourage the company chair and non-executive directors to hold separate meetings with their investors without the executive directors present, to explain the risks and opportunities of the transaction. In a contested takeover, we will aim to meet with both parties of the deal before making a final decision.

In addition, we believe that a strong governance framework is essential during any M&A activity. Therefore, companies should make sure the independent non-executive directors are informed at an early stage and can obtain independent advice at the company's cost, with advisers remunerated on a fixed-fee basis. A strong process should be in place to ensure there are no conflicts of interest. The skillset of the board must also be reviewed, including past M&A experience, to ensure the board is appropriately equipped to successfully lead the transaction and its impacts on the company.

The board may consider putting in place a separate ad hoc committee of independent non-executive directors to consider the merits of the transaction, and to engage with its investors.

Takeover defence plans – poison pills

'Poison pill' is the term given to a tactic adopted by a company to deter takeover bids. Well-designed poison pills may strengthen the board's negotiating position and allow it to obtain more favourable terms from an acquirer.

It is vital that this process is controlled by the independent members of the board that are typically more concerned with investor value than with protecting their own position. We do not expect a poison pill to entrench management or protect the company from market pressures, which is not in investors' best interests. Any poison pill should only be used for a finite period.

For more details on our approach on M&A and takeover defences, please refer to our thought piece on the topic, available here.

Related-party transactions

Related-party transactions (e.g., between a controlling shareholder and an issuer) are a concern for minority shareholders as there is a risk that a related party may take advantage of their position. We are therefore not generally supportive of related-party transactions.

In those cases when related-party transactions are undertaken, we expect adequate safeguards to be put in place to protect the company's interests and any shareholders who are not a related party, including minority shareholders.

All transactions must therefore be authorised by the board of directors. We also expect the company's audit committee to ensure that such transactions are conducted on the basis of an independent assessment and valuation.

For material related-party transactions, we expect companies to provide additional information to shareholders in their annual report. This should include information on whether board approval was unanimous or received majority support.

In addition, shareholders should be given the opportunity to approve material related-party transactions, including any transactions undertaken with directors. We expect companies to disclose sufficient information about such transactions in their annual disclosures to enable informed voting decisions to be made.

Shareholder proposals

We consider all shareholder proposals tabled at a company's shareholder meeting in the wider context of the company's corporate governance practices, our thematic policies and the long-term benefits for stakeholders. We expect companies to provide a meaningful discussion of the proposals to enable shareholders to make an informed judgement.

LGIM may support certain shareholder proposals on key topics where we want to draw attention to the importance of the topic for investors. The level of shareholder support for a topic is a helpful way for companies to learn about what thematic issues are material to shareholders.

We expect majority-supported shareholder proposals to be adopted. Where there is significant support (20% or more) we expect the company to consider the benefits of the proposal and to discuss this with its shareholders and to include any outcome in its annual disclosures.

Political donations and lobbying activity

We will not support direct donations by companies to political parties or individual political candidates. We believe that companies should fully disclose all political contributions, direct lobbying activity, political involvement and indirect lobbying via trade associations. There should be full transparency regarding the memberships of and monies paid to trade associations and lobbying groups including:

- A breakdown of payments to political parties, candidates and associations, trade associations, and think-tanks, and of direct and indirect lobbying activity on policy and legislative proposals
- A clear explanation of how each of the above associations, contributions and actions benefit the causes the company supports and how they are linked to the company's strategy.
- A public statement from the company outlining where it disagrees with the associations of which it is a member on a particular issue, and the reasons why it believes it is beneficial to remain a member
- Disclosure of where responsibility sits within the company for the oversight of such relationships

Sustainability

As a major global investor, we have a fundamental interest in ensuring that shareholder and bondholder value is not eroded by a company's failure to manage the risks associated with its natural and social environment. We believe that, if companies take advantage of the need to move towards a more sustainable economy, investors can benefit through protection from future risks and the potential of better long-term financial outcomes.

Sustainability governance, process and operations

With this in mind, we expect our investee companies to meet minimum standards on how they identify, assess, manage and disclose sustainability-related risks and opportunities across their business operations. Our key expectations are laid out below.

Risk identification and management

Material environmental and social (E&S) risks will vary between sectors and from company to company, depending on a range of factors. Stakeholders will also have different views on what issues are material for them. Despite this complexity, it is important that all companies across different sectors undertake an analysis of E&S issues that could be material to their business over varying timeframes.

