Stewardship Report 2023

About the Stewardship Report

This report summarises our ethical stewardship activities for FY23. Advocating for a better world is a core part of our business plan. We understand that advocating for change on behalf of our customers and shareholders is a privilege and a responsibility.

We strive to be transparent about our ethical stewardship activities so that these important stakeholders can hold us to account and see how we are leveraging their capital to influence for people, animals and the planet.

To focus our efforts, we pursue four strategic ethical stewardship initiatives targeting high impact sectors.

These are:

- turning off finance for unsustainable expansion of fossil fuels
- stopping livestock driven deforestation in Australia
- reducing building sector emissions
- advancing alternatives to animal research

You can read about how we chose these initiatives on page 3. With these guiding our main activities we advocate for change in the companies we invest in, as well as pursue positive change in the behaviour of peers, companies outside the portfolio, governments, consumers and citizens.

In the following pages we provide updates on the initiatives we pursued in FY23, as well as some examples of our tactical engagements including our long-term engagement with Lendlease about their Mt Gilead development and its impact on koalas, and a new engagement started with Microsoft in relation to its approach to human rights.

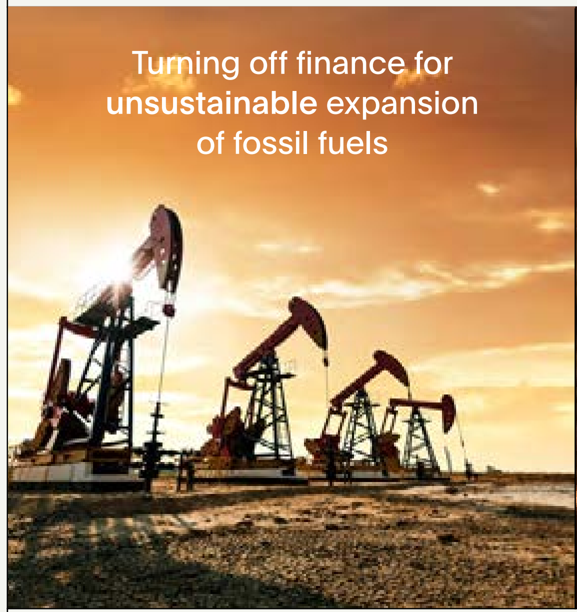
Please see our website for more information about our ethical stewardship.

FY23 Snapshot

The Impact & Ethics Research team engaged[1] over 250 companies for people, animals and the planet.*

- More than 65 of these were 'proactive' engagements (that is we did more than simply 'sign on' to an engagement coordinated by another organisation)[2]
- Companies committed to change following approximately 25% of our proactive engagements*
- 35 of our proactive engagements were 'in depth' engagements (involving 3+ activities in the FY, or had been part of a multi-year engagement)
- Companies committed to change in FY23 following approximately 40% of our in depth, proactive engagements
- 4 company engagements ended with divestment. Overall during the year there were 5 divestments on ethical grounds[3*]

Our four strategic ethical stewardship initiatives:



1. We count one engagement where we engaged with a company on a topic or series of topics. There may be multiple activities within that engagement. For example, our engagement with QBE is counted as one engagement which included a meeting, emails and co-filing a shareholder resolution. We may count two engagements with a company if there were separate activities on entirely separate topics. For example, we had one engagement with Boral in relation to its efforts to align with the climate transition (as lead CA100+ investor for Boral) and a separate engagement with Boral in relation to worker safety.
2. We distinguish proactive engagements from passive engagements. Our 'proactive' engagement count includes where we engaged directly with a company, actively contributed to collective engagements (as distinct from simply 'signing on'), used a nominal advocacy holding to support shareholder resolutions, or co-filed a resolution.
3. Not including companies excluded from initial investment or companies not held due to financial investment considerations.

Assurance*
KPMG have provided limited assurance over key metrics in our sustainability disclosures, including some engagement statistics. KPMG's assurance opinion is available here.

Using our influence

Now representing more than $9 billion invested, we are able to use our growing influence and the many tools at our disposal, to catalyse change aligned to our Ethical Charter. This influence extends to the companies we invest in, but also those we exclude and the broader world in which we operate.

Ethical stewardship is a key way we influence for the change we want to see in the world. We need systemic change across multiple industries to tackle the most difficult and important challenges of our time, such as climate change, nature loss, human rights abuse and industrialised animal cruelty. As an ethical investor, we use capital allocation to help drive this change, by investing in companies that on balance benefit people, animals and the planet, and restricting+ those which we consider cause unnecessary harm in accordance with the Principles of our Ethical Charter.

Ethics-driven capital allocation is critical, but on its own is not enough to achieve the economic and social transformation to a future where people, animals and the planet prosper. There are a few reasons for this:

- The fact that we do not allocate capital to harmful industries does not mean they will stop existing. We restrict+ our investment in fossil fuel companies for example, but new oil and gas projects are still being built in Australia.
- The companies we invest in have been assessed as positive under our Ethical Criteria, but this doesn't mean they can't improve. There will always be companies inside and outside our investable universe that we will need to engage with.
- Our ability to deliver healthy financial outcomes for customers relies on social and environmental foundations which are currently under threat, and therefore we see it as part of our responsibility as investors to help address these system-level risks.

Our rationale means we do not limit our efforts to ensuring that investee companies' financial returns versus the level of risk is acceptable. That is obviously important but on its own will not address - and can even exacerbate - system-level challenges. This is recognised in the PRI's guidance for investors on active ownership.[4]

A company can seek to strengthen its position by externalising costs onto others. This might be good for their financial performance but bad for humanity, the planet, and the other sentient beings we share it with. And from a purely financial point of view, those negative externalities can be a cost across the rest of the portfolio.

Our approach is to work backwards from solutions to these system-level issues and ask ourselves, "How can we best leverage our position as an investor to most effectively be part of that solution?". We are not claiming that we can solve any of these issues ourselves. We recognise that we can play a role in positively influencing and contributing towards resolving them. And that we have a responsibility to do so.

"... our approach is to work backwards from solutions to these system-level issues and ask ourselves, how can we best leverage our position as an investor to most effectively be part of that solution."

\+ We restrict investments in fossil fuel companies, nuclear, gambling or tobacco companies. Our investment restrictions include some thresholds. Thresholds may be in the form of an amount of revenue that a business derives from a particular activity, but there are other tolerance thresholds we can use depending on the nature of the investment. We apply a range of qualitative and quantitative analysis to the way we apply thresholds. For example, we may make an investment where we assess that the positive aspects of the investment outweigh its negative aspects. For information on how we make these assessments for a range of investment sectors and issues such as fossil fuels, nuclear power, gambling, tobacco, human rights, and many others, please read our Ethical Criteria.

4 Active Ownership 2.0 available at unpri.org/download?ac=9721

Our process for identifying our priority areas of focus

We have to be strategic about where we are investing our time and resources to influence change. We use the following framework to guide our strategic ethical stewardship initiatives:

We focus on issues related to the three pillars of the Ethical Charter – **people**, **animals** and **the environment**.

Where the issues are systemic, widespread, long term, or create an existential challenge

or

Where we can help reduce suffering, protect the voiceless, vulnerable or irreplaceable

Where we are in a position to influence e.g. as an investor; as a subject matter expert, because of our unique perspective; or because the topic is under-attended

or

Where we see a need to address harm caused or contributed to by the companies in our portfolio or we see an opportunity to help enhance the positive impacts of companies in our portfolio

Issues are ideally

- important to existing and prospective customers
- the subject of existing media interest with space for our voice or where we can generate such interest
- able to be efficiently acted on, such as where there are synergies with our ethical screening and impact measurement, where we can leverage previous work or existing relationships, where we can leverage the Foundation partnerships or where there are synergies with people powered advocacy campaigns

In addition we may engage in more opportunistic or 'tactical' ethical stewardship where we:

- need to engage to confirm an investment is aligned with the Ethical Charter or to encourage alignment (this engagement is informed by the Ethical Frameworks that apply the Ethical Charter to relevant industries and issues)
- can support others' initiatives that are aligned with our position on issues relevant to the Ethical Charter
- see any other opportunity to positively influence on issues aligned with the Ethical Charter

Although we don't refer to the Sustainable Development Goals (SDGs) in this framework, we see a strong alignment of the SDGs with our Ethical Charter, and as a result with our ethical stewardship.

The SDGs are the culmination of a lot of research, thought and discussion and are an excellent tool for governments, companies and investors to identify priority areas they should be seeking to address. We use them as part of our assessment of the impact of our investment portfolios.

Having said that, the SDGs don't address all important impacts on people, animals and the environment. They do not, for example, afford much consideration to the other sentient beings with which we share this planet, specifically the 70 billion+ raised and killed for meat each year[5] and the animals used for other commercial purposes (such as clothing, entertainment, research). The Ethical Charter explicitly recognises that non-human animals deserve dignity and wellbeing and should not be subjected to unnecessary harm.

5 ourworldindata.org/grapher/animals-slaughtered-for-meat. Note this data does not include animals killed for egg and dairy production or fish killed for consumption.

Strategic ethical stewardship initiatives

Turning off finance for fossil fuels

We do not invest* in companies whose main business is fossil fuels, and for over a decade we have leveraged our investment in the finance sector to seek to turn off sources of funding that enable unsustainable fossil fuel expansion to continue.

The International Energy Agency tells us that net zero by 2050 means gas needs to decline this decade. But Australian oil and gas companies continue to plan and invest in new oil and gas fields. There is a dangerous disconnect here.

