REPORT TO: **SUPERANNUATION INVESTMENT SUB-COMMITTEE OF THE POLICY AND RESOURCES COMMITTEE - 23 MAY 2011**

REPORT ON: **SOCIALLY RESPONSIBLE INVESTMENT - SIX MONTHLY REPORT**

REPORT BY: **DIRECTOR OF FINANCE**

REPORT NO: **269-2011**

1 PURPOSE OF REPORT

This report reviews the progress by the Fund Managers regarding the positive engagement Policy on Environmental, Social and Corporate Governance approved by the Sub-Committee on 17 November 2008.

2 RECOMMENDATIONS

The Sub-Committee is asked to note the information contained within this report with regard to the activities of the Fund Managers during the six month period ended 31 March 2011.

3 BACKGROUND

On 17 November 2008 the Sub-Committee approved a revised Policy on Environmental, Social Governance. This policy recognises the over-riding fiduciary duties but encourages the managers to engage with companies. They are requested to summarise this engagement activity quarterly. The key areas continue to be Employee Care, Human Rights, Sustainability and the Environment.

4 ALLIANCE BERNSTEIN

Alliance Bernstein's latest activity is shown at Appendix 1.

5 BAILLIE GIFFORD

Appendix 2 shows a summary of recent engagement activity. Highlighting the wide range of topics covered and the diversity of companies approached.

6 FIDELITY

Various examples of issues considered in the last quarter are shown at Appendix 3,

7 OVERALL CONCLUSION

The managers have continued to develop their strategy in this area and link more closely with the long-term effect on share value.

The fund is still committed to following the United Nations Principles of Responsible Investment.

8 POLICY IMPLICATIONS

This Report has been screened for any policy implications in respect of Sustainability, Strategic Environmental Assessment, Anti-Poverty, Equality Impact Assessment and Risk Management.

The Fund's policy on Socially Responsible Investment requires its investment managers to engage with companies on Sustainability and the Environment and Employee Care and Human Rights.

9 CONSULTATION

The Chief Executive and Depute Chief Executive (Support Services) have been consulted in the preparation of this report.

