FlexShares® Trust

Statement of Additional Information

Dated March 1, 2019

This Statement of Additional Information (the “SAI”) is not a prospectus. It should be read in conjunction with the current prospectus (the “Prospectus”) for the following Funds of the FlexShares® Trust (the “Trust”) as such Prospectus may be revised or supplemented from time to time:

<table>
<thead>
<tr>
<th>Fund</th>
<th>Ticker</th>
<th>Stock Exchange</th>
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<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>TILT</td>
<td>Cboe BZX</td>
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<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>TLTD</td>
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<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
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<td>FlexShares® Disciplined Duration MBS Index Fund</td>
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<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
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<td>NASDAQ</td>
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<tr>
<td>FlexShares® High Yield Value-Scored Bond Index Fund</td>
<td>HYGV</td>
<td>NYSE Arca</td>
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The Prospectus for the Funds of the Trust included in this SAI is dated March 1, 2019. Capitalized terms used herein that are not defined have the same meanings as in the Prospectus, unless otherwise noted. Copies of the Prospectus may be obtained without charge by visiting www.flexshares.com, writing to FlexShares ETFs, c/o Foreside Fund Services, LLC, Three Canal Plaza, Portland, Maine 04101 or calling 1-855-FLEXETF (1-855-353-9383). FlexShares is a registered trademark of Northern Trust Investments, Inc. (“NTI” or the “Investment Adviser”).

The audited financial statements for the FlexShares® Morningstar US Market Factor Tilt Index Fund, FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Quality Dividend Index Fund, FlexShares® Quality Dividend Defensive Index Fund, FlexShares® Quality Dividend Dynamic Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund, FlexShares® International Quality Dividend Dynamic Index Fund, FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and related report of Deloitte & Touche LLP, an independent registered public accounting firm, contained in the annual report to those Funds’ shareholders for the fiscal period ended October 31, 2018 are incorporated herein by reference in the section entitled “Financial Statements.” No other parts of the annual report are incorporated by reference herein. Copies of the Trust’s Annual Report may be obtained upon request and without charge, by writing to FlexShares ETFs, c/o Foreside Fund Services, LLC, Three Canal Plaza, Suite 100, Portland, ME 04101 or by calling 1-855-FLEXETF (1-855-353-9383).

An investment in a Fund is not a deposit of any bank and is not insured or guaranteed by the Federal Deposit Insurance Corporation (“FDIC”), any other government agency or The Northern Trust Company (“NTNC”), its affiliates, subsidiaries or any other bank. An investment in a Fund involves investment risks, including possible loss of principal.
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GENERAL DESCRIPTION OF THE TRUST AND ITS FUNDS

The Trust was formed as a Maryland Statutory Trust on May 13, 2010, originally named NT ETF Trust, and renamed FlexShares® Trust as of April 12, 2011. The Trust is authorized to have multiple series or portfolios. The Trust is an open-end, management investment company, registered under the Investment Company Act of 1940, as amended (the “1940 Act”). The offering of the Trust’s shares is registered under the Securities Act of 1933, as amended (the “Securities Act”). This SAI relates to the following funds (each, a “Fund” and collectively, the “Funds”):

FlexShares® Morningstar US Market Factor Tilt Index Fund
FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund
FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund
FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund
FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund
FlexShares® US Quality Large Cap Index Fund
FlexShares® STOXX® US ESG Impact Index Fund
FlexShares® STOXX® Global ESG Impact Index Fund
FlexShares® Morningstar Global Upstream Natural Resources Index Fund
FlexShares® STOXX® Global Broad Infrastructure Index Fund
FlexShares® Global Quality Real Estate Index Fund
FlexShares® Real Assets Allocation Index Fund
FlexShares® Quality Dividend Index Fund
FlexShares® Quality Dividend Defensive Index Fund
FlexShares® Quality Dividend Dynamic Index Fund
FlexShares® International Quality Dividend Index Fund
FlexShares® International Quality Dividend Defensive Index Fund
FlexShares® International Quality Dividend Dynamic Index Fund
FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund
FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund
FlexShares® Disciplined Duration MBS Index Fund
FlexShares® Credit-Scored US Corporate Bond Index Fund
FlexShares® Credit-Scored US Long Corporate Bond Index Fund
FlexShares® High Yield Value-Scored Bond Index Fund

The FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund and FlexShares® Credit-Scored US Long Corporate Bond Index Fund are non-diversified funds. Each of the other Funds are diversified funds.

The investment objective of each Fund is to provide investment results that correspond generally to the price and yield performance, before fees and expenses, of a specified benchmark index (each an “Underlying Index”). Each Fund is managed by NTI, a subsidiary of Northern Trust Corporation.

Currently, the FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund seeks to achieve its investment objective by investing a substantial portion of its assets in the FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund (“TLTD” or an “Underlying Fund”), and the FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund seeks to achieve its investment objective by investing a substantial portion of its assets in the FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund (“TLTE” or an “Underlying Fund”).

The FlexShares® Real Assets Allocation Index Fund is a fund of funds and seeks its investment objective by investing primarily in shares of the underlying funds that are eligible for inclusion in the Underlying Index of the Fund, rather than in securities of individual companies. The underlying funds themselves seek investment results corresponding to their own respective underlying indexes. Currently, the Underlying Index is comprised of the FlexShares® Morningstar Global Upstream Natural Resources Index Fund, the FlexShares® Global Quality Real Estate Index Fund and the FlexShares® STOXX® Global Broad Infrastructure Index Fund (each an “Underlying Fund” and together with TLTD and TLTE, the “Underlying Funds”). Each Underlying Fund is managed by NTI, a subsidiary of Northern Trust Corporation.
The Funds offer and issue shares at their net asset value per share (“NAV”) only in aggregations of a specified number of shares (each, a “Creation Unit” or a “Creation Unit Aggregation”), generally in exchange for a specified basket of securities (the “Deposit Securities”), together with the deposit of a specified cash payment (the “Cash Component”). The shares of the Funds are listed and traded on the NYSE Arca, Inc. (“NYSE Arca”), with the exception of the FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund and FlexShares® Credit-Scored US Long Corporate Bond Index Fund which are listed on the NASDAQ Stock Market LLC (“NASDAQ”), and the FlexShares® Morningstar US Market Factor Tilt Index Fund and FlexShares® STOXX® US ESG Impact Index Fund which are listed on the Cboe BZX Exchange, Inc. (“Cboe BZX Exchange”), each a national securities exchange (the “Listing Exchange”). Shares trade in the secondary market and elsewhere at market prices that may be at, above or below NAV. Shares are redeemable only in Creation Unit Aggregations, and, generally, in exchange for portfolio securities and a Cash Component. The number of shares of a Creation Unit of each Fund are as follows:

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>NUMBER OF SHARES PER CREATION UNIT</th>
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<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
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<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
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The Trust reserves the right to offer a “cash” option for creations and redemptions of shares as more fully described in the “Purchase and Redemption of Creation Unit Aggregations” section of this SAI. Shares may be issued in advance of receipt of Deposit Securities subject to various conditions including a requirement to maintain on deposit with the Trust cash at least equal to 110%, which percentage NTI may change from time to time, of the market value of the missing Deposit Securities. See the “Purchase and Redemption of Creation Unit Aggregations” section of this SAI. In each instance of cash creations or redemptions, transaction fees may be imposed that will be higher than the transaction fees associated with in-kind creations or redemptions. In all cases, such conditions and fees will be limited in accordance with the requirements of the U.S. Securities and Exchange Commission (the “SEC”) applicable to management investment companies offering redeemable securities.
ADDITIONAL INVESTMENT INFORMATION

EXCHANGE LISTING AND TRADING

A discussion of exchange listing and trading matters associated with an investment in each Fund is contained in the Prospectus in the “Shareholder Information” section. The discussion below supplements, and should be read in conjunction with, that section of the Prospectus.

Shares of each Fund are listed for trading on at least one Listing Exchange, and trade throughout the day on the Listing Exchange and other secondary markets. In addition, certain Funds may be traded on certain foreign exchanges. There can be no assurance that the requirements of a Listing Exchange necessary to maintain the listing of shares of any Fund will continue to be met. A Listing Exchange may, but is not required to, remove the shares of a Fund from listing if: (1) following the initial twelve-month period beginning upon the commencement of trading of a Fund, there are fewer than fifty (50) record and/or beneficial holders of the Fund for thirty (30) or more consecutive trading days; (2) the value of the Underlying Index on which the Fund is based is no longer calculated or available; (3) the “indicative optimized portfolio value” (“IOPV”) of a Fund is no longer calculated or available; or (4) any other event shall occur or condition exist that, in the opinion of the Listing Exchange, makes further dealings on the Listing Exchange inadvisable. A Listing Exchange will remove the shares of a Fund from listing and trading upon termination of the Fund.

As in the case of other publicly-traded securities, brokers’ commissions on transactions will be based on negotiated commission rates at customary levels.

In order to provide additional information regarding the indicative value of shares of each Fund, a Listing Exchange disseminates every fifteen seconds, through the facilities of the Consolidated Tape Association, an updated IOPV for each Fund as calculated by an information provider or market data vendors. The Trust is not involved in or responsible for any aspect of the calculation or dissemination of the IOPVs, and makes no representation or warranty as to the accuracy of the IOPVs.

An IOPV has a securities value component and a cash component. The securities values included in an IOPV are the values of the Deposit Securities for the applicable Fund. While the IOPV reflects the current market value of the Deposit Securities required to be deposited in connection with the purchase of a Creation Unit Aggregation, it does not necessarily reflect the precise composition of the current portfolio of securities held by the applicable Fund at a particular point in time because the current portfolio of the Fund may include securities that are not a part of the Deposit Securities. Therefore, a Fund’s IOPV disseminated during the Listing Exchange trading hours should not be viewed as a real time update of the Fund’s NAV, which is calculated only once a day.

In addition to the securities component described in the preceding paragraph, the IOPV for each Fund includes a cash component consisting of estimated accrued interest, dividends and other income, less expenses as well as the value of the applicable currency hedges for the FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund and FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund. If applicable, the IOPV also reflects changes in currency exchange rates between the U.S. Dollar and the applicable foreign currency.

The Trust reserves the right to adjust the share prices of Funds in the future to maintain convenient trading ranges for investors. Any adjustments would be accomplished through stock splits or reverse stock splits, which would have no effect on the net assets of the applicable Fund.

INVESTMENT OBJECTIVE, STRATEGIES AND RISKS

The following supplements the information contained in the Prospectus concerning the investment objectives, strategies and risks of the Funds.

The investment objective of each Fund may be changed without shareholder approval. Except as expressly noted below, each Fund’s investment strategies may be changed without shareholder approval. In addition to the instruments discussed below and in the Prospectus, each Fund may purchase other types of financial instruments, however designated, whose investment and credit quality characteristics are determined by NTI to be substantially similar to those of any other investment otherwise permitted by a Fund’s investment strategies. Each Fund operates as an index fund and will not be actively managed. Adverse performance of a security in a Fund’s portfolio will ordinarily not result in the elimination of the security from a Fund’s portfolio. Each Fund generally will invest under normal circumstances at least 80% of its total assets in the securities of its Underlying Index (including indirect investments through the applicable Underlying Fund for the FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund and FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund) and, (i) with respect to the FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor
Tilt Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund, in American Depositary Receipts (“ADRs”) and Global Depositary Receipts (“GDRs”) (collectively “Depositary Receipts”) based on the securities in its Underlying Index, and (ii) with respect to the FlexShares® Disciplined Duration MBS Index Fund in “TBA Transactions” that represent securities in the Underlying Index. Most transactions in mortgage pass-through securities occur through standardized contracts for future delivery in which the exact mortgage pools to be delivered are not specified until a few days prior to settlement, referred to as a “to-be announced transaction” or “TBA Transaction.” To the extent consistent with its investment policies, each Fund may also invest up to 20% of its assets in cash and cash equivalents, including shares of money market funds advised by NTI or its affiliates, futures contracts, options on futures contracts, forward currency contracts, options and swaps, as well as securities not included in the Underlying Index, but which NTI believes will help the Fund track its Underlying Index.

NTI uses a representative sampling strategy to manage each Fund, other than the FlexShares® Real Assets Allocation Index Fund, FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund and FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund. However, each of these Funds reserves the right to use a replication indexing strategy if NTI determines that it is in the best interests of the Fund. With respect to the FlexShares® Real Assets Allocation Index Fund, FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund and FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, NTI generally intends to use a replication indexing strategy, but may use a representative sampling strategy under certain circumstances such as when it may not be possible or practicable to fully implement a replication strategy. “Representative sampling” is investing in a representative sample of securities that collectively has an investment profile similar to the Underlying Index. Securities selected are expected to have, in the aggregate, investment characteristics (based on factors such as market capitalization and industry weightings), fundamental characteristics (such as return variability, earnings valuation, duration, maturity and yield) and liquidity measures similar to those of the Underlying Index. A Fund may or may not hold all of the securities that are included in its Underlying Index. “Replication” is an indexing strategy in which a fund invests in substantially all of the securities in its underlying index in approximately the same proportions as in the underlying index.

Each Fund has adopted a non-fundamental investment policy in accordance with Rule 35d-1 under the 1940 Act to invest, under normal circumstances, at least 80% of the value of its net assets, plus the amount of any borrowings for investment purposes, in securities of the Fund’s Underlying Index and, with respect to (i) the FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund, in Depositary Receipts and (ii) the FlexShares® Disciplined Duration MBS Index Fund, in TBA Transactions that represent securities in the Underlying Index. Each Fund has also adopted a policy to provide its shareholders with at least 60 days’ prior written notice of any change in such policy. If, subsequent to an investment, the 80% requirement is no longer met, a Fund’s future investments will be made in a manner that will bring the Fund into compliance with this policy. For these purposes, “net assets” is measured at the time of purchase.

Because the FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund and FlexShares® Real Assets Allocation Index Fund invest in the Underlying Funds, the risks of investment in particular types of securities, instruments and portfolio management techniques discussed below may be borne by each Fund through its investment in the Underlying Funds, in addition to the risks associated with those securities, instruments and portfolio management techniques if the Fund invested in them or engaged in them directly.

**ASSET-BACKED (INCLUDING MORTGAGE-BACKED) SECURITIES.** The FlexShares® Disciplined Duration MBS Index Fund primarily invests in mortgage-backed securities, a type of asset-backed security that is backed by mortgages, and the FlexShares® Credit-Scored US Corporate Bond Index Fund and FlexShares® Credit-Scored US Long Corporate Bond Index Fund, to the extent consistent with their investment objectives, may invest in asset-backed securities, which are securities that are backed by mortgages, installment contracts, credit card receivables, municipal securities or other financial assets. The investment characteristics of asset-backed securities differ from those of traditional fixed-income securities. Asset-backed securities represent interests in “pools” of assets in which payments of both interest and principal on the securities are made periodically, thus in effect “passing through” such payments made by the individual borrowers on the assets that underlie the securities, net of any fees paid to the issuer or guarantor of the securities. The average life of asset-backed securities varies with the maturities of the underlying instruments, and the average life of a mortgage-backed instrument, in particular, is likely to be substantially less than the original maturity of the mortgage pools underlying the securities as a result of mortgage prepayments. For this and other reasons, an asset-
backed security normally is subject to both call risk and extension risk, and an asset-backed security’s stated maturity may be shortened. In addition, the security’s total return may be difficult to predict precisely. These differences can result in significantly greater price and yield volatility than is the case with traditional fixed-income securities.

If an asset-backed security is purchased at a premium, a prepayment rate that is faster than expected will reduce yield to maturity, while a prepayment rate that is slower than expected will have the opposite effect of increasing yield to maturity. Conversely, if an asset-backed security is purchased at a discount, faster than expected prepayments will increase, while slower than expected prepayments will decrease, yield to maturity. In calculating a Fund’s average weighted maturity, the maturity of asset-backed securities will be based on estimates of average life. Prepayments on asset-backed securities generally increase with falling interest rates and decrease with rising interest rates; furthermore, prepayment rates are influenced by a variety of economic and social factors. In general, the collateral supporting non-mortgage asset-backed securities is of shorter maturity than mortgage loans and is less likely to experience substantial prepayments.

There are a number of important differences among the agencies, instrumentalities and sponsored enterprises of the U.S. government that issue mortgage-related securities and among the securities that they issue. Mortgage-related securities guaranteed by the Government National Mortgage Association (“Ginnie Mae”) include Ginnie Mae Mortgage Pass-Through Certificates, which are guaranteed as to the timely payment of principal and interest by Ginnie Mae and backed by the full faith and credit of the United States, which means that the U.S. government guarantees that the interest and principal will be paid when due. Ginnie Mae is a wholly-owned U.S. government corporation within the Department of Housing and Urban Development. Ginnie Mae certificates also are supported by the authority of Ginnie Mae to borrow funds from the U.S. Treasury to make payments under its guarantee.

Mortgage-backed securities issued by the Federal National Mortgage Association (“Fannie Mae”) include Fannie Mae Guaranteed Mortgage Pass-Through Certificates, which are solely the obligations of Fannie Mae and are not backed by or entitled to the full faith and credit of the United States, except as described below, but are supported by the right of the issuer to borrow from the U.S. Treasury. Fannie Mae is a stockholder-owned corporation chartered under an Act of the U.S. Congress. Fannie Mae certificates are guaranteed as to timely payment of the principal and interest by Fannie Mae. Mortgage-related securities issued by the Federal Home Loan Mortgage Corporation (“Freddie Mac”) include Freddie Mac Mortgage Participation Certificates. Freddie Mac is a corporate instrumentality of the United States, created pursuant to an Act of Congress. Freddie Mac certificates are not guaranteed by the United States or by any Federal Home Loan Banks and do not constitute a debt or obligation of the United States or of any Federal Home Loan Bank. Freddie Mac certificates entitle the holder to timely payment of interest, which is guaranteed by Freddie Mac. Freddie Mac guarantees either ultimate collection or timely payment of all principal payments on the underlying mortgage loans. When Freddie Mac does not guarantee timely payment of principal, Freddie Mac may remit the amount due on account of its guarantee of ultimate payment of principal after default.

From time to time, proposals have been introduced before Congress for the purpose of restricting or eliminating federal sponsorship of Fannie Mae and Freddie Mac. The Trust cannot predict what legislation, if any, may be proposed in the future in Congress with regard to such sponsorship or which proposals, if any, might be enacted. Such proposals, if enacted, might materially and adversely affect the availability of government guaranteed mortgage-backed securities and the Fund’s liquidity and value.

There is risk that the U.S. government will not provide financial support to its agencies, authorities, instrumentalities or sponsored enterprises. A Fund may purchase U.S. government securities that are not backed by the full faith and credit of the United States, such as those issued by Fannie Mae and Freddie Mac. The maximum potential liability of the issuers of some U.S. government securities held by a Fund may greatly exceed their current resources, including their legal right to support from the U.S. Treasury. It is possible that these issuers will not have the funds to meet their payment obligations in the future.

The extreme and unprecedented volatility and disruption that impacted the capital and credit markets during late 2008 and into 2009 have led to increased market concerns about Freddie Mac’s and Fannie Mae’s ability to withstand future credit losses associated with securities held in their investment portfolios, and on which they provide guarantees, without the direct support of the federal government. On September 7, 2008, both Freddie Mac and Fannie Mae were placed under the conservatorship of the Federal Housing Finance Agency (“FHFA”). Under the plan of conservatorship, the FHFA has assumed control of, and generally has the power to direct, the operations of Freddie Mac and Fannie Mae, and is empowered to exercise all powers collectively held by their respective shareholders, directors and officers, including the power to: (1) take over the assets of and operate Freddie Mac and Fannie Mae with all the powers of the shareholders, the directors, and the officers of Freddie Mac and Fannie Mae and conduct all business of Freddie Mac and Fannie Mae; (2) collect all obligations and money due to Freddie Mac and Fannie Mae; (3) perform all functions of Freddie Mac and Fannie Mae which are consistent with the conservator’s appointment; (4) preserve and conserve the assets and property of Freddie Mac and Fannie Mae; and (5) contract for assistance in
fulfilling any function, activity, action or duty of the conservator. In addition, in connection with the actions taken by the FHFA, the U.S. Treasury Department (the “Treasury”) entered into certain preferred stock purchase agreements with each of Freddie Mac and Fannie Mae, which established the Treasury as the holder of a new class of senior preferred stock in each of Freddie Mac and Fannie Mae, which stock was issued in connection with financial contributions from the Treasury to Freddie Mac and Fannie Mae.

The conditions attached to the financial contribution made by the Treasury to Freddie Mac and Fannie Mae and the issuance of this senior preferred stock place significant restrictions on the activities of Freddie Mac and Fannie Mae. Freddie Mac and Fannie Mae must obtain the consent of the Treasury to among other things: (i) make any payment to purchase or redeem its capital stock or pay any dividend other than in respect of the senior preferred stock issued to the Treasury, (ii) issue capital stock of any kind, (iii) terminate the conservatorship of the FHFA except in connection with a receivership, or (iv) increase its debt beyond certain specified levels. In addition, significant restrictions are placed on the maximum size of each of Freddie Mac’s and Fannie Mae’s respective portfolios of mortgages and mortgage-backed securities, and the purchase agreements entered into by Freddie Mac and Fannie Mae provide that the maximum size of their portfolios of these assets must decrease by a specified percentage each year. The future status and role of Freddie Mac and Fannie Mae could be impacted by (among other things) the actions taken and restrictions placed on Freddie Mac and Fannie Mae by the FHFA in its role as conservator; the restrictions placed on Freddie Mac’s and Fannie Mae’s operations and activities as a result of the senior preferred stock investment made by the Treasury; market responses to developments at Freddie Mac and Fannie Mae; and future legislative and regulatory action that alters the operations, ownership, structure and/or mission of these institutions, each of which may, in turn, impact the value of, and cash flows on, any mortgage-backed securities guaranteed by Freddie Mac and Fannie Mae, including any such mortgage-backed securities held by the Funds.

There is a heightened risk that the receivables and loans underlying the asset-backed securities purchased by the Funds may suffer greater levels of default than has been historically experienced.

**BANK LOANS.** The FlexShares® High Yield Value-Scored Bond Index Fund may invest in bank loans. The primary risk in an investment in loans is that borrowers may be unable to meet their interest and/or principal payment obligations. Loans in which the Fund invests may be made to finance highly leveraged borrowers which may make such loans especially vulnerable to adverse changes in economic or market conditions. Loans in which the Fund may invest may be either collateralized or uncollateralized and senior or subordinate. Investments in uncollateralized and/or subordinate loans entail a greater risk of nonpayment than do investments in loans that hold a more senior position in the borrower’s capital structure and/or are secured with collateral. If they do provide collateral, the value of the collateral may not completely cover the borrower’s obligations at the time of a default. If a borrower files for protection from its creditors under the U.S. bankruptcy laws, these laws may limit the Fund’s rights to its collateral. In addition, the value of collateral may erode during a bankruptcy case. In the event of a bankruptcy, the holder of a loan may not recover its principal, may experience a long delay in recovering its investment and may not receive interest during the delay. In addition, loans are generally subject to liquidity risk. The Fund may acquire interests in loans by purchasing participations in and/or assignments of portions of loans from third parties. Transactions in loans may settle on a delayed basis. As a result, the proceeds from the sale of a loan may not be available to make additional investments or to meet the Fund’s redemption obligations.

In certain circumstances, loans may not be deemed to be securities under certain federal securities laws. Therefore, in the event of fraud or misrepresentation by a borrower or an arranger, lenders and purchasers of interests in loans, such as the Fund, may not have the protection of the anti-fraud provisions of the federal securities laws as would otherwise be available for bonds or stocks. Instead, in such cases, parties generally would rely on the contractual provisions in the loan agreement itself and common-law fraud protections under applicable state law.

**BONDS.** The FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund invest primarily in bonds. A bond is an interest-bearing security issued by a company, governmental unit or, in some cases, a non-U.S. public or private entity. The issuer of a bond has a contractual obligation to pay interest at a stated rate on specific dates and to repay principal (the bond’s face value) periodically or on a specified maturity date. An issuer may have the right to redeem or “call” a bond before maturity, in which case the investor may have to reinvest the proceeds at lower market rates. Most bonds bear interest income at a “coupon” rate that is fixed for the life of the bond. The value of a fixed rate bond usually rises when market interest rates fall, and falls when market interest rates rise. Accordingly, a fixed rate bond’s yield (income as a percent of the bond’s current value) may differ from its coupon rate as its value rises or falls. Other types of bonds bear income at an interest rate that is adjusted periodically. Because of their adjustable interest rates, the value of “floating-rate” or “variable-rate” bonds fluctuates much less in response to market interest rate movements than the value of fixed rate bonds. The Funds may treat some of these bonds as having a shorter maturity for purposes of calculating the weighted average maturity of its investment portfolio.
Bonds may be senior or subordinated obligations. Senior obligations generally have the first claim on a corporation’s earnings and assets and, in the event of liquidation, are paid before subordinated obligations. Bonds may be unsecured (backed only by the issuer’s general creditworthiness) or secured (also backed by specified collateral).