A dynamic risk-mapping exercise should identify the degree to which a company is exposed to each risk element. It should also be used to identify business opportunities such as new products and services, and potential efficiency gains as a result of changing policy, technology and business environments.

Robust E&S risk management processes should be integrated into company Enterprise Risk Management (ERM) systems. The approach should be holistic and implemented across all business operations that either can be considered exposed to environmental and social-related risks, and/or that may produce negative externalities. Where possible, such systems and processes should be externally verified.

Where risks have been identified for the business, comprehensive policy statements should be disclosed to all stakeholders to demonstrate the company's commitment to managing these risks.

Governance and accountability

Responsibility for managing a company's E&S impact and related risks to the business is shared across all business functions. Ultimately, accountability sits at board level. We expect the fulfilment of sustainability targets and commitments to be the responsibility of the CEO and the board. We expect companies to disclose the governance processes they have in place to oversee and manage these risks. Where material to the business, we encourage companies to link executive remuneration to the delivery of these commitments.

Where specific material issues such as climate change are identified whether over the short, medium, or long term, we expect company boards to have sufficient expertise and experience to ensure effective strategic and operational oversight. More information can be found here.

Sustainability strategies

Building a sustainable business model that enhances performance and builds resilience should be at the core of business strategies. E&S issues should not be viewed as peripheral components of business operations or simply ethical and compliance obligations. Where material risks and opportunities have been identified, there should be a clear link to a company's overall strategic priorities. Plans to mitigate risks and realise opportunities should be disclosed clearly.

Reporting and disclosure

Target-setting
Companies should set targets to focus their efforts on realising their strategic E&S objectives, mitigating and managing material E&S risks and impacts, as well as maximising broader positive stakeholder impacts. While it is important for the targets to be achievable, companies may benefit from setting challenging goals to maximise their overall impact. We expect companies to report suitable metrics that allow progress against these targets to be tracked effectively.

Public disclosure and transparency expectations
Transparency and disclosure are key tools that enable investors to undertake a robust analysis of investment risks and opportunities and allocate capital accordingly. We expect companies to demonstrate their commitment to the disclosure of sustainability information and data in key company reporting; this includes the annual report and accounts, with supplementary information in sustainability reports and on their corporate website.

We are very supportive of the International Sustainability Standards Board's (ISSB's) first two standards, published in June 2023. The standards present a global baseline for sustainability disclosures acting to amalgamate previously disparate disclosure requirements. LGIM expects companies to align their sustainability disclosures with the ISSB's published and any new standards, building on much of the work already in place from previous disclosures through standards such as GRI, SASB, etc. Disclosing in a clear and consistent manner is important in facilitating the analysis of trends in this area.

We encourage our investee companies to be proactive and undertake where possible the verification of their sustainability data externally by a reputable independent assurance provider, based on recognised standards. This can be evidenced by making the assurance statement public. This verification exercise should provide comfort and credibility to stakeholders, including investors, around the sustainability data disclosed.

We encourage companies to make these discloses via third-party sustainability agencies, and in line with best- practice international guidelines.

Financial impact quantification

Quantification of sustainability risks and potential impacts can help investors make more informed capital allocation decisions, according to their risk, return and impact objectives. Quantification practices can also support companies to better understand their risk exposure and achieve a net benefit by managing sustainability impacts effectively.

We encourage companies to demonstrate a commitment to best sustainability practices and, where appropriate, quantify financial impacts to internalise the associated costs and benefits. For example, to the extent that they are material,[1] companies should explain how climate-related matters are considered in preparing their financial statements.

Industry collaboration

Companies may benefit greatly from sharing knowledge and experience with their peers by joining and contributing to industry-wide associations. We encourage collaboration between companies where appropriate to progress the broader sustainability agenda and broach cross-sectoral and inter-sectoral sustainability challenges. Where relevant, we expect companies to engage with regulatory bodies to promote best practices and policies to achieve sustainability targets.

Lobbying transparency

Whether companies perform individual engagement with regulators or policymakers, or collaborative engagement as part of an industry association, we expect them to be transparent and to comprehensively disclose their public policy engagement activities, including trade association memberships (see section above on political donations and lobbying).