10 BACKGROUND PAPERS

None

MARJORY STEWART
DIRECTOR OF FINANCE **12 MAY 2011**

Appendix 1

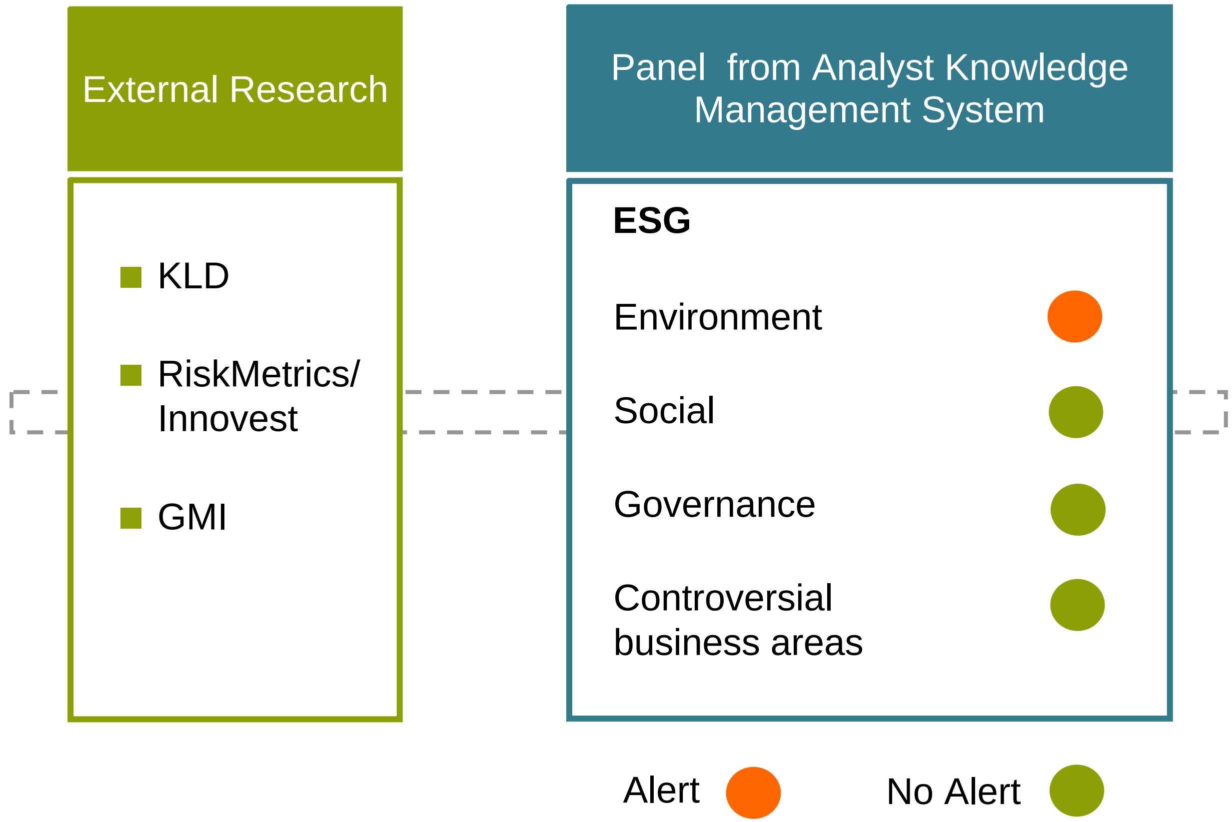
May 2011

Tayside Superannuation Fund—Global Diversified Value

AllianceBernstein

A More Systematic Way of Identifying Potentially Material ESG Issues

- We have added a new function to our equity analysts' knowledge management systems, which automatically alerts analysts to potential ESG issues
- Flagged ESG issues are addressed as an integral part of our research and stock selection process



ESG Examples: Some May be Material to Investment Performance

Environmental

- Environmental practices
- Sustainability
- Climate change/carbon emissions
- Use of water/land/energy
- Food safety

Social

- Human rights
- Labour standards
- Corruption
- Involves social stakeholders
  - Consumers
  - Suppliers
  - Community
  - Investors
  - Employees
  - Society

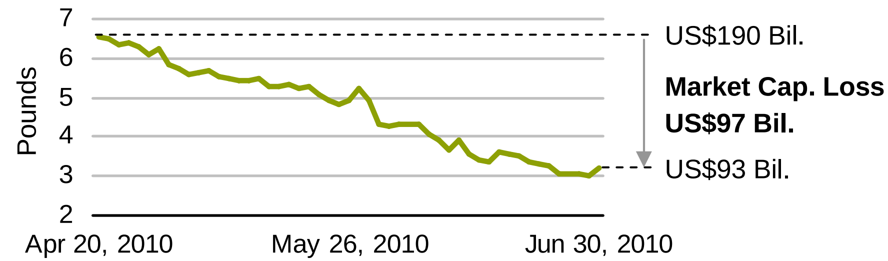
Governance

- Shareholder rights (Board, audit, voting rights)
- Executive compensation
- Corporate accountability and transparency
- Board accountability
- Financial disclosure and internal controls
- Social issues (e.g. workplace diversity)
- Environmental issues (e.g. reports on climate change)
- Political issues (e.g. political contributions, Sudan)

BP Oil Spill: Has the Market Overreacted to the Gulf of Mexico Disaster?

- Investors wiped $97 billion off BP's market capitalization in reaction to the oil spill
- We expect BP to suffer losses of about US$40 billion related to the spill. Many factors are still unknown and we are considering a range of potential outcomes
- When accounting for potential costs, BP shares trade at a substantial discount to the company's net asset value. BP's current market value is lower than the worst-case scenario, in which the company's US assets are completely written off

BP Share Price Since Oil Spill

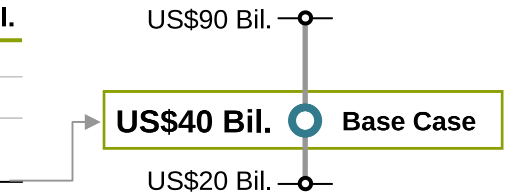


BP Projected Spill Costs: Simplified Scenario Analysis

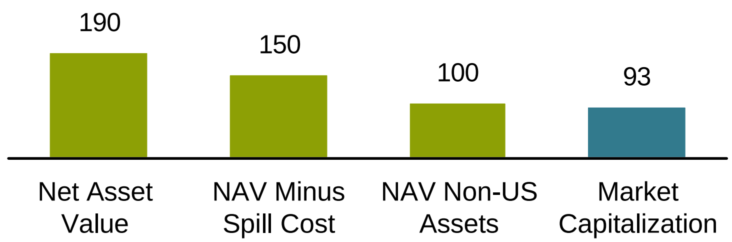
Base Case

	USD Bil.
Fine	8
Cleanup	12
Compensation	20
Total	**40**

Spill Costs: Range of Outcomes



Valuation Analysis* (USD Bil.)