Our theory of change is: if we can convince major banks and insurance companies to stop lending to and underwriting non-Paris aligned fossil fuel projects, it will:

- make those fossil fuel projects harder to finance, improving the relative return on investment of renewable energy, and
- help remove social license for these projects which in turn helps open the door for stronger government policies.

Over time we have seen financial institutions make commitments to align their lending, investing and underwriting activities to the Paris Agreement and to phase out coal.

This year our ethical stewardship focused on what we saw as the two major shortcomings of the banks' climate policies:

- giving high emission customers too much time to align their business with the transition to limit warming to 1.5 degrees, and
- not applying their climate-related restrictions to their general corporate lending facilities, which is a major loophole.

We have seen material progress.

In 2023, it was reported that all major banks refused Whitehaven Coal's $1bn debt refinance sending a signal to worry other large coal producers and potentially speeding up the demise of the sector.

CBA has ruled out project finance for new and expansionary oil and gas extraction, setting a high benchmark for the other major banks. The bank also made clear that by 2025, oil and gas companies will need to have a credible transition plan in place that must include the client's scope 3 emissions and be aligned with limiting warming to well below 2 degrees, to be eligible for finance.

Of course we cannot claim this progress as solely our achievement. There are many other people and organisations working hard toward similar objectives. Achieving change at the scale and pace we need to address the biggest ethical challenges of our time cannot be done by any one individual or organisation. We need multiple players using multiple sources of leverage, and positive feedback loops between them all. This includes policy makers, regulatory bodies, academics and research institutions, NGOs, responsible investors, responsible companies, proxy voting agencies, strategic litigants, journalists, consumers, and sometimes the occasional billionaire. It takes an ecosystem of people in different roles with a genuine desire to make the world a better place.

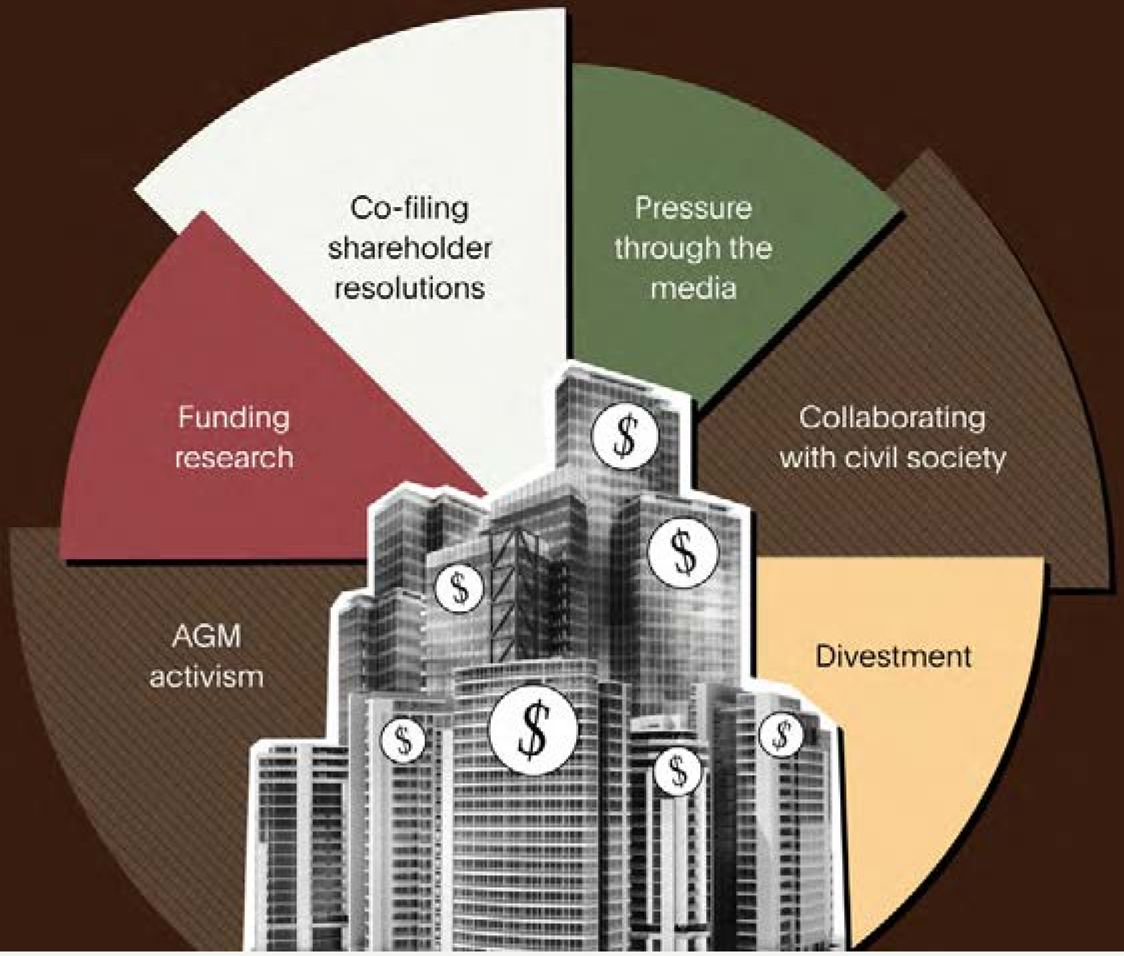
What we can say is that we are seeking to leverage our tools of influence within this ecosystem, and that these developments bring us closer to our ultimate objective of ending unsustainable fossil fuel expansion.

Influencing the finance sector to cut fossil fuels

We restrict* investment in fossil fuel companies+ and we leverage our investment in the finance sector to:

- Align their lending, underwriting and investing with the goals of the Paris Agreement
- Stop financing fossil fuel projects that are not aligned Paris Agreement
- Direct more funding to positive, clean and sustainable energy solutions

Change of this magnitude requires coordination and persistence.
We use all our stewardship tools to influence banks and insurers, including:



A decade of influencing the finance sector to help bring an end to unsustainable fossil fuel financing.

Banks

Banks disclose lending to fossil fuels and commit to Paris

In 2013 we asked the Australian big 4 banks to disclose the amount they lend to coal, oil and gas. We then called on the banks and major insurance companies to align all large-scale lending and insurance with the 2015 Paris Climate Agreement.

Banks and insurers start excluding coal

In 2017 Westpac and NAB announced exclusions for new thermal coal projects, including any Adani Carmichael mine. In 2019 QBE announced a phase out of its coal exposure after we co-filed a shareholder resolution with Market Forces.

AEI divests

In 2020 Marsh McLennan said it may refuse business if contrary to climate goals and SDGs. This vague commitment fell well short of what we asked. We divested our shares.

Banks introduce some oil and gas restrictions

In 2021 we met with QBE, NAB and Westpac to discuss their continued support of the fossil fuel sector. We called out the shortcomings of QBE's climate policy and called on the banks to assess climate alignment of all new oil and gas projects they fund. We co-filed a shareholder resolution, arranged by Market Forces, calling on QBE to align its underwriting and investments of oil and gas assets with the Paris Agreement, and at its AGM pointed out that many of its customers are not Paris aligned. At NAB and Westpac's AGMs we supported shareholder resolutions calling for Paris-aligned targets to reduce fossil fuel exposures and transparency about how any new fossil fuel finance is consistent with their net zero by 2050 commitments. We also helped finance and contributed to an IGCC-commissioned report which examined high impact planned Australian gas projects and their risks for non-alignment with the Paris Agreement.

NAB announced a cap on its exposure to the oil and gas sector, along with restrictions on lending for greenfield oil and gas extraction projects. Westpac announced requirements for public Paris-aligned business goals for new oil and gas exploration, production and refining customers. QBE subsequently announced it was joining the UN-convened Net Zero Insurance Alliance.

Continued pressure on QBE and other insurers for oil and gas exposure

In 2022 we met with QBE's sustainability team to understand how it was progressing on oil and gas exposure. We were disappointed with its lack of ambition. We co-filed a shareholder resolution calling on QBE to disclose Paris aligned targets to reduce exposure to oil and gas assets; and its plans and progress to achieve those targets. At QBE's AGM we challenged its policy which allows insurance of expansion of the oil and as sector until 2030. We highlighted that QBE was falling behind its competitors.

We divested from major energy insurer Travelers and from insurance broker Arthur J Gallagher for lack of Paris alignment.

Seeking to close down loopholes in bank climate commitments

In 2022 the major Australian banks announced new climate commitments for their lending criteria. We were disappointed that they are giving high emission customers too much time to align their businesses with the transition needed to limit warming to 1.5 degrees. They are also not applying their climate-related restrictions to their general corporate lending facilities. Together with Market Forces we co-filed shareholder resolutions for Westpac and NAB and questioned their policies at their AGMs.

Putting the pressure on QBE

At QBE's 2023 AGM, we voted against the re-election of two directors including the Chair, and against the remuneration report, because of QBE's continued lack of progress with respect to underwriting expansionary fossil fuel projects.

QBE leaves Net Zero Insurance Alliance

In May 2023, QBE announced its exit from the Net Zero Insurance Alliance, sending a concerning signal that the company is not taking seriously its net zero commitments.

All major banks refuse to lend to Whitehaven Coal

In 2023, it was reported that all major banks refused Whitehaven Coal's $1bn debt refinance sending a signal to worry other large coal producers and potentially speeding up the demise of the sector .

CBA strengthens climate commitments

In August 2023, CBA ruled out project finance for new and expansionary oil and gas extraction, setting a high benchmark for the other major banks. The bank also made clear that by 2025, oil and gas companies will need to have a credible transition plan in place that must include the client's scope 3 emissions and be aligned with limiting warming to well below 2 degrees, to be eligible for finance.

