



A COLLABORATION BETWEEN  
FIRST-FOURTH AP-FUNDS



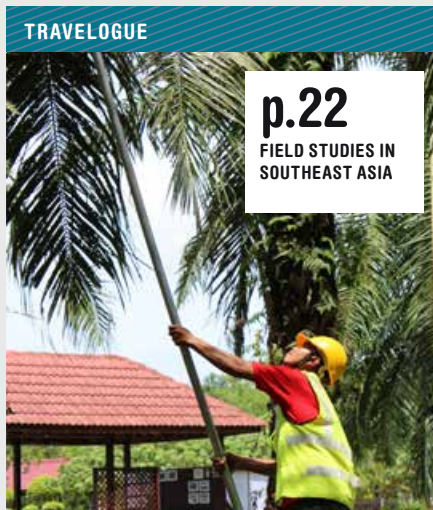
# COOPERATION AND ACTIVE ENGAGEMENT

SWEDISH NATIONAL AP FUNDS  
ETHICAL COUNCIL  
ANNUAL REPORT 2014

 **ethical council**

A COLLABORATION BETWEEN  
FIRST-FOURTH AP-FUNDS

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ETHICAL COUNCIL ANNUAL REPORT  
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# THE YEAR AT A GLANCE

The Ethical Council carried on both preventive and reactive dialogues in 2014 about human rights, anti-corruption, the environment and other sustainability issues with more than 300 global companies that do business in various industries.

## 2014

### MORE THAN 300 COMPANIES

The Ethical Council conducted preventive and reactive dialogues with 308 companies around the world. A particular dialogue frequently addressed more than one area of sustainable development.

### COLLABORATION AND PREVENTIVE INITIATIVES

Preventive initiatives, often in collaboration with other international investors, are integral to the Ethical Council's commitment to persuade companies to assume greater social responsibility. Among the companies that the Council dialogued with in 2014 were the palm oil and cocoa industries.

### RECOMMENDING DIVESTMENT

On the recommendation of the Ethical Council, the AP Funds divested two companies in 2014: Barrick Gold and Agrium. International conventions—including those that concern biological diversity—link the Council to Barrick Gold, which discharges mine wastes directly into river systems. Agrium trades in phosphates from Moroccan-occupied Western Sahara without demonstrating that the local population stands to benefit. The Council recommended in early 2015 that the AP Funds divest Motorola Solutions, which sells surveillance equipment to West Bank settlements in violation of international law. The Ethical Council does not believe that further dialogue with any of the above companies would serve a useful purpose.

### EDUCATIONAL SEMINAR

The Ethical Council arranged a seminar in autumn 2014 to raise awareness Swedish companies about the UN Guiding (Ruggie) Principles on Business and Human Rights.

### ANNUAL REPORTING

The Ethical Council's annual report and [www.ethicalcouncil.com](http://www.ethicalcouncil.com), as well as the corporate governance and annual reports of the AP Funds, all describe the joint sustainability effort.

## COMMITMENT

### COMMITMENT BY AREA OF SUSTAINABLE DEVELOPMENT

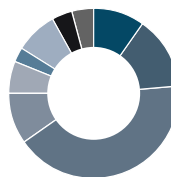
TOTAL 859



- Anti-corruption **16%**
- Labor rights, health and safety **15%**
- Environment **15%**
- Human rights **25%**
- Overall sustainability strategy **12%**
- Special weapons **8%**
- Business ethics **8%**

### COMMITMENT BY INDUSTRY

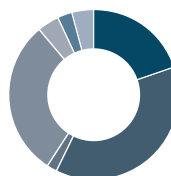
308 COMPANIES



- Energy **10%**
- Consumer products **14%**
- Commodities **42%**
- Industrials **10%**
- IT/Telecom **6%**
- Tobacco **3%**
- Financial **8%**
- Pharmaceutical **4%**
- Miscellaneous **4%**

### COMMITMENT BY REGION

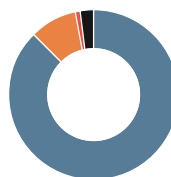
DOMICILE, 308 COMPANIES



- Asia **20%**
- Europe **38%**
- Central and South America **2%**
- North America **30%**
- Oceania **4%**
- Africa **3%**
- Middle East **4%**

### STATUS OF 2014 DIALOGUES AT YEAR-END

308 COMPANIES (SEE COLOUR SCHEME ON PAGE 8)



- Blue **218**
- Orange **76**
- Red **1**
- Black **13**

# A WORD FROM THE CHAIRMAN

Shareholders and other interested parties alike are increasingly convinced that the working methods employed by the Ethical Council over the past eight years for the purpose of encouraging companies to adopt improvements and commit themselves to resolving various problems yield the best long-term results. Companies cannot grow and perform well over the long term from either an operational or profitability point of view without integrating sustainability concerns into their day-by-day activities.



Arne Lööw  
Chairman, 2014

## ACTIVE ENGAGEMENT

Regular monitoring of corporate ethical, environmental and related sustainability efforts is in the DNA of the Ethical Council and AP Funds.

There is more than one way to demonstrate active engagement. The work of the Council is based on dialogue with companies to help prevent problems from arising and correct those that have already manifested. While it may seem obvious that we should contact companies directly to obtain additional information or express our views on various business activities, not all interest groups and stakeholders have accepted such a model at this point. Be that as it may, the Ethical Council and AP Funds feel that companies are the natural place to start when we have something to say about the way they do business. Most active owners and interest groups that want to make a real impact take that kind of approach. Our common objective is for companies to operate in a responsible manner and generate a satisfactory return on our investments under long-term sustainable conditions.

## ENGAGEMENT MAKES THE DIFFERENCE

The project that the Ethical Council has conducted in collaboration with the Seventh AP Fund and PGM, a Netherlands pension manager, illustrates the power of engagement to achieve real progress. Mining activities often have a heavy impact on human rights, health and

safety, corruption risks and the environment. Adopting effective internal corporate processes and routines for confronting such challenges to sustainable development is of the essence. The Ethical Council has dialogued with the mining industry for many years. A project that was launched in 2011 has involved some 30 mining companies focuses on a number of sustainability issues. To identify the strengths and vulnerabilities of the companies, we based an analysis of their strategies and policies on the ten sustainability principles of the International Council on Mining and Metals (ICMM). We performed a follow-up analysis in 2014. The results were gratifying. Unmistakable improvements emerged for each of the ten principles, most notably the key areas of biodiversity, contributions to social and economic development, and health and safety. Once again, engagement turned out to be the name of the game.

The palm oil industry faces major challenges as well. The Ethical Council is engaged in a PRI project with other investors to urge compliance with the production and consumption standard of the Roundtable on Sustainable Palm Oil (RSPO). Companies are increasingly following the standard, as well as incorporating timetables for traceability into their corporate policies. Verifying that palm oil has been harvested at plantations that abide by RSPO principles is vital to the project. Engagement is the key that has unlocked the door this time too.

## CLEAR DEMANDS

Despite its unwavering determination, the Ethical Council does not always accomplish what it sets out to do. We recommended during the year that the AP Funds divest Barrick Gold, a Canadian company, due to the way it disposes of its mine wastes in Papua Nya Guinea. The company's riverine tailings disposal system discharges the waste directly into waterways. Only Indonesia and Papua Nya Guinea permit the controversial method. The Council demanded that Barrick Gold adopt a policy prohibiting use of the method as part of future projects. Nevertheless, the company clearly stated that it had no intention of waiving the option of employing the disposal system. The Ethical Council recommended divestment of Freeport McMoRan in 2013 for the same reason.

Further on, The Ethical Council has also recommended divestment of Agrium, a Canadian company that signed a contract in 2014 to buy phosphates from Moroccan-occupied Western Sahara.

In collaboration with other investors, the Council informed the company that it had been unable to show that the business was consistent with the interests and wishes of the local population. But all attempts to address the problem fell on deaf ears. Finally the Council recommended divestment of Agrium.

The Council conducted a dialogue with Motorola Solutions concerning its sales of surveillance equipment to West Bank settlements. The objective was for the company to close the business and overhaul its human rights policies. Because the company did not exhibit any desire to move forward with the dialogue, the Council recommended divestment in early 2015.

#### **WHAT CAN REASONABLY BE EXPECTED OF THE ETHICAL COUNCIL?**

The Ethical Council and AP Funds receive frequent comments about the job they are doing. We are pleased that both individuals and organisations that care deeply about ethical and environmental issues make their voices heard. The attention that they draw to such vital matters is an invaluable source of the information that we need. Like other active shareholders, however, the Council cannot plunge into every area of concern, no matter how deserving. We are selective and confine ourselves to problems for which we can make a difference by exerting our influence, usually in collaboration with other shareholders. The most important thing is to take action. As Bill Clinton said at a recent investor conference with sustainability focus, “You cannot do everything, but you cannot choose to do nothing!”