**CALCULATION OF PORTFOLIO TURNOVER RATE.** The portfolio turnover rate for the Funds is calculated by dividing the lesser of purchases or sales of portfolio investments for the reporting period by the monthly average value of the portfolio investments owned during the reporting period. The calculation excludes all securities whose maturities or expiration dates at the time of acquisition are one year or less. Portfolio turnover may vary greatly from year to year as well as within a particular year, and be affected by many different factors, including reconstitution or rebalancing of an Underlying Index, cash requirements for redemption of shares and by requirements that enable the Funds to receive favorable tax treatment. The portfolio turnover rate for the FlexShares® STOXX US ESG Impact Index Fund was significantly higher for the fiscal year ended October 31, 2018 than the prior fiscal year as a result of reconstitution or rebalancing of its Underlying Index and tax loss harvesting. The portfolio turnover rate for the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund was significantly lower for the fiscal year ended October 31, 2018 than the prior fiscal year as a result of lower turnover of component securities in connection with the rebalancings of its Underlying Index. The portfolio turnover rate for the FlexShares® Disciplined Duration MBS Index Fund was significantly higher for the fiscal year ended October 31, 2018 than the prior fiscal year as a result of higher turnover of component securities in connection with the rebalancings of the Fund’s Underlying Index due to rising interest rates. The FlexShares® Disciplined Duration MBS Index Fund’s use of TBA rolls may cause the Fund to experience higher portfolio turnover, higher transaction costs and to pay higher capital gain distributions to shareholders (which may be taxable) than other Funds that do not use TBA rolls.

**COMMERCIAL PAPER, BANKERS’ ACCEPTANCES, CERTIFICATES OF DEPOSIT, TIME DEPOSITS AND BANK NOTES.** To the extent consistent with their investment objective and strategies, the FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund may invest in commercial paper, bankers’ acceptances, certificates of deposit, time deposits and bank notes. Commercial paper represents short-term unsecured promissory notes issued in bearer form by banks or bank holding companies, corporations and finance companies. Certificates of deposit are negotiable certificates issued against funds deposited in a commercial bank for a definite period of time and earning a specified return. Bankers’ acceptances are negotiable drafts or bills of exchange, normally drawn by an importer or exporter to pay for specific merchandise, which are “accepted” by a bank, meaning, in effect, that the bank unconditionally agrees to pay the face value of the instrument on maturity. Fixed time deposits are bank obligations payable at a stated maturity date and bearing interest at a fixed rate. Fixed time deposits may be withdrawn on demand by the investor, but may be subject to early withdrawal penalties that vary depending upon market conditions and the remaining maturity of the obligation. There are no contractual restrictions on the right to transfer a beneficial interest in a fixed time deposit to a third party. Bank notes generally rank junior to deposit liabilities of banks and pari passu with other senior, unsecured obligations of the bank. Bank notes are classified as “other borrowings” on a bank’s balance sheet, while deposit notes and certificates of deposit are classified as deposits. Bank notes are not insured by the FDIC or any other insurer. Deposit notes are insured by the FDIC only to the extent of $250,000 per depositor per bank.

Each Fund may invest a portion of its assets in the obligations of foreign banks and foreign branches of domestic banks. Such obligations include Eurodollar Certificates of Deposit (“ECDs”), which are U.S. dollar-denominated certificates of deposit issued by offices of foreign and domestic banks located outside the United States; Eurodollar Time Deposits (“ETDs”), which are U.S. dollar-denominated deposits in a foreign branch of a U.S. bank or a foreign bank; Canadian Time Deposits (“CTDs”), which are essentially the same as ETDs except they are issued by Canadian offices of major Canadian banks; Schedule Bs, which are obligations issued by Canadian branches of foreign or domestic banks; Yankee Certificates of Deposit (“Yankee CDs”), which are U.S. dollar-denominated certificates of deposit issued by a U.S. branch of a foreign bank and held in the United States; and Yankee Bankers’ Acceptances (“Yankee BAs”), which are U.S. dollar denominated bankers’ acceptances issued by a U.S. branch of a foreign bank and held in the United States.

Commercial paper is generally unsecured and usually discounted from its value at maturity. The value of commercial paper may be affected by changes in the credit rating or financial condition of the issuing entities and will tend to fall when interest rates rise and rise when interest rates fall. Commercial paper purchased by the Funds may include asset-backed commercial paper. Asset backed commercial paper is issued by a special purpose entity that is organized to issue the commercial paper and to purchase trade receivables or other financial assets. The credit quality of asset-backed commercial paper depends primarily on the quality of these assets and the level of any additional credit support. The repayment of asset-backed commercial paper depends primarily on the cash collections received from such an issuer’s underlying asset portfolio and the issuer’s ability to issue new asset-backed commercial paper. Investments in commercial paper are subject to the risk that the issuer cannot issue
The value of convertible securities is a function of their investment value (determined by yield in comparison with the yields of other securities of comparable maturity and quality that do not have a conversion privilege) and their conversion value (their worth, at market value, if converted into the underlying common stock). The investment value of convertible securities is influenced by changes in interest rates, with investment value declining as interest rates increase and increasing as interest rates decline, and by the credit standing of the issuer and other factors. The conversion value of convertible securities is determined by the market price of the underlying common stock. If the conversion value is low relative to the investment value, the price of the convertible securities is governed principally by their investment value. To the extent the market price of the underlying common stock approaches or exceeds the conversion price, the price of the convertible securities will be increasingly influenced by their conversion value. In addition, convertible securities generally sell at a premium over their conversion value determined by the extent to which investors place value on the right to acquire the underlying common stock while holding fixed-income securities.

In addition, a convertible security may be subject to redemption at the option of the issuer at a price established in the convertible security’s governing instrument. If a convertible security held by a Fund is called for redemption, the Fund would be required to (i) permit the issuer to redeem the security, (ii) convert it into the underlying common stock or (iii) sell it to a third party. Any of the actions could have an adverse effect on the Fund’s ability to achieve its investment objective.
In general, investments in lower quality convertible securities are subject to a significant risk of a change in the credit rating or financial condition of the issuing entity. Investments in convertible securities of medium or lower quality also are likely to be subject to greater market fluctuation and to greater risk of loss of income and principal due to default than investments of higher quality fixed-income securities. Such lower quality securities generally tend to reflect short-term corporate and market developments to a greater extent than higher quality securities, which react more to fluctuations in the general level of interest rates.

**CYBER SECURITY ISSUES.** With the increased use of the Internet and because information technology (“IT”) systems and digital data underlie most of the Funds’ operations, the Funds and the Adviser, the Administrator, the Transfer Agent, the Distributor, Authorized Participants, and the Funds’ other service providers and the vendors of each (collectively “Service Providers”) are exposed to the risk that their operations and data may be compromised as a result of internal and external cyber-failures, breaches or attacks (“Cyber Risk”). This could occur as a result of malicious or criminal cyber-attacks. Cyber-attacks include actions taken to: (i) steal or corrupt data maintained online or digitally, (ii) gain unauthorized access to or release confidential information, (iii) shut down a Fund or Service Provider website through denial-of-service attacks, or (iv) otherwise disrupt normal business operations. However, events arising from human error, faulty or inadequately implemented policies and procedures or other systems failures unrelated to any external cyber-threat may have effects similar to those caused by deliberate cyber-attacks.

Successful cyber-attacks or other cyber-failures or events affecting the Funds or their Service Providers may adversely impact a Fund or its shareholders or cause your investment in the Fund to lose value. For instance, they may impact a Fund’s ability to calculate its NAV, cause the release of confidential Fund information, impede trading, or cause reputational damage. They could also subject the Funds or their Service Providers to regulatory fines, penalties or financial losses, reimbursement or other compensation costs, and/or additional compliance costs. Insurance protection and contractual indemnification provisions may not be available or may be insufficient to cover these losses. The Funds or their Service Providers may also incur significant costs to manage and control Cyber Risk.

Cyber Risks are also present for issuers of securities or other instruments in which the Funds invest, which could result in material adverse consequences for such issuers, and may cause the Funds’ investment in such issuers to lose value.

While the Investment Adviser, Service Providers or Authorized Participants may have established business continuity plans and risk management systems to prevent such cyber attacks, there are inherent limitations in such plans and systems, including the possibility that certain risks have not been identified or that cyber attacks may be highly sophisticated. The Funds and their shareholders could be negatively impacted as a result.

**DEPOSITORY RECEIPTS.** The FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund’s investment in securities of non-U.S. issuers may also be in the form of ADRs and/or GDRs based on the securities in its Underlying Index. ADRs are receipts that are traded in the United States evidencing ownership of the underlying foreign securities and are denominated in U.S. dollars. GDRs are receipts issued by a non-U.S. financial institution evidencing ownership of underlying foreign or U.S. securities and usually are denominated in foreign currencies. GDRs may not be denominated in the same currency as the securities they represent. Generally, GDRs are designed for use in the foreign securities markets.

In addition to investment risks associated with the underlying issuer, ADRs and GDRs expose a Fund to additional risk associated with non-uniform terms that apply to ADR and GDR programs, credit exposure to the depository bank and to the sponsors and other parties with whom the depository bank establishes the programs, currency and liquidity risk. Some institutions issuing ADRs and GDRs may not be sponsored by the issuer. Unsponsored programs generally expose investors to greater risks than sponsored programs and do not provide holders with many of the shareholder benefits that come from investing in a sponsored ADR or GDR. Available information concerning the issuer may not be as current as for sponsored ADRs and GDRs and the prices of unsponsored ADRs and GDRs may be more volatile than if such instruments were sponsored by the issuer. ADRs and GDRs are generally subject to the same risks as the foreign securities that they evidence or into which they may be converted.
To the extent a Fund invests in ADRs, such ADRs will be listed on a national securities exchange. To the extent a Fund invests in GDRs, such GDRs will be listed on a foreign exchange. A Fund will not invest in any unlisted Depositary Receipt, any Depositary Receipt that NTI deems to be illiquid or any Depositary Receipt for which pricing information is not readily available. Generally, all depositary receipts must be sponsored.

DISTRESSED COMPANIES SECURITIES RISK. The FlexShares® High Yield Value-Scored Bond Index Fund may invest in distressed debt securities, many of which are not publicly traded and may involve a substantial degree of risk. Debt obligations of distressed companies typically are unrated, lower-rated or close to default. Distressed debt securities include securities of companies that are in financial distress and that may be in or about to enter bankruptcy. In certain periods, there may be little or no liquidity in the markets for these securities. In addition, the prices of such securities may be subject to periods of abrupt and erratic market movements and above-average price volatility. It may be difficult to obtain financial information regarding the financial condition of a borrower or issuer, and its financial condition may change rapidly. It may be more difficult to value such securities and the spread between the bid and asked prices of such securities may be greater than expected. The Fund may lose a substantial portion or all of its investment in such securities or it may be required to accept cash or securities with a value less than the Fund’s original investment. The purchase of defaulted debt securities involves risks such as the possibility of complete loss of the investment where the issuer does not restructure to enable it to resume principal and interest payments. If the issuer of a security held by the Fund defaults, the Fund may experience a significant or complete loss on the security. Securities tend to lose much of their value before the issuer defaults. The Fund may incur additional expenses to the extent it is required to seek recovery upon a default in the payment of principal or interest on its portfolio holdings.

The Fund’s potential exposure to financially or operationally troubled issuers involves a high degree of credit and market risk, which may be heightened during an economic downturn or recession. Should an issuer of securities held by the Fund become involved in a bankruptcy proceeding, reorganization or financial restructuring, a wide variety of considerations make an evaluation of the outcome of the Fund’s exposure to the issuer uncertain.

During the period of a bankruptcy proceeding, reorganization or financial restructuring, it is unlikely that the Fund will receive any interest payments on the securities of the issuer. The Fund will be subject to significant uncertainty as to whether the reorganization or restructuring will be completed, and the Fund may bear certain extraordinary expenses to protect and recover its investment. The Fund will also be subject to significant uncertainty as to when and in what manner and for what value the obligations evidenced by the securities of the issuer held by the Fund will eventually be satisfied. Even if a plan of reorganization or restructuring is adopted with respect to the securities of the issuer held by the Fund, there can be no assurance that the securities or other assets received by the Fund in connection with such plan of reorganization or restructuring will not have a lower value or income potential than may have been anticipated or no value. The Fund may be unable to enforce its claims or rights in any collateral or may have its claims or security interest in any collateral challenged, disallowed or subordinated to the claims or security interests of other creditors. In addition, amendments to the U.S. Bankruptcy Code or other relevant laws could alter the expected outcome or introduce greater uncertainty regarding the outcome of the Fund’s securities holdings in the issuer. In a bankruptcy proceeding, a reorganization or restructuring, the securities of the issuer held by the Fund could be re-characterized or the Fund may receive different securities or other assets, including equity securities. These types of equity securities include, but are not limited to: common stock; preferred stock (including convertible preferred stock); bonds, notes and debentures convertible into common or preferred stock; stock purchase warrants and rights; equity interests in trusts; and depositary receipts. Equity securities are subject to changes in value, and their value may be more volatile than those of other asset classes. Holders of equity securities are subject to more risk than holders of debt securities because the status of equity holders is subordinate to debtholders in an issuer’s capital structure. The value of equity securities received by the Fund could decline if the financial condition of the issuer deteriorates or if overall market and economic conditions, or conditions within the issuer’s region or industry, deteriorate. Equity securities received by the Fund through a bankruptcy proceeding, reorganization or restructuring of an issuer would not be component securities of the Fund’s Underlying Index, which could subject the Fund to additional tracking error risk.

To the extent that the Fund receives other assets in connection with a bankruptcy proceeding, reorganization or financial restructuring, the Fund may also be subject to additional risks associated with the assets received. One example of assets that the Fund could receive is an interest in one or more loans made to the issuer as part of a workout agreed to by a consortium of lienholders and creditors of the issuer. The Fund may receive such interests in loans to the extent permitted by the 1940 Act.

Securities or other assets received in a reorganization or restructuring typically entail a higher degree of risk than investments in securities of issuers that have not undergone a reorganization or restructuring and may be subject to heavy selling or downward pricing pressure after completion of the reorganization or restructuring. The post-reorganization/restructuring assets and securities may also be illiquid and difficult to sell or value. If the Fund participates in negotiations with respect to a plan of...
restructuring or reorganizing with respect to securities of the issuer held by the Fund, the Fund also may be restricted from disposing such securities for a period of time. If the Fund becomes involved in such proceedings, the Fund may have more active participation in the affairs of the issuer than that assumed generally by an investor.

**EQUITY SWAPS, TOTAL RATE OF RETURN SWAPS, CURRENCY SWAPS AND INTEREST RATE SWAPS.**

Each of the Funds may invest up to 20% of its total assets in swap agreements if NTI believes that it will help the Fund track its Underlying Index. Swap agreements may be structured in different ways.

To the extent consistent with its investment policies, each of the Funds, other than the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund may enter into equity swap agreements to invest in a market without owning or taking physical custody of securities in circumstances in which direct investment is restricted for legal reasons or is otherwise impracticable. The counterparty to an equity swap agreement will typically be a bank, investment banking firm or broker/dealer. Equity swap agreements may be structured in different ways. For example, a counterparty may agree to pay a Fund the amount, if any, by which the notional amount of the equity swap agreement would have increased in value had it been invested in particular stocks (or an index of stocks), plus the dividends that would have been received on those stocks. In these cases, the Fund may agree to pay to the counterparty the amount, if any, by which that notional amount would have decreased in value had it been invested in the stocks. Therefore, the return to a Fund on any equity swap agreement should be the gain or loss on the notional amount plus dividends on the stocks less the interest paid by the Fund on the notional amount. In other cases, the counterparty and the Fund may each agree to pay the other the difference between the relative investment performances that would have been achieved if the notional amount of the equity swap agreement had been invested in different stocks (or indexes of stocks).

To the extent consistent with its investment policies, each Fund may enter into total rate of return swaps, which are contracts that obligate a party to pay or receive interest in exchange for the payment by the other party of the total return generated by a security, a basket of securities, an index or an index component. The FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund also may enter into equity swaps, which involve the exchange of the rights of a Fund and another party to make or receive payments in specific currencies. Currency swaps involve the exchange of rights of the Fund and another party to make or receive payments in specific currencies. Currency swaps involve the exchange of rights of the Fund and another party to make or receive payments in specific currencies.

The FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund and the FlexShares® Credit-Scored US Long Corporate Bond Index Fund may enter into interest rate swaps. Interest rate swaps involve the exchange by a Fund with another party of their respective commitments to pay or receive interest, e.g., an exchange of floating rate payments for fixed rate payments with a notional amount of principal.

Some swap transactions, such as interest rate and total return swaps, are entered into on a net basis, i.e., the two payment streams are netted out, with a Fund receiving or paying, as the case may be, only the net amount of the two payments. A Fund will enter into equity swaps only on a net basis. Payments may be made at the conclusion of the swap agreement or periodically during its term. These swaps do not involve the delivery of securities or other underlying assets. Accordingly, the risk of loss with respect to equity swaps is limited to the net amount of payments that a Fund is contractually obligated to make. If the other party to any swap entered into on a basis defaults, a Fund’s risk of loss consists of the net amount of payments that such Fund is contractually entitled to receive, if any. In contrast, other transactions may involve the payment of the gross amount owed. For example, currency swaps usually involve the delivery of the entire principal amount of one designated currency in exchange for the other designated currency. Therefore, the entire principal value of a currency swap is subject to the risk that the other party to the swap will default on its contractual delivery obligations. To the extent that the amount payable by a Fund under a swap is offset by segregated cash or liquid assets, the Fund and the Investment Adviser believe that such transactions do not constitute senior securities under the 1940 Act and, accordingly, will not treat them as being subject to a Fund’s borrowing restrictions. Provisions in the Dodd-Frank Act include new capital and margin requirements and the mandatory use of clearinghouse mechanisms for many over-the-counter derivatives transactions.
A Fund will not enter into any swap transactions unless the unsecured commercial paper, senior debt or claims-paying ability of the other party is rated either A, or A-1 or better by S&P Global Ratings (“S&P”), or Fitch Ratings (“Fitch”); or A or Prime-1 or better by Moody’s Investors Services, Inc. (“Moody’s”), or has received a comparable rating from another organization that is recognized as a nationally recognized statistical rating organization (“NRSRO”) or, if unrated by such rating organization, is determined to be of comparable quality by the Investment Adviser. If there is a default by the other party to a swap transaction, a Fund will have contractual remedies pursuant to the agreements related to the transaction. These contractual remedies, however, may be subject to bankruptcy and insolvency laws that may affect such Fund’s rights as a creditor (e.g., a Fund may not receive the net amount of payments that it is contractually entitled to receive). The swap market has grown substantially in recent years with a large number of banks and investment banking firms acting both as principals and as agents utilizing standardized swap documentation. As a result, the swap market has become relatively liquid in comparison with markets for other similar instruments which are traded in the interbank market.

The use of equity, total rate of return, currency and interest rate swaps is a highly specialized activity, which involves investment techniques and risks different from those associated with ordinary portfolio securities transactions. If the Investment Adviser is incorrect in its forecasts of market values, interest rates and/or currency exchange rates, the investment performance of a Fund would be less favorable than it would have been if this investment technique were not used. For a description of Commodity Futures Trading Commission (“CFTC”) regulations affecting swap transactions and certain other derivatives, see “Futures Contracts and Related Options” below and Appendix B.

Regulations that will begin to take effect in 2019 will require certain bank-regulated counterparties and certain of their affiliates to include in certain financial contracts, including many derivatives contracts, terms that delay or restrict the rights of counterparties, such as a Fund, to terminate such contracts, foreclose upon collateral, exercise other default rights or restrict transfers of credit support in the event that the counterparty and/or its affiliates are subject to certain types of resolution or insolvency proceedings. It is possible that these new requirements, as well as potential additional government regulation and other developments in the market, could adversely affect a Fund’s ability to terminate existing derivatives agreements or to realize amounts to be received under such agreements.

**FIXED INCOME SECURITIES.** The FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund will invest primarily in fixed income securities. Each of the other Funds may invest in fixed income securities up to 20% of its total assets to help track its Underlying Index. Fixed income securities, including corporate debt obligations, generally expose a Fund to the following types of risk: (1) interest rate risk (the potential for fluctuations in bond prices due to changing interest rates); (2) income risk (the potential for a decline in a Fund’s income due to falling market interest rates); (3) credit risk (the possibility that a bond issuer will fail to make timely payments of either interest or principal to a Fund); (4) prepayment risk or call risk (the likelihood that, during periods of falling interest rates, securities with high stated interest rates will be prepaid, or “called” prior to maturity, requiring a Fund to invest the proceeds at generally lower interest rates); and (5) extension risk (the likelihood that as interest rates increase, slower than expected principal payments may extend the average life of fixed income securities, which will have the effect of locking in a below-market interest rate, increasing the security’s duration and reducing the value of the security).

In periods of declining interest rates, the yield (income from a fixed income security held by a Fund over a stated period of time) of a fixed income security may tend to be higher than prevailing market rates, and in periods of rising interest rates, the yield of a fixed income security may tend to be lower than prevailing market rates. In addition, when interest rates are falling, the inflow of net new money to a Fund will likely be invested in portfolio instruments producing lower yields than the balance of a Fund’s portfolio, thereby reducing the yield of a Fund. In periods of rising interest rates, the opposite can be true. The NAV of a Fund can generally be expected to change as general levels of interest rates fluctuate. The value of fixed income securities in a Fund’s portfolio generally varies inversely with changes in interest rates. Prices of fixed income securities with longer effective maturities are more sensitive to interest rate changes than those with shorter effective maturities.

Corporate debt obligations generally offer less current yield than securities of lower quality, but lower-quality securities generally have less liquidity, greater credit and market risk, and as a result, more price volatility.

Conditions in the U.S. and many foreign economies have resulted, and may continue to result, in fixed income instruments experiencing unusual liquidity issues, increased price volatility and, in some cases, credit downgrades and increased likelihood of default. These events have reduced the willingness and ability of some lenders to extend credit, and have made it more difficult for borrowers to obtain financing on attractive terms, if at all. As a result, the values of many types of securities have been reduced. In addition, global economies and financial markets are becoming increasingly interconnected, which increases
the possibilities that conditions in one country or region might adversely impact issuers in a different country or region. The severity or duration of adverse economic conditions may also be affected by policy changes made by governments or quasi-governmental organizations. In addition, political events within the U.S. and abroad, such as the U.S. government’s recent inability to agree on a long-term budget and deficit reduction plan, the federal government shutdown and threats to not increase the federal government’s debt limit, may affect investor and consumer confidence and may adversely impact financial markets and the broader economy, perhaps suddenly and to a significant degree. High public debt in the U.S. and other countries creates ongoing systemic and market risks and policymaking uncertainty.

FOREIGN CURRENCY TRANSACTIONS. The FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund and FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund expect to engage in currency transactions for the purpose of hedging against declines in the value of assets that are denominated in non-U.S. currency. The Funds may also enter into non-U.S. currency forward and non-U.S. currency futures contracts to facilitate local securities settlements or to protect against currency exposure in connection with their distributions to shareholders. These Funds, however, do not expect to engage in currency transactions for purposes of hedging against declines in the value of a Fund’s assets that are denominated in a foreign currency.

None of the Funds expect to engage in currency transactions for speculative purposes.

Forward foreign currency exchange contracts involve an obligation to purchase or sell a specified currency at a future date at a price set at the time of the contract. Forward currency contracts do not eliminate fluctuations in the values of portfolio securities, but rather allow a Fund to establish a rate of exchange for a future point in time.

When entering into a contract for the purchase or sale of a security, a Fund may enter into a forward foreign currency exchange contract for the amount of the purchase or sale price to protect against variations, between the date the security is purchased or sold and the date on which payment is made or received, in the value of the foreign currency relative to the U.S. dollar or other foreign currency.

Each Fund may use non-deliverable forward currency contracts ("NDFs") to execute its hedging transactions. NDFs are cash-settled, short-term forward contracts that may be thinly traded or are denominated in non-convertible foreign currency, where the profit or loss at the time of settlement date is calculated by taking the difference between the agreed upon exchange rate and the spot rate at the time of settlement, for an agreed upon notional amount of funds. All NDFs have a fixing date and a settlement date. The fixing date is the date at which the difference between the prevailing market exchange rate and the agreed upon exchange rate is calculated. The settlement date is the date by which the payment of the difference is due to the party receiving payment. NDFs are commonly quoted for time periods ranging from one month to up to two years, and are normally quoted and settled in U.S. dollars. They are often used to gain exposure to and/or hedge exposure to foreign currencies that are not internationally traded.

Foreign currency forward contracts and NDFs are subject to regulation under The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") in the U.S. and under comparable regimes in Europe, Asia and other non-U.S. jurisdictions. Physically-settled forwards between eligible contract participants, such as the Fund, are generally subject to lighter regulation in the U.S. than NDFs and cash-settled foreign currency forward contracts. Under the Dodd-Frank Act, NDFs are regulated as swaps and are subject to rules requiring central clearing and mandatory trading on an exchange or facility that is regulated by the CFTC. NDFs traded in the over-the-counter market are subject to margin requirements, and initial margining requirements will be phased in through 2020. Implementation of the regulations regarding clearing, mandatory trading and margining of NDFs are likely to increase the cost to a Fund of hedging currency risk and, as a result, may affect returns to investors in such Fund.

