

ARRIVA PASSENGER SERVICES PENSION PLAN

TRUSTEE'S REPORT YEAR ENDED 5 APRIL 2020

Investment report (continued)

Engagement Policy Implementation Statement - DB Section

Introduction

This document sets out the actions undertaken by the Trustee, its service providers and investment managers, to implement the stewardship policy as set out in the Plan's Statement of Investment Principles ('SIP') and includes voting and engagement information that has been gathered from the managers.

The report covers activities over the period 6 April 2019 to 5 April 2020. Basalt, CBRE, Basalt shared information not directly relating to the specific period covering the Plan's financial year, and so we have used the information as has been provided.

The Plan's Stewardship Policy

The Trustee recognises the importance of its role as a steward of capital and the need to ensure the highest standards of governance and promotion of corporate responsibility in the underlying companies and assets in which the Plan invests, as this ultimately creates long-term financial value for the Plan and its beneficiaries.

The relevant extract of the SIP, covering the Plan's voting and engagement policies, is as follows:

As part of their delegated responsibilities, the Trustee expects the Plan's investment managers to:

- *where appropriate, engage with investee companies with the aim to enhance the long-term value of assets; and*
- *exercise the Trustee's voting rights in relation to the Plan's assets.*

The Trustee regularly reviews the continuing suitability of the appointed managers and takes advice from the investment adviser with regard to any changes. This advice includes consideration of broader stewardship matters and the exercise of voting rights by the appointed managers.

The Trustee reviews the stewardship activities of their asset managers on an annual basis, covering both engagement and voting actions. Where the Trustee identifies significant concerns relating to performance, strategy, risks, social and environmental impact, corporate governance, the capital structure or management of conflicts of interest, of an investment manager or other stakeholder; they will consider the methods by which they would monitor and engage with such an investment manager or other stakeholders.

In determining which "Significant" manager votes to disclose within this report, Pension and Lifetime Savings Association ('PLSA') guidance suggests focusing on a range of potential criteria including, but not limited to:

- impact on financial outcome;
- impact on stewardship outcome;
- size of holding;
- high profile (or controversial) nature of vote;
- potential conflicts of interest; and
- existing trustee policies and information.

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The Plan's Stewardship Policy (continued)

It is the Trustee's (and their advisor's) expectation that the managers will provide a more comprehensive range of voting examples for future reports. This will ensure that the Trustee has more opportunity to provide examples which closer align to their specific policies.

Through this report, the Trustee reviews how the actions of its investment managers have aligned with the expectations and principles set out in the SIP. The Trustee will set out where they expect more information or engagement to be undertaken by managers (where necessary).

Plan activities over the year

The Trustee took some de-risking action over Q3 and Q4 2019. The Trustee reduced the Plan's allocation to risk assets by making full redemptions from Schroder's Emerging Market Equities and Diversified Growth Fund, the Newton Real Return Fund and a partial redemption from the LGIM Developed Balanced Factor Equity Index Fund. The proceeds were invested in the Schroder's Liability Driven Investment mandate.

The SIP for the Plan was reviewed and updated on 18 September 2019 to take account of new regulations which came into effect on 1 October 2019. The regulations require the Trustee to include several policies relating to Responsible Investment and Stewardship. The Trustee expanded the SIP to set out:

- How it takes account of financially material considerations, including climate change, in selecting and retaining the Plan's investments over the appropriate time horizon for the Plan;
- How it takes account (if at all) of 'non-financial matters' in selecting and retaining the investments. This means the views of members, such as (but not limited to) ethical views, and views in relation to social & environmental impact and present & future quality of life of the members and beneficiaries;
- Its policies in relation to the stewardship of investments, including engagement, monitoring and exercising voting rights associated with investments; and
- Its policies in relation to the relationships it has with its asset managers.

Updates post year end

The SIP has since been reviewed and revised over the course of 2020 to take account of further regulatory changes. The Trustee has outlined its policies regarding how it incentivises asset managers to achieve their long-term objectives, their policies on cost transparency and their policies on voting & stewardship.