#### **THE WORLD IS WATCHING US**

The Ethical Council’s model of modifying corporate behaviour by means of direct communication is increasingly popular in other countries as well. Both the Ethical Council and the AP Funds have attracted attention around the world. We are invited to speak and participate in various dialogues, collaborative efforts and conferences.

We as shareholders were represented at the United Nations Climate Change Conference that Secretary-General Ban Ki-Moon convened in New York last September. We were pleased that a number of collaborative projects among governments, companies and shareholders were presented at the conference – concrete evidence that targeted initiatives are much more widespread than they once were. Among the projects

were cooperative ventures of governments and companies to reduce destruction of rainforests and look to the future by replanting them – a vital ingredient of the attempt to preserve biodiversity. The conference also served as a venue for the announcement of several initiatives aimed at reducing greenhouse gas emissions. Investors were urged to calculate the total emissions released by the companies in which they had interests in order to gain a more reliable overview, as well as to monitor the impact of various corrective measures going forward.

**“UNMISTAKABLE  
IMPROVEMENTS  
EMERGED FOR  
EACH OF THE TEN  
PRINCIPLES”**

#### **PRI – A STEP IN THE RIGHT DIRECTION**

The AP Funds and the Ethical Council are active members in the UN Principles for Responsible Investment (PRI) initiative.<sup>1</sup> The Secretary-General of the Ethical Council is the chairman of the task force for PRI Clearinghouse, a digital platform for investors to work together on various projects.

With the new chairmanship of PRI, the effort progressed well during the year. Internal control and government was thoroughly reviewed, management communicated more readily with individual members, and current events were discussed with greater seriousness than ever before. The Council is looking forward to building on the constructive dialogue that it has developed with the initiative.

#### **CONCLUDING REMARKS**

My year as Chairman of the Ethical Council has demanded a great deal of effort, but it has also been incredibly stimulating and rewarding. Investments cannot yield an optimum long-term return unless they are managed with sustainability concerns in mind. It is very rewarding every time a project of the Ethical Council produces measurable results. The corporate world is amenable to thinking and behaving in a more long-term, sustainable manner. I am proud to turn the chairmanship over to the First AP Fund, which will be serving in that capacity this year for the third time.

Stockholm, January 2015

**ARNE LÖÖW**

<sup>1</sup> The First, Second, Third and Fourth AP Funds are all signatories.

# MORE EFFICIENT COLLABORATION BY TAKING ADVANTAGE OF PRI POTENTIAL

**The Ethical Council initiatives are based on collaboration among the AP Funds on dialogues with companies abroad. Institutional investors normally hold small interests in a number of different companies around the world. Such dialogues are resource-intensive at a time when everyone in the financial industry is out to cut costs. In the view of John Howchin, Secretary-General of the Ethical Council and Chairman of the steering committee for the PRI cooperative platform, the logical solution is to streamline collaboration.**

Almost 15 years have passed since the AP Funds assumed the responsibility of considering ethical and environmental principles without compromising the overall objective of obtaining a high return on their investments. The AP Funds quickly focused on devising strategies for employing dialogue and persuasion instead of blacklisting. The concept was to avoid resorting to divestment by addressing problems head on and doing everything in their power to work with companies in an attempt to resolve them amicably.

After having pursued separate initiatives for the first few years, the AP Funds set up the Ethical Council in 2007 to pool their resources and exert greater pressure, given that they often found themselves talking to the same companies. A coordinated effort generated synergies and avoided overlap.

Around the same time the UN launched its Principles for Responsible Investment (PRI) initiative, which also emphasised the importance of collaboration among institutional shareholders. The initiative included an online Clearinghouse to facilitate cooperation and pooling of resources. The initial users were the AP Funds and other investors that had grown accustomed to collaboration and were looking for a way to jointly identify companies and industries with which they could dialogue effectively. The Clearinghouse currently has a dozen projects on its plate and a couple hundred of PRI's 1,400 members have collaborated in one form or another.

The question I ask myself, however, is whether even more can be accomplished. The initiative has attracted members from virtually every corner of the globe that are heavily invested in their domestic markets. Essentially every company in the world is represented. The AP Funds are typical in that a disproportionate percentage of their holdings are in Swedish companies. In the experience of the Ethical Council, investors are generally in a much better position to effectively resolve ethical and sustainability issues with domestic companies by virtue

of smoother and established communication channels. The Ethical Council has established networks throughout the years for collaboration with many other investors on a number of issues. PRI could serve as an excellent springboard for expanding that effort.

Under the Ethical Council's chairmanship, the PRI steering committee has discussed structures and technical approaches to more effectively sharing knowledge and familiarity with the domestic markets of the various members. The PRI also embarked on a major project in 2014 to design the technical infrastructure for a social network of investors. The first version is set to be launched in 2015. The basic idea is to make it even easier for PRI members to contact each other and get the ball rolling on joint initiatives. Technological sophistication is certainly a useful tool but hardly a panacea.

Effective cooperation requires a common understanding between investors. Identifying possible partners is no easy task, given that investors vary in terms of their assumptions, objectives and expectations. Past ventures, as well as level of awareness about what individuals investors want and realistically hope to achieve by means of ethical and sustainability efforts, largely determine their ability to work together. In the experience of the Council, various constellations of investors with similar goals emerge, after which they cooperate with each other to exert greater influence and share their tasks. The companies they get in touch with benefit from the opportunity to hear views that are more representative of the investor community as a whole and to spare resources by receiving and responding to questions from a single source. Time will tell, but the new social network holds out the promise of being a useful tool for PRI, its members and corporates.

**“EFFECTIVE COOPERATION REQUIRES A COMMON UNDERSTANDING BETWEEN INVESTORS”**

**JOHN HOWCHIN**  
Secretary-General of the Ethical Council

# THE ETHICAL COUNCIL OF THE AP FUNDS IN BRIEF

Ever since 2007, the First, Second, Third and Fourth AP Funds have coordinated their environmental and ethical dialogues with foreign companies through the Ethical Council. All four of them serve as buffer funds in the Swedish national pension system. In 2001, the Government assigned them the joint task of investing the country's buffer capital in a way that serves the pension system best while generating high long-term return at low risk considering ethical and environmental principles.

## **THE WORKING PROCESS OF THE ETHICAL COUNCIL MUST BE SUCH AS TO MINIMISE RISK AND MAXIMISE LONG-TERM RETURN ON THE INVESTMENTS OF THE FUNDS**

The Ethical Council encourages companies to proceed from the activities they conduct to address relevant sustainability considerations and adopt appropriate guidelines, along with management and monitoring systems that enable them to do business as responsibly as possible.

The Council advocates for and participates in preventive initiatives to promote incorporation of sustainability principles into the way companies operate, as well as to pursue dialogues once incidents associated with violations of international environmental and human rights conventions have come to light.

## **CORE VALUES OF THE ETHICAL COUNCIL**

The AP Funds have translated their joint mission into a set of core values—acting in accordance with the principles of engagement, action and the need for change in order to make a difference.

Along with the core values of the Swedish state, the international conventions to which Sweden is a signatory and its positions on matters of international law are key tools in the efforts of the Ethical Council. The tenets of democracy, human equality, the freedom and dignity of the individual, and sustainable growth are central to these values. The Swedish Constitution also reflects these values and tenets.

The congruity of the core values held by the government and the Ethical Council adds power and cogency to dialogues with companies and other stakeholders. The values are easily communicated in international venues.

Each AP Fund is autonomous pursuant to the Swedish National Pension Funds Act and makes its own investment decision. Given that the AP Funds are competitors, they do not consult with each other about investments. Each Fund has shareholdings in somewhere between 1,500 and 3,500 companies, partly by means of passive management—a common vehicle for ensuring cost-effective exposure to various stock

markets and thereby holding shares of all the companies in a particular benchmark.

## **WORKING TOGETHER TO EXERT GREATER INFLUENCE**

The Ethical Council collaborates on influencing companies, mostly foreign holdings, in the listed equities portfolios of the AP Funds. Given that the AP Funds are relatively small shareholders of international companies, such holdings represent the greatest need for collaboration.

## **GLOBAL COLLABORATION IS IMPORTANT**

The Ethical Council collaborates with major international investors, primarily pension funds, in other countries for the purpose of sharing experience and conducting joint efforts to exert influence as shareholders and ensure improvements by the companies. The combined assets of the four Funds (approximately SEK 1.2 trillion) offer the kind of potential for making a difference that individual initiatives could never aspire to.