[1] In accordance with IAS 1. – Presentation of Financial Statements, information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements

Sustainability themes

LGIM focuses on material issues that can impact a company's long-term sustainability, both financially and reputationally. Some of these issues apply across multiple sectors such as climate change, biodiversity, health (e.g., antimicrobial resistance and nutrition) and human rights issues such as income inequality and modern slavery. Meanwhile, other issues such as food waste, reduction of waste and plastic use are more sector specific.

Below we highlight our expectations in relation to some of our key themes. More information and articles on our position on broader themes can be found here.

Climate change

Climate change is a defining factor in companies' long-term prospects. We expect companies to disclose how they may be impacted by climate-related risks and opportunities, and how these factors are considered within their strategy.

We are very supportive of the International Sustainability Standards Board's (ISSB's) first two standards, published in June 2023. The standards present a global baseline for sustainability disclosures acting to amalgamate previously disparate disclosure requirements. LGIM expects companies to align their sustainability disclosures with the ISSB's published and any new standards. Specifically in relation to climate disclosure, with the Financial Stabilities Board (FSB's) announcement that the TCFD will now be integrated into the ISSB, we expect companies to develop their climate disclosures in line with IFRS S2 requirements, with a focus on improving approaches to scenario analysis and the quantification of financial impacts that result from climate risks.

In addition to IFRS S2 disclosure, we expect companies to report using the CDP climate questionnaire, which is aligned with the TCFD and IFRS S2 frameworks and crucially provides investors with climate data on a large universe of companies in a comparable format. For sectors where it is material, we strongly encourage companies to also report via the CDP Water and Forest questionnaires.

Science Based Targets (SBTs) are decarbonisation targets aligned with the objective of the Paris Agreement. We therefore encourage all companies we invest in to commit to and work towards approved SBT's aligned with the Science Based Target initiative's recent net-zero standard. Additionally, we expect companies to articulate how their business models reflects a Paris-aligned transition.

As part of our Climate Impact Pledge, we expect companies to not only have greenhouse gas (GHG) reduction targets in place, but also to disclose board oversight of climate change and other sector-specific policies. More information on our expectations of different sectors, and the metrics we use to assess companies can be found here.

In relation to climate change, we would expect companies to publicly disclose any concerns they may have with current or evolving legislation and to publicly report on any lobbying activity that is undertaken in relation to such concerns. We recognise that achieving the Paris Agreement requires policy action in a wide range of areas. Therefore, we expect companies to engage with policymakers and regulators to encourage the introduction of policies to enable a net-zero transition for their respective sectors.

Companies that fail to meet our minimum standards with regards to climate disclosure will be removed from select LGIM funds, including our Future World funds, subject to tracking error constraints. In all other funds where we cannot divest, we will vote against the chair or other directors, to ensure we are using one voice across our holdings.

Please see more on LGIM's policy on climate change here, and our Climate Impact Pledge here.

Nature

Biodiversity
We believe that biodiversity loss presents a major global systemic risk. We expect companies to assess their impact and dependencies on biodiversity with a view to managing risk, as well as mitigating and, over time, reversing negative impacts. We encourage companies to commit to having an overall positive impact on biodiversity and to consider the direct as well as indirect activities of their supply chains. We will be seeking greater disclosure from investee companies in line with the Taskforce on Nature-related Financial Disclosures (TNFD) framework.

As a signatory to the Finance for Biodiversity Pledge, we have committed to collaborating and knowledge sharing, engaging with companies, assessing impacts, setting targets and reporting publicly. Our nature framework and related policies can be found on our website.

Deforestation
LGIM recognises the importance of ending commodity-driven deforestation to tackle climate change, reduce biodiversity loss, and support food security. We are a signatory to the COP26 Commitment on Eliminating Agricultural Commodity Driven Deforestation from Investment Portfolios. In 2022, LGIM published its deforestation policy. In line with our COP26 commitment, the policy commits LGIM to assessing commodity-driven deforestation risk in investment portfolios. This has been done, and where identified, we have contacted companies in high-risk sectors with little or no deforestation policies of their own. Since 2023, LGIM has voted against the board chair or other board directors of these companies. LGIM is also encouraging companies and data providers to improve the quality and availability of data on deforestation risk. You can read more in our deforestation policy.

LGIM has been engaging with key companies in high impact sectors on deforestation since 2017 as part of our Climate Impact Pledge commitment. In certain sectors the lack of a comprehensive deforestation policy constitutes one of our 'red lines' under our climate impact pledge.