The most recent SIP, including the changes outlined here, was adopted on 30 September 2020, ahead of the 1 October 2020 deadline. The SIP can be found here: www.arrivapensions.com.

The Trustee has informed the managers of the importance of appropriately considering environmental, social and corporate governance ('ESG') factors with regards to the companies that they invest in. Similarly, the Trustee has made it known its expectation that asset managers should use their shareholder rights to influence and improve the companies they invest in, to generate better long-term financial outcomes.

The Plan's managers, present to the Trustee's Funding and Investment Committee (the 'FIC') on a rolling basis. The FIC receives performance reporting from their investment advisors and presentations from their managers and the FIC engages with managers on performance, strategy, risk, corporate governance and ESG practice where needed.

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Voting and engagement – Equity managers

Legal and General Investment Management ('LGIM')

Engagement & voting policy

Over the year, the Plan was invested in equity funds managed by Legal and General Investment Management.

The following voting policy and example relate to LGIM overall as a manager rather than the individual funds. Consistent with a number of other investment managers, LGIM are evolving their policies and have not yet provide information around their engagement policy and, crucially, how it relates to ESG.

LGIM use the Institutional Shareholder Services ('ISS') as a proxy advisor for voting on this fund. LGIM regularly monitor the proxy voting services through quarterly due diligence meetings to ensure execution is in line with their voting policy. LGIM receive an electronic alert for rejected votes which require further action. LGIM are audited annually and receive an assessment report on their voting activities.

LGIM are currently in the process of building a tool to collate specific engagement and voting data at a strategy level and will align this and their definition of a significant vote with PLSA guidelines. Weekly voting meetings are recorded and audited annually within the team, with all votes having a rationale behind them.

Examples of significant votes: Rio Tinto/BP

One example of LGIM voting against a shareholder proposal was in relation to Rio Tinto in 2019. The proposal was for Rio Tinto, a mining company, to set out a transition plan and publish Scope 1, 2, and 3 targets aligned with the Paris agreement. LGIM considered this resolution (for Scope 3 targets) to be too prescriptive under current technology limitations for the sector but has been pushing the company to tackle this through their engagement.

LGIM supported and was a co-filer in the shareholder proposal put forward by Climate Action 100+ for BP to publish a strategy consistent with the Paris Agreement, including capital expenditure and targets. This was supported by over 99% of shareholders at the company's AGM, and support from the board was achieved.

Voting and engagement – Diversified Growth Funds

Over the year, the Plan was invested in the Diversified Growth Funds with the following managers:

- Schroders; and
- Newton

Schroder's Diversified Growth Fund

Voting Policy

Schroders recognise their responsibility to make considered use of voting rights. The overriding principle governing their approach to voting is to act in line with their fiduciary responsibilities in what they deem to be the interests of their clients. Schroders normally hope to support company management; however, they will withhold support or oppose management if they believe that it is in the best interests of their clients to do so.

Schroders vote on a variety of resolutions issues; however, the majority of resolutions target specific corporate governance issues which are required under local stock exchange listing requirements, including but not limited to: approval of directors, accepting reports and accounts, approval of incentive plans, capital allocation, reorganisations and mergers.

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Schroder's Diversified Growth Fund (continued)

Schroders do vote on both shareholder and management resolutions. Their Corporate Governance specialists assess resolutions, applying their voting policy and guidelines (as outlined in this Environmental, Social and Governance Policy) to each agenda item. These specialists draw on external research, such as the Investment Association's Institutional Voting Information Services, the ISS, and public reporting.

As active owners, Schroders recognise their responsibility to make considered use of voting rights. It is therefore their policy to vote all shares at all meetings globally, except where there are restrictions that make it onerous or expensive to vote compared with the benefits of doing so (for example, share blocking practice whereby restrictions are placed on the trading of shares which are to be voted). In these cases, Schroders will generally not vote.

An example of this is in Australia for locally managed clients where SIMAL will not vote where Schroders are excluded from doing so by the Corporations Act or other laws, or in cases of conflicts of interest or duty which cannot be resolved lawfully or appropriately.

Schroders use a third-party service to process all proxy voting instructions electronically. They regularly review arrangements with these providers and benchmark them against peers.