With respect to any forward foreign currency contract, it generally will not be possible to match precisely the amount covered by that contract and the value of the securities involved due to the changes in the values of such securities resulting from market movements between the date the forward contract is entered into and the date it matures. In addition, while forward
contracts may offer protection from losses resulting from declines or appreciation in the value of a particular foreign currency, they also limit potential gains, which might result from changes in the value of such currency. A Fund also may incur costs in connection with forward foreign currency exchange contracts and conversions of foreign currencies and U.S. dollars.

Liquid assets equal to the amount of a Fund’s assets that could be required to consummate forward contracts will be segregated except to the extent the contracts are otherwise “covered.” The segregated assets will be valued at market or fair value. If the market or fair value of such assets declines, additional liquid assets will be segregated daily so that the value of the segregated assets will equal the amount of such commitments by the Fund. A forward contract to sell a foreign currency is “covered” if a Fund owns the currency (or securities denominated in the currency) underlying the contract, or holds a forward contract (or call option) permitting a Fund to buy the same currency at a price that is: (i) no higher than the Fund’s price to sell the currency; or (ii) greater than the Fund’s price to sell the currency provided the Fund segregates liquid assets in the amount of the difference. A forward contract to buy a foreign currency is “covered” if a Fund holds a forward contract (or call option) permitting the Fund to sell the same currency at a price that is: (i) as high as or higher than the Fund’s price to buy the currency; or (ii) lower than the Fund’s price to buy the currency provided the Fund segregates liquid assets in the amount of the difference.

As a result of regulatory requirements under the 1940 Act, the Funds are required to maintain an amount of liquid assets, accrued on a daily basis, having an aggregate value at least equal to the value of the Fund’s obligations under the foreign currency forward contract or NDF. To the extent that foreign currency forward contracts are settled on a physical basis, a Fund will generally be required to maintain an amount of liquid assets equal to the notional value of the contract. In connection with NDFs and cash-settled foreign currency forward contracts, on the other hand, which are performed on a net basis, with a Fund receiving or paying only the net amount of a specified exchange rate, a Fund will generally maintain liquid assets, accrued daily, equal to the accrued excess, if any, of the Fund’s obligations over those of its counterparty under the contract. Accordingly, reliance by a Fund on physically-settled foreign currency forward contracts may adversely impact investors by requiring the Fund to set aside a greater amount of liquid assets than would generally be required if the Fund were relying on cash-settled foreign currency forward contracts or NDFs.

Foreign currency transactions involve a significant degree of risk and the markets in which foreign currency transactions are effected are highly volatile, highly specialized and highly technical. Significant changes, including changes in liquidity and prices, can occur in such markets within very short periods of time, often within minutes. Foreign currency trading risks include, but are not limited to, exchange rate risk, counterparty risk, maturity gap, interest rate risk, and potential interference by foreign governments through regulation of local exchange markets, foreign investment or particular transactions in non-U.S. currency. If NTI utilizes foreign currency transactions at an inappropriate time or judges market conditions, trends or correlations incorrectly, foreign currency transactions may not serve their intended purpose of improving the correlation of a Fund’s return with the performance of its Underlying Index and may lower the Fund’s return. A Fund could experience losses if the value of its currency forwards, options or futures positions were poorly correlated with its other investments or if it could not close out its positions because of an illiquid market. In addition, a Fund could incur transaction costs, including trading commissions, in connection with certain non-U.S. currency transactions.

FOREIGN INVESTMENTS – GENERAL. The FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund and FlexShares® STOXX® Global Broad Infrastructure Index Fund will invest a significant portion of their assets, while the FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund (through its investments in its Underlying Funds), FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund may invest in U.S. dollar-denominated obligations issued or guaranteed by one or more foreign governments or any of their political subdivisions, agencies, instrumentalities or sponsored enterprises, as well as other foreign issuers. These obligations may be issued by supranational entities, including international organizations (such as the International Bank for Reconstruction and Development (also known as the World Bank)) and international banking institutions and related government agencies. The FlexShares® High Yield Value-Scored Bond Index Fund may invest in U.S. registered U.S. dollar dominated bonds of non-U.S. corporate issuers and U.S. dollar denominated bonds of non-U.S. corporate issuers offered pursuant to Rule 144A under the Securities Act of 1933, with or without registration rights.

Investment in foreign securities involves special risks. These include market risk, interest rate risk and the risks of investing in securities of foreign issuers and of companies whose securities are principally traded outside the United States on foreign exchanges or foreign over-the-counter markets and in investments denominated in foreign currencies. Market risk involves the possibility that security prices will decline over short or even extended periods. The markets tend to be cyclical, with periods
of generally rising prices and periods of generally declining prices. These cycles will affect the value of a Fund to the extent that it invests in foreign securities. In addition, the performance of investments in securities denominated in a foreign currency will depend on the strength of the foreign currency against the U.S. dollar and the interest rate environment in the country issuing the currency. Generally, the prices of bonds and debt securities fluctuate inversely with interest rate changes. Absent other events which could otherwise affect the value of a foreign security (such as a change in the political climate or an issuer’s credit quality), appreciation in the value of the foreign currency generally can be expected to increase the value of a foreign currency-denominated security in terms of U.S. dollars. A rise in foreign interest rates or decline in the value of the foreign currency relative to the U.S. dollar generally can be expected to depress the value of a foreign currency-denominated security.

There are other risks and costs involved in investing in foreign securities, which are in addition to the usual risks inherent in domestic investments. Investment in foreign securities involves higher costs than investment in U.S. securities, including higher transaction and custody costs as well as the imposition of additional taxes by foreign governments. Foreign investments also involve risks associated with the level of currency exchange rates, less complete financial information about the issuers, less market liquidity, more market volatility and political instability. Future political and economic developments, the possible imposition of withholding taxes on dividend income, the possible seizure or nationalization of foreign holdings, the possible establishment of exchange controls, or the adoption of other governmental restrictions might adversely affect an investment in foreign securities. Additionally, foreign banks and foreign branches of domestic banks are subject to less stringent reserve requirements, and to different accounting, auditing and recordkeeping requirements. Also, the legal remedies for investors may be more limited than the remedies available in the U.S. Additionally, many countries throughout the world are dependent on a healthy U.S. economy and are adversely affected when the U.S. economy weakens or its markets decline. For example, the decline in the U.S. subprime mortgage market quickly spread throughout global credit markets, triggering a liquidity crisis that affected fixed-income and equity markets around the world.

Although a Fund may invest in securities denominated in foreign currencies, its portfolio securities and other assets are valued in U.S. dollars. Currency exchange rates may fluctuate significantly over short periods of time causing, together with other factors, the Fund’s NAV to fluctuate as well. Currency exchange rates can be affected unpredictably by the intervention or the failure to intervene by U.S. or foreign governments or central banks, or by currency controls or political developments in the U.S. or abroad. To the extent that a Fund’s total assets, adjusted to reflect the Fund’s net position after giving effect to currency transactions, are denominated in the currencies of foreign countries, the Fund will be more susceptible to the risk of adverse economic and political developments within those countries.

Each Fund also is subject to the possible imposition of exchange control regulations or freezes on the convertibility of currency. In addition, through the use of forward currency exchange contracts or other instruments, any net currency positions of a Fund may expose it to risks independent of its securities positions. Although the net long and short foreign currency exposure of a Fund will not exceed its total asset value, to the extent that the Fund is fully invested in foreign securities while also maintaining currency positions, it may be exposed to greater risk than it would have if it did not maintain the currency positions.

Dividends and interest payable on a Fund’s foreign portfolio securities may be subject to foreign withholding taxes. To the extent such taxes are not offset by credits or deductions allowed to investors under U.S. federal income tax law, they may reduce the net return to the shareholders. A Fund’s income and, in some cases, capital gains from foreign stocks and securities will be subject to applicable taxation in certain of the countries in which it invests, and treaties between the U.S. and such countries may not be available in some cases to reduce the otherwise applicable tax rates. See “Taxes” on page 106.

Investors should understand that the expense ratio of a Fund that invests primarily in foreign securities can be expected to be higher than those Funds investing primarily in domestic securities. The costs attributable to investing abroad usually are higher for several reasons, such as the higher cost of investment research, higher costs of custody of foreign securities, higher commissions paid on comparable transactions on foreign markets and additional costs arising from delays in settlements of transactions involving foreign securities.

A Fund’s foreign securities are generally held outside the United States in the primary market for the securities in the custody of certain eligible foreign banks and trust companies, as permitted under the 1940 Act (“foreign sub-custodians”). Settlement practices for foreign securities may differ from those in the United States. Some countries have limited governmental oversight and regulation of industry practices, stock exchanges, depositories, registrars, brokers and listed companies, which increases the risk of corruption and fraud and the possibility of losses to a Fund. In particular, under certain circumstances, foreign securities may settle on a delayed delivery basis, meaning that a Fund may be required to make payment for securities before the Fund has actually received delivery of the securities or deliver securities prior to the receipt of payment. Typically, in these cases, the Fund will receive evidence of ownership in accordance with the generally accepted settlement practices in the local market entitling the Fund to deliver payment at a future date, but there is a risk that the security will not be delivered to the Fund or that
payment will not be received, although the Fund and its foreign sub-custodians take reasonable precautions to mitigate this risk. Foreign markets also have different clearance and settlement procedures, and in certain markets there have been times when settlements have been unable to keep pace with the volume of securities transactions, making it difficult to conduct such transactions. Such delays in settlement could result in temporary periods when a portion of the assets of a Fund remain uninvested and no return is earned on such assets. The inability of a Fund to make intended security purchases or sales due to settlement problems could result in missed attractive investment opportunities, losses to the Fund due to subsequent declines in value of the portfolio securities or, if the Fund has entered into a contract to sell the securities, possible liability to the purchaser. Losses can also result from lost, stolen or counterfeit securities; defaults by brokers and banks; failures or defects of the settlement system; or poor and improper record keeping by registrars and issuers.

Share blocking refers to a practice in certain foreign markets under which an issuer’s securities are blocked from trading at the custodian or sub-custodian level for a specified number of days before and, in certain instances, after a shareholder meeting where a vote of shareholders takes place. The blocking period can last up to several weeks. Share blocking may prevent a Fund from buying or selling securities during this period, because during the time shares are blocked, trades in such securities will not settle. It may be difficult or impossible to lift blocking restrictions, with the particular requirements varying widely by country.

The FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund (through its investments in its Underlying Funds), FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund may invest a significant percentage of their assets in the securities of issuers located in geographic regions with securities markets that are highly developed, liquid and subject to extensive regulation, including Europe and Japan. The FlexShares® High Yield Value-Scored Bond Index Fund may also invest in such issuers to the extent consistent with its investment objective and strategies. The Economic and Monetary Union of the European Union (“EU”) requires compliance with restrictions on inflation rates, deficits, interest rates, debt levels and fiscal and monetary controls, each of which may significantly affect every country in Europe. Decreasing imports or exports, changes in governmental or EU regulations on trade, changes in the exchange rate of the euro, the default or threat of default by an EU member country on its sovereign debt, and recessions in EU economies may have a significant adverse effect on the economies of EU member countries and their trading partners. The European financial markets have recently experienced volatility and adverse trends due to concerns about the rising government debt levels of several European countries, including Greece, Spain, Ireland, Italy and Portugal. Recent concerns over the level and sustainability of the sovereign debt of the United States have aggravated this volatility. A default or debt restructuring by any European country would adversely impact holders of that country’s debt and sellers of credit default swaps linked to that country’s creditworthiness, which may be located in countries other than those listed above. These events have adversely affected the value and exchange rate of the euro and may continue to significantly affect the economies of every country in Europe, including countries that do not use the euro and non-EU member countries.

Additionally, in June of 2016, the United Kingdom (the “UK”) approved a referendum to leave the EU, commonly referred to as “Brexit,” which sparked depreciation in the value of the British pound and heightened risk of continued worldwide economic volatility. Pursuant to Article 50 of the Treaty of Lisbon, the UK gave notice in March 2017 of its withdrawal from the EU and commenced negotiations on the terms of withdrawal. As of the date of this SAI, the UK is scheduled to withdraw from the EU on March 29, 2019. If no agreement is reached as to the terms of the UK’s exit from the EU prior to March 29, 2019 (“hard Brexit”), the negative impacts of Brexit may be exaggerated. Brexit (and in particular a hard Brexit) may cause significant market volatility and illiquidity, currency fluctuations, deterioration in economic activity, a decrease in business confidence, and increased likelihood of a recession in the UK. This may increase redemptions from a Fund that holds impacted securities. Market factors, such as the demand for particular portfolio securities, may also cause the price of certain portfolio securities to fall while the price of other securities rise or remain unchanged. It is unclear what the potential consequences may be.

The UK has one of the largest economies in Europe and is a major trading partner with the other EU countries and the United States. If implemented, Brexit might negatively affect the City of London’s economy, which is heavily dominated by financial services, as banks might be forced to move staff and comply with two separate sets of rules or lose business to banks in Continental Europe. In addition, Brexit would likely create additional economic stresses for the UK, including the potential for decreased trade, capital outflows, devaluation of the British pound, wider corporate bond spreads due to uncertainty, and declines in business and consumer spending as well as foreign direct investment. Further, the UK’s departure from the EU would potentially cause volatility within the EU, which could trigger prolonged economic downturns in certain European countries or spark additional member states to contemplate departing the EU (thereby exacerbating political instability in the region).
The growth of Japan’s economy has historically lagged that of its Asian neighbors and other major developed economies. The Japanese economy is heavily dependent on international trade and has been adversely affected by trade tariffs, other protectionist measures, competition from emerging economies and the economic conditions of its trading partners. Japan’s relations with its neighbors, particularly China, North Korea, South Korea and Russia, have at times been strained due to territorial disputes, historical animosities and defense concerns. Most recently, the Japanese government has shown concern over the increased nuclear and military activity by North Korea. Strained relations may cause uncertainty in the Japanese markets and adversely affect the overall Japanese economy in times of crisis. China has become an important trading partner with Japan, yet the countries’ political relationship has become strained. Should political tension increase, it could adversely affect the economy, especially the export sector, and destabilize the region as a whole. Japan is located in a part of the world that has historically been prone to natural disasters such as earthquakes, volcanoes and tsunamis and is economically sensitive to environmental events. Any such event, such as the major earthquake and tsunami which struck Japan in March 2011, could result in a significant adverse impact on the Japanese economy. Historically, Japan has been subject to unpredictable national politics and may experience frequent political turnover. Future political developments may lead to changes in policy that might adversely affect a Fund’s investments. In addition, the Japanese economy faces several concerns, including a financial system with large levels of nonperforming loans, over-leveraged corporate balance sheets, extensive cross-ownership by major corporations, a changing corporate governance structure, and large government deficits. The Japanese yen has fluctuated widely at times and any increase in its value may cause a decline in exports that could weaken the economy. Furthermore, Japan has an aging workforce. It is a labor market undergoing fundamental structural changes, as traditional lifetime employment clashes with the need for increased labor mobility, which may adversely affect Japan’s economic competitiveness. Japan also remains heavily dependent on oil imports, and higher commodity prices could therefore have a negative impact on the economy. Furthermore, Japanese corporations often engage in high levels of corporate leveraging, extensive cross-purchases of the securities of other corporations and are subject to a changing corporate governance structure.

FOREIGN INVESTMENTS – EMERGING MARKETS. The FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund and FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund (through its investment in its Underlying Fund) will invest primarily, and the FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund (through its investments in its Underlying Funds), FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund may invest in countries with emerging economies or securities markets. These countries are generally located in the Asia and Pacific regions, the Middle East, Eastern Europe, Central America, South America and Africa. Political and economic structures in many of these countries may be undergoing significant evolution and rapid development, and these countries may lack the social, political and economic stability characteristics of more developed countries. In general, the securities markets of these countries are less liquid, subject to greater price volatility, have smaller market capitalizations and have problems with securities registration and custody. As a result, the risks presented by investments in these countries are heightened. Additionally, settlement procedures in emerging countries are frequently less developed and reliable than those in the United States and may involve a Fund’s delivery of securities before receipt of payment for their sale. Settlement or registration problems may make it more difficult for a Fund to value its portfolio securities and could cause the Fund to miss attractive investment opportunities, to have a portion of its assets uninvested or to incur losses due to the failure of a counterparty to pay for securities the Fund has delivered or the Fund’s inability to complete its contractual obligations.

Unanticipated political, economic or social developments may affect the value of a Fund’s investments in emerging market countries and the availability to the Fund of additional investments in these countries. Some of these countries may have in the past failed to recognize private property rights and may have at times nationalized or expropriated the assets of private companies. There have been occasional limitations on the movements of funds and other assets between different countries. The small size and inexperience of the securities markets in certain of such countries and the limited volume of trading in securities in those countries may make a Fund’s investments in such countries illiquid and more volatile than investments in Japan or most Western European countries, and a Fund may be required to establish special custodial or other arrangements before making certain investments in those countries. There may be little financial or accounting information available with respect to issuers located in certain parts of such countries, and it may be difficult as a result to assess the value or prospects of an investment in such issuers.

In certain countries, there may be fewer publicly traded securities and the market may be dominated by a few issuers or sectors. Issuers and securities markets in such countries are not subject to as extensive and frequent accounting, financial and other reporting requirements or as comprehensive government regulations as are issuers and securities markets in the U.S. In particular, the assets and profits appearing on the financial statements of emerging country issuers may not reflect their financial position or results of operations in the same manner as financial statements for U.S. issuers. Substantially less information may be publicly available about emerging country issuers than is available about issuers in the United States.
Emerging country securities markets are typically marked by a high concentration of market capitalization and trading volume in a small number of issuers representing a limited number of industries, as well as a high concentration of ownership of such securities by a limited number of investors. The markets for securities in certain emerging countries are in the earliest stages of their development. Even the markets for relatively widely traded securities in emerging countries may not be able to absorb, without price disruptions, a significant increase in trading volume or trades of a size customarily undertaken by institutional investors in the securities markets of developed countries. The limited size of many of these securities markets can cause prices to be erratic for reasons apart from factors that affect the soundness and competitiveness of the securities issuers. For example, prices may be unduly influenced by traders who control large positions in these markets. Additionally, market making and arbitrage activities are generally less extensive in such markets, which may contribute to increased volatility and reduced liquidity of such markets. The limited liquidity of emerging country securities may also affect a Fund’s ability to accurately value its portfolio securities or to acquire or dispose of securities at the price and time it wishes to do so or in order to meet redemption requests.

Certain emerging market countries may have antiquated legal systems, which may adversely impact the Funds. For example, while the potential liability of a shareholder in a U.S. corporation with respect to acts of the corporation is generally limited to the amount of the shareholder’s investment, the notion of limited liability is less clear in certain emerging market countries. Similarly, the rights of investors in emerging market companies may be more limited than those of shareholders in U.S. corporations. In addition, the systems of corporate governance to which issuers in certain emerging countries are subject may be less advanced than the systems to which issuers located in more developed countries are subject, and therefore, shareholders of such issuers may not receive many of the protections available to shareholders of issuers located in more developed countries. These risks may be heightened in Russia.

Transaction costs, including brokerage commissions or dealer mark-ups, in emerging countries may be higher than in developed securities markets. In addition, existing laws and regulations are often inconsistently applied. As legal systems in emerging countries develop, foreign investors may be adversely affected by new or amended laws and regulations. In circumstances where adequate laws exist, it may not be possible to obtain swift and equitable enforcement of the law.

Certain emerging countries may restrict or control foreign investments in their securities markets. These restrictions may limit a Fund’s investment in those countries and may increase the expenses of the Fund. Certain emerging countries require governmental approval prior to investments by foreign persons or limit investment by foreign persons to only a specified percentage of an issuer’s outstanding securities or a specific class of securities which may have less advantageous terms (including price) than securities of the company available for purchase by nationals. In addition, the repatriation of both investment income and capital from emerging countries may be subject to restrictions which require governmental consents or prohibit repatriation entirely for a period of time. Even where there is no outright restriction on repatriation of capital, the mechanics of repatriation may affect certain aspects of the operation of a Fund. Custodial and/or settlement systems in emerging countries may not be fully developed. To the extent a Fund invests in emerging countries, Fund assets that are traded in those markets which have been entrusted to sub-custodians in those markets may be exposed to risks for which the sub-custodian will have no liability.

Emerging countries may be subject to a substantially greater degree of economic, political and social instability and disruption than more developed countries. This instability may result from, among other things, the following: (i) authoritarian governments or military involvement in political and economic decision making, including changes or attempted changes in governments through extra-constitutional means; (ii) social unrest associated with demands for improved political, economic or social conditions; (iii) internal insurgencies; (iv) hostile relations with neighboring countries; (v) ethnic, religious and racial disaffection or conflict; and (vi) the absence of developed legal structures governing foreign private investments and private property. A Fund’s investments can also be adversely affected by any increase in taxes or by political, economic or diplomatic developments.

A Fund may invest in former “east bloc” countries in Eastern Europe. Most Eastern European countries had a centrally planned, socialist economy for a substantial period of time. The governments of many Eastern European countries have more recently been implementing reforms directed at political and economic liberalization, including efforts to decentralize the economic decision-making process and move towards a market economy. However, business entities in many Eastern European countries do not have an extended history of operating in a market-oriented economy, and the ultimate impact of Eastern European countries’ attempts to move toward more market-oriented economies is currently unclear. In addition, any change in the leadership or policies of Eastern European countries may halt the expansion of or reverse the liberalization of foreign investment policies now occurring and adversely affect existing investment opportunities.
The economies of emerging countries may suffer from unfavorable growth of gross domestic product, rates of inflation and hyperinflation, capital reinvestment, resources, self-sufficiency and balance of payments. Many emerging countries have experienced in the past, and continue to experience, high rates of inflation. In certain countries inflation has at times accelerated rapidly to hyperinflationary levels, creating a negative interest rate environment and sharply eroding the value of outstanding financial assets in those countries. Other emerging countries, on the other hand, have recently experienced deflationary pressures and are in economic recessions.

The economies of many emerging countries are heavily dependent upon international trade and are accordingly affected by protective trade barriers and the economic conditions of their trading partners. In addition, the economies of some emerging countries are vulnerable to weakness in world prices for their commodity exports.

Risks related to currencies and corporate actions are also greater in emerging countries than in developed countries. For example, some emerging countries may have fixed or managed currencies that are not free-floatting against the U.S. dollar. Certain emerging countries may experience sudden and large adjustments in their currency, which can have a disruptive and adverse effect on foreign investors. Some emerging countries have a higher risk of currency devaluations, and some of these countries may experience sustained periods of high inflation or rapid changes in inflation rates which can have negative effects on a country’s economy and securities markets. There may be no significant foreign exchange market for certain currencies making it difficult for the Funds to engage in foreign currency transactions. Some emerging countries may impose restrictions on the free conversion of their currencies into foreign currencies, including the U.S. dollar. Corporate action procedures in emerging countries may be less reliable and have limited or no involvement by the depositories and central banks. Lack of standard practices and payment systems can lead to significant delays in payment.

Many emerging countries are highly dependent on foreign loans for their operations. There have been moratoria on, and refinancing of, repayments with respect to these loans. Some of the refinancings have imposed restrictions and conditions on the economies of such nations that have adversely affected their economic growth.

Investment exposure to China subjects a Fund to risks specific to China. China may be subject to considerable degrees of economic, political and social instability. China is a developing market and demonstrates significantly higher volatility from time to time in comparison to developed markets. The Chinese government has undertaken reform of economic and market practices and expansion of the sphere for private ownership of property in China. However, Chinese markets generally continue to experience inefficiency, volatility and pricing anomalies resulting from governmental influence, a lack of publicly available information and/or political and social instability. Internal social unrest or confrontations with other neighboring countries, including military conflicts in response to such events, may also disrupt economic development in China and result in a greater risk of currency fluctuations, currency convertibility, interest rate fluctuations and higher rates of inflation. Export growth continues to be a major driver of China’s rapid economic growth. Reduction in spending on Chinese products and services, institution of tariffs or other trade barriers, or a downturn in any of the economies of China’s key trading partners may have an adverse impact on the Chinese economy.

The Funds may be invested in issuers located in Central and South American countries. Many economies in Latin America have experienced high interest rates, economic volatility, inflation, currency devaluations and high unemployment rates. Any adverse economic event in one country can have a significant effect on other countries of this region. In addition, commodities (such as oil, gas and minerals) represent a significant percentage of the region’s exports and many economies in this region, are particularly sensitive to fluctuations in commodity prices.