The banks

What we did

Meetings

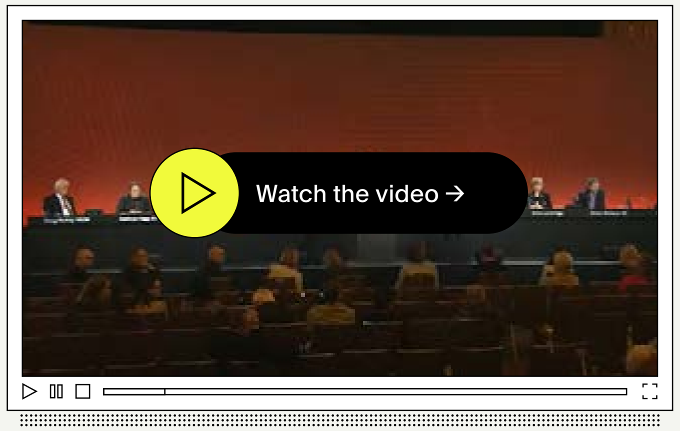
In FY23 we met with ANZ, Westpac and NAB through one-on-one meetings, roundtable discussions, climate policy meetings and pre-AGM meetings.

In our discussions we called on the banks to assess whether new lending to fossil fuel clients is aligned with the banks' own commitments to net zero, particularly having regard to where those clients are spending new capital today.

AGM activism

In FY23 we:

- Co-filed shareholder resolutions against NAB and Westpac, sponsored by Market Forces.
- Briefed other investors to encourage support for the shareholder resolutions
- Attended NAB and Westpac AGMs and questioned the respective Chairs about the loopholes in their lending restrictions that allow until 2025 new and renewal of loans, to companies who are actively planning and developing new fossil fuel projects. You can watch our exchange with the NAB Chair here:



Collective pressure

The shareholder resolutions received little support in FY23. Recognising we need the responsible investment community to put more pressure on banks, in the second half, we commenced an engagement program to understand what is driving low support and to encourage collaborative investor discussions and engagement (and identify opportunities to put pressure on investors holding back progress). This included speaking on an IGCC panel discussion about banks needing to have credible and transparent net zero transition plans.

ASFI submission

We made a submission to the Australian Sustainable Finance Initiative about their proposed green taxonomy. We called out that individual projects and their finance should not be considered green if they are facilitating a customer's pursuit of other new projects or activities which are not aligned with the Paris Agreement. Activity level and entity level criteria should generally apply for green-labelled specific use of proceeds finance.

Outcomes

We cannot claim attribution for all the following outcomes. There are many other people and organisations working hard toward similar objectives.

- All major Australian banks refused to refinance Whitehaven Coal.
- CBA has ruled out project finance for new and expansionary oil and gas extraction.
- The big 4 banks set targets for fossil fuel and some other carbon intensive sectors and will require that oil and gas customers have a transition plan by 2025. NAB also capped oil and gas exposure.
- We have a better understanding of why the FY23 climate resolutions received little support, and we are implementing a strategy to address issues identified.
- Other investors and investor groups have indicated support for convening discussions and collaboration with respect to fossil fuel financing.

What next?

The banks have said that oil and gas customers will be required to have a transition plan by 2025. In FY24 we are focused on ensuring that the banks impose robust transition plan requirements on their clients. We will question the banks on issues around:

- inclusion of scope 3 emissions
- capex plans and criteria
- use of offsets
- technological assumptions
- approach to climate lobbying
- bank process for assessing credibility of transition plans and their implementation
- scope of application to bank finance and other types of support

We will encourage the responsible investment community to also engage on these issues and help bring collective pressure on financial institutions.

Where we draw the line

We will only invest in large banks where we assess them to be aligning their institutional lending to the Paris Agreement. Our climate assessment considers their lending to:

- The fossil fuel sector, including the type of fuel and its emissions intensity;
- Renewable energy and energy storage; and
- Technologies and activities which reduce energy usage or store carbon (e.g. green buildings, low-emissions transport and reforestation).

We also look at the way banks facilitate financing by others. That is, how a bank might help companies raise financing for environmentally friendly initiatives, including through instruments such as green bonds.

We've been publicly challenging business leaders at company AGMs and co-filing shareholder resolutions. This sends a strong message, but it is not enough to get the job done. We are focusing on bringing collective pressure on financial institutions from the broader responsible investment community.

Holding ourselves accountable

We seek to hold ourselves accountable to what we said we would do and to achieving real world outcomes. Below we've compared our activities from FY23 to what we committed to do in our last sustainability report; and set out what interim indicators of success may look like for FY24 so we can better objectively assess our progress

In our last sustainability report we set out proposed FY23 activities towards achieving our real-world objective of ending finance to unsustainable fossil fuels. Here is how we stacked up against our commitments.

What we said we'd do	What we did
Assess banks' additional climate-related targets and criteria using IGCC, IPCC and IEA reports.	In our assessment of the banks' targets and criteria, we identified two key areas of weakness: • Insufficient urgency. High emissions customers are being given too much time – 2, 3 and more years – to align their business with the transition needed to limit warming to 1.5 degrees. • Too much latitude for general corporate finance. While the banks are increasing restrictions on project finance for new fossil fuel projects, these restrictions don't apply to their general corporate lending facilities. Banks should be testing whether high emissions customers are genuinely aligning with the Paris Agreement – including scrutinising new capital spending – before providing any type of financial support.
Seek further meetings with the banks to clarify their positions and signal our concerns	We met with ANZ, Westpac and NAB through one-on-one meetings, roundtable discussions, climate policy meetings and pre-AGM meetings. In our discussions we called on the banks to assess whether new lending to fossil fuel clients is aligned with the banks' own commitments to net zero, particularly having regard to where those clients are spending new capital today.
Make concerns public	We briefed the media about shortcomings of the banks' approach to climate alignment and our then Head of Ethics Research, Dr Stuart Palmer was quoted in the SMH: see here and here.
Co-file / support shareholder resolutions and encourage support from other responsible investors through our networks and the PRI collaboration platform	In FY23 we: • Co-filed shareholder resolutions against NAB and Westpac, sponsored by Market Forces. • Briefed other investors to encourage support for the shareholder resolutions
Challenge company management at AGMs	We attended NAB and Westpac AGMs and questioned the respective Chairs about the loopholes in their lending restrictions that allow until 2025 new and renewal of loans, to companies who are actively planning and developing new fossil fuel projects.
Consider pathways for other escalations (e.g. seeking to replace directors)	We have had internal discussions to explore alternative strategies. For any strategy to work, we need other investors to support our efforts. This has been our focus.

Potential indicators of success for FY24

- greater support for resolutions
- collaborative investor discussion / engagement initiative established
- evidence other investors are challenging the banks on their climate policy ambition
- Identify an opportunity for legal action (e.g. access to books, commissioning legal opinion on greenwashing)
- banks and other financial institutions undertake more rigorous climate analysis that provides results more aligned with scientific consensus of impacts of climate change
- evidence of banks committing to or applying restrictions to fossil fuel companies, and in particular oil and gas companies, for general corporate lending

"In our last sustainability report we set out proposed FY23 activities towards achieving our real-world objective of ending finance to unsustainable fossil fuels. Here is how we stacked up against our commitments."

Insurance companies

What we did

Engagement

We met with QBE's sustainability team in January 2023 reiterating the major gaps we see in QBE's climate policy that sets out how it will assess Paris-alignment when underwriting oil and gas companies.

Following the release of QBE's 2023 climate reporting, we wrote to QBE calling out critical shortcomings including that its underwriting criteria for oil and gas clients only requires them to have a transition plan by 2030 – far too late.

AGM activity

At QBE's AGM we voted against the remuneration report, the grant of conditional rights to the CEO and against the re-election of the chair and another director. We advised the company of our decision and our voting rationale that:

- the company is failing to make progress in addressing the climate concerns we have raised over multiple years, and
- the short and long term incentives in the remuneration plans are heavily weighted towards short term financial performance metrics, and there is no direct reference to climate related risks and opportunities.

We attended the AGM and questioned the Chair about QBE's serious shortcomings in its approach to climate.

What has been achieved?