Through June 30, 2010

*Net asset value is a discounted cash flow model, based on proven resources calculated on a field-by-field basis. Assumes oil prices at US$90 per barrel.

Source: Deepwater Horizon Response Unified Command; FactSet, National Oceanic and Atmospheric Association; Oil Pollution Act of 1990; States of Alabama, Florida, Louisiana and Mississippi; Wood Mackenzie; company reports; and Bernstein; see Disclosures and Important Information.

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Case Study: BHP Billiton's 2009 Fatality Rate

Situation

- BHP Billiton operations suffered 6 fatalities in 2009 financial year
- 5 in Iron Ore operations, 1 in Coal
- 4 were contractors

BHP Billiton responded quickly

- Informed market
- Reduced site access
- Limited excess working hours
- Enhanced traffic management standards

Our View on Incidents Led to Multiple Actions

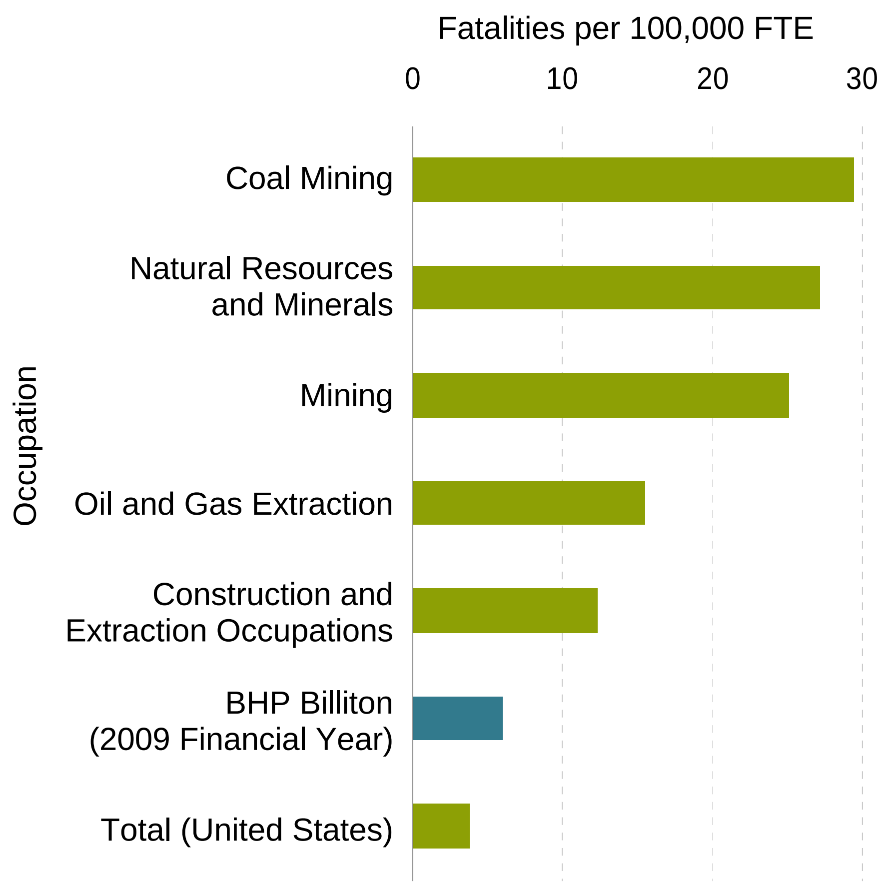
Our View

- Safety is one of the most important responsibilities of companies
- Safety statistics are a powerful indicator of operational control
- BHP Billiton's record is a concern, but it is not an outlier

Actions

- Multiple discussions with management
- Reduced 2009 iron ore production estimate by 5mt (USD250m EBIT effect)

Industrial Fatality Rates



As of December 31, 2007
Source: US Bureau of Labor Statistics and Bernstein Analysis

ESG Examples: Some May be Material to Investment Performance

Environmental	Social	Governance

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Well-Established Proxy Voting Policy and Structures Enable Us to Address Governance Controversies

E S G

Summary Statement of Policies and Procedures

- Public statement of proxy voting procedures and policies on key issues
- Update annually to reflect new issues and changed circumstances