Each of the FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund, FlexShares® International Quality Dividend Dynamic Index Fund and the FlexShares® Real Assets Allocation Index Fund (through its investments in its Underlying Funds) may be invested in issuers located in Russia. The Russian economy is heavily dependent on exports. Oil, natural gas, metals, and timber account for more than 80% of Russia’s exports. Therefore, Russia is vulnerable to fluctuations in world commodity prices and on the price and demand for these commodities and natural resources. Any changes in any of these sectors could have an adverse impact on the Russian economy. The Russian securities market is characterized by a limited volume of trading resulting in difficulty in obtaining accurate prices and trading. The Russian securities market, as compared to U.S. markets, has significant price volatility, less liquidity, a smaller market capitalization and a smaller number of traded securities. There is also little publicly-available information about issuers. Settlement, clearing and registration of securities transactions are subject to risks because of insufficient registration systems that may not be subject to effective government supervision. This may result in significant delays or problems in registering the transfer of shares. Ownership of shares in Russian companies is recorded
by companies themselves and by registrars instead of through a central registration system. It is possible that a Fund’s ownership rights could be lost through fraud or negligence. While applicable Russian regulations impose liability on registrars for losses resulting from their errors, it may be difficult for a Fund to enforce any rights it may have against the registrar or issuer of the securities in the event of loss of share registration. Adverse currency exchange rates are a risk and there is a lack of available currency hedging instruments. Investments in Russia may be subject to the risk of nationalization or expropriation of assets.

In addition, as a result of recent geopolitical events involving the Russian Federation, the United States, the European Union, and other countries have imposed sanctions on certain Russian individuals and Russian corporations. Additional broader sanctions may be imposed in the future. These sanctions, or even the threat of further sanctions, may result in the decline of the value and liquidity of Russian securities, a weakening of the ruble or other adverse consequences to the Russian economy. The sanctions could also result in Russia taking counter measures or retaliatory actions which may further impair the value and liquidity of Russian securities. These events could have a negative effect on the performance of the Funds. Compliance with each of these sanctions may impair the ability of the Funds to buy, sell, hold, receive, deliver or otherwise transact in the affected securities or other securities of such issuers. If it becomes impracticable or unlawful for the Funds to hold securities subject to, or otherwise affected by, sanctions, or if deemed appropriate by the Funds’ investment adviser, the Funds may prohibit in-kind deposits of the affected securities in connection with creation transactions and instead require a cash deposit, which may also increase the Funds’ transaction costs.

Also, if an affected security is included in a Fund’s Underlying Index, the Fund may, where practicable, seek to eliminate its holdings of the affected security by employing or augmenting its representative sampling strategy to seek to track the investment results of its Underlying Index. The increased use of a representative sampling strategy may increase the Fund’s tracking error risk. If the affected securities constitute a significant percentage of the Underlying Index, the Fund may not be able to effectively implement a representative sampling strategy, which may result in significant tracking error between the Fund’s performance and the performance of its Underlying Index.

Current or future sanctions may result in Russia taking counter measures or retaliatory actions, which may further impair the value and liquidity of Russian securities. These retaliatory measures may include the immediate freeze of Russian assets held by a Fund. In the event of such a freeze of any Fund assets, including depositary receipts, a Fund may need to liquidate non-restricted assets in order to satisfy any Fund redemption orders. The liquidation of Fund assets during this time may also result in the Fund receiving substantially lower prices for its securities.

These sanctions may also lead to changes in a Fund’s Underlying Index. Index Providers may remove securities from the Underlying Index or implement caps on the securities of certain issuers that have been subject to recent economic sanctions. In such an event, it is expected that the Fund will rebalance its portfolio to bring it in line with the Underlying Index as a result of any such changes, which may result in transaction costs and increased tracking error. These sanctions, the volatility that may result in the trading markets for Russian securities and the possibility that Russia may impose investment or currency controls on investors may cause a Fund to invest in, or increase the Fund’s investments in, depositary receipts that represent the securities of the Underlying Index or implement caps on the securities of certain issuers that have been subject to recent economic sanctions. In

FUTURES CONTRACTS AND RELATED OPTIONS. The FlexShares® Morningstar US Market Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® Quality Dividend Index Fund, FlexShares® Quality Dividend Defensive Index Fund, FlexShares® Quality Dividend Dynamic Index Fund, FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund each may invest up to 20% of its assets in U.S. futures contracts and the FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund may invest up to 20% of its assets in U.S. and foreign futures contracts if NTI believes that it will help the Fund track its Underlying Index. Each of these Funds may purchase and sell call and put options on futures contracts. These futures contracts and options will be used to simulate full investment in the respective Underlying Index, to facilitate trading or to reduce transaction costs. Each of these Funds will only enter into futures contracts and options on futures contracts that are traded on a U.S. or foreign exchange, as applicable. No Fund will use futures or options for speculative purposes.

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The Trust, on behalf of each Fund, has claimed an exclusion from the definition of the term “commodity pool operator” (“CPO”) under the Commodity Exchange Act, and, therefore, is not subject to registration or regulation as a commodity pool operator under that Act. The Investment Adviser is not subject to registration or regulations as a commodity pool operator with respect to the Funds under the Commodity Exchange Act. As a result, each Fund is limited in its ability to trade instruments subject to the CFTC’s jurisdiction, including commodity futures (which include futures on broad-based securities indexes, interest rate futures and currency futures), options on commodity futures, certain swaps or other investments (whether directly or indirectly through investments in other investment vehicles).

Under this exclusion, each Fund must satisfy one of the following two trading limitations whenever it enters into a new commodity trading position: (1) the aggregate initial margin and premiums required to establish the Fund’s positions in CFTC-regulated instruments may not exceed 5% of the liquidation value of the Fund’s portfolio (after accounting for unrealized profits and unrealized losses on any such investments); or (2) the aggregate net notional value of such instruments, determined at the time the most recent position was established, may not exceed 100% of the liquidation value of the Fund’s portfolio (after accounting for unrealized profits and unrealized losses on any such positions). The Fund would not be required to consider its exposure to such instruments if they were held for “bona fide hedging” purposes, as such term is defined in the rules of the CFTC. In addition to meeting one of the foregoing trading limitations, the Fund may not market itself as a commodity pool or otherwise as a vehicle for trading in the markets for CFTC-regulated instruments.

The Funds will engage in transactions in futures contracts and related options only to the extent such transactions are consistent with the requirement of the Internal Revenue Code of 1986, as amended (the “Code”), for maintaining their qualifications as regulated investment companies for federal income tax purposes.

Participation in foreign futures and foreign options transactions involves the execution and clearing of trades on or subject to the rules of a foreign board of trade. Neither the National Futures Association (the “NFA”) nor any domestic exchange regulates activities of any foreign boards of trade, including the execution, delivery and clearing of transactions, or has the power to compel enforcement of the rules of a foreign board of trade or any applicable foreign law. This is true even if the exchange is formally linked to a domestic market so that a position taken on the market may be liquidated by a transaction on another market. Moreover, such laws or regulations will vary depending on the foreign country in which the foreign futures or foreign options transaction occurs. For these reasons, persons who trade foreign futures or foreign options contracts may not be afforded certain of the protective measures provided by the Commodity Exchange Act, the CFTC regulations and the rules of the NFA and any domestic exchange, including the right to use reparations proceedings before the CFTC and arbitration proceedings provided them by the NFA or any domestic futures exchange. In particular, a Fund’s investments in foreign futures or foreign options transactions may not be provided the same protections in respect of transactions on United States futures exchanges. In addition, the price of any foreign futures or foreign options contract may be affected by any variance in the foreign exchange rate between the time an order is placed and the time it is liquidated, offset or exercised.

Provisions in the Dodd-Frank Act include new capital and margin requirements and the mandatory use of clearinghouse mechanisms for many over-the-counter derivatives transactions. In connection with a Fund’s position in a futures contract or related option, the Fund will segregate liquid assets or will otherwise cover its position in accordance with applicable SEC requirements.

For a further description of futures contracts and related options, see Appendix B to this SAI.

**HEDGING.** The FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund and the FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund will, and each of the other Funds may, engage in hedging. Hedging is a strategy in which a derivative is used to offset the risks associated with other Fund holdings. Losses on the other investment may be substantially reduced by gains on a derivative that reacts in an opposite manner to market movements. While hedging can reduce losses, it can also reduce or eliminate gains or cause losses if the market moves in a manner different from that anticipated by the Fund or if the cost of the derivative outweighs the benefit of the hedge. Hedging also involves correlation risk, i.e., the risk that changes in the value of the derivative will not match those of the holdings being hedged as expected by the Fund, in which case any losses on the holdings being hedged may not be reduced or may be increased. In connection with its trading in foreign currency forward contracts, a Fund will contract with a foreign or domestic bank, or foreign or domestic securities dealer, to make or take future delivery of a specified amount of a particular currency. There are no limitations on daily price moves in such foreign currency forward contracts, and banks and dealers are not required to continue to make markets in such contracts. There have been periods during which certain banks or dealers have refused to quote prices for such foreign currency forward contracts or have quoted prices with an unusually wide spread between the price at which the bank or dealer is prepared to buy and that at which it is prepared to sell. Governmental imposition of credit controls might limit any such foreign currency forward contract trading. With respect to their trading of foreign currency forward contracts, if any, a Fund will be subject to the risk of bank or
ILLIQUID OR RESTRICTED SECURITIES. Illiquid securities generally are any securities that cannot be disposed of promptly and in the ordinary course of business within seven days at approximately the amount at which a Fund has valued the securities. To the extent consistent with its investment policies, each Fund may invest up to 15% of its net assets in securities that are illiquid. In the event that a subsequent change in net assets or other circumstances cause a Fund to exceed this limitation, the Fund will take steps to bring the aggregate amount of liquid securities within the limitations as soon as reasonably practicable. Each Fund may purchase securities that are not registered under the Securities Act but can be sold to “qualified institutional buyers” in accordance with Rule 144A under the Securities Act (“Rule 144A Securities”). These securities will not be considered illiquid so long as the Investment Adviser determines, under guidelines approved by the Trust’s Board of Trustees (the “Board”), that an adequate trading market exists. This practice could increase the level of illiquidity for Rule 144A Securities during any period that qualified institutional buyers become uninterested in purchasing these securities. Under guidelines approved by the Board, the Investment Adviser monitors the liquidity of such securities and may consider a number of factors set forth in the guidelines to determine whether an adequate trading market exists. If an adequate trading market does not exist, the securities will be considered to be illiquid.

INFLATION-INDEXED SECURITIES. The FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund and FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund will invest most of their assets in U.S. Treasury Inflation-Protected Securities (“TIPS”).

Inflation-indexed securities issued by the U.S. Treasury have varying maturities and pay interest on a semiannual basis equal to a fixed percentage of the inflation-adjusted principal amount. If the periodic adjustment rate measuring inflation falls, the principal value of inflation-indexed bonds will be adjusted downward, and consequently the interest payable on these securities (calculated with respect to a smaller principal amount) will be reduced. Repayment of the original bond principal upon maturity (as adjusted for inflation) is guaranteed in the case of U.S. Treasury inflation-indexed bonds, even during a period of deflation. However, the current market value of the bonds is not guaranteed and will fluctuate. A Fund also may invest in other inflation-related bonds which may or may not provide a similar guarantee. If a guarantee of principal is not provided, the adjusted principal value of the bond repaid at maturity may be less than the original principal amount.

The value of inflation-indexed bonds is expected to change in response to changes in real interest rates. Real interest rates in turn are tied to the relationship between nominal interest rates and the rate of inflation. Therefore, if the rate of inflation rises at a faster rate than nominal interest rates, real interest rates might decline, leading to an increase in value of inflation-indexed bonds. In contrast, if nominal interest rates increase at a faster rate than inflation, real interest rates might rise, leading to a decrease in value of inflation-indexed bonds. Any increase in the principal amount of an inflation-indexed bond will be considered taxable ordinary income, even though investors do not receive their principal until maturity.

While these securities are expected to be protected from long-term inflationary trends, short-term increases in inflation may lead to a decline in value. If interest rates rise due to reasons other than inflation, investors in these securities may not be protected to the extent that the increase is not reflected in the bond’s inflation measure.

The periodic adjustment of U.S. inflation-indexed bonds is tied to the Consumer Price Index for Urban Consumers (“CPI-U”), which is calculated monthly by the U.S. Bureau of Labor Statistics. The CPI-U is a measurement of changes in the cost of living, made up of components such as housing, food, transportation and energy. There can be no assurance that the CPI-U will accurately measure the real rate of inflation in the prices of goods and services.

The taxation of inflation-indexed Treasury securities is similar to the taxation of conventional bonds. Both interest payments and the difference between original principal and the inflation-adjusted principal will be treated as interest income subject to taxation. Interest payments are taxable when received or accrued. The inflation adjustment to the principal is subject to tax in the year the adjustment is made, not at maturity of the security when the cash from the repayment of principal is received. If an upward adjustment has been made (which typically should happen), investors in non-tax-deferred accounts will pay taxes on this amount currently. Decreases in the indexed principal can be deducted only from current or previous interest payments reported as income. Inflation-indexed Treasury securities therefore have a potential cash flow mismatch to an investor, because investors must pay taxes on the inflation-adjusted principal before the repayment of principal is received. It is possible that, particularly for...
high income tax bracket investors, inflation-indexed Treasury securities would not generate enough income in a given year to cover the tax liability they could create. This is similar to the current tax treatment for zero-coupon bonds and other discount securities. If inflation-indexed Treasury securities are sold prior to maturity, capital losses or gains are realized in the same manner as traditional bonds. The FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund and FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, however, generally distribute income on a monthly basis. Investors in the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund and FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund will receive dividends that represent both the interest payments and the principal adjustments of the inflation-indexed securities held in the Funds.

INVESTMENT COMPANIES. With respect to the investments of the Funds in the securities of other investment companies, such investments will be limited so that, as determined after a purchase is made, either: (a) not more than 3% of the total outstanding stock of such investment company will be owned by a Fund, the Trust as a whole and its affiliated persons (as defined in the 1940 Act); or (b) (i) not more than 5% of the value of the total assets of a Fund will be invested in the securities of any one investment company; (ii) not more than 10% of the value of its total assets will be invested in the aggregate securities of investment companies as a group; and (iii) not more than 3% of the outstanding voting stock of any one investment company will be owned by the Fund. These limits will not apply to the investment of uninvested cash balances in shares of registered or unregistered money market funds whether affiliated or unaffiliated. The foregoing exemption, however, only applies to an unregistered money market fund that: (i) limits its investments to those in which a money market fund may invest under Rule 2a-7 of the 1940 Act; and (ii) undertakes to comply with all the other provisions of Rule 2a-7.

Investments by the Funds in other investment companies, including exchange-traded funds (“ETFs”), will be subject to the limitations of the 1940 Act except as permitted by SEC orders.

To the extent consistent with its investment policies, each Fund may invest in the other exchange-traded funds managed by NTI. To the extent that a Fund invests in other exchange-traded funds managed by NTI, it will be subject to the risks associated with investing in such funds.

Certain investment companies whose securities are purchased by the Funds may not be obligated to redeem such securities in an amount exceeding 1% of the investment company’s total outstanding securities during any period of less than 30 days. Therefore, such securities that exceed this amount may be illiquid.

If required by the 1940 Act, each Fund expects to vote the shares of other investment companies that are held by it in the same proportion as the vote of all other holders of such securities.

A Fund may adhere to other limitations with respect to its investments in securities issued by other investment companies if required or permitted by the SEC or deemed to be in the best interests of the Trust.

MONEY MARKET FUNDS INVESTMENTS. Certain money market funds in which the Funds may invest, including certain money market mutual funds managed by the Investment Adviser, must calculate their net asset value per share to the nearest 0.01%, which produces fluctuations in the shares’ value in response to small changes in market values. Because the share price of these money market funds will fluctuate, when a Fund sells its shares they may be worth more or less than what the Fund originally paid for them. A Fund could also lose money if the money market fund holds defaulted securities or as a result of adverse market conditions. These money market funds may impose a fee (“liquidity fee”) upon the redemption of their shares or may temporarily suspend the ability to redeem shares if the money market fund’s liquidity falls below the required minimums because of market conditions or other factors.

Funds may also invest in money market funds that invest at least 99.5% of their assets in U.S. government securities (“government money market funds”). Government money market funds may seek to maintain a stable price of $1.00 per share and are generally not permitted to impose liquidity fees or temporarily suspend redemptions. However, government money market funds typically offer materially lower yields than other money market funds with fluctuating share prices. A Fund could lose money invested in a government money market fund. An investment in a money market fund, including a government money market fund, is not insured or guaranteed by the Federal Deposit Insurance Corporation (“FDIC”) or any other government agency. A money market fund’s sponsor has no legal obligation to provide financial support to the money market fund, and you should not expect that the sponsor or any person will provide financial support to a money market fund at any time.

In addition to the fees and expenses that a Fund directly bears, the Fund indirectly bears the fees and expenses of any money market funds in which it invests, including affiliated money market funds. By investing in a money market fund, a Fund will be exposed to the investment risks of the money market fund in direct proportion to such investment.

INVESTMENTS IN UNDERLYING FUNDS. Each Underlying Fund of the FlexShares® Currency Hedged
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The FlexShares® STOXX® Global Broad Infrastru
the Funds that are convertible into a larger number of publicly traded (publicly traded) units for an initial period and then only converting to common if certain financial tests are met. As a motivatio

Participation interests acquired by the FlexShares® High Yield Value-Scored Bond Index Fund may take the form of a direct or co-lending relationship with the corporate borrower, an assignment of an interest in the loan by a co-lender or another participant, or a participation in the seller’s share of the loan. When the Fund acts as co-lender in connection with a participation interest or when the Fund acquires certain participation interests, the Fund will have direct recourse against the borrower if the borrower fails to pay scheduled principal and interest. In cases where the Fund lacks direct recourse, it will look to the agent bank to enforce appropriate credit remedies against the borrower. In these cases, the Fund may be subject to delays, expenses and risks that are greater than those that would have been involved if the Fund had purchased a direct obligation (such as commercial paper) of such borrower. For example, in the event of the bankruptcy or insolvency of the corporate borrower, a loan participation may be subject to certain defenses by the borrower as a result of improper conduct by the agent bank. Moreover, under the terms of the loan participation, the Fund may be regarded as a creditor of the agent bank (rather than of the underlying corporate borrower), so that the Fund also may be subject to the risk that the agent bank may become insolvent. The secondary market, if any, for these loan participations is limited and any loan participations purchased by the Fund normally will be regarded as illiquid.

MASTER LIMITED PARTNERSHIPS. The FlexShares® STOXX® Global Broad Infrastructure Index Fund (which is also an Underlying Fund of the FlexShares® Real Assets Allocation Index Fund) may invest in equity securities of master limited partnerships (“MLPs”) and their affiliates. An MLP generally has two classes of partners, the general partner and the limited partners. The general partner normally controls the MLP through an equity interest plus units that are subordinated to the common (publicly traded) units for an initial period and then only converting to common if certain financial tests are met. As a motivation for the general partner to successfully manage the MLP and increase cash flows, the terms of most MLPs typically provide that any additional distributions with respect to these units are subordinated to the distributions with respect to the common units.
MLP common units represent an equity ownership interest in a partnership, providing limited voting rights and entitling the holder to a share of the company’s success through distributions and/or capital appreciation. Unlike shareholders of a corporation, common unit holders do not elect directors annually and generally have the right to vote only on certain significant events, such as mergers, a sale of substantially all of the assets, removal of the general partner or material amendments to the partnership agreement. MLPs are required by their partnership agreements to distribute a large percentage of their current operating earnings. Common unit holders generally have first right to a minimum quarterly distribution prior to distributions to the convertible subordinated unit holders or general partner (including incentive distributions). Common unit holders typically have arrearage rights if the minimum quarterly distribution is not met. In the event of liquidation, MLP common unit holders have first right to the partnership’s remaining assets after bondholders, other debt holders, and preferred unit holders have been paid in full. MLP common units trade on a national securities exchange or over-the-counter. Some limited liability companies (“LLCs”) may be treated as MLPs for federal income tax purposes. Similar to MLPs, LLCs typically do not pay federal income tax at the entity level and are required by their operating agreements to distribute a large percentage of their current operating earnings. In contrast to MLPs, LLCs have no general partner and there are no incentives that entitle management or other unit holders to increased percentages of cash distributions as distributions reach higher target levels. In addition, LLC common unit holders typically have voting rights with respect to the LLC, whereas MLP common units have limited voting rights. MLP common units and other equity securities can be affected by macro-economic and other factors affecting the stock market in general, expectations of interest rates, investor sentiment toward MLPs or a MLP’s business sector, changes in a particular issuer’s financial condition, or unfavorable or unanticipated poor performance of a particular issuer (in the case of MLPs, generally measured in terms of distributable cash flow). Prices of common units of individual MLPs and other equity securities can also be affected by fundamentals unique to the partnership or company, including earnings power and coverage ratios.

MLP convertible subordinated units are typically issued by MLPs to founders, corporate general partners of MLPs, entities that sell assets to the MLP, and institutional investors, and may be purchased in direct placements from such persons. The purpose of the convertible subordinated units is to increase the likelihood that during the subordination period there will be available cash to be distributed to common unit holders. Convertible subordinated units generally are not entitled to distributions until holders of common units have received specified minimum quarterly distributions, plus any arrearages, and may receive less in distributions upon liquidation. Convertible subordinated unit holders generally are entitled to a minimum quarterly distribution prior to the payment of incentive distributions to the general partner, but are not entitled to arrearage rights. Therefore, they generally entail greater risk than MLP common units. They are generally convertible automatically into the senior common units of the same issuer at a one-to-one ratio upon the passage of time or their satisfaction of certain financial tests. These units do not trade on a national exchange or over-the-counter, and there is no active market for convertible subordinated units. The value of a convertible security is a function of its worth if converted into the underlying common units. Convertible subordinated units generally have similar voting rights to MLP common units. Because convertible subordinated units generally convert to common units on a one-to-one ratio, the price that the Fund could be expected to pay upon the purchase or to realize upon resale is generally tied to the common unit price less a discount. The size of the discount varies depending on a variety of factors including the likelihood of conversion, and the length of time remaining to conversion, and the size of the block purchased.

MLP I-Shares represent an indirect investment in MLP I-units. I-units are equity securities issued to affiliates of MLPs, typically a limited liability company, that own an interest in and manage the MLP. The issuer has management rights but is not entitled to incentive distributions. The I-Share issuer’s assets consist exclusively of MLP I-units. Distributions by MLPs to I-unit holders are made in the form of additional I-units, generally equal in amount to the cash received by common unit holders of MLPs. Distributions to I-Shareholders are made in the form of additional I-Shares, generally equal in amount to the I-units received by the I-Share issuer. The issuer of the I-Share is taxed as a corporation for federal income tax purposes; however, the MLP does not allocate income or loss to the I-Share issuer. Accordingly, investors receive a Form 1099, are not allocated their proportionate share of income of the MLPs and are not subject to state income tax filing obligations. The price of I-Shares and their volatility tend to be correlated to the price of common units, although the price correlation is not precise.

MISCELLANEOUS. Securities may be purchased on margin only to obtain such short-term credits as necessary for the clearance of purchase and sales of securities.

MORTGAGE-BACKED PASS-THROUGH SECURITIES. The FlexShares® Disciplined Duration MBS Index Fund
invests primarily in a category of pass-through securities backed by pools of mortgages and issued by Fannie Mae, Freddie Mac, or Ginnie Mae. In the basic mortgage-backed pass-through structure, mortgages with similar issuer, term and coupon characteristics are collected and aggregated into a “pool” consisting of multiple mortgage loans. The pool is assigned a CUSIP number and undivided interests in the pool are traded and sold as pass-through securities.

An investment in a specific pool of pass-through securities requires an analysis of the specific prepayment risk of mortgages within the covered pool (since mortgagors typically have the option to prepay their loans). The level of prepayments on a pool of mortgage securities is difficult to predict and can impact the subsequent cash flows and value of the mortgage pool. In addition, when trading specific mortgage pools, precise execution, delivery and settlement arrangements must be negotiated for each transaction.

The Fund seeks to obtain exposure to U.S. agency mortgage-backed pass-through securities, in whole or in part, through the use of TBA Transactions. “TBA” refers to a commonly used mechanism for the forward settlement of U.S. agency mortgage-backed pass-through securities, and not to a separate type of mortgage-back security. Most transactions in fixed-rate mortgage-backed pass-through securities occur through the use of TBA Transactions. TBA Transactions generally are conducted in accordance with widely-accepted guidelines which establish commonly observed terms and conditions for execution, settlement and delivery. In a TBA Transaction, the buyer and seller decide on general trade parameters, such as agency, settlement date, par amount and price. The actual pools delivered generally are determined two days prior to settlement date. The Fund may use TBA transactions in several ways. For example, the Fund may regularly enter into TBA agreements and “roll over” such agreements prior to the settlement date stipulated in such agreements. This type of TBA transaction is sometimes known as a “TBA Roll.” In a TBA Roll, the Fund generally will sell the obligation to purchase the pools stipulated in the TBA Agreement prior to the stipulated settlement date and will enter into a new TBA agreement for future delivery of pools of mortgage-backed pass-through securities. In addition, the Fund may enter into TBA agreements and settle such transactions on the stipulated settlement date by accepting actual receipt or delivery of the pools of mortgage-backed securities stipulated in the TBA agreement. The Fund is not required to use TBA Transactions to gain exposure to mortgage pools, and may choose to purchase those interests in any manner believed by the Investment Adviser to be in the best interest of the Fund. The Fund’s use of TBA rolls may cause the Fund to experience higher portfolio turnover, higher transaction costs and to pay higher capital gain distributions to shareholders (which may be taxable) than other FlexShares® Funds that do not use TBA rolls.