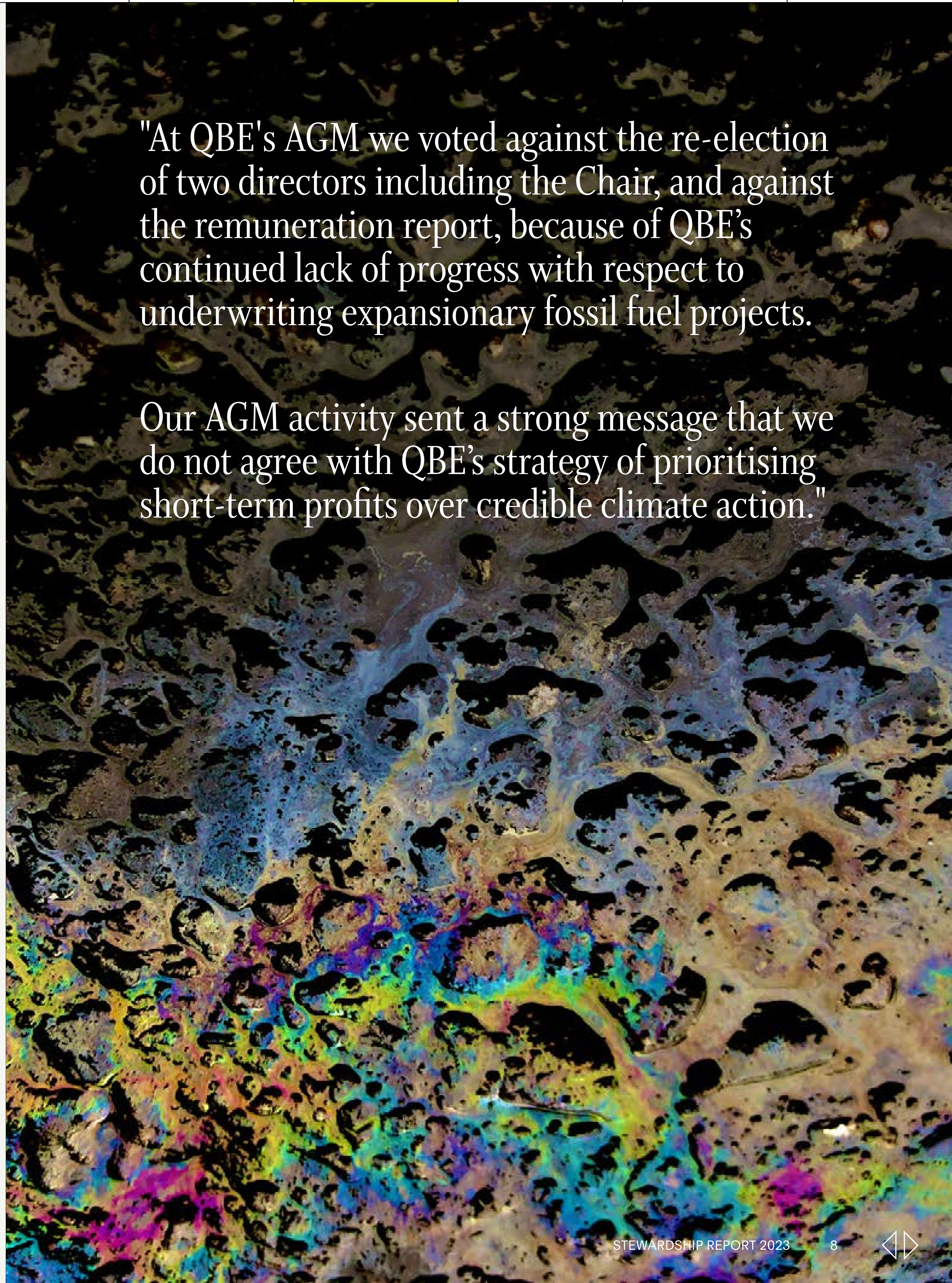
Our AGM activity sent a strong message that we do not agree with QBE prioritising short-term profits over credible climate action.

What next?

QBE has recently withdrawn from the UN-convened Net Zero Insurance Alliance. Together with their lack of progress on their own climate commitments, this sends concerning signals about the company's commitment to net zero. We are considering how to escalate this engagement most effectively.

Where we draw the line

We will only invest in large insurance companies that we assess to be aligning their underwriting to the Paris Agreement. Divestment is always on the table for insurance companies that fail the test.



Helping accelerate the advancement of alternatives to animal research

An estimated 190 million animals were used for scientific purposes in 2015 (not including observational studies).[6] Most of the animals used for scientific purposes will suffer. Their lives may be spent entirely in confinement. Many are bred or genetically altered to introduce a specific disease such as cancer or dementia. Some undergo surgery to mimic conditions such as deafness; many are subjected to invasive procedures, restraints or are forced into situations to induce stress. Generally animals are killed when an experiment ends (if they do not die as part of the experiment).

We do not invest in cosmetic companies that conduct or commission animal research because we do not think the animal suffering is justified. However, we recognise that animal research is currently a necessary part of developing health care products and so we may invest in companies that conduct or commission animal research for health care product purposes.

We have an opportunity to leverage our investment in healthcare companies to help accelerate a transition to alternatives to animal research. As one of only few investors in the sector that are awake to this issue, we also see this as our responsibility.

Our theory of change is that we can help accelerate the transition to alternatives to animal research by influencing:

- healthcare companies and universities involved in animal research to have policies in place to help ensure they are genuinely doing everything they can to replace animal research with alternatives wherever possible, including by consulting with people who have expertise in alternatives. They cannot simply rely on Animal Ethics Committees which can be conflicted and can lack knowledge and expertise in alternative models
- industry, academic and other research institutions, and government to collaborate to fund, validate and commercialise alternatives to animal research.

In FY23 we made progress on both.

We escalated engagements with two companies that had not made sufficient progress on developing animal research policies, sending letters notifying of potential divestment on these grounds. Both companies subsequently made commitments to introduce appropriate policies. This demonstrates the impact of forceful stewardship.

The Australian Ethical Foundation and Australian Ethical Investment jointly sponsored a CSIRO report which set out a strategy for accelerating the advancement of non-animal models in Australia. This sets us up well for impactful stewardship in FY24 focused on encouraging the collaboration needed to accelerate the transition (discussed on the following page).

6 journals.sagepub.com/doi/10.1177/0261192919899853

Five years of progress

FY18-19

We engaged with 14 companies and other stakeholders (including scientists on animal ethics committees and animal protection organisations) to help us better understand how companies approach the 3Rs, what best practice looks like, and where there are areas for improvement.

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FY19

We developed five minimum expectations of companies involved in animal research to demonstrate genuine application of the 3Rs.

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FY22

We wrote to nine Australian & NZ companies to confirm they are meeting our minimum expectations

Outcomes

- 5 substantially met our expectations
- 2 provided inadequate responses
- 1 did not respond
- 1 we did not continue with engagement as there were no prospects of imminent investment.

←

FY23

- We notified the two companies that provided inadequate responses in FY22 of our intention to divest if they were not committed to improving their approach to the 3Rs
- We followed up with the company that didn't respond in FY22
- AE and the Foundation co-sponsored a CSIRO project on development of Australian roadmap for non-animal models. We asked healthcare companies in our portfolio to also consider providing sponsorship
- We commenced engagement with six international healthcare companies in relation to their approach to the 3Rs
- We commenced engagement with the university sector with the intention of developing minimum expectations, following consultation with two NGOs
- We commenced engagement with industry association Ausbiotech

Outcomes

- The two companies we wrote to warning of potential divestment both made meaningful commitments to improve and remained in investable universe
- The company we followed up with committed to providing more public disclosures and commitments relating to the 3Rs
- None of the companies we wrote to provided financial support to the CSIRO project, but some engaged with CSIRO to provide industry perspective
- Ausbiotech is hosting a panel discussion on alternatives to animal research at its next conference, and has included a section on animal research in its draft ESG guidance to industry members

What we did

We have been pursuing two work streams aligned to our theory of change:

1. influencing healthcare companies and universities to have robust animal research policies in place to ensure genuine efforts to transition towards alternatives wherever possible
2. encouraging pre-competitive industry, academic, institutional and government collaboration to develop, validate and commercialise alternatives.

Influencing heathcare company & university animal research policies

Healthcare company engagement

We continued our five year company engagement program focused on promoting genuine commitment to the 3R principles (replace animals with alternatives wherever possible, reduce the number of animals used and refine the conditions and methods to reduce suffering). We commenced engagement on this topic in FY18. A common response we received from companies was that they only conduct or commission animal research when "absolutely necessary", and all research is approved by animal ethics committees. We do not consider this sufficient to demonstrate genuine application of the 3Rs. Generally, an Animal Ethics Committee sits within the organisation conducting the research and includes members who are independent. Based on our consultations, we are concerned that Animal Ethics Committees may not have the knowledge or may not be in the position to say no to an animal research proposal or to identify opportunities to use alternatives. Animal Ethics Committees certainly have their place, but they rarely challenge whether an animal research proposal should proceed and they have not always stopped questionable research on animals going ahead. They can sometimes entrench the status quo and are not a good vehicle to progress the use of alternatives.

In FY19, after consultation with relevant stakeholders, we developed our own minimum expectations of genuine application of the 3Rs. In FY22 we wrote to nine Australian and NZ healthcare companies asking them to confirm they are meeting our minimum expectations. Five companies confirmed that they did. Two provided inadequate responses and one did not respond at all. For one company we decided not to pursue the engagement as there were no prospects of investment.

In FY23 we:

- notified the two companies that provided inadequate responses of our intention to divest if they were not committed to improving their approach
- followed up with the company that did not respond
- expanded our engagement program to include six international healthcare companies
- engaged with industry association Ausbiotech about enhancing the animal ethics criteria in their ESG guide for Australian biotech companies

Benchmarking universities

We commenced our engagement program for the university sector. Animal research at universities is different to research in the commercial sector, which means our minimum expectations for healthcare companies are inadequate for this context. We therefore need to develop another set of minimum expectations that are appropriate for the breadth and type of animal research undertaken by universities. To this end, in FY23 we:

- consulted with relevant NGOs
- developed a draft expectations framework based on existing international standards and benchmarks
- conducted a desktop assessment of Australian universities against our draft expectations framework
- commenced engagement with some universities to discuss our findings and invite feedback.

Encouraging collaboration to develop, validate and commercialise alternatives

Animal welfare policies only go so far and the reality is, even under the best conditions with application of the best policies, animals suffer when they are used for research. Replacing animals with alternatives has to be the focus. Through our five year engagement program we have come to a better appreciation of the fact that when it comes to replacing animals with alternatives, individual companies are constrained by what they can achieve by virtue of regulatory requirements and commercial realities. But this is no excuse for inaction. We think there is opportunity to shift the dial on this issue through pre- competitive industry collaboration to fund, validate and commercialise alternatives to animal research.