Proxy Voting Manual

- More detailed set of guidelines and policies on how to vote on common issues (for, against or case-by-case)
- Updated annually to reflect new issues and changed circumstances

Proxy Voting Committees

- Provide formal oversight, update proxy policies and procedures and make final decisions for particularly difficult votes
- Heads of Value and Growth are proxy committee members

Conflicts of Interest

- Clear procedures to avoid conflicts of interest

Company	Engagement Report
Brambles Limited	Brambles' main business is Chep which is the world's largest pallet pool provider, with operations in the US, Canada, Latin America, Europe, Australia and South Africa. We had a meeting with the Chair of the Remuneration Committee who talked us through the remuneration strategy review. The initial outcome of this review was to make a few minor amendments to policy, which would bring Brambles into line with Australian remuneration best practice. We are supportive of their initial suggestions and look forward to receiving the final proposals later this year.
Gazprom	Gazprom, which is majority owned by the Russian Government, is the largest producer of natural gas in the world and currently supplies around a quarter of Western Europe's gas demand while continuing to dominate the domestic market. We had a conference call with Mr Valery Musin, their only independent non-executive director, to update us on the agenda items discussed at the board meeting which had been held earlier that day. Directors at Russian companies are elected via cumulative voting. This entitles shareholders to concentrate all of their votes and cast them for a single candidate, as we have done previously for Mr Musin, since we believe him to be the only truly independent non-executive director on the board. We fully support the election of independent directors, as their role is to provide a strong voice to represent, support and protect minority shareholders rights. It is significant and highly unusual that minority shareholders are able to hear about the discussions that have taken place at board meetings and to engage directly with an independent director of a Russian company. This was our first conference call with Mr Musin, and we found the call to be valuable and informative. We look forward to future conference calls and will use the opportunity to discuss this Russian gas company's corporate governance and its health & safety issues in more detail.
Petrobras	We followed up our conference call in Q2 2010 with a call to the management responsible for ensuring environmental, health and safety (EHS) policies are adhered to. This included speaking to the Head of Corporate Sustainability. Petrobras is a company we have described in the past as taking their EHS performance seriously and this has not changed. However, its importance continues to increase as projects in Brazil, its home market, become more complex; 600km pipelines through the Amazon and drilling 7000m wells are not without local community, employee, environmental and technical risk. Petrobras has developed an extensive knowledge of ultra deepwater offshore drilling technology and is conscious of the extreme nature of its projects. It is also aware of its responsibilities as a majority state-owned oil & gas exploration & production company. However, as Petrobras remains a company that is operating in a high impact sector with significant EHS risks, we will continue to review the company as it evolves in this complex operating environment.
Vale	We had a conference call with Vale. It is the largest iron ore mining company in the world, with operations in the logistic, steelmaking and energy sectors. We spoke to the General Manager of Sustainable Development. Vale has a complete and integrated environmental strategy but the recent acquisition of a 70% stake in a palm oil company and the Serra Sul Mine in Brazil's Amazon region, a national preservation area, has attracted some criticism from international environmental groups. The company is aware of the environmental and community risks associated with palm oil production, and all areas used to grow palm trees have been mapped and classified by the federal government as degraded areas. This is positive as it reassures us that, among other risks, deforestation is not a current concern. The palm oil bio-fuel will be used to replace 20 percent of diesel consumption in the company's northern operations, and this should have a positive impact on its hydrocarbon fuel consumption. The environmental licence for the Serra Sul Mine has not yet been granted; the assessment process is still in progress but, since the first technical survey, there have been alterations to the operational procedures including changing the mining techniques used, to reduce the use of trucks and use a less water-intensive process. We will monitor the situation to ensure we stay up-to-date with the company's progress towards being granted the environmental licence.