The Fund intends to invest cash pending settlement of any TBA Transactions in money market instruments, repurchase agreements or other high-quality, liquid short-term instruments, which may include money market funds advised by the Investment Adviser. The Fund will assume its pro rata share of fees and expenses of any money market fund that it may invest in, in addition to the each Fund’s own fees and expenses. It is possible that the Fund could lose money by investing in a money market fund. Investments in money market funds have traditionally not and currently are not federally insured.

Default by or bankruptcy of a counterparty to a TBA Transaction would expose the Fund to possible losses because of adverse market action, expenses or delays in connection with the purchase or sale of the pools of mortgage pass-through securities specified in the TBA Transaction. To minimize this risk, the Fund will enter into TBA Transactions only with established counterparties (such as major broker-dealers) and the Investment Adviser will monitor the creditworthiness of such counterparties. In addition, the Fund may accept assignments of TBA Transactions from Authorized Participants from time to time.

In addition, recently finalized rules of the Financial Industry Regulatory Authority (“FINRA”) include mandatory margin requirements that require a Fund to post collateral in connection with its TBA transactions. There is no similar requirement applicable to a Fund’s TBA counterparties. The required collateralization of TBA trades could increase the cost of TBA transactions to a Fund and impose added operational complexity.

**MORTGAGE DOLLAR ROLLS.** The FlexShares® Disciplined Duration MBS Index Fund may enter into mortgage “dollar rolls” in which the Fund sells securities for delivery in the current month and simultaneously contracts with the same counterparty to repurchase similar (same type, coupon and maturity), but not identical, securities on a specified future date. The Fund gives up the right to receive principal and interest paid on the securities sold. However, the Fund would benefit to the extent of any difference between the price received for the securities sold and the lower forward price for the future purchase (often referred to as the “drop”) or fee income plus the interest earned on the cash proceeds of the securities sold until the settlement date of the forward purchase. Unless such benefits exceed the income, capital appreciation, and gain or loss due to mortgage prepayments that would have been realized on the securities sold as part of the mortgage dollar roll, the use of this technique will diminish the investment performance of the Fund. The Fund will hold and maintain in a segregated account until the settlement date cash or liquid assets in an amount equal to the forward purchase price. The benefits derived from the use of mortgage dollar rolls may depend upon the Investment Adviser’s ability to correctly predict mortgage prepayments and interest rates. The use of this technique may diminish the investment performance of the Fund compared with what such performance would have been.
without the use of mortgage dollar rolls. There is no assurance that mortgage dollar rolls can be successfully employed.

For financial reporting and tax purposes, the Fund proposes to treat mortgage dollar rolls as two separate transactions: one transaction involving the purchase of a security and a separate transaction involving a sale. The Fund currently does not intend to enter into mortgage dollar rolls that are accounted for as a financing.

Mortgage dollar rolls involve certain risks, including the following: if the broker-dealer to whom the Fund sells the security becomes insolvent, the Fund’s right to purchase or repurchase the mortgage-related securities subject to the mortgage dollar roll may be restricted. Also, the instrument that the Fund is required to repurchase may be worth less than an instrument which the Fund originally held.

**NON-DIVERSIFICATION RISK.** Non-diversification risk is the risk that a non-diversified Fund may be more susceptible to adverse financial, economic or other developments affecting any single issuer, and more susceptible to greater losses because of these developments. The FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund and FlexShares® Credit-Scored US Long Corporate Bond Index Fund are classified as “non-diversified” for purposes of the 1940 Act. A “non-diversified” classification means that a Fund is not limited by the 1940 Act with regard to the percentage of its assets that may be invested in the securities of a single issuer. The securities of a particular issuer may dominate the Underlying Index of such a Fund and, consequently, the Fund’s investment portfolio.

Each Fund intends to maintain the required level of diversification and otherwise conduct its operations so as to qualify as a “regulated investment company” for purposes of the Code, and to relieve the Fund of any liability for federal income tax to the extent that its earnings are distributed to shareholders. Compliance with the diversification requirements of the Code may limit the investment flexibility of certain Funds and may make it less likely that such Funds will meet their investment objectives.

**OPERATIONAL RISK.** The Investment Adviser and other Fund Service Providers may experience disruptions or operating errors that could negatively impact the Funds. While Service Providers are required to have appropriate operational risk management policies and procedures, their methods of operational risk management may differ from the Funds’ in the setting of priorities, the personnel and resources available or the effectiveness of relevant controls. The Investment Adviser, through its monitoring and oversight of Service Providers, seeks to ensure that Service Providers take appropriate precautions to avoid and mitigate risks that could lead to disruptions and operating errors. However, it is not possible for the Investment Adviser or the other Fund Service Providers to identify all of the operational risks that may affect a Fund or to develop processes and controls to completely eliminate or mitigate their occurrence or effects.

**OPTIONS.** Each Fund may invest up to 20% of its total assets in options. Each Fund may buy put options, buy call options and write covered call and secured put options if NTI believes that it will help the Fund track its Underlying Index. These options may relate to particular securities, foreign and domestic stock indexes, financial instruments, foreign currencies or the yield differential between two securities (“yield curve options”) and may or may not be listed on a domestic or foreign securities exchange or issued by the Options Clearing Corporation. A call option for a particular security or currency gives the purchaser of the option the right to buy, and a writer the obligation to sell, the underlying security at the stated exercise price prior to the expiration of the option, regardless of the market price of the security or currency. The premium paid to the writer is in consideration for undertaking the obligation under the option contract. A put option for a particular security or currency gives the purchaser the right to sell the security or currency at the stated exercise price at the expiration date of the option, regardless of the market price of the security or currency. In contrast to an option on a particular security, an option on an index provides the holder with the right to make or receive a cash settlement upon exercise of the option. The amount of this settlement will be equal to the difference between the closing price of the index at the time of exercise and the exercise price of the option expressed in dollars, times a specified multiple.

Options trading is a highly specialized activity, which entails greater than ordinary investment risk. Options on particular securities may be more volatile than the underlying instruments and, therefore, on a percentage basis, an investment in options may be subject to greater fluctuation than an investment in the underlying instruments themselves.

The Funds will write call options only if they are “covered.” In the case of a call option on a security or currency, the option is “covered” if a Fund owns the security or currency underlying the call or has an absolute and immediate right to acquire that security without additional cash consideration (or, if additional cash consideration is required, liquid assets in such amount are segregated) upon conversion or exchange of other securities held by it. For a call option on an index, the option is covered if a
Fund maintains with its custodian a portfolio of securities substantially replicating the index, or liquid assets equal to the contract value. A call option also is covered if a Fund holds a call on the same security, currency or index as the call written where the exercise price of the call held is: (i) equal to or less than the exercise price of the call written; or (ii) greater than the exercise price of the call written provided the Fund segregates liquid assets in the amount of the difference.

All put options written by a Fund would be covered, which means that such Fund will segregate cash or liquid assets with a value at least equal to the exercise price of the put option or will use the other methods described in the next sentence. A put option also is covered if a Fund holds a put option on the same security or currency as the option written where the exercise price of the option held is: (i) equal to or higher than the exercise price of the option written; or (ii) less than the exercise price of the option written provided the Fund segregates liquid assets in the amount of the difference.

With respect to yield curve options, a call (or put) option is covered if a Fund holds another call (or put) option on the spread between the same two securities and segregates liquid assets sufficient to cover the Fund’s net liability under the two options. Therefore, the Fund’s liability for such a covered option generally is limited to the difference between the amount of the Fund’s liability under the option written by the Fund less the value of the option held by the Fund. Yield curve options also may be covered in such other manner as may be in accordance with the requirements of the counterparty with which the option is traded and applicable laws and regulations.

A Fund’s obligation to sell subject to a covered call option written by it, or to purchase a security or currency subject to a secured put option written by it, may be terminated prior to the expiration date of the option by the Fund’s execution of a closing purchase transaction, which is effected by purchasing on an exchange an option of the same series (i.e., same underlying security or currency, exercise price and expiration date) as the option previously written. Such a purchase does not result in the ownership of an option. A closing purchase transaction will ordinarily be effected to realize a profit on an outstanding option, to prevent an underlying instrument from being called, to permit the sale of the underlying security or currency or to permit the writing of a new option containing different terms on such underlying security. The cost of such a liquidation purchase plus transaction costs may be greater than the premium received upon the original option, in which event the Fund will have incurred a loss in the transaction. There is no assurance that a liquid secondary market will exist for any particular option. An option writer, unable to effect a closing purchase transaction, will not be able to sell the underlying security or currency (in the case of a covered call option) or liquidate the segregated assets (in the case of a secured put option) until the option expires or the optioned security or currency is delivered upon exercise with the result that the writer in such circumstances will be subject to the risk of market decline or appreciation in the instrument during such period.

When a Fund purchases an option, the premium paid by it is recorded as an asset of the Fund. When a Fund writes an option, an amount equal to the net premium (the premium less the commission) received by the Fund is included in the liability section of the Fund’s statement of assets and liabilities as a deferred credit. The amount of this asset or deferred credit will be subsequently marked-to-market to reflect the current value of the option purchased or written. The current value of the traded option is the last sale price or, in the absence of a sale, the current bid price. If an option purchased by a Fund expires unexercised, the Fund realizes a loss equal to the premium paid. If a Fund enters into a closing sale transaction on an option purchased by it, the Fund will realize a gain if the premium received by the Fund on the closing transaction is more than the premium paid to purchase the option, or a loss if it is less. If an option written by a Fund expires on the stipulated expiration date or if a Fund enters into a closing purchase transaction, it will realize a gain (or loss if the cost of a closing purchase transaction exceeds the net premium received when the option is sold) and the deferred credit related to such option will be eliminated. If an option written by a Fund is exercised, the proceeds of the sale will be increased by the net premium originally received and the Fund will realize a gain or loss.

There are several risks associated with transactions in certain options. For example, there are significant differences between the securities, currency and options markets that could result in an imperfect correlation between these markets, causing a given transaction not to achieve its objectives. In addition, a liquid secondary market for particular options, whether traded over-the-counter or on an exchange, may be absent for reasons which include the following: there may be insufficient trading interest in certain options; restrictions may be imposed by an exchange on opening transactions or closing transactions or both; trading halts, suspensions or other restrictions may be imposed with respect to particular classes or series of options or underlying securities or currencies; unusual or unforeseen circumstances may interrupt normal operations on an exchange; the facilities of an exchange or the Options Clearing Corporation may not at all times be adequate to handle current trading value; or one or more exchanges could, for economic or other reasons, decide or be compelled at some future date to discontinue the trading of options (or a particular class or series of options), in which event the secondary market on that exchange (or in that class or series of options) would cease to exist, although outstanding options that had been issued by the Options Clearing Corporation as a result of trades on that exchange would continue to be exercisable in accordance with their terms.
**REAL ESTATE INVESTMENT TRUSTS.** To the extent consistent with their respective investment objectives and strategies, each of the Funds, other than the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund and the FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund may invest in real estate investment trusts (“REITs”). The FlexShares® Global Quality Real Estate Index Fund (which is also an Underlying Fund of the FlexShares® Real Assets Allocation Index Fund) will invest a substantial amount of its assets in REITs. REITs are pooled investment vehicles that invest primarily in real estate or real estate related loans. REITs are generally classified as equity REITs, mortgage REITs or a combination of equity and mortgage REITs. Equity REITs invest the majority of their assets directly in real property and derive income primarily from the collection of rents. Equity REITs can also realize capital gains by selling properties that have appreciated in value. Equity REITs may further be categorized by the type of real estate securities they own, such as apartment properties, retail shopping centers, office and industrial properties, hotels, healthcare facilities, manufactured housing and mixed property types. Mortgage REITs invest the majority of their assets in real estate mortgages and derive income from the collection of interest payments. Hybrid REITs combine the characteristics of both equity and mortgage REITs. Like regulated investment companies such as the Funds, REITs are not taxed on income distributed to shareholders provided they comply with certain requirements under the Code. A Fund will indirectly bear its proportionate share of any expenses paid by REITs in which it invests in addition to the expenses paid by the Fund.

Investing in REITs involves certain unique risks. Equity REITs may be affected by changes in the value of the underlying property owned by such REITs, while mortgage REITs may be affected by the quality of any credit extended. REITs are dependent upon management skills, are not diversified (except to the extent the Code requires), and are subject to the risks of financing projects. REITs are subject to heavy cash flow dependency, default by borrowers, self-liquidation, and the possibilities of failing to qualify for the exemption from tax for distributed income under the Code and failing to maintain their exemptions from the 1940 Act. Investing in REITs also involves risks similar to those associated with investing in small capitalization companies. That is, they may have limited financial resources, may trade less frequently and in a limited volume and may be subject to abrupt or erratic price movements in comparison to larger capitalization companies. To the extent that assets underlying a REIT are concentrated geographically, by property type or in certain other respects, these risks may be heightened.

In addition, the value of such securities may fluctuate in response to the market’s perception of the creditworthiness of the issuers of mortgage-related securities owned by a Fund. Because investments in mortgage-related securities are interest sensitive, the ability of the issuer to reinvest or to reinvest favorably in underlying mortgages may be limited by government regulation or tax policy. For example, action by the Board of Governors of the Federal Reserve System to limit the growth of the nation’s money supply may cause interest rates to rise and thereby reduce the volume of new residential mortgages. Additionally, although mortgages and mortgage-related securities are generally supported by some form of government or private guarantees and/or insurance, there is no assurance that private guarantors or insurers will be able to meet their obligation. REITs (especially mortgage REITs) are also subject to interest rate risks. When interest rates decline, the value of a REIT’s investment in fixed rate obligations can be expected to rise. Conversely, when interest rates rise, the value of a REIT’s investment in fixed rate obligations can be expected to decline. In contrast, as interest rates on adjustable rate mortgage loans are reset periodically, yields on a REIT’s investments in such loans will gradually align themselves to reflect changes in market interest rates, causing the value of such investments to fluctuate less dramatically in response to interest rate fluctuations than would investments in fixed rate obligations.

**REPURCHASE AGREEMENTS.** To the extent consistent with its investment policies, each Fund may agree to purchase portfolio securities from financial institutions subject to the seller’s agreement to repurchase them at a mutually agreed upon date and price (“repurchase agreements”). Repurchase agreements may be considered loans under the 1940 Act. Although the securities subject to a repurchase agreement may bear maturities exceeding one year, settlement for the repurchase agreement will never be more than one year after a Fund’s acquisition of the securities and normally will be within a shorter period of time. Securities subject to repurchase agreements normally are held either by the Trust’s custodian or sub-custodian (if any), or in the Federal Reserve/Treasury Book-Entry System. The seller under a repurchase agreement will be required to maintain the value of the securities subject to the agreement in an amount exceeding the repurchase price (including accrued interest). Default by the seller would, however, expose the Fund to possible loss because of adverse market action or delay in connection with the disposition of the underlying obligations. In addition, in the event of a bankruptcy, a Fund could suffer additional losses if a court determines that the Fund’s interest in the collateral is unenforceable. If a Fund enters into a repurchase agreement with a foreign financial institution, it may also be subject to risks associated with foreign investments. (see “Foreign Investments – General” above.) As a result, repurchase agreements with a foreign financial institution may involve higher credit risks than repurchase agreements with domestic financial institutions. In addition, repurchase agreements with foreign financial institutions located in emerging markets, or relating to emerging markets, may involve foreign financial institutions or counterparties with lower credit ratings than domestic financial institutions.
Regulations that will begin to take effect in 2019 will require certain bank-regulated counterparties and certain of their affiliates to include in certain financial contracts, including many repurchase agreements and purchase and sale contracts, terms that delay or restrict the rights of counterparties, such as a Fund, to terminate such agreements, take foreclosure action, exercise other default rights or restrict transfers of credit support in the event that the counterparty and/or its affiliates are subject to certain types of resolution or insolvency proceedings. It is possible that these new requirements, as well as potential additional government regulation and other developments in the market, could adversely affect a Fund’s ability to terminate existing repurchase agreements and purchase and sale contracts or to realize amounts to be received under such agreements.

**REVERSE REPURCHASE AGREEMENTS.** To the extent consistent with its investment policies, each Fund may borrow funds by selling portfolio securities to financial institutions such as banks and broker/dealers and agreeing to repurchase them at a mutually specified date and price (“reverse repurchase agreements”). The Funds may use the proceeds of reverse repurchase agreements to purchase other securities either maturing, or under an agreement to resell, on a date simultaneous with or prior to the expiration of the reverse repurchase agreement. Reverse repurchase agreements may be considered borrowings under the 1940 Act. Reverse repurchase agreements involve the risk that the market value of the securities sold by a Fund may decline below the repurchase price. The Funds will pay interest on amounts obtained pursuant to a reverse repurchase agreement. While reverse repurchase agreements are outstanding, the Funds will segregate liquid assets in an amount at least equal to the market value of the securities, plus accrued interest, subject to the agreement.

**RISKS RELATED TO MEDIUM AND LOWER QUALITY SECURITIES.** The FlexShares® High Yield Value-Scored Bond Index Fund may invest in or hold medium and lower quality securities. Fixed-income securities rated Baa3 or BBB- are considered medium quality obligations with speculative characteristics. Fixed-income securities rated below Baa3 or BBB- are considered lower quality and are regarded as having significant speculative characteristics. Investment grade bonds are rated at least Baa3 by Moody’s or BBB- by S&P, the equivalent by another NRSRO or, if unrated, of equal quality in the opinion of the Investment Adviser. Investments in medium and lower quality securities present special risk considerations. Medium quality securities, although considered investment grade, also are considered to have speculative characteristics. Lower quality securities are considered predominantly speculative by traditional investment standards. In some cases, these lower quality obligations may be highly speculative and have poor prospects for reaching investment grade standard. While any investment carries some risk, certain risks associated with lower quality securities are different than those for investment-grade securities. The risk of loss through default is greater because lower quality securities usually are unsecured and are often subordinate to an issuer’s other obligations. Additionally, the issuers of these securities frequently have high debt levels and are thus more sensitive to difficult economic conditions, individual corporate developments and rising interest rates. Consequently, the market price of these securities may be quite volatile and may result in wider fluctuations of the Fund’s NAV per share.

There remains some uncertainty about the performance level of the market for lower quality securities under adverse market and economic conditions. An economic downturn or increase in interest rates could have a negative impact on both the market for lower quality securities (resulting in a greater number of bond defaults) and the value of lower quality securities held in the portfolio of investments.

The economy and interest rates can affect lower quality securities differently than other securities. For example, the prices of lower quality securities are more sensitive to adverse economic changes or individual corporate developments than are the prices of higher quality investments. In addition, during an economic downturn or period in which interest rates are rising significantly, highly leveraged issuers may experience financial difficulties, which, in turn, would adversely affect their ability to service their principal and interest payment obligations, meet projected business goals and obtain additional financing.

The market value of lower quality securities tends to reflect individual corporate developments to a greater extent than that of higher quality securities, which react primarily to fluctuations in the general level of interest rates. Lower quality securities are often issued in connection with a corporate reorganization or restructuring or as a part of a merger, acquisition, takeover or similar event. They also are issued by less established companies seeking to expand. Such issuers are often highly leveraged, may not have available to them more traditional methods of financing and generally are less able than more established or less leveraged entities to make scheduled payments of principal and interest in the event of adverse economic developments or business conditions.

A holder’s risk of loss from default is significantly greater for lower quality securities than is the case for holders of other debt securities because such securities generally are unsecured and are often subordinated to the rights of other creditors of the issuers of such securities. Investment by the Fund in defaulted securities poses additional risk of loss should nonpayment of principal and interest continue in respect of such securities. Even if such securities are held to maturity, recovery by the Fund of its initial investment and any anticipated income or appreciation will be uncertain. The Fund also may incur additional expenses in
seeking recovery on defaulted securities. If an issuer of a security defaults, the Fund may incur additional expenses to seek recovery. In addition, periods of economic uncertainty would likely result in increased volatility for the market prices of lower quality securities as well as the Fund’s NAV. In general, both the prices and yields of lower quality securities will fluctuate.

The secondary market for lower quality securities is concentrated in relatively few market makers and is dominated by institutional investors, including mutual funds, insurance companies and other financial institutions. Accordingly, the secondary market for such securities is not as liquid as, and is more volatile than, the secondary market for higher quality securities. In addition, market trading volume for high yield fixed-income securities generally is lower and the secondary market for such securities could contract under adverse market or economic conditions, independent of any specific adverse changes in the condition of a particular issuer. These factors may have an adverse effect on the market price and the Fund’s ability to dispose of particular portfolio investments. A less developed secondary market also may make it more difficult for the Fund to obtain precise valuations of the high yield securities in its portfolio.

The adoption of new legislation could adversely affect the secondary market for high yield securities and the financial condition of issuers of these securities. The form of any future legislation, and the probability of such legislation being enacted, is uncertain.

In certain circumstances, it may be difficult to determine a security’s fair value due to a lack of reliable objective information. Such instances occur where there is not an established secondary market for the security or the security is lightly traded. As a result, the Fund’s valuation of a security and the price it is actually able to obtain when it sells the security could differ.

Adverse publicity and investor perceptions, whether or not based on fundamental analysis, may decrease the value and liquidity of lower-quality convertible securities held by the Fund, especially in a thinly traded market. Illiquid or restricted securities held by the Fund may involve special registration responsibilities, liabilities and costs, and could involve other liquidity and valuation difficulties.

**RISKS RELATED TO SMALL COMPANY SECURITIES.** The FlexShares® Morningstar US Market Factor Tilt Index Fund, FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund and FlexShares® Real Assets Allocation Index Fund (through its investments in its Underlying Funds) may invest a portion of their assets in small company securities. Investing in the securities of such companies involves greater risk, portfolio price volatility and cost. Securities of such issuers may lack sufficient market liquidity to enable a Fund to effect sales at an advantageous time or without a substantial drop in price. Small companies often have narrower markets and more limited managerial and financial resources than larger, more established companies and may have a greater sensitivity to changing economic conditions. Smaller companies also face a greater risk of business failure. As a result, their performance can be more volatile, which could increase the volatility of a Fund’s portfolio. Generally, the smaller the company size, the greater these risks.

The values of small company stocks will frequently fluctuate independently of the values of larger company stocks. Small company stocks may decline in price as large company stock prices rise, or rise in price as large company stock prices decline. You should, therefore, expect that the NAV of a Fund’s shares will be more volatile than, and may fluctuate independently of, broad stock market indexes such as the S&P 500 Index.

The additional costs associated with the acquisition of small company stocks include brokerage costs, market impact costs (that is, the increase in market prices that may result when a Fund purchases thinly traded stock) and the effect of the “bid-ask” spread in small company stocks. These costs will be borne by all shareholders and may negatively impact investment performance.

**RULE 144A SECURITIES.** To the extent consistent with its investment objective and strategies, each Fund may invest in securities offered pursuant to Rule 144A under the Securities Act of 1933, which are restricted securities. They may be less liquid and more difficult to value than other investments because such securities may not be readily marketable in broad public markets. A Fund may not be able to sell a restricted security promptly or at a reasonable price. A restricted security that was liquid at the time of purchase may subsequently become illiquid and its value may decline as a result. Restricted securities that are deemed illiquid will count towards a Fund’s 15% limitation on illiquid securities. In addition, transaction costs may be higher for restricted securities than for more liquid securities. A Fund may have to bear the expense of registering Rule 144A securities for resale and the risk of substantial delays in effecting the registration.

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**SECURITIES LENDING.** In order to generate additional income, a Fund may lend securities to banks, brokers and dealers or other qualified institutions. In exchange, the Fund will receive collateral equal to at least 100% of the value of the securities loaned. Securities lending may represent no more than one-third of the value of the Fund’s total assets (including the loan collateral).

Collateral for loans of portfolio securities made by a Fund may consist of cash, cash equivalents, securities issued or guaranteed by the U.S. government or its agencies or foreign governments (or any combination thereof). Any cash collateral received by a Fund in connection with these loans may be invested in a variety of short-term investments, either directly or indirectly through registered or unregistered money market funds. Loan collateral (including any investment of the collateral) is not included in the calculation of the percentage limitations described elsewhere in the Prospectus or SAI regarding a Fund’s investments in particular types of securities. The borrower of securities will be required to maintain the market value of the collateral at not less than the market value of the loaned securities, and such value will be monitored on a daily basis.

When a Fund lends its securities, it continues to receive payments equal to the dividends and interest paid on the securities loaned and simultaneously may earn interest on the investment of the cash collateral. Investing the collateral subjects it to market depreciation or appreciation, and the Fund is responsible for any loss that may result from its investment in borrowed collateral. Additionally, the amount of a Fund’s distributions that qualify for taxation at reduced long-term capital gains rates for individuals, as well as the amount of the Fund’s distributions that qualify for the dividends received deduction available to corporate shareholders (together, “qualifying dividends”) may be reduced as a result of the Fund’s securities lending activities. This is because any dividends paid on securities while on loan will not be deemed to have been received by the Fund, and the equivalent amount paid to the Fund by the borrower of the securities will not be deemed to be a qualifying dividend.