To that end, in FY23:

- the Australian Ethical Foundation and Australian Ethical co-sponsored a CSIRO project to develop a national roadmap for non-animal models. We encouraged healthcare companies in our portfolio to also consider sponsorship
- we asked Ausbiotech to include non-animal models on the agenda of their industry conference.

What the companies did

- Cochlear committed to establishing a formal policy on animal ethics.
- Opthea committed to using only AAALAC accredited vendors for animal research; formalise the creation of an Animal Research Subcommittee to oversee Opthea's external toxicology and animal research studies and ensure the 3Rs are incorporated into experimental designs; updating the company's ESG framework to include a section on the 3R principles and animal welfare; and to communicate to other Australian biotechnology companies the importance of applying the 3Rs.
- Ausbiotech committed to including non-animal models on the agenda for their November 2023 conference. Opthea also provided support for this proposal.
- No companies we engaged provided sponsorship for the CSIRO project. However a number engaged with CSIRO to provide valuable industry perspective.
- UTS provided feedback on our draft benchmark.

What next?

We propose to:

- monitor Cochlear's delivery on its commitment to introduce an animal ethics policy
- progress our engagement with the six international healthcare companies seeking to bring them into alignment with our minimum expectations
- progress our university benchmark, seeking feedback from a larger number of universities
- contribute to the Ausbiotech panel discussion on alternatives to animal research
- leverage the recommendations in the CSIRO report by developing a sign-on-statement that can be supported by industry, the university sector, other research institutions and other investors. This statement will call on the Australian government to develop a collaborative and strategic approach to advance alternatives to animal research.

Where we draw the line

Where healthcare companies or universities are involved in animal research, we require evidence of genuine commitment to the 3Rs. Our understanding of what genuine commitment to the 3Rs looks like is evolving as we learn more about the complicated and opaque world of animal research. Currently, our expectations of healthcare companies are:

1. The company engages research institutions that are in a jurisdiction with adequate animal welfare standards, or apply those standards.
2. The company confirms that any research institution it uses upholds the 3Rs principle. Confirmation to be based on the research institution's reputation, questioning the institution in relation to specific practices, and assessments by internal or external experts on animal welfare in scientific research.
3. The company ensures that individuals or organisations with scientific expertise in alternatives to animal research are consulted at the design stage of proposed animal studies.
4. The company ensures that its contracts with research institutions include requirements that the research institution will:
   a. apply high welfare standards at all stages of the animals' life for which they are responsible, including transport and housing
   b. apply the 3Rs at all stages of the process including experiment design
   c. report on its application of the 3Rs in contracted research.
5. The company does at least one of the following:
   a. puts some funding towards the development of alternatives to animal research models
   b. supports regulatory changes and public funding of research to improve application of the 3Rs and to support the use of alternatives where they are available. We are happy to discuss further the ways in which companies could show this support to regulators and others; or
   c. has a public statement on the company website that outlines the specific steps the company is taking in relation to the 3Rs.

We are currently developing expectations of universities that are involved in animal research.

Holding ourselves accountable

We seek to hold ourselves accountable to what we said we would do and to achieving real world outcomes. Below we've:

- compared our activities from FY23 to what we committed to do in our last sustainability report
- set out what interim indicators of success may look like for FY24 so we can better objectively assess our progress going forward

In our last sustainability report we set out proposed FY23 activities for our animal research engagement. Here is how we stacked up against our commitments.

What we said we'd do	What we did
Escalate engagements with companies that did not adequately respond in FY22.	We notified the two companies that provided inadequate responses of our intention to divest if they were not committed to improving their approach. Both companies subsequently made commitments to improve.
Commence an engagement program with select Australian universities	We commenced our engagement program for the university sector. Specifically we: • consulted with relevant NGOs • developed a draft expectations framework based on existing international standards and benchmarks • conducted a desktop assessment of Australian universities against our draft expectations framework • commenced engagement with some universities to discuss our findings and invite feedback.
Publish a statement on the PRI collaboration platform	We did not do this as we did not think the engagement had sufficiently progressed to a stage where a statement on the PRI platform would get traction and have impact. However, as discussed above, we think the CSIRO report creates opportunities that could include using it as a basis to galvanise broader investment support for the transition to alternatives.
Engage with industry associations to understand their perspectives on an industry-wide 3R initiative	We engaged with Ausbiotech, an Australian industry body representing and advocating for organisations doing business in the life sciences economy, about enhancing the animal ethics criteria in their ESG guide for Australian biotech companies, as well as about including a discussion on non-animal models on the agenda of their industry conference.

Potential indicators of success for FY24

- identify opportunities to have 3Rs and alternatives to animal research included on the agenda at relevant industry forums
- obtain strong industry, academic and investor support for the statement
- international companies meet or receptive to meet minimum expectations, and / or help evolve expectations
- minimum expectations of universities developed, universities meet or receptive to meet minimum expectations and / or help evolve expectations
- evidence of positive change following engagements

Livestock driven deforestation in Australia: a contributor to climate change and nature loss

Today we face the double, interlinked emergencies of human induced climate change and nature loss. Deforestation is a key contributor to both, and we cannot solve either without stopping deforestation. Australia is the only developed country in the world with an identified global deforestation hotspot.[7] Livestock is the primary driver. In QLD, 93% of deforestation and land clearing in 2018-19 was for conversion to pasture.[8]

We also have one of the worst track records for animal extinctions. Clearing of native vegetation is a major cause of habitat loss and fragmentation and has been implicated in the listing of 60% of Australia's threatened species.[9] Estimates suggest that almost 4.9 million animals died due to land clearing every year in the decade between 2005 and 2015.[10] In QLD, around 80% of likely or known koala habitat cleared between 2018 and 2019 was cleared for beef production.[11]

In addition to being a primary driver of deforestation, animal agriculture also uses a disproportionate amount of land and other resources relative to the nutritional value it provides. About half of Australia's total land area is used for agriculture. Of this land, 86.5% is used for grazing.[12] This does not include land used to grow animal feed.

Using so much land for livestock is hugely inefficient. Research suggests that if we moved from current diets to a diet that excludes animal products the world could reduce food's land use by around 3.1 billion ha (a 76% reduction).[13] Why does this disproportionately large land footprint matter? Every hectare of land we use for animal agriculture is a hectare that cannot support wild forests, savannahs, wetlands and other crucial ecosystems. And all that land we could free up with a change in diet could be used to sequester carbon and restore native habitats and ecosystems.

For example, one study found that the land that could be spared through a transition to a plant-based diet could remove 8.1 billion metric tons of CO_2 from the atmosphere each year over 100 years.[13]

We restrict* investments in conventional animal agriculture companies because we assess the harm to animals, and the high environmental impact, to be unnecessary when there are less impactful alternatives. But rather than divest and forget, we consider the impact of livestock in Australia, and in particular its impact on deforestation, an issue over which we can have positive influence.

Our theory of change is that we can help address livestock driven deforestation in Australia by bringing attention to the issue through investor forums and engagement initiatives.

Key to our theory of change is that farmers need to be incentivised to protect and restore nature. Farmers need to be compensated for land management that results in restoration of nature, and there needs to be supply chain and financing challenges for engaging in practices that harm nature.

Investors have a role to play in creating this ecosystem. Collectively, investors can put pressure on companies in the livestock value chain (such as banks and food retailers) to commit to no deforestation policies. Investors can also bring collective pressure on government to create the positive incentives needed for a just transition.

This requires greater understanding amongst the financial sector of the systemic risks posed by deforestation and its contribution to climate change and nature loss, the fact that deforestation occurs at a globally significant scale in Australia, the drivers of deforestation in Australia and the need for a plant-based food transition.

What we did

In FY23 we built on what we started in FY22, which was to create or participate in forums where we thought collective conversations about these issues can happen.

We joined the UN Race to Zero's Financial Sector Deforestation Action (FSDA) initiative in FY22. That initiative seeks to influence companies with exposure to high risk commodities to commit to no deforestation in the supply chains or financing, in accordance with the directives on deforestation as set out in the Accountability Framework. This also accords with expectations in the SBTI guidance for the Food Land and Agricultural sectors. In FY23 we commenced engagement with Woolworths, as lead investor. We also helped inform the engagement with an Australian financial institution and a global meat processing company that sources from Australia. We drew attention to evidence of deforestation in Australia when target companies sought to characterise it as a low-risk issue. This highlights the importance of our involvement as the only Australian investor in the conversations.

Having joined the Nature Working Group of the Responsible Investment Association of Australia, in FY23 we looked for ways to include livestock-driven deforestation on the agenda, on the basis that it is the most significant driver of nature and biodiversity loss in Australia. We also encouraged the Investor Group on Climate Change to include deforestation on their agenda.

7 WWF Australia (13 January 2021), Australia remains the only developed nation on the list of global deforestation fronts; wwf. org.au/news/news/2021/australia-remains-the-only-developed- nation-on-the-list-of-global-deforestation-fronts
8 Wilderness Society (August 2019), Drivers of Deforestation and land clearing in Queensland; wilderness.org.au//images/ resources/The_Drivers_of_Deforestation_Land-clearing_Qld_Report.pdf; and wilderness. org.au/qlddeforestation, wilderness. org.au/qlddeforestation. See also: Evans, Megan (January 2016), Deforestation in Australia: drivers, trends and policy responses; researchgate.net/publication/301942515_ Deforestation_in_ Australia_Drivers_trends_and_policy_responses
9 soe.dcceew.gov.au/land/pressures/industry#land-clearing
10 https://wwf.org.au/what-we-do/living-planet-report/
11 wilderness.org.au/protecting-nature/deforestation
12 soe.dcceew.gov.au/land
13 josephpoore.com/Poore%20and%20Nemecek%20(2018)%20Reducing%20foods%20environmental%20impacts%20through%20producers%20and%20consumers.pdf

Key to our theory of change is that farmers need to be incentivised to protect and restore nature

We had some preliminary discussions as part of the new Nature 100 investor engagement initiative to draw attention to nature loss in Australia. Notwithstanding the fact Australia has one of the worst records for mammal extinctions of any country and the east coast of Australia has been identified as a globally significant deforestation hotspot, Australia usually doesn't feature high on the global priority list relative to places like the Congo and the Amazon.