Circular economy
Our current globalised economic model can be described as 'linear.' Many of our production processes follow the same route, extraction of raw materials, manufacture, use and disposal ('take-make-waste').

This system does not put a value on materials that are at the 'end-of-life' stage, or the environmental and social implications.

We believe this traditional linear system can be reformed, accelerating our 'Just Transition' to net zero and nature-positive economies, with ecosystems restored. The economic model that can reform our system at scale is the introduction of the 'circular economy'. This is a key component of LGIM's approach to nature. It is based on three principles, driven by design: eliminate waste and pollution, circulate products and materials (at their highest value), and regenerate nature.

LGIM will focus its engagement efforts on supporting a transition from a ‘linear’ economic model to a ‘circular economy’ model. LGIM’s expectation of companies will be increasingly expanded; it currently includes:

- Strengthened disclosures on the approach to circular economy and reduction of waste and pollution;
- A circular economy commitment, strategy, business model and policy across the value chain;
- Disclosure of the proportion of raw, re-used, recycled and compostable materials;
- Explanation of how the strategy is embedded, including any targets and progress;
- Board-level oversight;
- Activities undertaken to protect and regenerate nature and the ecosystems; and
- Any lobbying activities.

Water

Globally, we need a ‘Just Transition’ to economies that are both net zero and nature-positive, and in which ecosystems are restored. Water is a key element of this, as it is the very essence of life on this planet. It permeates our lives and has an impact on all of us, reaching across all sectors, businesses and economies. Water can have a diversified impact along a company’s value chain, directly impacting operating risks and financial performance.

In its current form, the water system presents a long-term systemic market risk that will impact LGIM, the markets that we invest in and our investment returns, and ultimately our clients. The challenges are significant and there is insufficient global scale action being taken to protect our most precious resource.

LGIM will focus engagement activities on key areas of the water system, i.e., water scarcity and security, and water quality. LGIM’s expectation of companies will be expanded and will include: strengthening disclosures on approach to impact on water quantity and quality; whether a commitment, strategy and policy is in place across the value chain; explanation of how the strategy is embedded, targets and progress; board level oversight; protection and regeneration of nature and ecosystems; and lobbying activities.

Health

Antimicrobial Resistance (AMR)

The importance of tackling AMR should not be underestimated. It can have a material financial impact on investments, The World Bank has estimated that AMR could result in a 3.8% loss in global GDP, an impact comparable to that of the 2008 global financial crisis.

We ask pharmaceutical companies involved in antimicrobial manufacturing to manage their effluent waste to reduce the risks of AMR, and we ask animal pharmaceutical companies to transparently disclose their AMR stewardship efforts. We also ask companies in sectors such as the food industry to apply the World Health Organisation’s guidelines on antibiotic use in food-producing animals, including in their supply chain. Further, we expect all water utility companies to be aware of the possible risks of AMR from contaminated water.

For more information on our concerns please read our health policy and blogs on the scale of the AMR problem, why the issue matters to investors, and how we’re engaging with water utility companies on AMR.

Nutrition

Poor nutrition can have a negative health impact on individuals, workforces and broader societies. This can create a financial burden on economies from increased healthcare costs, both private and public, and on companies from absenteeism. For consumers to make informed decisions about the food they consume and to promote healthier diets, we encourage companies to be transparent on their nutrition strategies; demonstrate progress on these strategies; commit to disclose the share of the company's portfolio and sales associated with healthy food and drink products (using government-endorsed nutrient-profiling models such as the Health Star Rating or NutriScore); and set targets to increase the proportion of these sales.

For more information, please read our health policy.

People

Employees are one of the greatest assets a company has. We believe the value they bring to a company's long-term sustainability should not be underestimated. Therefore, our approach to this topic covers issues such as human capital management, employee welfare, human rights, modern slavery, income inequality, diversity and inclusion. We consider these topics to be financially material and have published policies on several of these, with plans to publish more in 2024.

Human capital management

As an investor, it is important for us to understand the culture of the companies in which we invest our clients' money and how that culture affects the people working within its operations. We expect companies to disclose information that will provide a holistic view of their culture. We would ask companies to disclose metrics such as: workforce turnover and how that compares with the sector average, skills and development training, compensation, benefits, workforce demographics including diversity and health and safety.