# WORKING PROCESS OF THE ETHICAL COUNCIL

**The working process of the Ethical Council must be such as to minimise risk and maximise long-term return on the investments of the AP Funds. Its activities proceed from the principles of commitment, action and the need for change with the goal of being a long-term, responsible and committed shareholder. As responsible, dynamic shareholders, the AP Funds help companies do business in a manner that is sustainable over the long haul.**

## DIALOGUE AS A TOOL

A fundamental tenet of the Ethical Council is that the AP Funds avoid investing in companies that systematically violate the international conventions to which Sweden is a signatory. Dialogue is the Ethical Council's most effective tool for promoting change and persuading companies to behave in a more socially responsible manner. The Ethical Council supports the AP Funds in exercising active corporate governance by persuading companies to both correct documented violations and engage in preventive efforts.

Influence can be exerted either directly at the corporate level or indirectly by means of various international initiatives to shape legislation and encourage the kind of self-regulation that persuades companies to accept their share of ethical and social responsibility.

All of the four AP Funds that participate in the Ethical Council are signatories to the UN Principles for Responsible Investment (PRI) initiative, which provides a venue for actively prevailing upon companies and other investors to take social and environmental concerns seriously. PRI is also fertile soil for launching collaborative efforts among international investors.

## REACTIVE EFFORTS

The Ethical Council pursues its reactive working process in several different steps. A biannual review of the equities portfolios of the AP Funds detects violations of international conventions. Ongoing corporate dialogues monitor incidents that have come to the attention of the Council.

The AP Funds and Ethical Council rely on the media, interest groups, stakeholders, trade organisations, public authorities, judiciary, UN bodies and many other sources to monitor corporate incidents. Some incidents are inevitably overlooked. The Council incorporates all information that it receives about such incidents into its systematic process.

The problems at the companies with which the Council conduct in-depth dialogues are deemed to be palpable, well documented and amenable to correction. The purpose of dialogue is to persuade a company to stop committing the violation and to adopt preventive measures going forward.

## FOUR-YEAR LIMIT

As long as a dialogue is moving along and the company is receptive, the Ethical Council continues to devote its time and resources. Generally speaking, a dialogue concludes once its objective has been achieved. As of 2014, the Council limits reactive dialogues that concern violations of international conventions confirmed by external experts to four years. Unless the Council has achieved its objectives by that time, it recommends that the AP Funds divest the company.

The Council views divestment as the last resort, knowing full well that the problem is unlikely to go away. Without pressure from active shareholders that demand improvements, the improprieties will inevitably continue.

## PREVENTIVE INITIATIVES

The Ethical Council is increasingly turning its attention to preventive initiatives for the purpose of averting serious incidents and bolstering corporate endeavours to address sustainability issues. The Council has placed growing emphasis in recent years on preventive initiatives as a demonstrably effective way of persuading companies to act with a greater sense of social urgency and responsibility. Along with anti-corruption projects, the Ethical Council's involvement with the mining, pharmaceutical and palm oil industries reflect this orientation.

Other investors often participate in such dialogues, which encourage companies to focus on management of various environmental and social risks, improve their internal processes and make their activities more transparent. The Council analyses a company's strengths and vulnerabilities on the basis of corporate disclosures and best practice in the particular industry.

## WORKING PROCESS OF THE ETHICAL COUNCIL

STEP	PREVENTIVE DIALOGUES	REACTIVE DIALOGUES (WHEN VIOLATIONS OF INTERNATIONAL CONVENTIONS ARE SUSPECTED)
1. → REVIEW OF AP FUND HOLDINGS	The Council engages in systematic business intelligence concerning approximately 4,000 companies. Among the sources are media, investors, interest groups, stakeholders and UN bodies.	
2. → IN-DEPTH EXAMINATION	The Council reviews and analyses companies, industries, problem areas and investor initiatives.	Between 100 and 300 companies each year are examined more closely for possible implication in violation of international conventions. The Council, other investors and various service providers are all involved in the examination.
3. → CHOOSING COMPANIES TO DIALOGUE WITH AND SETTING OBJECTIVES	The Council chooses companies and any preventive projects that it wants to work with. The choice of focus areas does not represent a statement that one is more important than another but is simply a deliberate strategy to earmark the resources of the Council in ways that are most likely to yield the greatest benefits.	The Council carries on direct dialogues with a number of companies whose violations of international conventions are palpable and well documented. The Council also collaborate with various investors and service providers to dialogue with companies in response to alleged violations.
4. → HOW DIALOGUES PROCEED	In-depth corporate analyses and possible comparisons with minimum requirements and best practice for the industry in question.	Collaboration with other investors, submission of proposals and voting at general meetings, and other forms of pressure.
5A. → THE OBJECTIVE OF THE DIALOGUE HAS BEEN ACHIEVED	The dialogue is concluded.	The dialogue is concluded. The company is monitored closely for five years.
5B. → THE OBJECTIVE OF THE DIALOGUE HAS NOT BEEN ACHIEVED	The dialogue continues.	Unless a dialogue has produced the desired results after four years, the Council recommends that the AP Funds divest the company. Each AP Fund makes its own divestment decisions. The Council checks once a year to see whether the situation has changed and the company has begun to comply with international conventions.

# STEADY FLOW OF DIALOGUES CONTINUE

The dialogues that the Ethical Council conducted with more than 300 companies in 2014 often addressed several different areas of sustainability. Following is a snapshot of the status of the dialogues at the end of the year.



## BLUE-CODED DIALOGUE

A preventive dialogue that the Ethical Council carried on or that concerned an incident that the company sufficiently explained and/or addressed during the year. A total of 218 companies at the end of 2014.

## ORANGE-CODED DIALOGUE

A dialogue that the Council pursued during the year due to an incident or the participation of the company in a preventive project that requires it to take additional corrective measures. The Council will continue to dialogue with the company. A total of 76 companies at the end of 2014.

## RED-CODED DIALOGUE


Dialogue with a company whose violation of an international convention has been verified. The dialogue is subject to a limit of four years. Unless the dialogue has generated improvements by that time, the Council will recommend that the AP Funds divest the company. One company was red-coded at the end of 2014.

## BLACK-CODED COMPANY

A company that the Council has recommended that the AP Funds divest. Each year, the Council determines whether or not the violation of international conventions that occasioned the divestment has been corrected. At the end of 2014 the Ethical Council had made recommendations to the AP Funds to divest a total of 13 companies. The Funds have followed each recommendation.

## A FEW DIALOGUES AND THEIR STATUS AT THE END OF 2014


### Nike

 The company is collaborating with suppliers, the government and Better Factories Cambodia to protect basic worker's rights.


### Total

 Total has signed agreements with Morocco to conduct reconnaissance (geological surveys) off the Western Saharan coast. If the project expands to include oil prospecting and extraction, violations of international law may result.

### Siam Cement

 After having adopted a new code of conduct for suppliers in 2013, Siam Cement reviewed them in 2014 with an eye to their environmental and human rights efforts. The company is targeting review of all suppliers by 2015.


### MTN

 MTN has clarified its position with respect to human rights, as well as information and communication technology. The company has undertaken to protect and defend its consumers when it comes to freedom of speech and the right to data confidentiality. An ongoing project is intended to shed light on incorporation of human rights issues into risk analysis.


### Motorola Solutions

 Selling surveillance equipment to West Bank settlements is a violation of human rights. The company remains steadfast after four years of dialogue. The Council recommended after the report period that the Funds divest their holdings.

### Agrium

 Buying and selling natural resources from occupied territory. Despite several years of dialogue, the company had exhibited scant interest in modifying its behaviour.

### Barrick Gold

 Discharging mine waste into river systems is unacceptable. The company has replied in writing that it has no intention of adopting a policy to limit its use of the controversial method going forward.

# AN ASSORTMENT OF DIALOGUES DURING THE YEAR

Given that the dialogues are confidential, they cannot always be reported to the general public. But the AP Funds and the Ethical Council embraces transparency and attempts to release as much information about its activities as possible without jeopardizing its objectives. The following presentations cover an assortment of the dialogues that the Ethical Council pursued in 2014.

## EXTRACTION OF NATURAL RESOURCES IN WESTERN SAHARA POSES ONGOING CHALLENGES

As part of an initiative launched in 2009 to address extraction of natural resources in Western Sahara, the Ethical Council also dialogued with **AGRIUM** in 2014.

The Ethical Council and a handful of other investors first got in touch with Agrium during spring 2012 in response to reports that the company had signed a contract to import phosphates from Morocco, some of which originated from occupied Western Sahara. Nevertheless, the company began importing phosphates in 2013 pursuant to a contract that would not set to expire until 2020. While fully acquainted with the questionable nature of the occupation, Agrium does not feel that it violates Canadian or international law by purchasing phosphates. The Council does not believe that the company has been able to show that the business is consistent with the interests and wishes of the local population. Based on an assessment that further

dialogue will not be productive, the Council has recommended that the AP Funds divest Agrium.