A Fund will have the right to terminate a loan at any time and recall the loaned securities within the normal and customary settlement time for securities transactions. Although voting rights, or rights to consent, attendant to securities on loan pass to the borrower, such loans may be called so that the securities may be voted by the Fund if a material event affecting the investment is to occur. As with other extensions of credit there are risks of delay in recovering, or even loss of rights in, the collateral should the borrower of the securities fail financially. In the event of a default by a borrower with respect to any loan, the securities lending agent will exercise any and all remedies provided under the applicable borrower agreement. These remedies include purchasing replacement securities for the Fund by applying the collateral held from the defaulting borrower against the purchase cost of the replacement securities. If the proceeds from the collateral are less than the purchase cost of the replacement securities, the securities lending agent is responsible for such shortfall, subject to certain limitations that are set forth in detail in the securities lending agency agreement. In this event, a Fund could experience delays in recovering its securities and possibly may incur a capital loss.

Regulations that will begin to take effect in 2019 will require certain bank-regulated counterparties and certain of their affiliates to include in certain financial contracts, including many securities lending agreements, terms that delay or restrict the rights of counterparties, such as a Fund, to terminate such agreements, foreclose upon collateral, exercise other default rights or restrict transfers of credit support in the event that the counterparty and/or its affiliates are subject to certain types of resolution or insolvency proceedings. It is possible that these new requirements, as well as potential additional government regulation and other developments in the market, could adversely affect a Fund’s ability to terminate existing securities lending agreements or to realize amounts to be received under such agreements.

JPMorgan Chase Bank, N.A. (“JPMorgan”) serves as securities lending agent for the Funds. For such services, JPMorgan receives a percentage of securities lending revenue generated for the Funds.

**SHORT-TERM INSTRUMENTS AND TEMPORARY INVESTMENTS.** To the extent consistent with its investment policies, each Fund may invest in short-term instruments, including money market instruments, on an ongoing basis to provide liquidity or for other reasons. Money market instruments are generally short-term investments that may include but are not limited to: (i) shares of money market funds (including those advised by NTI); (ii) obligations issued or guaranteed by the U.S. government, its agencies or instrumentalities (including government-sponsored enterprises); (iii) negotiable certificates of deposit (“CDs”), bankers’ acceptances, fixed time deposits, bank notes and other obligations of U.S. and foreign banks (including foreign branches) and similar institutions; (iv) commercial paper rated at the date of purchase “Prime-1” by Moody’s, “A-1” by S&P or, if unrated, of comparable quality as determined by NTI; (v) non-convertible corporate debt securities (e.g., bonds and debentures) with remaining maturities at the date of purchase of not more than 397 days and that satisfy the rating requirements set forth in Rule 2a-7 under the 1940 Act; (vi) repurchase agreements; and (vii) short-term U.S. dollar-denominated obligations of foreign banks (including U.S. branches) that, in the opinion of NTI, are of comparable quality to obligations of U.S. banks which may be purchased by a Fund. Any of these instruments may be purchased on a current or a forward-settled basis.
Time deposits are non-negotiable deposits maintained in banking institutions for specified periods of time at stated interest rates. Bankers’ acceptances are time drafts drawn on commercial banks by borrowers, usually in connection with international transactions. Commercial paper represents short-term unsecured promissory notes issued in bearer form by banks or bank holding companies, corporations and finance companies. Certificates of deposit are negotiable certificates issued against funds deposited in a commercial bank for a definite period of time and earning a specified return. Bankers’ acceptances are negotiable drafts or bills of exchange, normally drawn by an importer or exporter to pay for specific merchandise, which are “accepted” by a bank, meaning, in effect, that the bank unconditionally agrees to pay the face value of the instrument on maturity. Fixed time deposits are bank obligations payable at a stated maturity date and bearing interest at a fixed rate. Fixed time deposits may be withdrawn on demand by the investor, but may be subject to early withdrawal penalties that vary depending upon market conditions and the remaining maturity of the obligation. There are no contractual restrictions on the right to transfer a beneficial interest in a fixed time deposit to a third party. Bank notes generally rank junior to deposit liabilities of banks and pari passu with other senior, unsecured obligations of the bank. Bank notes are classified as “other borrowings” on a bank’s balance sheet, while deposit notes and certificates of deposit are classified as deposits. Bank notes are not insured by the FDIC or any other insurer. Deposit notes are insured by the FDIC only to the extent of $250,000 per depositor per bank.

The FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund (through its investments in its Underlying Funds), FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund, FlexShares® International Quality Dividend Dynamic Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund and FlexShares® Credit-Scored US Long Corporate Bond Index Fund may invest a portion of their assets in the obligations of foreign banks and foreign branches of domestic banks. Such obligations include Eurodollar Certificates of Deposit (“ECDs”), which are U.S. dollar-denominated certificates of deposit issued by offices of foreign and domestic banks located outside the United States; Eurodollar Time Deposits (“ETDs”), which are U.S. dollar-denominated deposits in a foreign branch of a U.S. bank or a foreign bank; Canadian Time Deposits (“CTDs”), which are essentially the same as ETDs except that they are issued by Canadian offices of major Canadian banks; Schedule Bs, which are obligations issued by Canadian branches of foreign or domestic banks; Yankee Certificates of Deposit (“Yankee CDs”), which are U.S. dollar-denominated certificates of deposit issued by a U.S. branch of a foreign bank and held in the United States; and Yankee Bankers’ Acceptances (“Yankee BAs”), which are U.S. dollar-denominated bankers’ acceptances issued by a U.S. branch of a foreign bank and held in the United States.

STRIPPED SECURITIES. To the extent consistent with its investment policies, the FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund and FlexShares® Credit-Scored US Long Corporate Bond Index Fund may purchase stripped securities. The Treasury Department has facilitated transfers of ownership of zero coupon securities by accounting separately for the beneficial ownership of particular interest coupon and principal payments on Treasury securities through the Federal Reserve book-entry record-keeping system. The Federal Reserve program as established by the Treasury Department is known as “Separate Trading of Registered Interest and Principal of Securities” or “STRIPS.” The Funds may purchase securities registered in the STRIPS program. Under the STRIPS program, the Fund will be able to have its beneficial ownership of zero coupon securities recorded directly in the book-entry record-keeping system in lieu of having to hold certificates or other evidences of ownership of the underlying U.S. Treasury securities.

Other types of stripped securities may be purchased by the Funds, including stripped mortgage-backed securities (“SMBS”). SMBS usually are structured with two or more classes that receive different proportions of the interest and principal distributions from a pool of mortgage backed obligations. A common type of SMBS will have one class receiving all of the interest, while the other class receives all of the principal. However, in some instances, one class will receive some of the interest and most of the principal while the other class will receive most of the interest and the remainder of the principal. If the underlying obligations experience greater than anticipated prepayments of principal, a Fund may fail to recoup fully its initial investment in these securities. The market value of the class consisting entirely of principal payments generally is extremely volatile in response to changes in interest rates. The yields on a class of SMBS that receives all or most of the interest generally are higher than prevailing market yields on other mortgage backed obligations because their cash flow patterns also are volatile and there is a risk that the initial investment will not be recouped fully. SMBS issued by the U.S. government (or a U.S. government agency, instrumentality or sponsored enterprise) may be considered liquid under guidelines established by the Board if they can be disposed of promptly in the ordinary course of business at a value reasonably close to that used in the calculation of the NAV per share.

STRUCTURED SECURITIES. To the extent consistent with its investment objective and strategies, the FlexShares®
Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund may purchase structured securities. These fixed-income instruments are structured to recast the investment characteristics of the underlying security or reference asset. If the issuer is a unit investment trust or other special purpose vehicle, the structuring will typically involve the deposit with or purchase by such issuer of specified instruments (such as commercial bank loans or securities) and/or the execution of various derivative transactions, and the issuance by that entity of one or more classes of securities (structured securities) backed by, or representing interests in, the underlying instruments. The cash flow on the underlying instruments may be apportioned among the newly issued structured securities to create securities with different investment characteristics, such as varying maturities, payment priorities and interest rate provisions, and the extent of such payments made with respect to structured securities is dependent on the extent of the cash flow on the underlying instruments. Investments in these securities may be structured as a class that is either subordinated or unsubordinated to the right of payment of another class. Subordinated structured securities typically have higher rates of return and present greater risks than unsubordinated structured products.

Each Fund’s investments in these instruments are indirectly subject to the risks associated with derivative instruments, including, among others, credit risk, default or similar event risk, counterparty risk, interest rate risk, leverage risk and management risk. Because structured securities typically involve no credit enhancement, their credit risk generally will be equivalent to that of the underlying instruments. These securities generally are exempt from registration under the Securities Act. Accordingly, there may be no established trading market for the securities and they may constitute illiquid investments. Structured securities may entail a greater degree of market risk than other types of debt securities because the investor bears the risk of the underlying security or reference asset. Structured securities may also be more volatile, less liquid, and more difficult to price accurately than less complex securities or more traditional debt securities.

**TRACKING VARIANCE.** As discussed in the Prospectus, the Funds are subject to the risk of tracking variance. Tracking variance may result from share purchases and redemptions, transaction costs, expenses and other factors. Share purchases and redemptions may necessitate the purchase and sale of securities by a Fund and the resulting transaction costs, which may be substantial because of the number and the characteristics of the securities held. In addition, transaction costs are incurred because sales of securities received in connection with spin-offs and other corporate reorganizations are made to conform a Fund’s holdings to its investment objective. Tracking variance also may occur due to factors such as the size of a Fund, the maintenance of a cash reserve pending investment or to meet expected redemptions, changes made in the Fund’s Underlying Index or the manner in which the index is calculated or because the indexing and investment approach of the Investment Adviser does not produce the intended goal of the Fund. Tracking variance is monitored by the Investment Adviser at least quarterly. In the event the performance of a Fund is not comparable to the performance of its Underlying Index, the Board will evaluate the reasons for the deviation and the availability of corrective measures.

**TRUST PREFERRED SECURITIES.** The FlexShares® High Yield Value-Scored Bond Index Fund may invest in trust preferred securities. Trust preferred securities have the characteristics of both subordinated debt and preferred stock. Generally, trust preferred securities are issued by a trust that is wholly-owned by a financial institution or other corporate entity, typically a bank holding company. The financial institution creates the trust and owns the trust’s common securities. The trust uses the sale proceeds of its common securities to purchase subordinated debt issued by the financial institution. The financial institution uses the proceeds from the subordinated debt sale to increase its capital while the trust receives periodic interest payments from the financial institution for holding the subordinated debt. The trust uses the funds received to make dividend payments to the holders of the trust preferred securities. The primary advantage of this structure is that the trust preferred securities are treated by the financial institution as debt securities for tax purposes and as equity for the calculation of capital requirements.

Trust preferred securities typically bear a market rate coupon comparable to interest rates available on debt of a similarly rated issuer. Typical characteristics include long-term maturities, early redemption by the issuer, periodic fixed or variable interest payments, and maturities at face value. Holders of trust preferred securities have limited voting rights to control the activities of the trust and no voting rights with respect to the financial institution. The market value of trust preferred securities may be more volatile than those of conventional debt securities. Trust preferred securities may be issued in reliance on Rule 144A under the Securities Act of 1933 and subject to restrictions on resale. There can be no assurance as to the liquidity of trust preferred securities and the ability of holders, such as the Fund, to sell their holdings. In identifying the risks of the trust preferred securities, the Investment Adviser will look to the condition of the financial institution as the trust typically has no business operations other than to issue the trust preferred securities. If the financial institution defaults on interest payments to the trust, the trust will not be able to make dividend payments to holders of its securities, such as the Fund.

**U.S. GOVERNMENT OBLIGATIONS.** To the extent consistent with their respective investment objectives and strategies, the Funds may invest in a variety of U.S. Treasury obligations and obligations issued by or guaranteed by the U.S. government or by its agencies, instrumentalities or sponsored enterprises. Not all government obligations carry the same credit
support. No assurance can be given that the U.S. government would provide financial support to its agencies, instrumentalities or sponsored enterprises if it were not obligated to do so by law. There is no assurance that these commitments will be undertaken or complied with in the future. In addition, the secondary market for certain participations in loans made to foreign governments or their agencies may be limited. In the absence of a suitable secondary market, such participations generally are considered illiquid.

Many states grant tax-free status to dividends paid to shareholders of a fund from interest income earned by that fund from direct obligations of the U.S. government, subject in some states to minimum investment requirements that must be met by the fund. Investments in securities issued by Ginnie Mae or Fannie Mae, bankers’ acceptances, commercial paper and repurchase agreements collateralized by U.S. government securities do not generally qualify for tax-free treatment.

The FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund and FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund invest primarily in U.S. Treasury Inflation-Protected Securities (“TIPS”). Examples of other types of U.S. government obligations that may be acquired by each of the Funds include U.S. Treasury Bills, Treasury Notes and Treasury Bonds and the obligations of Federal Home Loan Banks, Federal Farm Credit Banks, Federal Land Banks, the Federal Housing Administration, Farmers Home Administration, Export-Import Bank of the United States, Small Business Administration, the Federal National Mortgage Association, the Government National Mortgage Association, General Services Administration, Central Bank for Cooperatives, the Federal Home Loan Mortgage Corporation, Federal Intermediate Credit Banks and the Maritime Administration.

Securities guaranteed as to principal and interest by the U.S. government or by its agencies, instrumentalities or sponsored enterprises also are deemed to include: (i) securities for which the payment of principal and interest is backed by an irrevocable letter of credit issued by the U.S. government or by any agency, instrumentality or sponsored enterprise thereof; and (ii) participations in loans made to foreign governments or their agencies that are so guaranteed.

**VARIABLE AND FLOATING RATE INSTRUMENTS.** To the extent consistent with its investment objective and strategies, the FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund may invest in variable and floating rate instruments. Variable and floating rate instruments have interest rates that periodically are adjusted either at set intervals or that float at a margin in relation to a generally recognized index rate. These instruments include long-term variable and floating rate bonds where a Fund obtains at the time of purchase the right to put the bond back to the issuer or a third party at par at a specified date and also includes leveraged inverse floating rate instruments (“inverse floaters”). The FlexShares® High Yield Value-Scored Bond Index Fund does not intend to invest in inverse floaters. With respect to the variable and floating rate instruments that may be acquired by the Funds, the Investment Adviser will consider the earning power, cash flows and other liquidity ratios of the issuers and guarantors of such instruments and, if the instruments are subject to demand features, will monitor their financial status and ability to meet payment on demand. Where necessary to ensure that a variable or floating rate instrument meets a Fund’s quality requirements, the issuer’s obligation to pay the principal of the instrument will be backed by an unconditional bank letter or line of credit, guarantee or commitment to lend.

A Fund will invest in variable and floating rate instruments only when the Investment Adviser deems the investment to involve minimal credit risk. Unrated variable and floating rate instruments will be determined by the Investment Adviser to be of comparable quality at the time of the purchase to rated instruments that may be purchased by a Fund. In determining weighted average portfolio maturity, an instrument may, subject to the SEC’s regulations, be deemed to have a maturity shorter than its nominal maturity based on the period remaining until the next interest rate adjustment or the time a Fund can recover payment of principal as specified in the instrument. Variable and floating rate instruments eligible for purchase by the Funds include variable amount master demand notes, which permit the indebtedness thereunder to vary in addition to providing for periodic adjustments in the interest rate.

Variable and floating rate instruments also include leveraged inverse floaters. The interest rate on an inverse floater resets in the opposite direction from the market rate of interest to which the inverse floater is indexed. An inverse floater may be considered to be leveraged to the extent that its interest rate varies by a magnitude that exceeds the magnitude of the change in the index rate of interest. The higher degree of leverage inherent in inverse floaters is associated with greater volatility in their market values. Accordingly, the duration of an inverse floater may exceed its stated final maturity. The Funds may deem the maturity of variable and floating rate instruments to be less than their stated maturities based on their variable and floating rate features and/or their put features. Unrated variable and floating rate instruments will be determined by the Investment Adviser to be of comparable quality at the time of purchase to rated instruments which may be purchased by the Funds.
Variable and floating rate instruments including inverse floaters held by a Fund will be subject to the Fund’s limitation on illiquid investments, absent a reliable trading market, when the Fund may not demand payment of the principal amount within seven days. Because there is no active secondary market for certain variable and floating rate instruments, they may be more difficult to sell if the issuer defaults on its payment obligations or during periods when a Fund is not entitled to exercise its demand rights. As a result, the Funds could suffer a loss with respect to these instruments.

**WARRANTS.** To the extent consistent with their investment policies, each of the Funds, other than the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund may purchase warrants and similar rights, which are privileges issued by corporations enabling the owners to subscribe to and purchase a specified number of shares of the corporation at a specified price during a specified period of time. The prices of warrants do not necessarily correlate with the prices of the underlying shares. The purchase of warrants involves the risk that a Fund could lose the purchase value of a warrant if the right to subscribe to additional shares is not exercised prior to the warrant’s expiration. Also, the purchase of warrants involves the risk that the effective price paid for the warrant added to the subscription price of the related security may exceed the value of the subscribed security’s market price such as when there is no movement in the level of the underlying security.

**YIELDS AND RATINGS.** The yields on certain obligations, including the instruments in which the Funds may invest, are dependent on a variety of factors, including general market conditions, conditions in the particular market for the obligation, financial condition of the issuer, size of the offering, maturity of the obligation and ratings of the issue. The ratings of S&P, DBRS Ratings Limited, Moody’s and Fitch represent their respective opinions as to the quality of the obligations they undertake to rate. Ratings, however, are general and are not absolute standards of quality. Consequently, obligations with the same rating, maturity and interest rate may have different market prices. For a more complete discussion of ratings, see Appendix C to this SAI.

**ZERO COUPON AND CAPITAL APPRECIATION BONDS AND PAY-IN-KIND SECURITIES.** To the extent consistent with their respective investment objectives and strategies, the Funds may invest in zero coupon bonds, capital appreciation bonds and pay-in-kind (“PIK”) securities. Zero coupon and capital appreciation bonds are debt securities issued or sold at a discount from their face value and which do not entitle the holder to any periodic payment of interest prior to maturity or a specified date. The original issue discount varies depending on the time remaining until maturity or cash payment date, prevailing interest rates, the liquidity of the security and the perceived credit quality of the issuer. These securities also may take the form of debt securities that have been stripped of their unmatured interest coupons, the coupons themselves or receipts or certificates representing interests in such stripped debt obligations or coupons. The market prices of zero coupon bonds, capital appreciation bonds and PIK securities generally are more volatile than the market prices of interest bearing securities and are likely to respond to a greater degree to changes in interest rates than interest bearing securities having similar maturities and credit quality.

PIK securities may be debt obligations or preferred shares that provide the issuer with the option of paying interest or dividends on such obligations in cash or in the form of additional securities rather than cash. Similar to zero coupon bonds, PIK securities are designed to give an issuer flexibility in managing cash flow. PIK securities that are debt securities can either be senior or subordinated debt and generally trade flat (i.e., without accrued interest). The trading price of PIK debt securities generally reflects the market value of the underlying debt plus an amount representing accrued interest since the last interest payment.

Zero coupon bonds, capital appreciation bonds and PIK securities involve the additional risk that, unlike securities that periodically pay interest to maturity, a Fund will realize no cash until a specified future payment date unless a portion of such securities is sold and, if the issuer of such securities defaults, the Fund may obtain no return at all on its investment. In addition, even though such securities do not provide for the payment of current interest in cash, the Fund is nonetheless required to accrue income on such investments for each taxable year and generally is required to distribute such accrued amounts (net of deductible expenses, if any) to avoid being subject to tax. Because no cash generally is received at the time of the accrual, a Fund may be required to liquidate other portfolio securities to obtain sufficient cash to satisfy federal tax distribution requirements applicable to the Fund.
THE INDEXES

Morningstar® US Market Factor Tilt IndexSM

NUMBER OF COMPONENTS: APPROXIMATELY 2,553

INDEX DESCRIPTION. The Morningstar US Market Factor Tilt Index measures the performance of a broad exposure of stocks with increased exposure, or a tilt, toward small-capitalization and value stocks. Stocks that are deemed to be small-capitalization or value will have a slight overweighting compared to their weight in a broad market capitalization weighted index. Likewise, stocks designated as “large” or “growth” stocks will have a slight underweight compared to a standard market-capitalization weighting. The Morningstar index methodology defines “total market” stocks as those stocks that form the top 99.50% of the market capitalization of the stocks eligible to be included in Morningstar’s investable universe. All stocks are then designated as “core,” “growth” or “value” based on Morningstar’s value style orientation. Stocks of companies with, for example, relatively low valuations based on price-to-book ratios, price-to-earnings ratios and other factors, are designated as “value” securities. Similarly, stocks of companies with relatively high valuations based on price-to-book ratios, price-to-earnings ratios and other factors, would be designated as “growth” securities. Stocks that are not designated as “growth” or “value” securities are designated as “core” securities.

Morningstar® Developed Markets ex-US Factor Tilt IndexSM

NUMBER OF COMPONENTS: APPROXIMATELY 3,434

INDEX DESCRIPTION. The Morningstar Developed Markets ex-U.S. Factor Tilt Index measures the performance of developed equity markets (excluding the U.S.) with increased exposure, or a tilt, toward small-capitalization and value stocks. Developed markets are defined as countries that fall in the high annual per capita gross national income bracket for the most recent 3 consecutive years; have a high degree of stock market transparency, regulation, and operational efficiency; and have an absence of investment restrictions for non-domiciled investors. Stocks that are deemed to be small-capitalization or value will have an overweighting compared to their weight in a corresponding market capitalization weighted index. Likewise, stocks designated as “large” or “growth” stocks will have an underweighting compared to a standard market-capitalization weighting. The Morningstar index methodology uses 97% market capitalization of the stocks eligible to be included in Morningstar’s investable universe. These stocks are then designated as “value”, “core” or “growth” based on factors such as price-to-book ratios and price-to-earnings ratios; and are modified free float market capitalization weighted. Stocks of companies with, for example, relatively low valuations based on price-to-book ratios, price-to-earnings ratios and other factors, are designated as “value” securities. Similarly, stocks of companies with relatively high valuations based on price-to-book ratios, price-to-earnings ratios and other factors, would be designated as “growth” securities. Stocks that are not designated as “growth” or “value” securities are designated as “core” securities.

Morningstar® Emerging Markets Factor Tilt IndexSM

NUMBER OF COMPONENTS: APPROXIMATELY 2,519

INDEX DESCRIPTION. The Morningstar Emerging Markets Factor Tilt Index measures the performance of emerging equity markets with increased exposure, or a tilt, toward small-capitalization and value stocks. Emerging markets are defined as countries that do not fall in the high annual per capita gross national income bracket, but have significant market size and stock market transparency; reasonable regulations and operational efficiency; and modest restriction to foreign investors. Stocks that are deemed to be small-capitalization or value will have an overweighting compared to their weight in a corresponding market capitalization weighted index. Likewise, stocks designated as “large” or “growth” stocks will have an underweighting compared to a standard market-capitalization weighting. The Morningstar index methodology uses 97% market capitalization of the stocks eligible to be included in Morningstar’s investable universe. These stocks are then designated as “value”, “core” or “growth” based on factors such as price-to-book ratios and price-to-earnings ratios; and are modified free float market capitalization weighted. Stocks of companies with, for example, relatively low valuations based on price-to-book ratios, price-to-earnings ratios and other factors, are designated as “value” securities. Similarly, stocks of companies with relatively high valuations based on price-to-book ratios, price-to-earnings ratios and other factors, would be designated as “growth” securities. Stocks that are not designated as “growth” or “value” securities are designated as “core” securities.
Morningstar® Developed Markets ex-US Factor Tilt Hedged Index℠

NUMBER OF COMPONENTS: APPROXIMATELY 3,434

INDEX DESCRIPTION. The Morningstar Developed Markets ex-US Factor Tilt Hedged Index (the “Currency Hedge Index”) methodology measures the performance of the Morningstar Developed Markets ex-US Factor Tilt Index (the “Benchmark Index”) after applying a practical hedging program, limiting the effects of currency fluctuations. Hedging each foreign currency in the portfolio, relative to an investor’s home currency, is a close estimation of the return a local investor can achieve. The U.S. dollar is the default home currency for the Currency Hedge Index.

The Currency Hedge Index is long the Benchmark Index and short currency forwards whose notional amount is based on market capitalization of foreign currencies in the Benchmark Index. In other words, the hedge ratio, that is, the proportion of the portfolio’s currency exposure that is hedged is set to 100%.

