LIONTRUST
PRIDE IN OUR PROCESSES

SCREENING CRITERIA

Liontrust UK Ethical Fund

The Liontrust Sustainable Investment team's process starts with a thematic approach in identifying the key structural growth trends that will shape the global economy of the future and then invests in well-run companies whose products and operations capitalise on these transformative changes and, therefore, may benefit financially.

While the team's primary focus is on finding companies positively exposed to long-term transformative themes, they also want to limit or completely avoid an investment in companies exposed to activities that cause damage to society and the environment. To the team, this is an obvious and intuitive move and better reflects the companies they choose to hold across their sustainable investment funds. These activities are set out in this document on Screening Criteria.

To achieve this, the team has thresholds on the revenues that companies can derive from unsustainable and unethical activities and still be included in their funds. From July 2018, all funds managed by the team moved from a threshold of 10% of revenues from activities such as tobacco, gambling, intensive farming, weapon systems and nuclear to 5%.

This Screening Criteria form part of the sustainability analysis of each company and fund managers also carry out screening on stocks as part of their analysis. They do not have separate fund management and environmental, social and governance (ESG) divisions. Instead, every team member is responsible for all aspects of financial and ESG relating to an investment decision.

Because of this approach, the team engages with companies across a broad range of issues relating to steps in our investment process, including screening criteria, sustainable investment themes and company-specific ESG issues.

Screens on human rights, labour standards and infrastructure are less absolute than, say, involvement in tobacco so the screening process highlights any controversies for the analyst to assess on a case-by-case basis.

There are four elements to the assurance and oversight of the screens:

The sustainability analysis of each company is presented at team meetings where challenge from peers is invited.

The external advisory committee, made up of experts from key areas of social and environmental impact, sees a list of all holdings and transactions and will request clarification on any positions they feel warrant greater scrutiny.

Ethical Screening conducts a formal audit of all holdings every quarter to ensure adherence with the team's stated screening criteria.

All holdings are published quarterly so clients can see each position and challenge any holdings they feel do not meet with the spirit of our sustainable approach.

The Liontrust Sustainable Investment team has identified 15 issues, ranging from alcohol and climate change through human rights and labour standards to tobacco and weapons systems. Over the following three pages, we list all 15 of these issues, discuss the team's position on each of them and the screening criteria used.

Alcohol

While alcohol is consumed and enjoyed by a large percentage of the population, the excessive consumption of alcohol, sale to underage drinkers and irresponsible marketing of products can have negative social and health impacts. Companies selling alcohol must take steps to mitigate these impacts through responsible policies and practices.

- Excludes all companies that derive >5% of turnover from the production, distribution and/or sale of alcohol products

Animal welfare

Testing products on animals is clearly undesirable. However, it also forms an essential part of some necessary human and environmental safety testing and is sometimes required by law, for example in medical research and development, and the EU Directive on chemicals and their safe use (REACH).

- Avoids investing in any company involved with animal testing. The Fund is provided for investors who disagree with any form of animal testing for whatever reason

Climate change

It is becoming increasingly clear that greenhouse gas emissions from human activity is driving the rise in global average temperature [1]. A renewed global policy response to reduce green house gas emissions has been slow in being formulated, however, the Conference of Parties in 2015 saw a commitment to reduce global warming to 2 degrees centigrade, with an aspiration to tighten this further to limit the global average temperature rise to 1.5 degrees centigrade [2]. To do this there is an urgent need to reduce emissions, and the quicker this is done, the lower the ultimate cost of combating climate change [3]. To have a 66% chance of remaining below 1.5 degrees centigrade the Intergovernmental Panel on Climate Change (IPCC) worked out the maximum amount of carbon that can be emitted – the carbon budget. Their analysis suggests that if emissions remain as they are today we have only six years to use up the carbon budget, after that there would have to be net zero carbon emissions for the rest of the century to keep the rise in global average temperatures with 1.5 degrees centigrade [4]. While going carbon neutral within six years is highly unlikely, this research highlights the pace at which we need to decarbonise – which is faster than most realise.