The Council, which has had ongoing contact with the oil company **TOTAL**, is monitoring its reconnaissance (geological surveys) of oil off the Western Saharan coast. Now that the survey

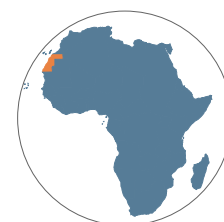
has been completed, the company is evaluating the data. Assuming that the data are favourable and Total decides to begin test drilling, the Council will ask it to demonstrate that the project is consistent with the interests and wishes of the local population.

### WESTERN SAHARA

Western Sahara, which Morocco has been occupying since 1975, is on the UN list of Non-Self-Governing Territories that must be decolonised. The UN Legal Counsel stated in January 2002 that extraction of mineral resources in Western Sahara without local consent would be in breach of the UN Covenant on Civil and Political Rights and the UN Covenant on

Economic, Social and Cultural Rights. The UN's Security Council voted in 2002 that contracts for reconnaissance and evaluation do not constitute exploitation or physical removal of mineral resources. The conclusion is that reconnaissance does not violate international law but would do so if exploration or extraction were inconsistent with

the interests and wishes of the Western Saharan population.



## REFOCUSING ON DISCHARGES OF MINE WASTES INTO RIVER SYSTEMS

The Ethical Council began dialoguing with **BARRICK GOLD**, a Canadian company, in 2013. The objective was to persuade the company to adopt a public policy and commitment to refrain from discharging mine wastes into river

systems as part of future projects. The method has been controversial, given that it violates the UN Convention on Biological Diversity. The Council has no progress to report. A written reply by Barrick Gold made it clear that no

policy to restrict its waste disposal options was on the drawing board.

The Council has concluded that ongoing dialogue is unlikely to lead anywhere, given the risk of recurring violations in view of the

company's refusal to rule out use of the method at one point or another. The Council has recommended that the AP Funds divest their holdings.

### WORKING CONDITIONS AT SUPPLIERS FOR TOY MANUFACTURERS

A number of reports have called attention to poor working conditions at Chinese suppliers for toy manufacturers. Among the problems are dangerous workplaces, various types of official harassment and unlawful terms of employment.

Many of the reports have turned the spotlight on **MATTEL**. The Ethical Council had long tried to establish a constructive dialogue with the company about these issues but had little luck. In 2014, however, Mattel expressed willingness to discuss their relationships with suppliers and the working conditions at their own plants.

### HUMAN RIGHTS RESOLUTIONS

The Ethical Council continued its dialogue with **MOTOROLA SOLUTIONS** in 2014 about its sales of customised surveillance equipment to West Bank settlements in contravention of international humanitarian law.

One objective of the dialogue was to persuade the company to stop supplying settlements in occupied territory with surveillance systems and associated services. An additional objective was for the company to adopt a corporate policy that prohibits violations of international humanitarian law.

In collaboration with American investors, the Ethical Council submitted a proposal for consideration by the 2014 annual general meeting of Motorola Solutions.

The proposal was that the company overhaul its human rights policy, as

well as its approach to compliance with the Fourth Geneva Convention relative to the Protection of Civilian Persons in Time of War and other international agreements. Although the company had gone ahead and made small amendments to its policy, the Council and other investors tried to submit a new proposal to the 2015 general meeting in a bid to effect more comprehensive reforms. However, the company blocked the attempt in reference to Securities and Exchange Commission regulations. The Council concluded that all available resources had been exhausted in four years of attempts to make a difference. In early 2015, the Ethical Council recommended that the AP Funds divest the company, whose activities are implicated in violations of the Fourth Geneva Convention.

### SUPPLIERS STILL AT CENTRE STAGE

Although many companies in various industries are pursuing determined sustainability efforts, the Ethical Council regularly receives reports about problems at their suppliers.

A number of reports over the past few years have mentioned **NIKE'S** suppliers in Indonesia and Cambodia. Among the improprieties have been poor working conditions, low wages and unpaid overtime. Nike's suppliers in Indonesia reportedly pay below the minimum wage there. Cambodian workers have been fired for striking against poor working conditions and low wages. Nike has notified the Council that all of the workers have finally been rehired.

Nike is collaborating with Better Factories Cambodia—an initiative supported by the International Labour Organisation, and the International Finance Corporation of the World Bank Group—plant management and the government to improve working conditions, as well as institute collective bargaining and improve compliance with other fundamental worker's rights.



# MINING INDUSTRY MAKES PROGRESS

The Ethical Council launched a project in 2011 to target the mining industry. An analysis of the results shows that the dialogues have led to improvements in all areas of sustainability discussed.

The project included some 30 mining companies in which the AP Funds held interests in 2011. The Ethical Council's 2011, 2012 and 2013 annual reports presented the effort in great detail.

The reason for pursuing a preventive, industry-wide initiative was that the Council had long dialogued with a number of mining companies about water contamination and human rights, particularly those of indigenous populations.

The Ethical Council bases its sustainability project on the ten principles of the International Council of Mining and Metals (ICMM).<sup>\*</sup> An external analytical firm sent the Council summaries of the preventive efforts of the individual companies to address the various principles and performed a gap analysis. The Council got in touch with the companies to discuss the results.

More than 20 dialogues over a period of two years required a good many contacts and meetings.

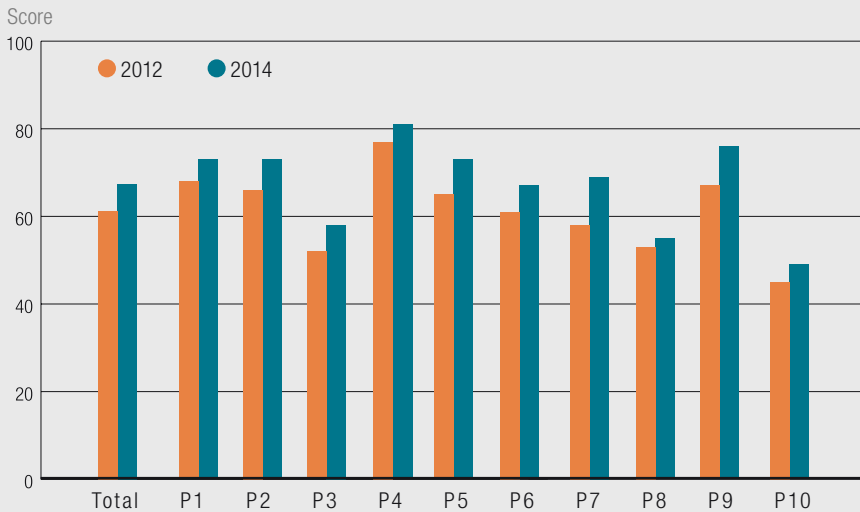
## IMPROVEMENTS ACROSS THE BOARD

Both oral and written reassurances from the companies indicated that they would be dealing with several of the issues highlighted by the analysis. The palpable vigour of the discussions in the industry and with many other stakeholders accelerated the momentum for change. All the attention that the mining industry attracted during this period generated expectations that the project's indicators would reflect progress. An examination of the results found that the average score had increased by better than six percentage points, a solid improvement.

## BIODIVERSITY INITIATIVE PAID OFF

The initial analysis in 2011–2012 revealed that many of the companies were behind the curve when it came to the seventh ICMM principle (biodiversity). Representatives of local populations, NGOs, the ICMM and other stakeholders stressed that biodiversity demands greater corporate attention. The ICMM drew up a new policy document

### TO WHAT EXTENT ARE COMPANIES OBSERVING THE ICMM PRINCIPLES?



<sup>\*</sup>www.icmm.com

#### Analysis of 25 companies based on the ten ICMM principles

Five of the companies included in the 2011–2012 analysis have been either bought out or delisted. Accurately tracking the changes that have occurred since then required them to be deleted from the analysis.

Average score per principle —100 is the maximum according to the analysis.

See next page for a description of the principles.

regarding biodiversity for mining companies. The Council brought the matter up again and again when talking with many of the companies. The Council is extremely pleased that all exertion paid off. Biodiversity has increased by 11 percentage points, more than any other indicator. While it goes without saying that implementation must be monitored on the ground, the Council has every reason to believe that corporate strategies are set to be more conscious and effective.

**PROMOTING COMMUNITY DEVELOPMENT NEAR THE MINES**

The Ethical Council has identified a number of complex issues through the years related to social and economic development in communities located near the mines. Expectations of the resources that a mine can plough back into nearby communities frequently generate conflicts due to broken corporate promises or lack of realism on the part of the local population. That particular issue, which the ninth ICMM principle deals with, frequently arose during dialogues with the companies. We are pleased to report that it is among the areas that have shown the greatest improvement. The indicator has climbed nine percentage points.