We also made a submission on the Nature Repair Market Bill proposed by the Federal government. In that submission we raised concerns about provisions that looked like they were intended to protect the status quo instead of facilitating a just land use transition. We also raised concerns about the extent to which government can rely on the private market to pay for the protection and restoration of nature through a market mechanism in the absence of broader reforms, and the risk that biodiversity certificates will be used to justify, legitimise and thereby potentially encourage harms to nature.

What has been achieved?

Woolworths has greatly improved its deforestation policy. It previously committed to no net deforestation by 2025 in the supply chains of its Own Brand high risk commodities (falling short of the no deforestation ask put forward by investors in the FSDA initiative). In its latest Sustainability Plan Woolworths has more closely aligned to the asks we put forward through the FSDA engagement. It has included a cut-off date of 2020 (that is, by 2025, land cleared post 2020 will not be included in the relevant supply chains), it has committed to assess a transition to deforestation and conversion free supply chains (as distinct from no net deforestation), and it is seeking to align with the Accountability Framework Initiative directives on deforestation.

We have heard anecdotally that the Australian financial institution is going to look at their exposure to deforestation in Australia, but we note their existing agricultural lending policies fail to address this issue.

The IGCC invited us to be on a panel to discuss deforestation at their annual summit., which had over 400 registered attendees. They have also provided investor education sessions on the topic.

Small changes were made to the Nature Repair Market Bill that helps address some of the concerns we raised.

What next?

Proposed FY24 activities:

- Consider opportunities to continue to encourage Woolworths to apply the higher no deforestation and conversion standard through: Nature Action 100, Climate Action 100+, IGCC and / or escalating FSDA engagement. Through these engagements seek to understand barriers for Woolworths and identify opportunities for how investors could support them to take stronger action.
- Commence engagement with Coles
- Continue / begin engagements with banks in relation to their agricultural sector targets including through finance / fossil fuel engagements where possible
- Continue to explore ways to increase financial sector understanding of the extent of deforestation in Australia, its drivers and the solutions available to halt and reverse, including through involvement on the deforestation panel at the IGCC summit
- Continue to explore ways to contribute to policy discussion including on biodiversity markets and subsidies

Holding ourselves accountable

We seek to hold ourselves accountable to what we said we would do and to achieving real world outcomes. Below we've:

- compared our activities from FY23 to what we committed to do in our last sustainability report
- set out what interim indicators of success may look like for FY24 so we can better objectively assess our progress going forward

In our last sustainability report we set out proposed FY23 activities for our livestock deforestation engagement. Here is how we stacked up against our commitments.

What we said we would do	What we did
Continue to pursue collaborative engagements on the climate and biodiversity impacts of Australian livestock through the forums we worked with in FY22	Through FSDA we commenced engagement with Woolworths, as lead investor and helped inform the engagement with an Australian financial institution and a global meat processing company that sources from Australia. We continued to draw attention to deforestation through the RIAA Nature Working Group and IGCC.
Develop a research proposal on the climate and biodiversity impacts of Australian livestock and commission that research with the goal of using the output to raise awareness and inform collective engagement	We explored this further in FY23 but ultimately decided not to pursue a research project for two main reasons: (1) NGOs like the Australian Conservation Foundation, The Wilderness Society and Climate Works were already in the process of producing excellent research on related issues (2) We recognise we need to do more engagement to then identify where the gaps in knowledge are, to then identify the most effective research question to address.

Potential indicators of success for FY24

- Through RIAA NWG and/or IGCC we put livestock driven deforestation in Australia on the investor agenda
- Evidence of other investors looking at livestock driven deforestation in Australia
- Livestock driven deforestation becomes part of existing or developing investor engagement initiatives e.g. Climate Action 100+, separate IGCC engagement or Nature 100 (to be determined which we focus on)
- We understand the barriers for supermarkets taking stronger action to address deforestation in their beef supply chains and identify opportunities for future stewardship work to help address those barriers
- We encourage banks to commit to no deforestation in lending, or understand the barriers to them doing so and identify opportunities for future stewardship work to help address those barriers
- We identify research or policy advocacy opportunities that we assess might make a meaningful contribution to stronger action on deforestation in Australia

Reducing embodied emissions in building products and addressing negative lobbying

Building materials are a large contributor to global carbon emissions. It is a hard-to-abate sector but one that we will need through the energy transition and into the next economy. As new technologies are being developed and the sector pathways to climate alignment are becoming clearer, we are now investing selectively in those companies that meet our science-based, sector-specific, ethical requirements.

Given our investment in this emissions-intensive industry, we see it as our responsibility to influence more urgent progress towards alignment with the Paris Climate Agreement. We also are concerned that emission-intensive companies, and the industry groups that represent them, may be lobbying against appropriate and ambitious climate policies. As long-term investors we see it as our responsibility to seek to address negative lobbying that may be in the short-term financial interests of individual companies but can exacerbate system risks like climate change.

What we did

In FY23 we continued our role as the lead investor responsible for the Climate Action 100+ engagement with cement company Boral. We also became the lead investor for the Climate Action 100+ engagement with cement company Adbri. Cement production is a large contributor to carbon pollution – accounting for around 8% of total global emissions in 2018, according to think tank Chatham House.

Boral

We commenced as a co-lead on the Boral Climate Action 100+ engagement in April 2021. In September 2021 we were pleased to see Boral become the first in the global construction materials industry to set FY30 science-based scope 1 and 2 targets aligned with limiting global warming to 1.5°C. The company also developed a detailed transition plan and worked to expand its lower embodied carbon products as a proportion of its business.

In FY23, we became the sole lead investor on the engagement, and continued our dialogue with the company focused on:

- The expansion of the company's internal carbon price pilot program to be applied consistently across all of its capital expenditure decisions and at an appropriate price.
- The continued build out of lower emissions products as a key lever of their reduction pathway, to become the company's main offering, to continue to develop lower carbon products, and to expand their work to other products like asphalt.
- The lobbying engaged in by the company and its industry groups on climate policy, to raise concerns around the transparency and alignment of those activities with the company's own stated positions.

Adbri

In January 2023, we joined the Adbri Climate Action 100+ engagement as lead investor. We do not currently invest in Adbri as its climate performance does not meet our ethical requirements for investment. We are engaging as a potential investor with the goal of seeing the company lift its performance and become investable.

We met with support investors and established focus areas for the engagement:

- The setting of science based short, medium and scope 3 emissions reduction targets
- The development of lower emissions products, including appropriate allocation of resources to research and development of emissions reduction initiatives
- The lobbying engaged in by the company and its industry groups on climate policy, to raise concerns around the transparency and alignment of those activities

Adbri is yet to agree to meet with the Climate Action 100+ engagement group. We have engaged with the company via email and attended an earnings reporting meeting. We will continue to work to commence a dialogue with the company.

Mecla

Accelerating the sector towards Paris Alignment requires strong demand signals for lower embodied carbon products by those commissioning, constructing and designing buildings, homes and infrastructure. As well as engaging with suppliers of cement, we try to encourage demand for lower embodied carbon building products.

We became a founding partner of the Materials and Embodied Carbon Leadership Alliance (MECLA) in September 2021, and we are a member of the demand working group.

Through MECLA, we've been working to circumvent demand barriers, and regulation and procurement practices that make innovation in lower carbon building products difficult to adopt. We've sought out opportunities to leverage the investor perspective to further these objectives.

- In particular, we've been working toward the development of requirements from state governments for the measurement and disclosure of whole of life carbon emissions for built environment projects, to create a benchmark that can be used to set an emissions reduction target, and ultimately a carbon budget embedded in the National Building Code.
- This resulted in a MECLA submission on the NABERS Embodied Carbon Consultation paper to the New South Wales Government, which looks to expand the existing NABERS efficiency rating scheme to encompass embodied emissions. We stressed the importance of this becoming a mandatory tool across all built environment project types, and that the tool should be shared with other state governments for broader take up.

What has been achieved?

- The focus areas for the Climate Action 100+ engagements with Boral and Adbri have been agreed with support investors and include addressing negative lobbying
- We commenced relationship building with Adbri
- We contributed to and strengthened the MECLA submission on the NABERS Embodied Carbon Consultation paper

What next

- Continue to gather information on embodied emissions and solutions, to develop appropriate expectations of building material producers and purchasers.
- Seek out opportunities to increase awareness of embodied emissions, lower carbon alternatives, and the need for producers and purchasers of building materials to consider embodied emissions in the footprint of buildings and other projects.
- Focus on understanding Boral and Adbri's current climate lobbying activities, including through industry groups, and applying pressure where we see their activities are not aligned with the goals of the Paris Agreement.
- Work to encourage the uptake and retention of science based targets by Boral and Adbri, supported by detailed transition plans and appropriate research and development expenditure.