Company	Engagement Report
BHP Billiton (UK)	We met the Chairman to discuss recent changes to the board, follow up on our letter to him last year regarding our concerns at the high level of transaction and M&A advisory fees paid for the failed Potash Corp deal, and to hear the board's views on the mining and carbon taxes in Australia and their impact on the business. Two non-executive directors (NED), including the chairman of the audit committee, will leave the board in 2011. New NED appointments include Lindsay Maxsted, former Chief Executive at KPMG; Baroness (Shriti) Vadera of Holland Park, who is a Labour peer, NED at AstraZeneca, and adviser to the governments of Dubai and Korea; and Carolyn Hewson, chairman of the audit committee at Westpac Banking, who has a background in corporate restructuring and risk management. The Chairman has spent a lot of time considering the composition of the board, with the plan to look out five years when considering the skills and experience of the members. For example, there will be gaps in the oil and gas experience on the board when John Buchanan (formerly at BP) and John Schubert leave in 2012. With regard to the high level of transaction and M&A advisory fees, we reiterated our concerns and encouraged the board to look carefully at these in future, paying particular attention to value for money for our clients. The Chairman acknowledged that the legal and financing fees were high but explained that the scale of the Potash Corp deal was unprecedented: few banks were able to provide this level of capital funding and, since the deal would have been very earnings accretive for shareholders, the board felt that the fees were justified. Nevertheless, the Chairman understood our concerns and appeared to recognise that as a large company, the board should at least endeavour to use its influence and seek better terms from the investment banks in future.
Johnson Matthey	Johnson Matthey is one of the world's largest suppliers of environmental catalysts, used in the manufacture of autos and in a number of other industrial processes. We met the Chairman designate, Tim Stevenson (TS), to discuss forthcoming board changes, board diversity and board evaluation, and to get his perspective on the company as a new member of the board. Within the next six months, three independent non-executive directors (NED) will retire including the current Chairman, Sir John Banham. Alan Ferguson, former CFO at Lonmin, is a new NED appointment and will take over as Chair of the audit committee. As Johnson Matthey is a company which operates in 30 countries and generates most of its profits outside the UK, TS acknowledges the benefits of increasing board diversity by appointing, for example, a Chinese or Indian board member. In the next few months, he plans to organise an external board evaluation which will look at all aspects of the board's performance and experience. We are encouraged that there will be continued focus on improving the NEDs' understanding of the business and developing relationships with executives by holding board meetings at various operational sites away from the company's headquarters. We look forward to future discussions with the Chairman regarding the outcome of the board evaluation.
Royal Dutch Shell	We met the Remuneration Committee (Remco) Chairman to discuss the company's remuneration policy for 2011. Following the voting down of the remuneration report at the AGM in May 2009, and shareholders' concerns that executive directors could be entitled under Dutch laws to substantial payoffs upon resignation, the Remco has conducted a full review of service contracts. Contracts for future executive appointments will cap damages for loss of employment at one times bonus and salary, which is more in line with best practice. The Remco has also introduced new contracts seeking to limit payoffs for current directors. We welcome this development. We also discussed the company's removal from the Dow Jones Sustainability Index (DJSI). A proportion of executive remuneration is based on its inclusion in the DJSI, therefore the Remco acknowledged there would be no payout for 2010. The Remco disagrees with the DJSI's rating system and suspects that the DJSI has increased its focus on the company's activities in Nigeria because of the heightened sensitivity re oil spills following the Gulf of Mexico disaster. However, importantly, it appears to have overlooked Shell's overall improved safety and environmental performance. The Remco has therefore decided that for 2011 it will focus on its own safety and environmental performance metrics and will only refer to the DJSI in passing. We will continue to monitor the company's safety and environmental performance.

Company	Engagement Report
Unilever	We met the Anglo-Dutch consumer group Unilever's Investor Relations and its SRI Engagement Manager to discuss the company's strategy regarding nutrition concerns and responsible marketing. These issues are rising up the media, political and consumer agenda and it is therefore important that companies with exposure to the sector proactively respond to the risks and opportunities. On the face of it, Unilever appears aware of the risks and opportunities associated with food; nutrition, health claims, actual health benefits and marketing, and the balance between them all. It has proactively implemented a programme to improve its portfolio's nutritive quality and has voluntarily censored advertising to children. The company aims to double the proportion of its products meeting internationally accepted nutrition guidelines by 2020 (44% at the end of 2009); a challenging objective which should be achieved by implementing higher nutrition standards in emerging markets as well as the developed world. To achieve the target will require reformulation and innovation of products, as well as some reorientation on the product portfolio. The company seems to have a sensible and pragmatic approach to its product development processes, responsible marketing and nutrition challenges. Raising consumers' awareness has given real pricing power to companies able to develop complex food products with health value added. We will continue to monitor Unilever's progress towards its targets which are important in order to cope with the global regulatory environment.