**HUMAN RIGHTS ARE RESPECTED MORE THAN EVER, BUT A LOT REMAINS TO BE DONE**

Ever since the UN adopted its Guiding (Ruggie) Principles on Business and Human Rights in 2011, the Ethical Council has not only kept a close eye on human rights violations among mining companies but also a number of other industries. Dialogues with mining companies made it clear that most of them were working on understanding

and interpreting the principles, as well as identifying the new policies and programmes they needed to adopt in order to ensure implementation of the third ICMM principle. An evaluation in autumn 2014 found that the associated indicator had increased by six percentage points, though from a relatively low level, but that some of the companies still had a good way to go. The fact that there is more work to do in order to implement the UN Guiding Principles on Business and Human Rights not only applies to the mining industry but to most other industries as well.

**LETTER TO 75 OTHER MINING COMPANIES**

The Ethical Council wrote a letter summarising the goals and objectives of the project, the results of the discussions with the various companies and a number of general recommendations. The letter was sent to 75 mining companies in the listed equities portfolios of the AP Funds that did not participate in the project.

**BRINGING CHANGES TO FRUITION**

There are a number reasons that the Ethical Council is favourably disposed to large preventive industry projects. Companies are more amenable to improvement if they have not faced any significant problems yet, while major issues are more effectively addressed when sustainability is discussed on an industry-wide basis. The ability to identify a company’s strengths in addition to its vulnerabilities always facilitates constructive dialogue. The Council is only one of many stakeholders that are involved in examining the challenges posed by mining companies and advocating for various solutions.

**TEN ICMM SUSTAINABLE DEVELOPMENT PRINCIPLES**

- 1. Implement and maintain ethical business practices and sound systems of corporate governance.
- 2. Integrate sustainable development considerations within the corporate decision-making process.
- 3. Uphold fundamental human rights and respect cultures, customs and values in dealings with employees and others who are affected by our activities.
- 4. Implement risk management strategies based on valid data and sound science.
- 5. Seek continual improvement of our health and safety performance.
- 6. Seek continual improvement of our environmental performance.
- 7. Contribute to conservation of biodiversity and integrated approaches to land use planning.
- 8. Facilitate and encourage responsible product design, use, re-use, recycling and disposal of our products.
- 9. Contribute to the social, economic and institutional development of the communities in which we operate.
- 10. Implement effective and transparent engagement, communication and independently verified reporting arrangements with our stakeholders.

From the ICMM website.

**For more information**  
[www.icmm.com/our-work/sustainable-development-framework/10-principles](http://www.icmm.com/our-work/sustainable-development-framework/10-principles)



# PALM OIL – PRIORITIZING BIODIVERSITY AND TRACEABILITY

**Palm oil is a key ingredient of many consumer products and therefore an important commodity for a number of the companies in which the AP Funds have holdings. Nevertheless, the product poses many environmental and social challenges. The Ethical Council made a deliberate decision to dialogue with companies in hopes of making the industry more conscious of sustainability issues. The PRI task force in palm oil is the nexus of much of the effort. The task force talked with 25 companies in 2014.**

## COLLABORATION FOR SUSTAINABLE PRODUCTION

Palm trees produce the most popular vegetable oil in the world. Not only is it used for cooking, but it is an ingredient of many foods, cosmetics, soaps, detergents, biodiesel fuels and other products.

The Ethical Council joined a collaborative PRI initiative in autumn 2013. The members of the task force are working together to raise investor awareness and reach a consensus on developing a sustainable product.

The Council participated in a 2013 international investor initiative for the purpose of persuading companies to produce and purchase certified palm oil. Sime Darby, Asian Agri, IOI Corporation, Kuala Lumpur Kepong Berhad and Musim Mas—five of the biggest companies—have subsequently stated that they will not start new plantations in areas with great biological diversity and high climate value. Meanwhile, they are conducting a one-year study to identify the areas that may be suitable for new plantations. The companies have made it clear that the views of the investors were integral in causing them to reconsider their positions.

## ENVIRONMENTAL DAMAGE AND CARBON FOOTPRINT

Palm oil plantations can thrive only in a narrow belt around the Equator, an area of high biodiversity. The greater the demand on the global market, the more land is needed. Destruction of rainforests to make room for palm trees radically transforms the habitat for tigers, orangutans and other species. Such activities leave a carbon footprint as well. Cultivating plantations on peatland contributes even more to global warming by releasing carbon into the atmosphere. The process also violates the rights of the local population to their land. Several environmental activists have campaigned against what they refer to as dirty palm oil.

## MAKING PALM OIL SUSTAINABLE

The Roundtable on Sustainable Palm Oil (RSPO) emerged in 2004 for the purpose of coming up with a global standard for production and use of a sustainable

product. RSPO certified the first plantations in 2008. Approximately 16 percent of all palm oil has now been given the stamp of approval. The RSPO has been criticised for not ensuring that companies fully comply with the standard and for failing to make stricter demands when it comes to deforestation, peatland and other problems.

The PRI task force supports the RSPO and stresses the importance of adopting a global standard of sustainability. Conditions throughout the industry stand to benefit from the use of such a tool. Dialogues with producers have zeroed in on promoting RSPO certification and traceability. The discussions have also encouraged companies to implement policies that repudiate deforestation, plantations on peatland and violations of local rights.

## SIGNIFICANT ADVANCES

A number of companies adopted policies in 2014 clearly prohibiting destruction of rainforests, plantations on peatland and violations of the right of the local population to free and prior informed consent (FPIC). Such policies now cover 96 percent of global palm oil production. That kind of clarity represents an important first step. But no real change occurs until companies engage in systematic efforts to implement a policy and persuade the entire organisation, including the supply chain, to comply. Reliable reports are needed if external stakeholders are going to monitor and assess results. That is why the task force is so anxious to ensure transparency and traceability.

## TRANSPARENCY AND TRACEABILITY

One of the targeted companies, Wilmar, publishes a quarterly report describing implementation of its “no deforestation, no peat, no exploitation” policy.

Many companies specify a timetable for guaranteeing traceability in their policies. Given that a refinery can process from many different areas, the ability to track down the plantation from which palm

oil was harvested poses a particularly daunting challenge. A refinery needs palm oil from approximately 250,000 acres and normally from a number of different mills as well. As the first processing step, a mill ordinarily services some 25,000 acres. A large company may have mills that process oil from its own plantation only. Other mills obtain their oil from many different suppliers.

#### INVESTORS COLLABORATE

The PRI task force consists of 44 investors that teleconference every other week to discuss and update each other about the dialogues that they are in charge of. One or two investors assume primary responsibility for each dialogue, making sure that letters are written and meetings scheduled. Other investors have the option of supporting one or more of the dialogues. DNB and the Ethical Council have primary responsibility for AAK, a Swedish company. The Council supports other dialogues by signing the letters that are sent to the companies.

DNB and Council representatives visited the AAK head office in Malmö last June. The company briefed the representatives on its efforts and said that it had overhauled its palm oil purchasing policy. The new policy states that AAK will purchase only palm oil that has been produced “without deforestation or destruction of peatland and that plantations will be built only with the free and prior informed consent of local communities.” Furthermore, mills are to be traceable by the end of 2014 and plantations by the end of 2017. The sustainability report for 2014 states that 78 percent of the oil can be traced to a particular mill.

Harvesters cut  
branches off  
palm trees.



# COCOA INDUSTRY COLLABORATES FOR CHANGE

**Like tobacco and other industry sectors, the cocoa industry is starting to collaborate on disengaging from child labour practices. Industry-wide cooperation frequently enables major reforms.**

For the past several years, the Ethical Council has been backing a project to ensure abolition of child labour at cocoa plantations. Dialogues have been conducted with a number of purchasers and other industry representatives.

Criticism of the industry has long been particularly harsh in West Africa, where 70 percent of the world's cocoa beans are produced, for its complicity with child labour among suppliers. Millions of farmers grow the beans on a small scale and sell them to a complex chain of suppliers. Hundreds of thousands of children are thought to work on the farms, some of them carrying heavy sacks, risking exposure to pesticides and performing other dangerous tasks. Meanwhile, they are unable to attend school.

## CONFERENCE IN COPENHAGEN

The World Cocoa Foundation<sup>2</sup> held a conference in Copenhagen last autumn attended by representatives of the chocolate and cocoa industry, dealers, governments from the cocoa producing countries, NGOs, academia and research institutes from more than 20 countries. They shared information about the latest developments with respect to sustainability, as well as improvements in the working conditions and financial circumstances of farmers.

The Ethical Council took part in a concluding roundtable discussion among representatives of investors and the cocoa industry. Various solutions for ending child labour were tossed around and light was shed on the complexity of the issue. Child labour is not limited to the cocoa industry but is common in poor agricultural communities as a means of ensuring that farmers can earn a subsistence living. The lack of opportunity sends young people to the cities in quest of employment. The challenge faced by the cocoa industry is not simply to combat child labour but to make farming attractive and profitable enough that the next generation will remain on the land. Only that way will there be enough farmers to grow the beans. The average age of West African cocoa farmers is well over 50.