Potential indicators of success for FY24

- Boral and Adbri disclose their direct and indirect climate lobbying activities and their alignment with the Paris agreement, and support Paris aligned climate policy in Australia.
- Boral and Adbri commit to develop or retain science based emissions reduction targets

> "Given our investment in this emissions-intensive industry, we see it as our responsibility to ensure it is getting to Paris alignment as quickly as possible.*

Tactical engagements

Lendlease: an example of divestment with impact

In March 2023, our multi-year engagement with Lendlease ended with divestment. Specifically we divested our debt and equity positions in the Lendlease Group. We intend to sell our investment in an unlisted property trust, the Australian Prime Property Fund – Retail, which is managed by Lendlease, at the first available liquidity window.

We divested because we did not have sufficient certainty that Lendlease or the NSW government was taking appropriate steps to protect the koala colony that will be impacted by Lendlease's Mount Gilead development.

Our divestment announcement reached a potential audience of 8.5 million Australians through 110 unique pieces of earned media coverage, including the ABC, Channel 9 News, the Guardian, The Australian and Bloomberg.

Following our request for support, 1,799 people copied us in on their letters to the then NSW Minister for Environment and Heritage, the Hon. James Griffin, requesting a transparent public consultation on the environmental impacts of the development.

Post divestment, we sent briefings to the new NSW ministers (the Hon. Penny Sharpe, Minister for the Environment; and the Hon. Paul Scully, Minister for Planning). We met with the Minister for Environment's Office. We also gave briefings to other investors explaining our concerns with the proposed development.

Impact

We believe divesting from Lendlease so publicly, at the time we did it, has had an impact:

- The new NSW Minister for Environment has said publicly she will closely review Lendlease's plans for its Mount Gilead development, with particular focus on the corridors.
- NSW government approvals have been delayed, and we believe this has resulted in a costly delay of the development project (prior to our divestment it seemed approval was on track for July).
- Anecdotally we have heard from NGOs that our public divestment has helped them in their conversations with relevant authorities.
- We have given briefings to other investors who have wanted to understand the issues for the purposes of their own engagements.

Why we divested

For over four years we had been engaging with Lendlease about its housing development at Mount Gilead, which is next to one of the last healthy koala colonies in NSW. We have been concerned about this development and its potential impacts on the local koala colony since we first became aware of it at the end of 2018.

There is a housing crisis in NSW. But koalas and other native species across Australia are also facing a housing crisis which for them poses an existential threat. Koalas are endangered across QLD, NSW and the ACT, and habitat loss is a key threat.

We believe there are ways to solve one housing crisis without exacerbating the other. At one stage, we were hopeful that Lendlease's development would provide a blueprint for how housing developments can be aligned with, and protect and restore, nature.

But we lost faith when Lendlease and the NSW government failed to disclose key information about proposed koala corridors. The survival of the local koala colony hinges on the existence of appropriately sized wildlife corridors to provide safe passage across the site, according to advice from a panel established by the Independent Office of the NSW Chief Scientist and Engineer (OSCE).

We have serious concerns about how Lendlease and the NSW Department of Planning are interpreting the reports from the OSCE. They have formed the view that there is no minimum width requirement for koala corridors, meaning that corridors can narrow for long stretches to make way for development. This risks creating exactly what the OSCE warned about - functional dead ends, which can become population sink holes. We do not think this interpretation is a good faith reading of the OSCE's recommendations.

We also have serious concerns about lack of transparency in the approvals process. There have been several public consultations relating to this development including at council, state and federal government levels. But detailed measurements for the proposed koala corridors across Mount Gilead has not been made public, nor have plans for critical koala road crossings, or important information about why Lendlease needs to rely on koala offsets and how they will protect the affected colony. We are perplexed as to why critical aspects of this development are only going to be made public after consultations have closed. It seems an illogical order of events and makes it hard for investors to have faith in government approval processes for potentially high impact developments.

The importance of engagement and divestment

There is some debate in the responsible investment community about whether investors should divest or engage when investee companies fail to meet the investor's standards. In our view, this debate is too often used as cover to justify continued investment where there is slow or no progress by companies. Divestment and engagement aren't alternatives, we need both.

Together with engagement, divestment and the threat of divestment, are tools investors can use to drive change. If done at scale, divestment can affect a company's cost of capital, making it less competitive than its more sustainable competitors. If done publicly, it can impact a company's reputation. It can also create market signals that help influence broader change. Sometimes it is helpful to have different investors take different approaches. An ethical investor withholding capital or divesting early can mean companies see the consequences of continued inaction and may be more receptive to the asks put by the investors that remain.

Australian Ethical does not take divestment lightly and we use this tool as a last resort. We have been engaging closely with Lendlease since 2018. Our engagement included meetings with the project team, with Lendlease's Group Head of Sustainability and Head of Sustainability Australia, and with the CEO.

We also employed various escalatory tactics. We publicly challenged the company at its 2022 half year results presentation. We wrote a letter notifying Lendlease of our ongoing concerns and suggestions for how they may address them. We sent a divestment notification letter setting out our detailed analysis of how the proposed development fails to meet the recommendations of the OSCE. We also put Lendlease on notice publicly that we would divest if they did not address our concerns.

Over the course of our engagement we saw material progress. Lendlease committed to restoring high quality habitat on site, building koala underpasses to provide safe crossing, creating koala corridors and ensuring that at no point during the development will there be less core koala habitat on site than existed before the development started.

However, Lendlease did not make any further commitments following our letter notifying of ongoing concerns and failed to respond substantively to our assessment of how they were falling short of OSCE recommendations. We concluded that engagement had stalled, and that we would make no further progress by pursuing it. Accordingly we made the difficult decision to publicly divest. We sought to do so in a way that would have the most impact.

What next?

This process has demonstrated to us how poorly nature is protected at all levels of government and how urgent the need for reform of our environmental protection laws, including the federal Environmental Protection and Biodiversity Conservation Act (EPBC Act). We look forward to seeing the Federal government's reform proposal.

We will also continue to agitate with respect to Lendlease's Mt Gilead development where opportunities arise. For example, in September 2023 we made a submission under the EPBC Act assessment process about this development.

Microsoft and Human Rights

In FY23 we commenced engagement with Microsoft about its provision of products and services that may enable human rights abuses by the Chinese Communist Party (CCP). The CCP uses information and technology products and services and to invade privacy and to enable censorship and mass surveillance of its citizens, as well as to advance military goals. We are concerned that Microsoft is working with and providing services to entities that may facilitate these activities by the CCP.

Under our human rights framework, we seek to avoid investments in companies that are not making genuine efforts to discharge their business responsibility for human rights (as set out by the UN Guiding Principles). This includes where there is evidence of a company directly causing or contributing to adverse human rights impacts by knowingly providing products or services to a third party, that supports that part's abuse of human rights.

We believe AI and other modern technology can have a beneficial impact for people without necessarily impeding human rights. We also believe companies can positively contribute to human rights while operating in countries with authoritarian regimes. However, we are concerned about the use and proliferation of technology in a country with an open agenda to use technology to maintain control of its populace without regard for human rights.

We are engaging with Microsoft to understand how human rights risks have been factored into Microsoft's rationale for its presence in China and how the company is managing and mitigating these risks to justify its continued business arrangements in the country. Microsoft says it conducts due diligence to assess the impact of its technologies on human rights, including the impact of technologies it makes available in China. Microsoft also applies international principles and norms such as the UN Guiding Principles on Business and Human Rights to guide its due diligence. However, Microsoft was not able to comment on evidence of partnerships it has with high-risk Chinese entities, so we do not have enough comfort at this stage that it is not facilitating human rights abuse, notwithstanding a level of due diligence.

Policy advocacy

We've been using our voice to encourage ambitious action by the government to avoid harm to people, planet and animals and promote a prosperous economy, communities and ecosystems. Policy is one of the most direct ways to ensure groups are operating responsibly in the economy, and is an important tool for issues that require collective action, like climate change.

We contributed to submissions that related to some of our key advocacy areas, including the NABERS Embodied Carbon Consultation paper for building materials, and the Nature Repair Market for deforestation and biodiversity.

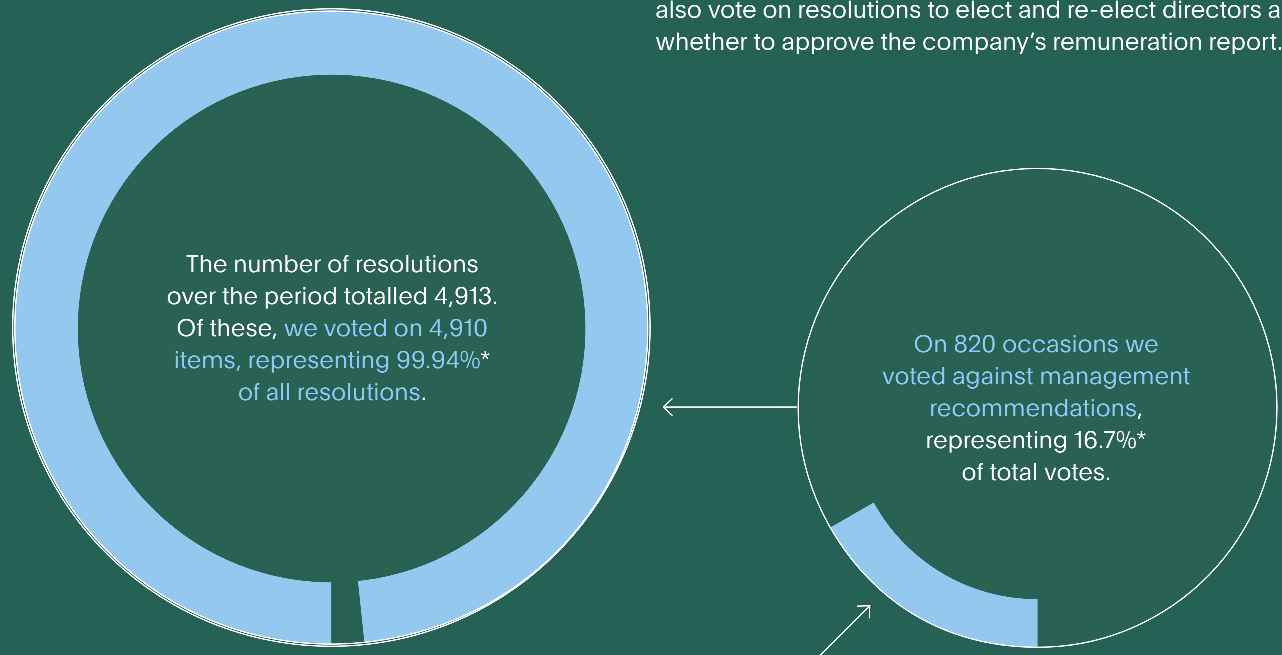
We also submitted, and contributed to submissions, across the climate policy space, including on the NSW Climate Plan, on the EPBC review process for 19 new fossil fuel projects, on the next Nationally Determined Contribution (the target that will be set by the Federal government for 2035 under the Paris agreement), as well as on the changes to the Safeguard Mechanism and climate disclosure requirements. On all of these issues, we stressed the need for urgent ambitious action to avoid the worst impacts of warming, and to seize the opportunities presented by transition.