The Benchmark Index measures the performance of developed equity markets (excluding the U.S.) with increased exposure, or a tilt, toward small-capitalization and value stocks. Developed markets are defined as countries that fall in the high annual per capita gross national income bracket for the most recent 3 consecutive years; have a high degree of stock market transparency, regulation, and operational efficiency; and have an absence of investment restrictions for non-domiciled investors. Stocks that are deemed to be small-capitalization or value will have an overweighting compared to their weight in a corresponding market capitalization weighted index. Likewise, stocks designated as “large” or “growth” stocks will have an underweighting compared to a standard market-capitalization weighting. The Morningstar index methodology uses 97% market capitalization of the stocks eligible to be included in Morningstar’s investable universe. These stocks are then designated as “value”, “core” or “growth” based on factors such as price-to-book ratios and price-to-earnings ratios; and are modified free float market capitalization weighted. Stocks of companies with, for example, relatively low valuations based on price-to-book ratios, price-to-earnings ratios and other factors, are designated as “value” securities. Similarly, stocks of companies with relatively high valuations based on price-to-book ratios, price-to-earnings ratios and other factors would be designated as “growth” securities. Stocks that are not designated as “growth” or “value” securities are designated as “core” securities.

Morningstar® Emerging Markets Factor Tilt Hedged Index℠

NUMBER OF COMPONENTS: APPROXIMATELY 2,519

INDEX DESCRIPTION. The Morningstar Emerging Markets Factor Tilt Hedged Index (the “Currency Hedge Index”) methodology measures the performance of the Morningstar Emerging Markets Factor Tilt Index (the “Benchmark Index”) after applying a practical hedging program, limiting the effects of currency fluctuations. Hedging each foreign currency in the portfolio, relative to an investor’s home currency, is a close estimation of the return a local investor can achieve. The U.S. dollar is the default home currency for the Currency Hedge Index.

The Currency Hedge Index is long the Benchmark Index and short currency forwards whose notional amount is based on market capitalization of foreign currencies in the Benchmark Index. In other words, the hedge ratio, that is, the proportion of the portfolio’s currency exposure that is hedged is set to 100%.

The Benchmark Index measures the performance of emerging equity markets with increased exposure, or a tilt, toward small-capitalization and value stocks. Emerging markets are defined as countries that do not fall in the high annual per capita gross national income bracket, but have significant market size and stock market transparency; reasonable regulations and operational efficiency; and modest restriction to foreign investors. Stocks that are deemed to be small-capitalization or value will have an overweighting compared to their weight in a corresponding market capitalization weighted index. Likewise, stocks designated as “large” or “growth” stocks will have an underweighting compared to a standard market-capitalization weighting. The Morningstar index methodology uses 97% market capitalization of the stocks eligible to be included in Morningstar’s investable universe. These stocks are then designated as “value”, “core” or “growth” based on factors such as price-to-book ratios and price-to-earnings ratios; and are modified free float market capitalization weighted. Stocks of companies with, for example, relatively low valuations based on price-to-book ratios, price-to-earnings ratios and other factors, are designated as “value” securities. Similarly, stocks of companies with relatively high valuations based on price-to-book ratios, price-to-earnings ratios and other factors would be designated as “growth” securities. Stocks that are not designated as “growth” or “value” securities are designated as “core” securities.

Northern Trust Quality Large Cap Index℠

NUMBER OF COMPONENTS: APPROXIMATELY 136

Inception Date: July 31, 2015
INDEX DESCRIPTION. The Northern Trust Quality Large Cap Index is designed to measure the performance of a universe of large capitalization securities which demonstrate characteristics of better quality¹, attractive valuation² and positive momentum³.

Eligible Securities
In order to be eligible for inclusion in the Northern Trust Quality Large Cap Index, a security must be a top 600 corporation, as measured by largest float adjusted market capitalization, within the Northern Trust 1250 Index at the time of the annual reconstitution in August.

Methodology
The construction of the Index begins with a universe of eligible securities (defined in “Eligible Securities” section). Eligible constituent weights are then optimized to maximize exposure to quality, as defined by a proprietary scoring model, value and momentum.

The main objective of the optimization is to maximize exposure to the composite of factors (quality score + value + momentum) while minimizing the overall risk of the index relative to the eligible universe, as measured by standard risk models. In addition to the main objective, the optimization seeks to manage systematic risk utilizing several constraints.

Rebalancing and Reconstitution
The Northern Trust Quality Large Cap Index is reconstituted quarterly (i.e., in February, May, August, and November) and adjusted intra-period only in connection with errors, securities’ eligibility, exchange connectivity, float changes and corporate actions, including, but not limited to, initial public offerings and spin-offs.

The index’s reconstitution occurs quarterly on the last business day of the month on which the U.S. equity markets are open for a full day of trading and becomes effective immediately after the close on such day. The Northern Trust Quality Large Cap Index reserves the right to postpone each reconstitution date for up to one week with prior public notice of such a postponement.

All changes to constituents and weightings will be announced to the public at least two (2) days prior to reconstitution or rebalancing and with definitive weights after the close of the reconstitution or rebalancing date and before the following day’s market opening.

¹ This factor seeks to identify companies that exhibit financial strength and stability relative to the market, a characteristic which the index provider defines as quality.
² The value factor is defined as the current worth of a company relative to its own historical value, book value, or valuation versus peers. Commonly used valuation metrics include: book-to-market value, price-to-earnings ratios, and enterprise value to earnings before, interest taxes, depreciation and amortization. The optimization sequence seeks to maximize exposure to securities trading at lower valuations.
³ The momentum factor reflects market sentiment defined as the slope of a stock’s price or other commonly used metrics measured over time. The optimization sequence seeks to maximize exposure to securities with positive momentum.

STOXX® USA ESG Impact Index℠

NUMBER OF COMPONENTS: APPROXIMATELY 270

INDEX DESCRIPTION: The STOXX® USA ESG Impact Index offers exposure to a set of U.S. companies that is tilted towards companies scoring better with respect to a select set of environmental, social, and governance (ESG) key performance indicators (KPIs). Eligible U.S. securities are selected from the STOXX® Global 1800 Index. The bottom 50% of such companies based on their ESG KPI scores are excluded from the Index, as are companies that do not adhere to the UN Global compact principles, are involved in controversial weapons or are coal miners (ICB Subsector 1771). Components are then weighted by free-float market cap combined with a cap factor that is based on a company’s aggregate ESG KPI score. Component weightings may also be adjusted to ensure that the weight of a single company is less than 5% at time of each index rebalancing or reconstitution.
STOXX® Global ESG Impact IndexSM

NUMBER OF COMPONENTS: APPROXIMATELY 908

INDEX DESCRIPTION: The STOXX® Global ESG Impact Index offers exposure to a set of global, developed-market companies that is tilted towards companies scoring better with respect to a select set of environmental, social, and governance (ESG) key performance indicators (KPIs). Eligible securities are selected from the STOXX® Global 1800 Index. The bottom 50% of such companies based on their ESG KPI scores are excluded from the Index, as are companies that do not adhere to the UN Global compact principles, are involved in controversial weapons or are coal miners (ICB Subsector 1771). Components are then weighted by free-float market cap combined with a cap factor that is based on a company’s aggregate ESG KPI score. Component weightings may also be adjusted to ensure that the weight representation of each country in the Underlying Index does not vary from that in the STOXX® Global 1800 Index by more than +/-1 percentage point and that the weight of a single company is less than 5% at time of each index rebalancing or reconstitution.

Morningstar® Global Upstream Natural Resources IndexSM

NUMBER OF COMPONENTS: APPROXIMATELY 120

INDEX DESCRIPTION. The Morningstar Global Upstream Natural Resources Index measures the performance of stocks issued by companies that have significant business operations in the ownership, management and/or production of natural resources in energy, agriculture, precious or industrial metals, timber and water resources sectors as defined by Morningstar’s industry classification standards. The Morningstar index methodology uses Morningstar proprietary industry classifications to identify companies within the five natural resource sectors, a minimum market capitalization test and a market liquidity measure to produce stocks eligible to be included in the Index for each sector. Each sector is then assigned a prescribed fixed weighting and number of equities to be included in the index subject to Index constraints for geographic regions and individual equity concentration.

STOXX® Global Broad Infrastructure Index

NUMBER OF COMPONENTS: APPROXIMATELY 149

INDEX DESCRIPTION: The STOXX® Global Broad Infrastructure Index measures the performance of companies that generate at least half of their revenues from one of the following 17 sectors defined as infrastructure-specific by a propriety classification system used by STOXX®: Communication (Cable & Satellite, Data Centers, Wireless, Wireless Towers, Wireline), Energy (Energy Utilities, Midstream Energy), Government Outsourcing / Social (Correctional Facilities, Hospitals, Postal Services), Transportation(Air Transportation, Passenger Transportation, Rail Transportation, Road Transportation, Water Transportation) and Utilities (Waste Management and Water Utilities).

The universe of securities for STOXX® Global Broad Infrastructure Index encompasses all constituents of the STOXX® Global Total Market Index listed in developed or emerging markets. The companies within the index universe for the STOXX® Global Broad Infrastructure Index which derive at least 50% of their revenues from one of the 17 sectors above are screened to meet a minimum liquidity measurement and sorted by their free-float market capitalization. The index methodology limits the number of index constituents from each supersector (Communication, Energy, Government Outsourcing/Social, Transportation, Utilities). Further, a maximum number of constituents per sector within each supersector is defined.

Northern Trust Global Quality Real Estate IndexSM

NUMBER OF COMPONENTS: APPROXIMATELY 140

Inception Date: October 15, 2013

The Northern Trust Global Quality Real Estate Index is designed to maximize exposure to quality, value and momentum factors, within a universe of companies operating in the real estate sector. The proprietary Northern Trust quality factor (henceforth referenced as the “Northern Trust Quality Score” or “NTQS”) is used to identify companies that exhibit strength in profitability, management expertise and cash flow, while value and momentum factors are included to help provide long term capital appreciation.

Eligible Securities

In order to be eligible for inclusion in the Northern Trust Global Quality Real Estate Index, a security must be a constituent of the Northern Trust Global Real Estate Index. The Northern Trust Global Real Estate Index is designed to provide broad-based exposure to companies operating in the Real Estate sector.

The Northern Trust Global Real Estate Index is a subset of the Northern Trust Global Index, which is designed to track the performance of the global investable equity markets covering approximately 97.5% of world’s float adjusted market capitalization.
Companies classified as engaging in the following activities, as defined by the Thomson Reuters Business Classification scheme, are excluded from the Underlying Index:

Mortgage REITs: Companies engaged in investment and ownership of property mortgages.

Other Real Estate Services: Companies engaged in providing real estate brokerage and agency services, real estate appraisal services, consulting services and management services.

Other Specialized REITs: Companies involved in two or more activities under the Specialized REIT Industry, with none being dominant.

Rebalancing and Reconstitution

The Northern Trust Global Quality Real Estate Index is reconstituted quarterly and adjusted intra-period only in connection with errors, securities’ eligibility, exchange connectivity, float changes and corporate actions, including, but not limited to, initial public offerings and spinoffs.

The indexes are reconstituted in February, May, August, and November on the last business day of the month in which the U.S. equity markets are open for trading, and becomes effective immediately after the close. The Northern Trust Global Quality Index reserves the right to postpone each reconstitution date for up to one week with prior public notice of such postponement.

All changes to constituents and weightings will be announced to the public at least two (2) days prior to reconstitution or rebalancing and with definitive weights after the close of the reconstitution or rebalancing date before the following day’s market opening.

Northern Trust Real Assets Allocation IndexSM

NUMBER OF COMPONENTS: 3

Inception Date: October 30, 2015

INDEX DESCRIPTION. The Northern Trust Real Assets Allocation Index is designed to reflect the performance of a universe of inflation sensitive securities operating in the following sectors: global infrastructure, global real estate and global natural resources. The index is intended to reflect an exposure to “real”1 assets, and is constructed using a proprietary optimization in an effort to reduce volatility of returns, while maintaining diversification amongst the eligible securities.

Eligible Securities

The following securities are eligible for inclusion in the Northern Trust Real Assets Allocation Index:

1. FlexShares® STOXX® Global Broad Infrastructure Index Fund - representing the index’s allocation to the global infrastructure sector of real assets
2. FlexShares® Global Quality Real Estate Index Fund - representing the index’s allocation to the global real estate sector of real assets
3. FlexShares® Morningstar® Global Upstream Natural Resources Index Fund - representing the index’s allocation to the global natural resources sector of real assets

Methodology

The construction of the index begins with a universe of eligible securities (defined in “Index Eligibility” section). Eligible securities are then optimized, with a main objective of lowering the absolute total risk of the index, as measured by volatility of returns, while maintaining diversification amongst the eligible securities. In order to obtain robust estimates of expected portfolio volatility, standard risk models2 are incorporated into our process to isolate both common factor and idiosyncratic risk3 at the underlying asset level4. In addition to solving for the main objective, constituent level weight constraints5 are utilized to maintain diversification within the index during each optimization.

All of the systematic risk constraints are placed in a constraint hierarchy so when a solution is not feasible due to hard constraints, a relaxed solution can be found.

Any changes to this methodology will be announced to the public at least sixty (60) days in advance prior to becoming effective.

Rebalancing

The Northern Trust Real Assets Allocation Index is rebalanced annually (i.e. April) at minimum and semi-annually (i.e. April and October) if the relative volatility estimates at the security level have breached an established threshold6. In addition, the index may be adjusted intra-period in connection with errors, securities’ eligibility, exchange connectivity, and corporate actions.
Real Assets are physical or tangible assets. Examples of real assets include but are not limited to commodities, precious metals, oil and real estate.

Risk models are statistical applications which help provide predictive risk estimates, by quantitatively de-constructing individual equity price movements and attributing those movements to common investment categories or factors (e.g. sector, industry, style, etc.) The use of standard risk models in the process provides an additional layer of constraints on the optimization outcome, and assists in reducing the index’s overall active risk exposure to any one single factor.

For the purpose of the index’s construction, an asset’s risk is defined by evaluating the volatility in returns, a figure which can be estimated through the use of standard risk models.

Eligible securities are de-constructed to the asset level to more precisely evaluate risk utilizing the underlying asset level exposures.

The maximum absolute constituent weight permitted during the optimization is 50%, while the minimum absolute constituent weight permitted during the optimization is 10%.

Cross asset volatility z-scores for each eligible security are tracked by Northern Trust. If the absolute change of z-scores is greater than 0.25 standard deviations — our established threshold — as evaluated on the second Friday of the month of October, a rebalance will be effected on the index effective as of the end of the month.

FlexShares® Quality Dividend Index Fund, FlexShares® Quality Dividend Defensive Index Fund, FlexShares® Quality Dividend Dynamic Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund

Brief descriptions of the Underlying Indexes of the above-listed Funds are provided below. Additional information about each of these Fund’s Underlying Indexes, including the components and weightings of the Underlying Indexes, as well as the rules that govern inclusion and weighting in the Underlying Indexes, is available at http://www.northerntrust.com/insights-research/asset-management-research/investment-insights/index-services.

Eligible Securities
In order to be eligible for inclusion in the Northern Trust Quality Dividend Indices, a security must be a constituent of the Northern Trust 1250 IndexSM. In order to be eligible for inclusion in the Northern Trust International Quality Dividend Indices, a security must be a constituent of the Northern Trust International Large Cap IndexSM. The Northern Trust 1250 Index is a float-adjusted market capitalization weighted index comprised of the 1250 largest U.S. domiciled companies by market capitalization. The Northern Trust International Large Cap Index is a float-adjusted market capitalization weighted index comprised of eligible large capitalization securities of developed or emerging market countries as determined by the Index Provider, pursuant to its index methodology. Additional information about the Northern Trust 1250 Index and Northern Trust International Large Cap Index (also referenced herein as a benchmark or benchmark index), including the components and weightings of the indexes, as well as the rules that govern inclusion and weighting in each of the indexes, is available at http://www.northerntrust.com/insights-research/asset-management-research/investment-insights/index-services.

Methodology
The construction of the Underlying Indexes begins with a universe of eligible securities (above). Securities ranking in the lowest quintile of quality based on a proprietary scoring model, as well as those which do not pay a dividend are removed prior to optimization. All remaining eligible securities are then optimized based on their exposure to quantitative factors such as: Quality (as defined by the proprietary scoring model), Dividend yield and Beta. The main objective of the optimization is to maximize exposure to the quality factor, realize a dividend yield above the benchmark index, and achieve the desired beta target all while minimizing the overall risk of the index versus its benchmark as measured by standard risk models.

Rebalancing and Reconstitution
The indexes are reconstituted in February, May, August and November on the last business day of the month in which the U.S. equity markets are open for trading, and becomes effective immediately after the close. Intra-quarter adjustments are made only in connection with errors, securities’ eligibility, exchange connectivity, float changes, and corporate actions, including, but not limited to, initial public offerings and spin-offs.

All changes to constituents and weightings will be announced to the public at least two (2) days prior to reconstitution or rebalancing, and with definitive weights after the close of the reconstitution or rebalancing date before the following day’s market opening.
Northern Trust Quality Dividend Index℠
NUMBER OF COMPONENTS: APPROXIMATELY 137
INCEPTION DATE: December 3, 2012
INDEX DESCRIPTION. The Northern Trust Quality Dividend Index℠ is designed to provide exposure to a high-quality income-oriented universe of long-only U.S. equity securities, with an emphasis on long-term capital growth and a targeted overall beta that is similar to that of the Northern Trust 1250 Index (the benchmark). Companies included in the index are selected based on expected dividend payment and fundamental factors such as profitability, management expertise and cash flow.

Northern Trust Quality Dividend Defensive Index℠
NUMBER OF COMPONENTS: APPROXIMATELY 156
INCEPTION DATE: December 3, 2012
INDEX DESCRIPTION. The Northern Trust Quality Dividend Defensive Index℠ is designed to provide exposure to a high-quality income-oriented universe of long-only U.S. equity securities, with an emphasis on long-term capital growth and a targeted overall beta that is generally between 0.5 to 1.0 times that of the Northern Trust 1250 Index (the benchmark). Companies included in the index are selected based on expected dividend payment and fundamental factors such as profitability, management expertise and cash flow.

Northern Trust Quality Dividend Dynamic Index℠
NUMBER OF COMPONENTS: APPROXIMATELY 132
INCEPTION DATE: December 3, 2012
INDEX DESCRIPTION. The Northern Trust Quality Dividend Dynamic Index℠ is designed to provide exposure to a high-quality income-oriented universe of long-only U.S. equity securities, with an emphasis on long-term capital growth and a targeted overall beta that is generally between 1.0 to 1.5 times that of the Northern Trust 1250 Index (the benchmark). Companies included in the index are selected based on expected dividend payment and fundamental factors such as profitability, management expertise and cash flow.

Northern Trust International Quality Dividend Index℠
NUMBER OF COMPONENTS: APPROXIMATELY 179
INCEPTION DATE: December 3, 2012
INDEX DESCRIPTION. The Northern Trust International Quality Dividend Index℠ is designed to provide exposure to a high-quality income-oriented universe of long-only international equity securities issued by non-U.S.-based companies, with an emphasis on long-term capital growth and a targeted overall beta that is similar to that of the Northern Trust International Large Cap Index (the benchmark). Companies included in the index are selected based on expected dividend payment and fundamental factors such as profitability, management expertise and cash flow.

Northern Trust International Quality Dividend Defensive Index℠
NUMBER OF COMPONENTS: APPROXIMATELY 187
INCEPTION DATE: December 3, 2012
INDEX DESCRIPTION. The Northern Trust International Quality Dividend Defensive Index℠ is designed to provide exposure to a high-quality income-oriented universe of long-only international equity securities issued by non-U.S.-based companies, with an emphasis on long-term capital growth and a targeted overall beta that is generally between 0.5 to 1.0 times that of the Northern Trust International Large Cap Index (the benchmark). Companies included in the index are selected based on expected dividend payment and fundamental factors such as profitability, management expertise and cash flow.

Northern Trust International Quality Dividend Dynamic Index℠
NUMBER OF COMPONENTS: APPROXIMATELY 161
INCEPTION DATE: December 3, 2012
INDEX DESCRIPTION. The Northern Trust International Quality Dividend Dynamic Index℠ is designed to provide exposure to a high-quality income-oriented universe of long-only international equity securities issued by non-U.S.-based companies, with an emphasis on long-term capital growth and a targeted overall beta that is generally between 0.5 to 1.0 times that of the Northern Trust International Large Cap Index (the benchmark). Companies included in the index are selected based on expected dividend payment and fundamental factors such as profitability, management expertise and cash flow.
INDEX DESCRIPTION. The Northern Trust International Quality Dividend Dynamic Index℠ is designed to provide exposure to a high-quality income-oriented universe of long-only international equity securities issued by non-U.S.-based companies, with an emphasis on long-term capital growth and a targeted overall beta that is generally between 1.0 to 1.5 times that of the Northern Trust International Large Cap Index (the benchmark). Companies included in the index are selected based on expected dividend payment and fundamental factors such as profitability, management expertise and cash flow.

iBoxx 3-Year Target Duration TIPS Index

NUMBER OF COMPONENTS: APPROXIMATELY 19

INDEX DESCRIPTION. The iBoxx 3-Year Target Duration TIPS Index measures the performance of Treasury Inflation Protected Securities (TIPS) as determined by Markit iBoxx’s proprietary index methodology. The iBoxx index methodology targets a modified adjusted duration of 3.0 years and defines the eligible universe of TIPS as having no less than one year and no more than ten years until maturity as of the Index rebalancing date. A proprietary regression calculation is then used to determine the modified adjusted duration of the TIPS and weight the TIPS in the Index at a modified adjusted duration level within a range of 3.0 years, plus or minus 5% within Index constraints.

iBoxx 5-Year Target Duration TIPS Index

NUMBER OF COMPONENTS: APPROXIMATELY 21

INDEX DESCRIPTION. The iBoxx 5-Year Target Duration TIPS Index measures the performance of Treasury Inflation Protected Securities (TIPS) as determined by Markit iBoxx’s proprietary index methodology. The iBoxx index methodology targets a modified adjusted duration of 5.0 years and defines the eligible universe of TIPS as having no less than 3 years and no more than 20 years until maturity as of the Index rebalancing date. A proprietary regression calculation is then used to determine the modified adjusted duration of the TIPS and weight the TIPS in the Index at a modified adjusted duration level within a range of 5.0 years, plus or minus 5% within Index constraints.

The ICE® BofAML® Constrained Duration US Mortgage Backed Securities Index℠

NUMBER OF COMPONENTS: APPROXIMATELY 185

INDEX DESCRIPTION. The ICE® BofAML® Constrained Duration US Mortgage Backed Securities Index℠ tracks the performance of US dollar denominated 30-year, 20-year and 15-year fixed rate residential mortgage pass-through securities publicly issued by US agencies in the US domestic market. Fixed rate mortgage pools are included in the Underlying Index provided they have at least one year remaining term to final maturity and a minimum amount outstanding of at least $5 billion per generic coupon. In addition, individual production years within a generic coupon must have at least $1 billion outstanding face value to enter the Underlying Index and at least $250 million outstanding face value to remain in the index. Balloon, mobile home, graduated payment and quarter coupon fixed rate mortgages are excluded from the index, as are all collateralized mortgage obligations. The Underlying Index constituents are capitalization weighted, based on their outstanding face value times price plus accrued interest, adjusted to achieve an effective duration for the Underlying Index that is generally between 3.25 and 4.25 years.

Neither the FlexShares® Disciplined Duration MBS Index Fund (the “Product”) nor NTI (the “Licensee”) are not sponsored, endorsed, sold or promoted by ICE. ICE has not passed on the legality or suitability of, or the accuracy or adequacy of descriptions and disclosures relating to, the Product, nor makes any representation or warranty, express or implied, to the owners of Product or any member of the public regarding the Product or the advisability of investing in the Product, particularly the ability of the Index to track performance of any market or strategy. ICE’s only relationship to the Licensee is the licensing of certain trademarks and trade names and the Index or components thereof. ICE is the administrator of the Index and the Index is determined, composed and calculated by ICE without regard to the Licensee or the Product or its holders. ICE has no obligation to take the needs of the Licensee or the holders of the Product into consideration in determining, composing or calculating the Index. ICE is not responsible for and has not participated in the determination of the timing of, prices of, or quantities of the Product to be issued or in the determination or calculation of the equation by which the Product is to be priced, sold, purchased, or redeemed. ICE has no obligation or liability in connection with the administration, marketing, or trading of the Product.
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Northern Trust Credit-Scored US Corporate Bond IndexSM

NUMBER OF COMPONENTS: APPROXIMATELY 1,378

Inception Date: October 10, 2014

INDEX DESCRIPTION. The Northern Trust Credit-Scored US Corporate Bond IndexSM is designed to measure the performance
of a diversified universe of intermediate maturity, US-dollar denominated bonds of companies with investment grade-like charac-
teristics, and enhanced short-term and long-term solvency.

Eligible Securities

In order to be eligible for inclusion in the Northern Trust Credit-Scored US Corporate Bond Index, each bond issue must be: i) a
constituent of the Northern Trust Investment Grade US Corporate Bond Index; ii) from a top 80% issuer based on outstanding
market capitalization of debt1; iii) $500 million or greater in terms of outstanding principal at each rebalance; and iv) issued by a
publically traded company2.