## COCOA ACTION

The World Cocoa Foundation is coordinating the Cocoa Action initiative that began in 2014. The goal of the initiative is to synchronise and fine tune sustainability efforts at the largest cocoa and chocolate manufacturers by promoting collaboration between the industry and the governments of the producing countries. Cocoa Action is now focusing on Ghana and Côte d'Ivoire, which account for 55 percent of cocoa beans on the world market. The initiative will eventually be expanded to include other countries as well.

Among the 24 companies involved in the project in May 2014 were ADM, Barry Callebaut, Cargill, Hershey's, Mondelez International, Nestlé and Olam. They have come together under the direction of the World Cocoa Foundation, which schedules meetings and facilitates implementation of the comprehensive Cocoa Action strategy.

Given that a number of different representatives are discussing solutions to the challenges faced by the industry, the Ethical Council is optimistic about the prospects for change. The Council will be monitoring trends and evaluating the results of the corrective measures that are currently being talked about.



<sup>2</sup> Established to coordinate various programmes for raising farm incomes and promoting sustainable growing methods. Among the projects are teacher education, training in refinement and processing, microloans for farmers and health care.

# ENCOURAGING SIGNS OF PROGRESS IN THE FOOD INDUSTRY

The Ethical Council has been talking with Olam International about sustainability issues since 2012. Not only has the company contributed to gradual improvement in the circumstances of cotton and cocoa growers, but the Ethical Council has gained valuable insights into food industry trends.



**CHRIS BRETT**

► SENIOR VICE-PRESIDENT, HEAD OF CORPORATE RESPONSIBILITY AND SUSTAINABILITY, OLAM INTERNATIONAL

INTERVIEW

Over the past 25 years, Olam International has emerged as a leading agricultural firm that deals with the entire supply chain from field to fork in 65 countries, as well as shipment of food and commodities to more than 13,800 customers around the world. The company's 23,000 employees have helped it carve out a leading position in cocoa, coffee, nuts, rice, cotton and many other sectors. As a result, the company possesses highly useful knowledge about the state of the agricultural and food industries. The Ethical Council sat down with Chris Brett, Vice-president, Head of Corporate Responsibility and Sustainability at Olam—and asked him to share his impressions of current events in the industry and their impact on his company.

## PROGRESS IN THE SUPPLY CHAIN

The supply chain for agricultural products has changed significantly in recent years. According to Mr Brett:

► “Pressure by both investors and Olam’s customers has increased dramatically – virtually all of our major customers have updated their supplier codes. As a result, we have had no choice but to familiarize ourselves with the entire supply chain in a much more effective way. In addition to greater pressure from customers, the International Finance Corporation (IFC) and the Dutch Development Bank (FMO) – two of our financiers – have offered helpful advice.”

**Commodity traceability is a central tenet of the industries that Olam serves.**

► “Olam has decided to participate in Global Map of Environmental and Social Risks in Agro-Commodity Production (GMAP), a

**“OUR CUSTOMERS ARE ACUTELY AWARE THESE DAYS THAT STRENGTHENING THE SUPPLY CHAIN REQUIRES THEM TO WORK WITH US ON MORE FULLY UNDERSTANDING THE DYNAMICS OF ADDED VALUE CREATION”**

comprehensive database for identifying product origin. You can search for virtually any commodity in the database and obtain a complete risk assessment”, Mr Brett says.

**Olam is gradually implementing its updated supplier code.**

The pace varies according to geographic area and type of commodity. The code is easier to enforce among coffee growers in Latin American and other areas, whereas cotton growers in Africa pose the biggest challenge. Olam’s goal is that all suppliers abide by the code no later than 2020.

**Adopting a supplier code is an important first step, but systems and processes are also needed to ensure compliance.**

► “Olam has reinforced its internal processes and designed software to support its monitoring system. The software will facilitate analysis of the situation on the 3.9 million small farms that supply Olam with commodities”, Mr Brett says. The analysis covers production and finances, along with family circumstances and other social factors. Olam is also reviewing the distance to schools and healthcare facilities. Such information can be used to talk with public authorities or make decisions about the financing of educational projects.

**While benefiting everyone, fortifying the supply chain also generates higher costs for Olam.**

► “Customers initially passed the costs on to us, which represents a long-term risk for the farmers at the lower end of the supply chain. But the situation has evolved with time and our customers are acutely aware these days that strengthening the supply chain requires them to work with us on more fully understanding the dynamics of added value creation. Olam cannot do the whole job by itself while selling its products at the same price as always. Fortunately, our customers realise that sustainability is a valuable asset for a brand and are willing to absorb some of our increased costs”, Mr Brett concludes.

The dialogue with Olam International is not only an excellent example of means by which the Ethical Council can persuade a company to act more responsibly, but evidence of how important it is to maintain direct contact in order to more fully monitor the evolution of sustainability challenges, as well as the ways that the corporate world views and responds to such changes.

# HUMAN RIGHTS ON THE GROUND

Three years have passed since the UN adopted its Guiding Principles on Business and Human Rights (UNGP). The AP Funds and the Ethical Council brought together a number of Swedish companies at an October seminar to discuss their implementation of UNGP.

The AP Funds, the Ethical Council and SHIFT invited 20 companies to a seminar on the topic of “How to Implement the Guiding Principles on Business and Human Rights?” The Ethical Council started off by talking about its experience of corporate efforts and how important it was for each company to begin identifying the areas of human rights in which it was at risk. A representative of SHIFT described the process of drawing up the principles and the way that the

organisation had put them into practice. According to representatives of Ericsson and H&M, their efforts had revealed the need and importance of continuing to share information. The lively discussion that followed the presentations brought various dilemmas and challenges to the surface when it came to both implementation and interpretation, convincing both the AP Funds and the Ethical Council that they had every reason to move forward with their involvement.

## SHIFT

**SHIFT is an unaffiliated, nonprofit centre for businesses and the promotion of human rights issues.**

“ The organisation helps governments, businesses and their stakeholders make UNGP a reality on the ground. SHIFT was formed in July 2011 after the United Nations Human Rights Council (UNHRC) unanimously ratified the principles in response to demands for implementation of Professor John Ruggie’s Protect, Respect, Remedy framework. Professor Ruggie serves as the UN Special Representative on Business and Human Rights and Chairman of the SHIFT Foundation.



Anna Triponel  
Advisor at SHIFT

## GUIDING PRINCIPLES ON BUSINESS AND HUMAN RIGHTS

**A framework cobbled together by Professor John Ruggie, UN Special Representative on Business and Human Rights.**

The framework consists of three guiding principles for companies.

### Three spheres of responsibility are stressed:

- Governments must protect human rights (Protect)
- Companies must respect human rights (Respect)
- Governments and companies must jointly remedy violations of human rights (Remedy).

While governments retain the basic responsibility to protect human rights, the principles make it clear that companies need to take action as well. They must thoroughly review the human rights challenges that they face, which makes it easier for investors to analyse corporate risk management and possible violations.

### For additional information, see

[www.business-humanrights.org/SpecialRepPortal/Home/Protect-Respect-Remedy-Framework/GuidingPrinciples](http://www.business-humanrights.org/SpecialRepPortal/Home/Protect-Respect-Remedy-Framework/GuidingPrinciples)

# SPOTLIGHT ON ONGOING ANTI-CORRUPTION EFFORTS

Combatting corruption has been one of the Ethical Council's focus areas for a number of years. Most preventive industry-wide projects, not to mention individual dialogues, address these issues. Corruption is among the most serious problems that the world must come to grips with if sustainable development is to be a reality. Such practices not only plunder financial resources but undermine the credibility of companies, authorities and investors.

## SUSTAINED ANTI-CORRUPTION EFFORT

The Ethical Council participates in the PRI project to combat corporate corruption. The project is in its fourth year.

The first phase, which lasted from 2010 to 2012, involved some 20 companies around the world. An external party analysed their efforts to prevent corruption. A larger group of investors subsequently got in touch with the companies to discuss the analysis and propose improvements. The companies responded favourably to the project and incorporated many of the proposals into their policies and reporting structures.

The second phase started in autumn 2013. The project contacted some 30 companies and began dialoguing with some 20 of them.

The Ethical Council is responsible for four dialogues in Asia and participates in several others. Asia was chosen because the Council had observed that certain areas of the continent demand greater engagement and that corruption must be combatted at the global level. Two of the companies are in the oil sector and two in the banking industry. Both oil companies have responded constructively and dialogues are under way. The banks have been less forthcoming. Assisted by an external fund manager with familiarity and connections in the Asian market, the Council finally succeeded in making initial contact.

## COUNCIL ATTENDED AN ANTI-CORRUPTION CONFERENCE IN PRAGUE

The World Forum on Governance invited leading representatives of the private sector, civil society, governments and investors to a two-day discussion on ways of combatting corporate corruption. The talks centred on various initiatives in Central and East Europe, best practice and initiatives by institutional investors. The Ethical Council feels confident that anti-corruption efforts are moving ahead in these parts of the world but realises that more time is required.

