

PENSION FUND COMMITTEE – 25 JUNE 2010

SOCIALLY RESPONSIBLE INVESTMENT –TAR SANDS

Report by Head of Finance & Procurement

Introduction

1. Oxfordshire Pension Fund holds shares in BP and Royal Dutch Shell. At the 2010 AGM's for both companies, shareholders were asked to vote on a resolution which called for each company to provide a full report about the risks of planned tar sands development in Canada.
2. Tar sands (also known as oil sands) are deposits of sand and clay saturated with bitumen. They are found in large quantities in Canada. Campaigners argue that tar sands extraction is costly and damaging to the environment, and that the investment risks include doubts over whether oil prices will be high enough to justify the cost of converting tar sands into fuel. 'Fair-Pensions' and over 100 other shareholders, submitted a proposal requesting a report on the risks involved in the 'Sunrise' steam assisted gravity drainage oil sands operations in Canada.

Voting Policy

3. In accordance with the Pension Fund's Statement of Investment Principles, Oxfordshire Pension Fund Managers have been instructed to exercise the Pension Fund's voting rights in accordance with the guidance set by RiskMetric Group. However, in exceptional circumstances managers may vote differently to the RiskMetric Group guidance, if in their judgement this would be in the best interests of the fund. Where managers take a contrary view to the RiskMetric Group they must obtain permission from officers to vote differently. Fund Managers are required to report quarterly on action taken.
4. Following queries from fund members received via 'Fair Pensions', the Investment team asked those fund managers holding BP and Royal Dutch Shell shares about their engagement with the companies. The Fund Managers were asked to indicate their views on the resolutions prior to the release of the RiskMetrics recommendation. The views expressed by the Fund Managers and RiskMetrics are included in Annex 1.

Votes Exercised

5. Baillie Gifford and Alliance Bernstein voted inline with the RiskMetrics recommendation to support the management of BP and Royal Dutch Shell. Both Fund Managers voted against the resolution to commission a review of tar sands development.

Annual General Meeting – Resolution Vote Result

6. The BP AGM was held on 15 April 2010. 93.79% of shareholders voted against the resolution.
7. The Royal Dutch Shell AGM was held on 18 May 2010. 94.26% of shareholders voted against the resolution.

RECOMMENDATIONS

8. **The Committee is RECOMMENDED to receive the report and note the votes exercised.**

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May 2010

Vote recommendations for resolution to commission review of tar sand developments**Royal Dutch Shell****Baillie Gifford**

Baillie Gifford supported the management and decided to vote against the resolution for the following reasons:-

- As worded, the resolution requests that the company discloses the commercial considerations that it uses in evaluating the projects. We believe that the disclosure of commercially, and potentially politically sensitive, information may not be in the interests of shareholders.
- The company, in response to the resolution, has increased its disclosure.
- We believe the relevant data for understanding the potential social and environmental impacts of these projects, and the mitigation measures undertaken is available.
- The company has well established policies and processes in place to monitor and manage environmental and social risks, and reports extensively on these in its Annual Sustainability Report. It has a track record of good transparency and shareholder engagement.

We will continue our dialogue with the company about all the environmental, social and governance risks and opportunities it faces; risks related to oil sand projects and the opportunities associated with biofuels and carbon capture and storage, for example.

Baillie Gifford held 362,400 'A' shares in Royal Dutch Shell with a value of £6.398m at 26 May 2010. 427,171 'B' shares were held with a value of £7.229m at 26 May 2010.

Alliance Bernstein

Alliance Bernstein voted against the resolutions and provided the following comments:-

Oil produced from oil sands has an inherently larger carbon footprint than that from conventional sources, and is therefore subject to uncertainty surrounding future carbon taxation. It typically also has a larger local environmental impact, and is thus subject to remedial costs following extraction.

Nonetheless, our research indicates that oil sands are likely to prove economically viable, as well as strategically attractive as the largest source of incremental oil outside the Middle East. In general, we are satisfied with the availability of data on

this subject, and we note also that this is a relatively small part of both BP and Shell's businesses, accounting for less than 10% of earnings.

Since both our analysis and the work undertaken by BP and Shell themselves indicates that oil sands are an interesting opportunity, our current thinking suggests that commissioning an independent assessment of the business risks involved is likely to be superfluous and the costs and management time associated with such a report, as well as potential disclosure of confidential information, may make it unnecessarily burdensome.

Based on the information currently available, we do not therefore plan to support this resolution.

Alliance Bernstein held 218,800 shares in Royal Dutch Shell with a value of £3.759m at 26 May 2010.

Alliance Bernstein held 301,600 shares in BP with a value of £1.483m at 26 May 2010.

Risk Metrics Recommendation

BP

Risk Metrics recommended a vote against the resolution to 'approve that the audit committee or risk committee of the board commissions and reviews a report setting out the assumptions made by the company in planning to proceed with the Sunrise Project' because:-

- BP has recently increased disclosure which provides details including its oil price volatility estimates; its demand for oil scenario, consistent with the IEA's energy demand estimates; and has established a pricing estimate for carbon emissions for its projects.
- BP provides regular auditing and board review mechanisms for its projects and has committed to producing a Canadian sustainability report in 2011.
- BP's current disclosure is largely in line with its peer Royal Dutch Shell.

Royal Dutch Shell

Risk Metrics recommended a vote against the resolution because Shell has recently increased its disclosure specifically addressing many of the proponents' concerns. Specifically, Shell's 17 March 2010 comprehensive oil sands report provides details surrounding the viability of its oil sands operations, including assumptions and information on future carbon prices, oil price volatility, demand for oil, anticipated regulation of GHG emissions, and legal and reputational risks, all of which are largely in-line with its peer BP.