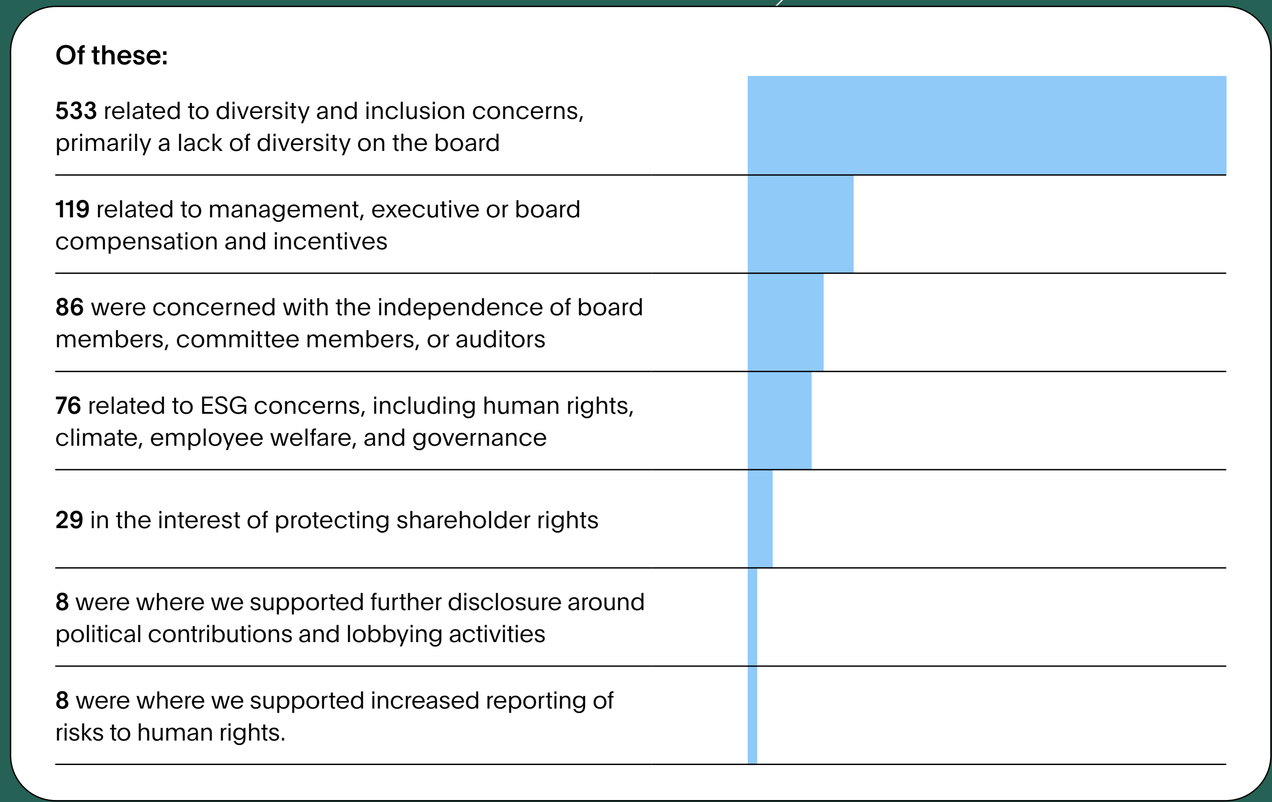
If policy aligns with the science and with our international commitments under the Paris Agreement, we believe the economy will do better, and so will people, the planet and animals.

We'll continue to leverage our voice to increase ambition on key issues like climate and nature, as well as agitating for other investors, companies and the public to be positively advocating too.

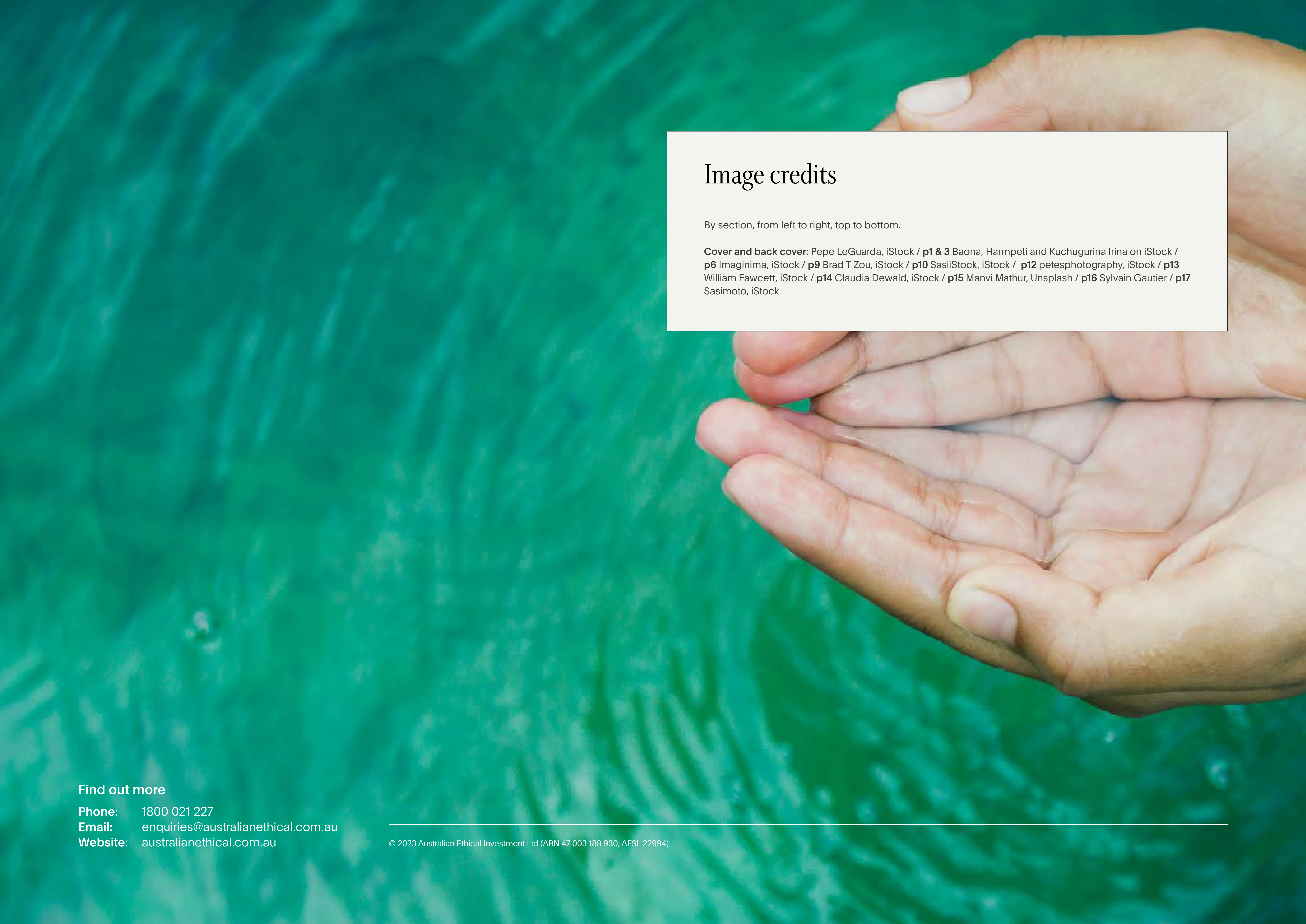
How we voted[14]

Voting is an important lever for shareholders to influence company boards and management. This can be voting on shareholder resolutions, commonly resolutions initiated by shareholders about climate; diversity of directors; transparency or other matters of concern. Shareholders also vote on resolutions to elect and re-elect directors and whether to approve the company's remuneration report.





14 This breakdown provides the number of instances where a vote was cast due to the reasons mentioned. However, a decision to vote against management recommendations may be attributed to multiple reasons and therefore this breakdown does not reflect numbers of individual votes.
Assurance*
KPMG have provided limited assurance over key metrics in our sustainability disclosures, including some engagement statistics. KPMG's assurance opinion is available here.



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