## NATURAL RESOURCES DEMAND TRANSPARENCY

Many countries that have abundant natural resources are wrestling with corruption at the highest levels. These kinds of practices pose a major obstacle to democratic development and economic growth. Given the power of transparency as a tool for combating corruption, the Ethical Council has been supporting the Extractive Industries Transparency Initiative (EITI) for the past several years.

The goal of the EITI is to persuade governments – along with oil, gas and mining companies – to report payments from the companies to the governments. That way the initiative can verify the payments and determine whether or not they end up in the right hands. The ultimate objective is to ensure that a country's natural resources benefit the population as a whole. A total of 31 countries are reporting in accordance with the EITI standard and another seven are preparing to do so. Almost all public oil, gas or mining companies – as well as a number of volunteer organisations – support the EITI.\* More than 80 investors have lent their formal support to the EITI, sending an unmistakable signal to governments and companies with mining operations that shareholders value transparent reporting.

The board is made up of representatives from countries, companies, NGOs and investors. The EITI is central to the development of reporting standards and serves as a key venue for stakeholders to discuss these matters.

The Council and other investors that back the EITI teleconference regularly to exchange information and talk about the activities of the initiative. The forum serves as a foundation for investor collaboration on transparency matters.



\*Source: [www.eiti.org](http://www.eiti.org) as of 9 January 2015

# CLIMATE CHANGE – A THORNY ISSUE IN THE ABSENCE OF GLOBAL REGULATION

Expectations that governments will take meaningful action swirl in the air as the 2015 UN Climate Change Conference in Paris approaches. A global agreement will be needed if the goal of preventing the average temperature on Earth from increasing by more than two degrees is to be met. Policy measures to achieve the goal are still conspicuous by their absence. While both investors and companies need clear long-term ground rules in order to evaluate and plan their decisions, a host of daunting challenges remain to be addressed.

## GLOBAL WARMING

The UN Intergovernmental Panel on Climate Change (IPCC) published its fifth evaluation in 2013 of the current state of knowledge in the field. The first report was released seven years ago – the new one makes it eminently clear that global warming is now an incontrovertible fact. For example, the Greenland ice sheet and glaciers around the world are continuing to shrink, while the oceans are getting warmer at deeper and deeper levels. Ecosystems increasingly exhibit the effects of climate change.

The challenge is to decide what kind of investments will both benefit from and contribute to the transition to a low-carbon society. Industries associated with renewable energy have been consolidating rapidly and experiencing volatile share price performance.

## CONVERSION REQUIRES LONG-TERM GROUND RULES

The 21st United Nations Climate Change Conference (COP21) will be held in Paris in November, 2015. The goal is to adopt a legally binding agreement to limit greenhouse gas emissions. A failed attempt at the 2009 conference in Copenhagen left a trail of disappointment in its wake. If expectations are somewhat muted this time around, the need for clear signals about what various countries are willing to do is greater than ever.

The Institutional Investors Group on Climate Change (IIGCC),\* of which the AP Funds are members, represents a constructive approach to building a transparent, long-term framework for regulating greenhouse gas emissions. The ability to make wise long-term investments in renewable fuels for energy, infrastructure, construction and transport purposes is dependent on that kind of clarity.

During the year, the IIGCC submitted recommendations to the newly constituted European Commission concerning climate change priorities.\*\* Among the proposals are reform of the emissions trading scheme to generate unambiguous price signals and a dynamic programme to ensure that the EU will be firmly in the driver's seat by 2030.

## UN CLIMATE CHANGE CONFERENCE IN NEW YORK

Representatives of the AP Funds and the Ethical Council attended the September 2014 United Nations Climate Change Conference in New York. The purpose of the event was to reach greater consensus among the private sector, governments and investors. The conference was constructive in the sense that leading businesses and investors made impressive commitments in a number of different areas. The forest industry is an example of significant progress. A number of the companies with which the Ethical Council has dialogued announced far-reaching commitments. Some of them are collaborating with countries such as Indonesia, where extensive deforestation has long been employed to clear the way for palm oil plantations. During the runup to the conference, the IIGCC\*\*\* organised an appeal by 360 institutions around the world for long-term frameworks and price signals that can facilitate decisions about investments in renewable energy. Both institutional investors and the private sector are primed to participate in conversion to a society that leaves a much smaller carbon footprint. They were not shy about communicating their readiness to the UN during the New York conference.

## AP FUNDS TO MEASURE THEIR CARBON FOOTPRINT

As part of the AP Funds' climate work each AP Fund has decided to measure and evaluate its carbon footprint. Their participation in the CDP, earlier known as the Carbon Disclosure Project, whose reporting and that of the companies is increasingly transparent, led to the decision. The hope is that the commitment of the AP Funds and other institutional investors to report their carbon footprint will spur companies to be more open about their emissions as well. Standardisation of analytical and reporting methods for calculating the carbon footprint of investors would also be very helpful.

\* [www.iigcc.org](http://www.iigcc.org)

\*\* [http://www.iigcc.org/files/publication-files/IIGCC\\_2014\\_Statement\\_on\\_Climate\\_Change\\_and\\_Energy\\_Priorities.pdf](http://www.iigcc.org/files/publication-files/IIGCC_2014_Statement_on_Climate_Change_and_Energy_Priorities.pdf)

\*\*\* <http://www.iigcc.org/files/publication-files/GISCC2Dec2014.pdf>

# SUSTAINABILITY IN EMERGING MARKETS – MAJOR CHALLENGES AND OPPORTUNITIES TO MAKE A DIFFERENCE

The challenges posed by conversion to a sustainable society tend to be greatest in emerging markets and the companies in these countries are usually less well-equipped to cope with them than developed markets. Many companies do not have basic structures that allow them to analyse their activities from a sustainability point of view.

With that gap in mind, the Ethical Council joined a small group of investors in 2014 to carry on active dialogues with some 15 companies that are deemed to face substantial sustainability challenges though lacking the wherewithal to handle them. The companies are in Eastern Europe, Africa, Central America, South America and Asia. A number of the dialogues revolve around the need for reliable risk assessment, whereas others address environmental issues, transparency and working methods.

Patience is a cardinal virtue when it comes to persuading companies that are unaccustomed to talking with their shareholders. Trust between investors and companies is the foundation of any real change. The group of investors gets together with the companies face to face

at least once a year. Initial meetings are largely concerned with reaching a consensus about the types of sustainability challenges that the particular company is facing. The more specific the group's proposals and the stronger the relationship to the bottom line, the greater the likelihood that the company can be induced to proceed in the right direction. That is why the dialogues largely explore business opportunities, not simply risk management.

The approach has been shown to bear fruit but requires determination, insistence and a long view. Convincing a company to implement a monitoring and reporting system is a vital step towards long-term sustainable development.

COUNTRY	INDUSTRY	FOCUS AREA
<b>BRAZIL</b>	Energy	Risk assessment
<b>PHILIPPINES</b>	Real estate	Risk assessment
<b>CHINA</b>	Energy	Risk assessment
<b>CHINA</b>	Food	Risk assessment
<b>MALAYSIA</b>	Conglomerates	Assessment of risks and worker's rights
<b>MEXICO</b>	Food	Health considerations
<b>MEXICO</b>	Mining	Transparency
<b>RUSSIA</b>	Energy	Risk assessment
<b>RUSSIA</b>	Energy	Risk assessment
<b>RUSSIA</b>	Finance	Lending principles
<b>RUSSIA</b>	Mining	Risk assessment
<b>SOUTH AFRICA</b>	Telecom	Human rights
<b>SOUTH AFRICA</b>	Energy	Environment
<b>SOUTH KOREA</b>	Mining	Risk assessment
<b>THAILAND</b>	Construction	Risk assessment



# FIELD STUDIES IN SOUTHEAST ASIA

An Ethical Council representative visited Southeast Asian companies in spring 2014 to learn more about their sustainability efforts. Because the emphasis of the trip was on commodities, a palm oil plantation and a gold mine were on the agenda.



FIELD STUDIES  
► SOUTHEAST ASIA

**About the trip:** Both European and Asian investors participated in the trip, which was arranged by Sustainalytics, a provider of services for the Ethical Council. We visited ten companies in the course of a week.

**Text:** Excerpts from the travelogue of Christina Olivecrona, member of the Ethical Council.

## PALM OIL

**On the first day,** we visited a Sime Darby plantation in Malaysia. Looking out the window on the road from Kuala Lumpur International Airport to the plantation, we saw palm trees on all sides. The company greeted us with a series of presentations about their activities and sustainability projects before taking us out to demonstrate how palm oil is harvested and processed.

### Cutting branches off palm trees

requires great skill, particularly when the knife is sited atop a long pole. A single branch weighs approximately 25 kilograms. Workers gather the branches together and take them to the nearest mill, which squeezes out raw palm oil and preserves the kernels. The kernels are subsequently refined to palm kernel oil and other consumer products.