Summary voting behaviour

	6 April 2019 – 5 April 2020
% resolutions voted	99%
% of resolutions voted against management	8%
% resolutions abstained	0.3%

Engagement Policy:

When engaging with companies their purpose is to either seek additional understanding or, where necessary, to seek change that will protect and enhance the value of investments for which Schroders are responsible. Their focus will be on issues material to the value of the company's shares or debt instruments.

These may include, but are not limited to, business strategy, performance, financing and capital allocation, management, acquisitions and disposals, internal controls, risk management, the membership and composition of governing bodies/ boards and committees, sustainability, governance, remuneration, climate change, environmental and social performance.

Schroders engagement activities combine the perspectives of their portfolio managers, fixed income and equity investment analysts and, where appropriate, ESG specialists in order to form a rounded and deep opinion of each company and the issues it faces. Intervention will generally begin with a process of enhancing their understanding of the company and helping the company to understand our position.

The extent to which Schroders would expect to effect change will depend on the specific situation, the amount that we own and where they sit in the capital structure.

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Schroder's Diversified Growth Fund (continued)

Schroders generally engage for one of three reasons:

1. To seek improvement in performance and processes in order to enhance and protect the value of our investments
2. To monitor developments in ESG practices, business strategy and financial performance within a company
3. To enhance our analysis of a company's risks and opportunities

Schroders prioritise engagement activities based on the materiality of the issue and the exposure to the individual company, which is based on the absolute amount invested or percentage owned on an instrument.

Newton Real Return Fund

Voting policy

All voting policies and procedures are formulated and approved by Newton's Responsible and Ethical Investment Oversight Group. Implementation of the voting policy and procedures involves the head of responsible investment and responsible investment analysis in collaboration with the global sector analyst and portfolio managers. Voting notifications are communicated to the responsible investment team by way of an electronics voting platform, allowing the review of all resolutions for contentious issues, aided by advice from proxy research service providers.

Newton employ a variety of research providers that aid them in the vote decision-making process. They use ISS for the purpose of administering proxy voting, as well as its research reports on individual company meetings. All voting decisions are made by Newton on a case-by-case basis and only in the event of a conflict of interest will they follow the voting recommendations from a service provider.

Summary voting behaviour

Over the year to 31 March 2020, Newton voted at 893 meetings, of which they voted against management recommendations on one or more resolutions around 42% of the time. More detail on Newton voting and engagement statistics can be found in their responsible investment quarterly reports. <https://www.newtonim.com/us-institutional/responsible-investment/responsible-investment-report-archive/>

Example of a significant vote: Apple

At Apple's AGM in February of 2020, Newton voted against the executive compensation arrangements and members of the compensation committee, with Newton's concern centred on the excessive portion of executives' long-term incentive awards that vest subject only to time served. Newton also supported a further shareholder resolution (which Apple management recommended voting against) where it was requested that the company report on the feasibility of integrating sustainability measures into the company's compensation arrangements. While Apple has a well-developed sustainability programme, Newton wanted to see executives held accountable and believed it would help enhance the company's approach.

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Newton Real Return Fund (continued)

Engagement policy

Active engagement with the companies Newton invests in allows them to monitor changes in management processes, remuneration and social and environmental issues. By taking a proactive approach to their engagement, Newton are able to work with the companies they invest in to increase the sustainability of their businesses over time. Newton also take an active role in the external ESG debate across the wider industry and help to shape policy and thought leadership.

Newton aim to identify ESG-related risks and opportunities to ensure that challenges are identified and managed. This applies not only to equities, but also in a fixed-income context. They also consider ESG issues when looking at sovereign risk, as well as across the credit spectrum from investment grade to high yield. Every security which their sector research analysts wish to recommend must have an in-depth ESG quality review completed by Newton's responsible investment team.