Appendix Environmental, Social & Gov ("ESG") Overview - Q1 2011

FIL has a well established approach to responsible investment which is integral to the research process. FIL's integrated approach incorporates environmental, social, and governance ("ESG") issues into its investment process when ESG related issues may have a material impact on either investment risk or return. This role is facilitated by our Head of ESG, who acts as a focal point within FIL globally for environmental, social, and governance related activities. The Head of ESG will work within the framework as outlined in our Principles of Ownership:

> FIL believes that high standards of corporate responsibility will generally make good business sense and have the potential to protect and enhance investment returns. Consequently, our investment process takes environmental, social, and governance ("ESG") issues into account when, in our view, these have a material impact on either investment risk or return. ESG best practice should be encouraged provided they enhance long term financial return.
>
> We do not screen out companies from our investment universe purely on the grounds of poor ESG performance but rather adopt a positive engagement approach whereby we discuss these issues with the management of the companies in which we invest or consider investing on behalf of our clients. We use the information gathered during these meetings both to inform our investment decisions and also to encourage company management to improve procedures and policies. We strongly believe that this is the most effective way to improve the attitude of business towards corporate responsibility.

As stated above, FIL incorporates ESG into its investment process when ESG related issues may have a material impact on either investment risk or return. Examples of such risks or opportunity could include physical threats (severe weather), security of supply (geopolitical risk of oil supply), the impact of regulation (the carbon market, energy efficiency alternatives etc...), cost implications (cost of environmental improvements), or impacts to brand equity (reputational risks, supply chain concerns, etc...).

Below are highlights of potential issues, dialogue and company engagement noted by our investment teams in the last quarter.

Physical Threats (Japanese earthquake & tsunami)

Following the earthquake and tsunami on 11th March, the Fukushima nuclear power station faced a loss of cooling, overheating of fuel pools, and contamination of ground, air and water resources. The size and duration of the accident is unprecedented, and at the time of this report is still ongoing. While we are still in the early days, this incident has impacted not only the energy industry, but other industries through their supply chain.

FIL analysts are globally reviewing the impact of the earthquake and tsunami on their respective sectors. Below are highlights of the investment analyst's team ongoing assessment of this incident:

Regulatory & safety considerations:
Most countries operating nuclear plants have already announced that they will conduct a full review of nuclear safety and development plans. Regulatory reviews could focus on safety standards of existing plants (inclusive of back-up systems and crisis management procedures), review of reactor age and sensitivity to seismic activity. Nuclear operators will need to make decisions on a case-by-case basis in regards to potential plant closures, and retrofitting and reconfiguration to comply with new safety standards.

The above regulatory & safety considerations will also impact new nuclear.

Utilities and energy:
Reconfiguration of the energy mix as a result of increased nuclear power costs will also affect gas, coal and renewable energy producers.

Supply chain:
The Fukushima incident has multiple effects on the supply chain from purchasing, manufacturing, warehousing, transportation and production. FIL analysts are actively reviewing the impact to the supply chain in all sectors. Samples of research written include in-depth analysis of the automotive and logistics sectors, technology, healthcare, insurance, chemicals and resources.

Security of Supply (oil security)

During the quarter, FIL's energy analysts examined how unrest across the Middle East and North Africa impacts the global oil supply. Further analysis looked at how different oil price scenarios would impact the Integraged Oil Companies, E&Ps, Refiners and Oil and Gas Service companies.

The Impact of Regulation

Product Packaging (Tobacco)

On 7th April the Australian government unveiled new laws for plain packaging of tobacco products to be implemented in 2012. The proposed change was widely expected and would increase health warnings on packs from 30% to 75% of space on the front and 90% on the back. All brands / imagery would be removed and all packets would be produced in olive green. In addition to the legislation in Australia, the UK is currently consulting on the issue and other countries such as New Zealand and Canada have considered similar policies. Tobacco companies have publicly stated that they will fight this in the courts on intellectual property grounds.

FIL analysts have been examining the impact of product packaging regulations on an on-going basis.

Carbon Emission Reductions & Fuel Mix

The EU Emissions Trading Scheme (ETS) was approved in 2008. The ETS limits the carbon dioxide (CO2) emissions of certain industries and requires companies seeking to emit above those limits to purchase the requisite amount of credits/allowances, creating a secondary market. We continue to monitor how EU limitations on emissions under the ETS affect companies in which we invest. In our view, companies that can reduce their direct and indirect CO2 emissions are potentially at a competitive advantage in markets where there are limits on carbon emissions.