The value a company places on employees can be measured by its efforts to receive and act upon employee feedback. Therefore, companies should also support workers' rights by allowing participation in freedom of association and collective bargaining.

Employee welfare

Companies should ensure that their workforce receive adequate training to gain the appropriate skills to carry out their jobs safely and effectively. Workers should be protected from harassment, discrimination and all forms of forced or compulsory labour. Their working environment should be safe, and annual training on health and safety within the workplace should be compulsory. All workers should receive benefits such as paid sick leave, maternity leave and paternity leave. Where possible, companies should provide access to services to help workers with any medical issues, such as mental health, private health cover etc.

Diversity and inclusion

Just as we believe a diverse mix of skills, experience and perspectives is essential for boards to function and perform optimally, we similarly expect the companies they oversee to embrace different forms of diversity, including gender, ethnicity and neurodiversity. Our expectations on diversity and inclusion extend beyond the executive level and apply throughout the company. For more information on this topic, please refer to our diversity policy.

Human rights

We expect companies to respect workers' human rights as set out in the Universal Declaration of Human Rights and the main instruments through which it is codified, such as the International Labour Organization's eight core conventions. In addition, we expect companies to comply with the principles of the United Nations Global Compact, OECD guidelines for multinational enterprises and all local and national laws and regulations relating to the protection of employees.

Modern slavery

Modern slavery can take a number of forms, such as child labour, forced labour and human trafficking. Companies should ensure that they are not permitting modern slavery to take place either within their own operations or within their supply chains. As such, we expect companies to adhere to all applicable laws pertaining to modern slavery, which could otherwise result in financial and reputational risks to the company as well as potentially causing distress to those workers involved.

We believe merely putting in place a code of conduct is not sufficient to ensure that modern slavery does not exist within the supply chain. We expect companies to have a more rigorous process that includes, but is not limited to, due diligence audits, local workforce interviews; and technology to provide full traceability of all components of goods or merchandise sourced.

For more information please read our human rights policy.

Income inequality

Living wage: As a minimum, we expect all companies to pay their workers the minimum wage as mandated by local law. However, we believe it is important that employers pay a living wage to ensure employees avoid the poverty trap, which can create hardship, stress and health problems that combined may have an impact on the operational performance of the company.

A living wage should be sufficient to afford a decent standard of living for the worker and their family. Elements of a decent standard of living include food, water, housing, education, healthcare, transportation, clothing and other essential needs including provision for unexpected events. Our expectation that workers receive a living wage extends to all contractors that operate within a company's operational premises. Procurement practices should ensure that workers' pay is ring-fenced from negotiations on price to ensure they receive a living wage.

To better inform investors, we are calling for greater transparency on employee practices. We expect companies to say in their annual disclosures whether they are paying a living wage to their employees. We also ask companies to disclose the steps being taken to ensure their suppliers are paying or working towards paying their workers a living wage. Additionally, we want to understand whether companies are offering all employees the opportunity to work for a minimum of 15 hours a week and what other benefits are in place to alleviate financial hardship, such as free meals, interest free loans etc.

Financial wellbeing training: It is not only important to ensure that all workers are receiving a living wage, but it is equally important that they receive guidance on issues such as money management, and where to get financial help. We encourage all companies to provide their employees with training on this important topic.

Pensions: companies should consider the long-term health and wealth of their employees and where possible, increase the non-contributory element of pension provisions.

Equity ownership: we encourage all companies to offer employees the opportunity to participate in equity ownership. We believe that this can be a performance motivator and retention tool. To ensure sufficient take-up, we encourage companies to offer free shares to all employees or to those earning below the national median pay level. The offer of shares should be linked to continued service.

Gender pensions gap/ethnicity pay gaps: we expect companies to make themselves aware of the inequalities that exist in their organisation and to take positive steps to reduce them.

Why adherence to these principles is important for LGIM

We believe that integrating environmental, social and governance considerations into investment processes can help mitigate risks and improve long-term financial outcomes. For this reason, we embed both top-down and bottom-up sustainability analysis into our investment processes. In addition, positive and negative externalities generated by companies can have consequences for the economy and society at large. We believe that investors have a responsibility to a broad set of stakeholders and the market as a whole. We need and expect companies to play their part. Our sustainability principles set out our minimum expectations of companies with regard to the prioritisation, management and disclosure of sustainability issues. These principles naturally feed into our voting and investment decisions, and for certain themes we have very structured processes in place.

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