**Harvesting is heavy** and perilous labour. The man who showed us how to cut down the branches was wearing both a helmet and a protective jacket, and the knife had a safety catch. Given that it's more than 30 degrees Celsius out, I wondered how often workers actually used such equipment. On the way back, I noticed several harvesters without protective equipment on.

Palm trees bear fruit all year round. As a result, they yield four times as much oil per acre as soybeans and ten times as much as rapeseeds or sunflower seeds.

**Palm trees flaunt fresh fruit bunches** at various stages of development. The trees are harvested once every ten days or so. The bunches are taken to the nearest mill to ensure that production gets under way as soon as possible. Short lead-times are integral to optimising quality. Raw palm oil is shipped from the mill to a refinery. Because Sime Darby owns many plantations and mills, as well as a refinery, it is well positioned to control and trace the palm oil it produces. Traceability was one of our talking points. The company made it clear that there is no significant market for RSPO<sup>3</sup>-certified palm oil at the present time. Most of that demand comes from European companies.

**Later that week, we visited** Golden Agri Resources (GAR) and Wilmar at their head offices in Singapore. Golden Agri Resources

offered a fascinating account of its decision to embark on a serious sustainability effort as a result of the Greenpeace Kit-Kat campaign in 2010, as well as its switch from a confrontational to cooperative strategy. The company has been working with both Greenpeace and The Forest Trust (TFT) ever since. They have devised a High Carbon Stock (HCS) model to determine the climate value of various types of vegetation. The model assigns vegetation to one of six categories ranging from high-density (rain)forests to open fields. The idea is to identify the areas that must be preserved if deforestation is to be averted.

**We also had an opportunity to** observe the Golden Agri management system for entering data about the various plantations: harvest times, type of seed, age and total volume. Traceability is essential to verifying implementation of RSPO. The company is targeting RSPO-certification of all its palm oil by the end of 2015.

**Wilmar, the third** palm oil producer we met with during the week, adopted a "no deforestation, no peat, no exploration" policy in December 2013. Many of our discussions concerned implementation, particularly by their suppliers. Since only ten percent of the company's palm oil is harvested on its own plantations, it is dependent on small farmers and external mills. Wilmar told us that they devoted a great deal of time to persuading suppliers and other stakeholders that the

<sup>3</sup> The Roundtable for Sustainable Palm Oil is a sustainability standard.

Harvesters using a special knife.

Harvested palm oil fruits.



## TRAVELOGUE

policy needs to be fully implemented. The company would very much like all refineries to comply with the same requirements. (Refer to the discussion of palm oil on page 14)

### GOLD

**On the second day, we got off to an early start** and headed for the G-Resources gold mine in the North Sumatra province of Indonesia. The area had not hosted any mines before. Several members of the management team greeted us. The local manager talked about the history of the mine and the labour involved in starting one up. It had been operating for approximately a year and a half and required additional construction, particularly dams for fine particles.

**The company has** proactively got the local population involved. The issue of water assumed centre stage early on. The company needed to demonstrate that the mine would not contaminate the waterways that communities directly depend on. G-Resources identified the impact that the mine would have on surrounding villages and devised a robust policy for employing people who lived nearby.

**My overall impression** is that the efforts of the company when it comes to environmental and social issues demonstrate that mining companies can act in a responsible manner that promotes the growth and development of local communities.

### OTHER VISITS

**Singapore is an important** financial centre and Southeast Asian port. We visited the Singapore Stock Exchange and learned about its commodities trading setup. We also stopped by the biggest Shell refinery in the area. A meeting with Neptune Orient Limited, a large shipping firm, gave us the chance to talk about efforts to reduce emissions from its vessels and ways of handling those that had been scrapped. A discussion with GMG Global, which owns rubber plantations in Asia and Africa, covered various environmental and social projects.

**Singapore** is dependent on imports for 96 percent of its drinking water and food. The country has an agreement with Malaysia for import of drinking water. In an attempt to become more self-sufficient, Singapore is building parks and playgrounds capable of collecting rainwater. The country also has a purification plant that takes water directly from a sewage works. Though the water is used mostly for industrial purposes, visitors to the plant can drink it out of bottles.

**The authorities** are hard at work promoting domestic food production. Aquaculture is one piece of the puzzle. We visited both an aquaculture facility and a vegetable garden in vertical greenhouses on the outskirts of Singapore. Their height enables five to ten times as much production per unit area as ordinary greenhouses.

### SUMMARY

**The jam-packed trip** included many visits and discussions about sustainability, both with companies and among ourselves. All production relies on raw materials and commodities. The conditions under which they are harvested and processed affect the subsequent chain of production. The efforts of so many palm oil manufacturers to minimise environmental damage is encouraging. The Council will be keeping an eye on these projects. Excavating new mines often leads to conflicts with the local population. So we were pleased by the opportunity to talk with representatives of G-Resources, whose mine in the North Sumatra province of Indonesia demonstrates that companies willing to factor in local needs can find ways of doing business that benefit the entire region.

# RETROSPECTIVE

Since the Ethical Council started in 2007, its efforts have evolved from a focus on reactive dialogues to a growing emphasis on preventive dialogues as part of industry-wide initiatives. We adopted a more flexible process, as well as a time limit, in 2013.

## EVOLUTION OF THE ACTIVITIES OF THE ETHICAL COUNCIL

2007	<b>COUNCIL ESTABLISHED.</b>	<b>FOCUS ON SCRUTINY</b> of companies for violations of international conventions as well as reactive dialogues.		
2008	<b>PUBLICATION OF FIRST ANNUAL REPORT.</b>	<b>FIRST ROUNDTABLE DISCUSSIONS</b> with stakeholders and interest groups. Focus on the need to identify a clearer purpose for dialoguing.	<b>"ETHICS, PENSIONS AND THE ENVIRONMENT"</b> (SOU 28) is published. Among the recommendations of the commission are that the AP Funds proceed from more transparent core values, become less dependent on a single ethical consulting firm and cultivate more of its own analytical support to quality assure information obtained from external consultants.	<b>COLLABORATION</b> launched with a number of European pension funds for the purpose of sharing experience and exerting joint influence.
2009	<b>THE FOUR AP FUNDS DRAW UP NEW CORE VALUES</b> on behalf of the Ethical Council.	<b>THE ANNUAL REPORT EXPANDS</b> to include the objectives of the dialogues and their accomplishments during the year.	<b>GREATER FOCUS</b> on preventive dialogues.	
2010	<b>THE COUNCIL EMPLOYS</b> a Secretary-general to assume responsibility for day-to-day activities, quality assurance of analyses, dialogues and collaboration with other investors.	<b>THE COUNCIL PROCURES</b> additional service providers to minimise its dependence on a single consulting agency.	<b>THE COUNCIL DEVELOPS</b> a website for greater transparency and dissemination of information.	
2011 2012	<b>GREATER FOCUS</b> on preventive industry-wide initiatives.	<b>AS PART OF ONE SUCH INITIATIVE,</b> the Council analyses the extent to which a number of mining companies are complying with the sustainability principles established by the industry.		
2013 2014	<b>OVERHAUL OF THE COUNCIL'S WORKING PROCESS,</b> followed by development of its working model and adoption of more dynamic classification of processes for carrying on reactive and preventive dialogues.	<b>TIME LIMIT</b> imposed on reactive dialogues as of 2014.		

# MEMBERS OF THE ETHICAL COUNCIL

The Ethical Council had one member from each AP Fund in 2014. The Chairmanship, which rotates among the Funds, was held by the AP4 in 2014 and has been handed over to the AP1 for 2015. As of 2015, each Fund will appoint two members to the Council.



**LEFT TO RIGHT:** Ossian Ekdahl, Pia Axelsson, Lil Larås Lindgren, John Howchin, Christina Olivecrona, Peter Lundkvist, Arne Lööv, Ulrika Danielson, Nadine Viel Lamare

#### FIRST AP FUND

[www.ap1.se](http://www.ap1.se)

#### OSSIAN EKDAHL

Chairman  
and Spokesperson, 2015

#### NADINE VIEL LAMARE

#### SECOND AP FUND

[www.ap2.se](http://www.ap2.se)

#### ULRIKA DANIELSON

#### CHRISTINA OLIVECRONA

#### THIRD AP FUND

[www.ap3.se](http://www.ap3.se)

#### PETER LUNDKVIST

#### LIL LARÅS LINDGREN

#### FOURTH AP FUND

[www.ap4.se](http://www.ap4.se)

#### ARNE LÖÖV

#### PIA AXELSSON

#### ETHICAL COUNCIL

[www.ethicalcouncil.com](http://www.ethicalcouncil.com)

#### JOHN HOWCHIN

Secretary-General,  
Ethical Council