- Excludes companies that derive >5% of turnover from the extraction and production of coal, oil, and natural gas

- Excludes companies that derive >5% of turnover from airlines and the manufacture of cars* and trucks (*unless they are specialised in making components that improve the efficiency or safety of cars)

- Excludes companies that derive >5% of turnover from the production of energy intensive materials unless they are making significant efforts and investment to make their processes more efficient and less energy intensive

Deforestation

According to the United Nations Food and Agriculture Organisation (FAO), although deforestation has been slowing since the 1990's, globally we still lose around 13 million hectares of forests through conversion to agricultural land or natural causes each year [5]. Deforestation and poor forestry management have significant impacts on the environment and biodiversity and must be managed effectively by companies.

- Excludes forestry and paper companies that do not have policies and practices in place to ensure that forests are managed in a sustainable way

- Excludes companies that are involved in the deforestation of primary or virgin forest or illegal logging practices

Gambling

There are concerns regarding the negative social impact of gambling addiction, especially on vulnerable groups such as children. The UK Ethical Fund expect companies involved in the gambling industry to be aware of the potential negative effects of gambling on individuals and communities and to recognise their responsibilities in this regard.

- Excludes companies that derive >5% of turnover from the management or ownership of gambling facilities

Genetic engineering

A decade or so after the introduction and widespread commercial adoption of GE technology, the scientific debate on the benefits and risks associated with the technology continues. We have fundamental concerns regarding the lack of clear protection of both the environment and consumers. Corporate behaviour has also generated alarm regarding disturbing commercial practices such as the use of terminator and traitor technology, threatening farmer independence and food security and further distancing Genetically Modified (GM) technology from application as a sustainability solution. However, given extended use of the technology outside Europe without materialisation of the earlier primary safety concerns, and given considerations of world food security and climate change, we do not feel it appropriate to completely discount the potential that this technology may in due course bring. For example, it may have the potential to improve agricultural productivity and mitigate environmental damage associated with more conventional forms of intensive farming. Consequently, we take a precautionary approach and expect careful management of the risks surrounding this technology such as threats to biodiversity and ecosystem disruption. We will approach GE on a case-by-case basis, applying core sustainability principles of precaution, environmental protection and future global food security. At the time of writing, we were not aware of any cases that pass this test.

- Assess companies on a case-by-case basis and exclude companies involved in the uncontrolled release of genetically engineered organisms into the environment unless the benefits clearly outweigh the risks

[1] Synthesis Report IPCC, 2014, [2] Wikipedia Summary, 2015, [3] Stern Review: the economics of climate change, 2006, [4] Six years worth of current emissions would blow the carbon budget Carbon brief based on data from IPCC 2014, cited in Limits revisted: a review of the limits to growth debate, Tim Jackson, Robin, [5] United Nations Food and Agriculture Organization (FAO), 2015

Human rights

The term 'human rights' encompasses a number of issues ranging from civil and political rights, labour rights (see also labour standards criteria) and economic and social rights such as the right to housing or the right to education. The challenges that companies face in connection with human rights will therefore vary from company to company, sector to sector, and country to country. This diversity of human rights managerial challenges is most acute when companies operate in countries with weak governance, in other words, where governments are unable or unwilling to assume their responsibilities. If human rights issues are poorly managed by companies, then this can lead to litigation, extortion, sabotage, lost production, higher security costs and increased insurance premiums. In our view, companies operating in countries of concern have a responsibility to put in place appropriate human rights policies, systems and reporting.

- Assess companies on a case-by-case basis and encourage those that are operating in weak governance zones to demonstrate their commitment to the integration of human rights standards into business practices and to put in place appropriate human rights policies, systems and reporting
- Exclude companies judged not to be addressing serious allegations of violations of international human rights laws and standards including the Organisation for Economic Co-operation and Development (OECD) Guidelines for Multi-National Enterprises (2000) and the UN Global Compact (2000), among others

Infrastructure projects

Airport, road and dam building can play an important role in meeting people's needs through provision of essential infrastructure, job creation, and regional development. But these large-scale infrastructure projects can also be environmentally damaging and disruptive to local communities. Companies involved in large-scale infrastructure projects should adapt project designs to suit local environmental and community needs and undertake extensive stakeholder consultation to ensure that those adversely affected are properly compensated.