As part of the future energy landscape of the UK, the Department of Energy & Climate Change published its Consultation document on Energy Market Reform in mid-December. This document aims to provide a framework for how the UK will ensure sufficient inward investment in energy supply, decarbonise its energy generation, generate a decent return for shareholders and deliver reasonable energy prices for consumers.

In previous papers we've outlined our utilities analysts' examination of key proposals such as the introduction of a carbon floor price in the UK, a contract for differences based on Feed in Tariff for renewables, capacity payments to support backup generation, and the introduction of emission performance standards.

During the quarter, the UK government introduced a carbon floor tax. This was one of the measures outlined in the Energy Market Reform document published last December. The EMR is due to be published as a White Paper (having just completed the consultation stage), before moving through the remainder of the legislative process during the year.

The UK carbon floor tax will act as a supplement to the existing CO2 price, which is set by the Emissions Trading Scheme, as administered by the EU (the carbon floor price in the UK is at a premium to the EU ETS price).

The UK floor price for carbon will be introduced on 1st April 2013. The budget statement specified that the carbon price floor would start at £16 per tonne of carbon dioxide, increasing to £30 per tonne linearly to 2020. However, the actual floor price set is higher, as the £16 and £30 numbers are quoted in 2009 prices and will be inflated upwards. In nominal terms, assuming ~2% inflation, the 2013 support level is £19.18/ tonne, rising to £41.3/ tonne in 2020.

Assuming that the additional tax burden for the marginal plant is passed through into the wholesale price then the tax change should be positive for low carbon generation such as renewables and nuclear, neutral for gas and negative for coal.

An example of a company continually examined in response to changes in CO2 regulation and renewable incentives is **Drax**, currently a coal-fired power generator although awaiting the conclusion of government discussions concerning biomass and coal co-firing in the hope of becoming the UK's largest biomass co-firing plant.

Renewable Energy - Solar & Wind Use

The EU Commission has established a broad set of energy targets as part of its "20-20-20" goals. The purpose of the goals is to reduce the EU's greenhouse gas emissions by 20% compared to 1990 levels and to increase the use of renewable energy sources in overall energy consumption by 20% by 2020. To meet these targets, EU Member States have been working towards improving their energy mix and increasing their energy efficiency through various measures and regulation specific to each country.

Following the nuclear disaster in Japan there has been a significant shift in public sentiment towards renewables. Policy makers in Europe, particularly Germany, as well as those in China are in the process of re-assessing their nuclear programmes. Although it is hard to quantify what the exact regulatory outcome may be for renewables there can be little doubt that public sentiment, at least in the short term, has been very favourable and heightened public discussions. The recent victory by the Greens (German: Die Gruenen) in Baden-Wuerttemberg, Germany, are the clearest demonstration of this given that this is the first time in 58 years the incumbent CDU has not been in power.

The impact of recent events is significant and during the quarter the Fidelity's renewables analyst examined the implications of potential policy shift for both wind and solar companies within Europe and globally. In terms of wind, the position of the key turbine manufacturers (**Vestas Wind Systems, Gamesa Corporation,** and **Nordex SE**) was re-examined. For solar, our analyst assessed the potential implications of a softening regulatory environment in Europe where discussions are currently ongoing in Germany and Italy, in particular.

Cost Implications

Industry requires energy and typically generates waste which requires treatment or disposal. Such waste can be hazardous and potentially result in environmental degradation and increased cost to businesses through increased regulation. As part of our ongoing assessment of **Norilsk Nickel**, our natural resources analyst examined the cost implications of environmental improvements and capital expenditures on operations in the company's Polar Division.

Brand Equity & Reputational Risks

Negative perceptions of a Company's product supply chain can affect sales and brand equity; retailers are particularly exposed to such risks. First, companies that fail to screen suppliers adequately may unknowingly encourage dangerous and/or repressive working conditions. Second, if retailers lack appropriate controls over their supply chain (for example, due to lack of Company presence in the sourcing countries), they may be exposed to product safety risks, which could lead to product recalls, fines or lawsuits. Finally, as consumers become more sensitive to the overall sustainability and ethics of supply chains, companies that do not take account of these issues may face reputational risks.

Health & Safety

A safe and healthy workplace contributes to a company's operational efficiency. Companies with poor health and safety policies & records may face prosecution, fines and potential withdrawal of their licence to operate in certain markets. As part of our ongoing assessment of health and safety practices, our oil and gas analysts continue to examine practices at companies such as **BP Plc.**