Voting and engagement – Property and infrastructure

Over the year, the Plan was invested in funds with the following Property and infrastructure managers:

- CBRE
- Innisfree
- Basalt

CBRE Global Investors Property

Voting & Engagement Policy

Prior to investing, Global Investment Partners ("GIP"), CBRE's business line which invests in other funds and with operating partners, actively ensures that the manager/local operating partner has the policies, systems and expertise needed to integrate environmental considerations into their investment decisions and ownership activities; that the manager/operating partner will not engage in socially irresponsible activities; that the operating partner's governance provisions meet best practice standards; and that reporting will meet GIP requirements for transparency.

Once invested in an indirect vehicle, CBRE's on-going role encompasses voting, monitoring how the manager/local operating partner is integrating ESG issues into their investment decisions and asset management along with engaging on specific ESG issues.

GIP will typically exclude investments where the major use of buildings acquired by the manager/local operating partner includes industries involved with armaments (manufacture or storage), nuclear or tobacco.

Basalt Infrastructure Partners II

Voting & Engagement Policy

Basalt Infrastructure Partners' Responsible Contractor Policy is designed to guide the selection of independent contractors who provide construction, repairs, maintenance and infrastructure operating services to assets and operating companies holding such assets.

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Basalt Infrastructure Partners II (continued)

The Policy seeks to ensure that the selection process for contractors will include among other things, a demonstrated ability to provide reliable and high quality services which may be evidenced by their compliance with applicable statutes and payment of fair compensation and benefits to employees, as well as by their relevant experience, reputation, dependability, and ability to provide cost-efficient services, thereby also enhancing the value of Basalt Infrastructure Partners' investments. In conjunction with the Policy, they will also seek to comply and adhere to the Principles of Responsible Investment of which they are signatory.

Innisfree PFI Secondary Fund 2

Voting & Engagement Policy

Innisfree Limited is an active manager of its long-term assets. ISF2's investment policy requires each asset to have a significant minority equity stake and board representation. Innisfree has at least two executives on the board of each asset and their presence is required for quorum. Innisfree's significant equity stakes mean that significant votes cannot pass without their approval. These same decisions typically require the approval of shareholders and the project's senior funders as specified in the project documentation. These documents often stipulate a certain course of action.

It is an investment policy requirement that Innisfree Funds take either a significant minority or majority holding in a project company and has board representation. These are not typically publicly listed companies. Innisfree's executives attend board meetings in their capacity as non-executive directors typically on a monthly or quarterly basis where they will actively exercise voting rights on the Fund's behalf to protect the interests of investors.

Innisfree manages four long term income funds including ISF2. The strategy for all four funds is almost identical with a degree of commonality of assets in addition. Therefore, there is an alignment between the Manager and the strategy for the fund. Engagement with investments and stakeholders is straightforward as ISF2 owns a significant minority interest in each investment with a board seat. Investment directors are present at each board meeting (which meet at a minimum quarterly) and meet regularly with their government client and main service providers. In addition, another Innisfree fund owns the management company HCP Social Infrastructure Limited which manages the majority of our assets.

Innisfree requires all its investee companies to have ESG policies in place, covering compliance with relevant laws and codes of practice together with support of energy efficient practices, plus policies covering several social and governance matters, e.g. health and safety, anti-bribery, anti-slavery. These project vehicles contract most of their obligations down to large construction and facilities management companies which will have sophisticated ESG policies in place. Most project vehicles do not have employees as they employ management companies like HCP Social Infrastructure Limited which provide the day-to-day managers and will have ESG and other policies in place covering those employees and compliance monitoring, among other things, but if they do have employees they will have appropriate policies to protect them.

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Conclusion

The Trustee considers that all the Plan's fund managers are exercising their respective voting and engagement abilities in a thoughtful, responsible manner and that the Trustee's stewardship policy is being appropriately implemented on their behalf to a large extent.

The Trustee recognises that it has a responsibility as an institutional investor to encourage and promote high standards of stewardship in relation to the assets that the Plan invests in.

The Trustee will continue to use its influence to drive positive behaviour and change among the managers they have employed to invest the assets of the Plan, and with other third parties that the Trustee relies on such as their investment advisor. The Trustee will set increasingly higher standards for these parties in future, and will monitor, assess and ultimately hold them to account to ensure that the assets of the Plan are appropriately invested.