- Excludes companies that are directly involved in the construction of large dam projects in developing countries if those projects have not met best practice standards
- Will only invest in companies involved in the building of large scale infrastructure projects such as roads, airports or dams if they are viewed as leaders within their sector with respect to stakeholder dialogue, environmental management and social and environmental impact assessment

Intensive farming

Intensive farming practices raise serious animal welfare, health and hygiene concerns. Intensification of crop production has resulted in use of large quantities of pesticides and artificial fertilisers some of which can contain hazardous substances and impurities that adversely affect health and the environment.

- Excludes companies that derive >5% of turnover from intensive meat and fish farming
- Excludes companies that derive >5% of turnover from the manufacture of chemical pesticides
- Excludes companies that derive >5% of turnover from the fur trade

Labour standards

Individuals have a fundamental right to expect certain standards in their place of work. These labour standards are enshrined within international benchmarks such as the Universal Declaration of Human Rights (see also the human rights criteria) and the International Labour Office (ILO) Core Labour Standards.

- Assess companies on a case-by-case basis, and encourage those that are operating in weak governance zones to demonstrate their commitment to the integration of international labour standards into business practices by putting in place appropriate labour standards policies, systems and reporting
- Exclude companies judged not to be addressing serious allegations of breaches of labour standards such as those on child labour, forced labour, discrimination, union rights, working hours and health and safety
- The international laws and standards, which we refer to when making this assessment, include the conventions which are regarded and promoted by the ILO as "core" conventions. In summary these are: – Child labour – Equal opportunities – Forced labour – Freedom of association/Collective bargaining

Nuclear

The team takes the view that despite the benefits of nuclear power as a low carbon source of energy, it is not a viable alternative to other forms of energy generation because of the significant environmental risks and liabilities related to waste and decommissioning. Accidents or terrorist attacks on nuclear power stations also pose a serious risk.

- Excludes companies that derive >5% of turnover from owning or operating nuclear power stations, unless the company has made significant investment (>10% generation capacity) in renewable energy and does not have the option to divest its nuclear capacity [6]
- Excludes companies that derive >5% of turnover from uranium mining or reprocessing of nuclear fuel
- Excludes companies that derive >5% turnover from the development or manufacture of non-safety related products for nuclear power plants

[6] This can be due to regulatory constraints that require utilities to operate nuclear facilities, as is the case in Spain.

Ozone depleting substances
The depletion of the ozone layer continues to be a critical environmental issue with significant human health and biodiversity implications.

- Excludes companies that derive >5% of turnover from the manufacture or sale of ozone depleting substances

Pornography
The abusive and degrading portrayal of individuals in pornography contributes to sexual discrimination and exploitation of the vulnerable and can be a contributor to violence.

- Excludes companies that derive >5% of turnover from the production or distribution of pornographic material

- Excludes companies that derive >5% of turnover from owning or operating adult establishments

Tobacco
The team takes the view that tobacco is fundamentally in conflict with the concept of sustainable development because of the health impacts of smoking, the cost of treating individuals, and the effects of passive smoking.

- Excludes companies that derive >5% of turnover from the manufacture or sale of tobacco products

Weapons systems
The manufacture of armaments is in conflict with sustainable development. Arms can inflict death and injury and cause damage to natural and manmade capital. While we recognise and accept the need for armaments for defence and peacekeeping, their ability to be used for aggression and oppression renders them socially unacceptable.

- Excludes companies that are major producers of full weapons systems or critical components of weapon systems. Major producers are defined as having >5% of turnover and/or >£100m revenue from offensive weapons systems

- Excludes companies with confirmed involvement in the manufacture of anti-personnel mines or cluster munitions, or their critical components, as defined by the Ottawa Mine Ban Convention and the Oslo Convention on Cluster Munitions

Sustainable Equities team

Peter Michaelis, Simon Clements and Neil Brown are the lead managers of a team of experienced investment professionals. With over 45 years of combined experience, the team transferred to Liontrust from Alliance Trust Investments (ATI) in April 2017 and were previously running the running the Sustainable Future Fund range at Aviva Investors. Peter was previously Head of SRI at Aviva Investors and has been running the funds since their launch in 2001. Simon was previously Head of Global Equities at Aviva Investors. Neil was an SRI Fund Manager at Aviva Investors. Sustainable Future Fund range at Aviva Investors. Peter was previously Head of SRI at Aviva Investors and has been running the funds since their launch in 2001. Simon was previously Head of Global Equities at Aviva Investors. Neil was an SRI Fund Manager at Aviva Investors.

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