Methodology

The construction of the Underlying Index begins with a securities screen to determine eligible securities (as described above).
Once all eligible securities have been identified, the securities are then optimized based on their exposure to quantitative factors
such as: Credit-Score3, as determined by Northern Trust’s Quantitative Research team’s proprietary scoring model4, Option
Adjusted Spread (OAS)5, and Effective Duration6. The primary objective of the optimization is to maximize exposure to the credit-
score factor, and maintain a similar Option Adjusted Spread and Effective Duration profile relative to the eligible universe. In
addition to that main objective, systematic risk is managed during the optimization utilizing several constraints.

These constraints are listed below (bounds show as relative weightings unless otherwise noted): Security level constraint: to limit
an index constituent’s maximum or minimum weight versus the eligible universe to either full underweight or two times (2x) the
weight in the eligible universe; Minimum absolute constituent constraint: to require that each index constituent has a weight of at
least one basis point (0.01%); Minimum absolute turnover constraint: to require that index turnover at the constituent level is
larger than one basis point (0.01%) for each change made during the rebalance; Credit-Score constraint: to remove bonds ranking
in the lowest quintile in non-Financial sectors7; Issuer level constraint: to limit each issuer’s absolute weight to 8% or less; and
Sector constraint: to limit the index’s maximum or minimum sector weight exposure to +/-10% versus the eligible universe. All the
systematic risk constraints are placed in the constraint hierarchy so when a solution is not feasible due to hard constraints, a
relaxed solution is found.

Any changes to this methodology will be announced to the public at least sixty (60) days in advance prior to becoming effective.

Rebalancing and Reconstitution

The Northern Trust Credit-Scored US Corporate Bond Index is rebalanced monthly8 on the last business day of the month in
which U.S. bond markets are open for trading9, and becomes effective immediately after the market close. Intra-period adjustments
may be made at the discretion of the index provider in connection with errors, changes in eligibility, and corporate actions. All
changes to constituents and weightings will be announced to the public at least two (2) days prior to rebalancing, and again with
definitive weights after the close of the rebalance date, before the following business day’s market open.

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1 All issuers within the Northern Trust Investment Grade US Corporate Bond Index are sorted by weight in descending order,
and issuers are selected as eligible until the index has reached the 80% cumulative market capitalization level of total debt outstanding in the evaluated universe.

2 Issuer is required to have an active listing on one of the global equity exchanges.

3 This factor seeks to identify companies that exhibit strength in both short-term and long term solvency.

4 The core components of the proprietary credit scoring model are based on quantitative ranking of various metrics obtained from company filings and recent price activity. These scores have three components: Management Efficiency (e.g. corporate finance activities), Profitability (e.g. assess the reliability and sustainability of financial performance) and Solvency (short and long term).

5 A measurement of the spread of a security’s rate of return and the risk-free rate of return, adjusted to account for any embedded options.

6 A measure of the sensitivity of the price of a bond to a change in interest rates, adjusted for embedded options, and commonly utilized to evaluate a bond’s theoretical change in value given a shift in the yield curve.

7 Northern Trust’s Asset Management (“NTAM”) team categorizes all issues present in the Northern Trust Investment Grade US Corporate Bond Index into the following sectors: Consumer, Energy, Financials, Industrials, and Telecom, Technology & Media (TTM).

8 Data used to strike the forward index is locked down for construction purposes eight business days prior to month end.

9 Per the US holiday schedule posted at www.sifma.org/services/holiday-schedule/.

Northern Trust Credit-Scored US Long Corporate Bond Index®

NUMBER OF COMPONENTS: APPROXIMATELY 856

Inception Date: July 7, 2015

INDEX DESCRIPTION. The Northern Trust Credit-Scored US Long Corporate Bond Index is designed to measure the performance of a diversified universe of longer term maturity,1 US-dollar denominated bonds of companies with investment grade credit quality and enhanced short-term and long-term solvency.

Eligible Securities

In order to be eligible for inclusion in the Northern Trust Credit-Scored US Long Corporate Bond Index, each bond issue must be: (i) a constituent of the Northern Trust Investment Grade US Long Corporate Bond Index; (ii) $500 million or greater in terms of outstanding principal at each rebalance; and (iii) issued by a publicly traded company².

Methodology

The construction of the index begins with a securities screen to determine eligible securities (as described above). Once all eligible securities have been identified, the securities are then optimized based on their exposure to quantitative factors such as: Credit-Score³, as determined by Northern Trust’s Quantitative Research Team’s proprietary scoring model⁴, Option Adjusted Spread (OAS)⁵, and Effective Duration⁶.

The primary objective of the optimization is to maximize exposure to the credit-score factor, and maintain a similar Option Adjusted Spread and Effective Duration profile relative to the eligible universe. In addition to that main objective, systematic risk is managed during the optimization utilizing several constraints. These constraints are listed below (bounds show as relative weightings unless otherwise noted): Security level constraint: to limit an index constituent’s maximum or minimum weight versus the eligible universe to either full underweight or three times (3.0x) the weight in the eligible universe; Minimum absolute constituent constraint: to require that each index constituent has a weight of at least one basis point (0.01%); Minimum absolute turnover constraint: to require that index turnover at the constituent level is larger than one basis point (0.01%) for each change made during the rebalance; Credit-Score constraint: to remove bonds ranking in the lowest quintile in non-Financial sectors⁷; Issuer level constraint: to limit each issuer’s absolute weight to 5% or less; and Sector constraint: to limit the index’s maximum or minimum sector weight exposure to +/-10% versus the eligible universe. All the systematic risk constraints are placed in the constraint hierarchy so when a solution is not feasible due to hard constraints, a relaxed solution is found.

Any changes to this methodology will be announced to the public at least sixty (60) days in advance prior to becoming effective.

Rebalancing and Reconstitution

The Northern Trust Credit-Scored US Long Corporate Bond Index is rebalanced monthly⁸ on the last business day of the month in which U.S. bond markets are open for trading⁹, and becomes effective immediately after the market close. Intra-period adjustments may be made at the discretion of the index provider in connection with errors, changes in eligibility, and corporate actions. All changes to constituents and weightings will be announced to the public at least two (2) days prior to rebalancing, and again with definitive weights after the close of the rebalance date, before the following business day’s market open.
Longer term maturity is defined as 10 years or longer to maturity date at the time of each rebalance.

Issuer is required to have an active listing on one of the global equity exchanges.

This factor seeks to identify companies that exhibit strength in both short-term and long-term solvency.

The core components of the proprietary credit scoring model are based on quantitative ranking of various metrics obtained from company filings and recent price activity. These scores have three components: Management Expertise (e.g. corporate finance activities), Profitability (e.g. assess the reliability and sustainability of financial performance) and Solvency (short- and long-term).

A measurement of the spread of a security’s rate of return and the risk-free rate of return, adjusted to account for any embedded options.

A measure of the sensitivity of the price of a bond to a change in interest rates, adjusted for embedded options, and commonly utilized to evaluate a bond’s theoretical change in value given a shift in the yield curve.

Northern Trust’s Asset Management team categorizes all issues present in the NT Investment Grade US Long Corporate Bond Index into the following sectors: Consumer, Energy, Financials, Industrials, and Telecom, Technology & Media (“TTM”).

Data used to strike the forward index is locked down for construction purposes eight business days prior to month end.

Per the US holiday schedule posted at www.sifma.org/services/holiday-schedule.

**Northern Trust High Yield Value-Scored US Corporate Bond Index**

**Number of Components:** Approximately 1,007

**Inception Date:** April 30, 2018

**Index Description.** The Northern Trust High Yield Value-Scored US Corporate Bond IndexSM is designed to measure the performance of a diversified universe of high yield, US-dollar denominated bonds of companies exhibiting favorable fundamental qualities, market valuations and liquidity, as defined by NTI’s proprietary scoring models.

**Eligible Securities**

In order to be eligible for inclusion in the Northern Trust High Yield Value-Scored US Corporate Bond Index (the “Index”), each bond issue must be a constituent of the Northern Trust High Yield US Corporate Bond Index.

**Methodology**

The construction of the Index begins with a securities screen to determine eligible securities. Once all eligible securities have been identified, the securities are then optimized based on their exposure to quantitative factors such as: Value-Score1, Credit-Score2 and Liquidity-Score3, as determined by NTI’s Quantitative Research team’s proprietary scoring models.

The primary objective of the optimization is to maximize the exposure to the value-score factor relative to the eligible universe. In addition to that objective, systematic risk is managed during the optimization through the use of several constraints. These constraints are listed below (bounds show as relative weightings unless otherwise noted):

- Minimum absolute constituent constraint: to require that each Index constituent has a weight of at least one basis point (0.01%);
- Minimum absolute turnover constraint: to require that Index turnover at the constituent level is larger than one basis point (0.01%) for each change made during the reconstitution;
- Issuer level constraint: to limit each issuer’s absolute weight to 5% or less;
- Sector constraint: to limit the Index’s maximum or minimum sector weight exposure to +/-8% versus the eligible universe (i.e., the Parent Index);
- Effective Duration4: to constrain the Index’s effective duration to +/- 0.10 versus the eligible universe at each reconstitution;
- Proprietary Credit-Score constraint: to remove bonds ranking in the lowest decile of proprietary score;
- Proprietary Liquidity Score constraint: to restrict new issuances that fall in the bottom 5% of liquidity within each sector, per the proprietary score, at each reconstitution; and
- Turnover constraint: to limit the Index’s turnover at each reconstitution to 15%.
All the systematic risk constraints are placed in the constraint hierarchy so when a solution is not feasible due to hard constraints, a relaxed solution is found.

Any changes to this methodology will be announced to clients at least sixty (60) days in advance prior to becoming effective.

**Rebalancing and Reconstitution**

The Index is reconstituted monthly\(^5\) on the last business day of the month in which U.S. bond markets are open for trading\(^6\), and becomes effective immediately after the market close. Intra-period adjustments may be made at the discretion of the index provider in connection with errors, changes in eligibility, and corporate actions.

The Index reserves the right to postpone each reconstitution date for up to one week with prior client notification of such a postponement.

All changes to constituents and weightings will be announced to clients at least two (2) days prior to the reconstitution or rebalancing date, and again with definitive weights after the close of the reconstitution or rebalancing date, before the following business day’s market open.

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1. The core components of the proprietary value scoring model are based on quantitative ranking of various metrics obtained from company filings with the SEC, as well as recent security price activity. The scores have multiple components, and include but are not limited to the following: Valuation (e.g. to assess the relative value of the security versus other similar securities), spread analysis (e.g. to assess the risk/return trade-off associated with each security versus other similar securities) and solvency (e.g. to assess the corporation’s short term and long term solvency and also its risk of default).

2. The core components of the proprietary credit scoring model are based on quantitative ranking of various metrics obtained from company filings with the SEC and recent price activity. These scores have three components: management expertise (e.g. corporate finance activities), profitability (e.g. assess the reliability and sustainability of financial performance) and solvency (short and long term).

3. The core components of the proprietary liquidity score are based on a quantitative ranking of security characteristics obtained from company filings with the SEC. Examples of data sets utilized to determine liquidity include but are not limited to: time to maturity (e.g. time until the security reaches its maturity date as measured in years), total issuer debt outstanding (e.g. the sum of all debt outstanding for a single corporate issuer), and time since original issuance (e.g. the time that has elapsed since the security was originally issued as measured in years).

4. A measure of the sensitivity of the price of a bond to a change in interest rates, adjusted for embedded options, and commonly utilized to evaluate a bond’s theoretical change in value given a shift in the yield curve.

5. Data used to strike the forward index is locked down for construction purposes eight business days prior to month end.

6. Per the US holiday schedule posted at www.sifma.org/services/holiday-schedule/.

**INVESTMENT RESTRICTIONS**

Each Fund, except the FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund, is subject to the fundamental investment restrictions enumerated below which may be changed with respect to a particular Fund only by a vote of the holders of a majority of such Fund’s outstanding shares as described in “Description of Shares” on page 93.

No Fund may:

1) Make loans, except through: (a) the purchase of debt obligations in accordance with the Fund’s investment objective and strategies; (b) repurchase agreements with banks, brokers, dealers and other financial institutions; (c) loans of securities; and (d) loans to affiliates of the Fund to the extent permitted by law.

2) Purchase or sell real estate or real estate limited partnerships, but this restriction shall not prevent a Fund from investing directly or indirectly in portfolio instruments secured by real estate or interests therein or from acquiring securities of real estate investment trusts or other issuers that deal in real estate.

3) Purchase or sell physical commodities unless acquired as a result of ownership of securities or other instruments (but this shall not prevent the Funds: (i) from purchasing or selling options, futures contracts or other derivative instruments; or (ii) from investing in securities or other instruments backed by physical commodities).
4) Act as underwriter of securities, except as a Fund may be deemed to be an underwriter under the Securities Act in connection with the purchase and sale of portfolio instruments in accordance with its investment objective and portfolio management strategies.

5) Borrow money, except that to the extent permitted by applicable law: (a) a Fund may borrow from banks, other affiliated investment companies and other persons, and may engage in reverse repurchase agreements and other transactions which involve borrowings, in amounts up to 33 1/3% of its total assets (including the amount borrowed) or such other percentage permitted by law; (b) a Fund may borrow up to an additional 5% of its total assets for temporary purposes; (c) a Fund may obtain such short-term credits as may be necessary for the clearance of purchases and sales of portfolio securities; and (d) a Fund may purchase securities on margin. If due to market fluctuations or other reasons a Fund’s borrowings exceed the limitations stated above, the Trust will promptly reduce the borrowings of a Fund in accordance with the 1940 Act.

6) Issue any senior security, except as permitted under the 1940 Act, as amended and as interpreted, modified or otherwise permitted by regulatory authority having jurisdiction, from time to time.

7) Concentrate its investments (i.e., invest 25% or more of its total assets in the securities of a particular industry or group of industries), except that a Fund will concentrate to approximately the same extent that its Underlying Index concentrates in the securities of such particular industry or group of industries. For purposes of this limitation, securities of the U.S. government (including its agencies and instrumentalities), repurchase agreements collateralized by U.S. government securities, and securities of state or municipal governments and their political subdivisions are not considered to be issued by members of any industry.

8) With respect to 75% of the Fund’s assets (i) purchase securities of any issuer (except securities issued or guaranteed by the U.S. Government, its agencies or instrumentalities and repurchase agreements involving such securities) if, as a result, more than 5% of the total assets of the Fund would be invested in the securities of any one issuer, or (ii) acquire more than 10% of the outstanding voting securities of any one issuer (applies ONLY to the FlexShares® Morningstar US Market Factor Tilt Index Fund, FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Quality Dividend Index Fund, FlexShares® Quality Dividend Defensive Index Fund, FlexShares® Quality Dividend Dynamic Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund).

The following fundamental investment restrictions, which may be changed only by a vote of the holder of a majority of a Fund’s outstanding shares as described in “Description of Shares” on page 93, apply only to FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund.

Each Fund may not:

1) Make loans, except to the extent permitted under the 1940 Act, rules and regulations thereunder or any exemption therefrom as such statute, rules or regulations may be amended or interpreted from time to time.

2) Purchase or sell real estate, except to the extent permitted under the 1940 Act, rules and regulations thereunder or any exemption therefrom as such statute, rules or regulations may be amended or interpreted from time to time.

3) Purchase or sell commodities, except to the extent permitted under the 1940 Act, rules and regulations thereunder or any exemption therefrom as such statute, rules or regulations may be amended or interpreted from time to time.

4) Act as underwriter of securities, except to the extent permitted under the 1940 Act, rules and regulations thereunder or any exemption therefrom as such statute, rules or regulations may be amended or interpreted from time to time.

5) Borrow money, except to the extent permitted under the 1940 Act, rules and regulations thereunder or any exemption therefrom as such statute, rules or regulations may be amended or interpreted from time to time.
6) Issue any senior security, except to the extent permitted under the 1940 Act, rules and regulations thereunder or any exemption therefrom as such statute, rules or regulations may be amended or interpreted from time to time.

7) Concentrate its investments (i.e., invest 25% or more of its total assets in the securities of a particular industry or group of industries), except that the Fund will concentrate to approximately the same extent that its Underlying Index concentrates in the securities of such particular industry or group of industries. For purposes of this limitation, securities of the U.S. government (including its agencies and instrumentalities), repurchase agreements collateralized by U.S. government securities, and securities of state or municipal governments and their political subdivisions are not considered to be issued by members of any industry.

8) With respect to 75% of the Fund’s assets (i) purchase securities of any issuer (except securities issued or guaranteed by the U.S. Government, its agencies or instrumentalities and repurchase agreements involving such securities) if, as a result, more than 5% of the total assets of the Fund would be invested in the securities of any one issuer, or (ii) acquire more than 10% of the outstanding voting securities of any one issuer. (applies ONLY to the FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund and FlexShares® Disciplined Duration MBS Index Fund).

9.) Make any investment inconsistent with the Fund’s classification as a diversified company under the 1940 Act (applies ONLY to the FlexShares® High Yield Value-Scored Bond Index Fund).

The following descriptions from the 1940 Act may assist shareholders in understanding the above policies and restrictions.

**Borrowing.** The 1940 Act presently allows a fund to borrow from any bank (including pledging, mortgaging or hypothecating assets) in an amount up to 33-1/3% of its total assets, including the amount borrowed (not including temporary borrowings not in excess of 5% of its total assets).

**Senior Securities.** Senior securities may include any obligation or instrument issued by a fund evidencing indebtedness. The 1940 Act generally prohibits funds from issuing senior securities, although it does not treat certain transactions as senior securities, such as certain borrowings, short sales, reverse repurchase agreements, firm commitment agreements and standby commitments, with appropriate earmarking or segregation of assets to cover such obligation.

**Lending.** Under the 1940 Act, a fund may only make loans if expressly permitted by its investment policies. The Funds’ non-fundamental investment policy on lending is set forth below.

**Underwriting.** Under the 1940 Act, underwriting securities involves a fund purchasing securities directly from an issuer for the purpose of selling (distributing) them or participating in any such activity either directly or indirectly. Under the 1940 Act, a diversified fund may not make any commitment as underwriter, if immediately thereafter the amount of its outstanding underwriting commitments, plus the value of its investments in securities of issuers (other than investment companies) of which it owns more than 10% of the outstanding voting securities, exceeds 25% of the value of its total assets.

**Real Estate.** The 1940 Act does not directly restrict a fund’s ability to invest in real estate, but does require that every fund have a fundamental investment policy governing such investments. The FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund have adopted a fundamental policy that would permit direct investment in real estate. However, each Fund has a non-fundamental investment limitation that prohibits it from investing directly in real estate. This non-fundamental policy may be changed only by vote of the Board.

**Commodities.** The 1940 Act does not directly restrict a fund’s ability to invest in commodities, but does require that every fund have a fundamental investment policy governing such investments. The FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund have adopted a fundamental policy that would permit direct investment in commodities. However, each of these Funds has a non-fundamental investment limitation that prohibits it from investing directly in physical commodities.
This non-fundamental policy may be changed only by vote of the Board.

The following investment restrictions are non-fundamental policies of the FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund, which may be changed by the Board without a vote of shareholders:

Each Fund may not:

1) Make loans, except through: (a) the purchase of debt obligations in accordance with each Fund’s investment objective and strategies; (b) repurchase agreements with banks, brokers, dealers and other financial institutions; (c) loans of securities; and (d) loans to affiliates of the Funds to the extent permitted by law.

2) Purchase or sell real estate or real estate limited partnerships, but this restriction shall not prevent the Funds from (a) investing directly or indirectly in portfolio instruments secured by real estate or interests therein; (b) from acquiring securities of real estate investment trusts or other issuers that deal in real estate or mortgage-related securities; or (c) holding and selling real estate acquired by the Funds as a result of ownership of securities. (FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund only).

3) Purchase or sell real estate or real estate limited partnerships, but this restriction shall not prevent the Funds from investing directly or indirectly in portfolio instruments secured by real estate or interests therein or from acquiring securities of real estate investment trusts or other issues that deal in real estate. (FlexShares® STOXX® Global Broad Infrastructure Index Fund only).

4) Purchase or sell physical commodities unless acquired as a result of ownership of securities or other instruments (but this shall not prevent the Funds: (i) from purchasing or selling options, futures contracts or other derivative instruments; or (ii) from investing in securities or other instruments backed by physical commodities).

5) Act as underwriter of securities, except as each Fund may be deemed to be an underwriter under the Securities Act in connection with the purchase and sale of portfolio instruments in accordance with its investment objective and portfolio management strategies.

6) Borrow money, except that to the extent permitted by applicable law: (a) each Fund may borrow from banks, other affiliated investment companies and other persons, and may engage in reverse repurchase agreements and other transactions which involve borrowings, in amounts up to 33 1/3% of its total assets (including the amount borrowed) or such other percentage permitted by law; (b) each Fund may borrow up to an additional 5% of its total assets for temporary purposes; (c) each Fund may obtain such short-term credits as may be necessary for the clearance of purchases and sales of portfolio securities; and (d) each Fund may purchase securities on margin. If due to market fluctuations or other reasons a Fund’s borrowings exceed the limitations stated above, the Trust will promptly reduce the borrowings of the Fund in accordance with the 1940 Act.

Notwithstanding other fundamental investment restrictions (including, without limitation, those restrictions relating to issuer diversification, industry concentration and control), each Fund may purchase securities of other investment companies to the full extent permitted under Section 12 or any other provision of the 1940 Act (or any successor provision thereto) or under any regulation or order of the SEC.

For the purpose of industry concentration, in determining industry classification, the Trust may use any one or more of the following: the Bloomberg Industry Group Classification, Standard & Poors, J.J. Kenny Municipal Purpose Codes, FT Interactive Industrial Codes, Securities Industry Classification Codes, Global Industry Classification Standard or the Morgan Stanley Capital International industry classification titles or Barclays Capital sector classification scheme. Also for the purpose of
industry concentration, industrial development bonds issued by non-governmental issuers may be considered to be issued by members of an industry. Non-governmental issuers are issuers other than the U.S. government (including its agencies and instrumentalities) and state or municipal governments and their political subdivisions.

Any Investment Restriction which involves a maximum percentage (other than the restriction set forth above in Fundamental Investment Restriction No. 5 for the FlexShares® Morningstar US Market Factor Tilt Index Fund, FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Global Upstream Natural Resources Index Fund, FlexShares® Quality Dividend Index Fund, FlexShares® Quality Dividend Defensive Index Fund, FlexShares® Quality Dividend Dynamic Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund, FlexShares® International Quality Dividend Dynamic Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund) will not be considered violated unless an ex-cess over the percentage occurs immediately after, and is caused by, an acquisition or encumbrance of securities or assets of a Fund. The 1940 Act requires that if the asset coverage for borrowings at any time falls below the limits described in Fundamental Investment Restriction No. 5 and Non-Fundamental Investment Restriction No. 6, the Fund will, within three days thereafter (not including Sundays and holidays), reduce the amount of its borrowings to an extent that the net asset coverage of such borrowings shall conform to such limits.

Each Fund has adopted a non-fundamental investment policy in accordance with Rule 35d-1 under the 1940 Act to invest, under normal circumstances, at least 80% of the value of its net assets, plus the amount of any borrowings for investment purposes, in securities of the Fund’s Underlying Index and, with respect to (i) the FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund, in Depositary Receipts and (ii) the FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund) will not be considered violated unless an excess over the percentage occurs immediately after, and is caused by, an acquisition or encumbrance of securities or assets of a Fund. The 1940 Act requires that if the asset coverage for borrowings at any time falls below the limits described in Fundamental Investment Restriction No. 5 and Non-Fundamental Investment Restriction No. 6, the Fund will, within three days thereafter (not including Sundays and holidays), reduce the amount of its borrowings to an extent that the net asset coverage of such borrowings shall conform to such limits.

CONTINUOUS OFFERING

The method by which Creation Unit Aggregations of shares are created and traded may raise certain issues under applicable securities laws. Because new Creation Unit Aggregations of shares are issued and sold by the Funds on an ongoing basis, at any point a “distribution,” as such term is used in the Securities Act, may occur. Broker-dealers and other persons are cautioned that some activities on their part, depending on the circumstances, result in their being deemed participants in a distribution in a manner which could render them statutory underwriters and subject them to the prospectus delivery requirement and liability provisions of the Securities Act.

For example, a broker-dealer firm or its client may be deemed a statutory underwriter if it takes Creation Unit Aggregations after placing an order with the Distributor, breaks them down into constituent shares, and sells such shares directly to customers, or if it chooses to couple the creation of a supply of new shares with an active selling effort involving solicitation of secondary market demand for shares. A determination of whether one is an underwriter for purposes of the Securities Act must take into account all the facts and circumstances pertaining to the activities of the broker-dealer or its client in the particular case, and the examples mentioned above should not be considered a complete description of all the activities that could lead to a categorization as an underwriter. Broker-dealer firms should also note that dealers who are not “underwriters” but are effecting transactions in shares, whether or not participating in the distribution of shares, generally are required to deliver a prospectus. This is because the prospectus delivery exemption in Section 4(3) of the Securities Act is not available in respect of such transactions as a result of Section 24(d) of the 1940 Act. Firms that incur a prospectus delivery obligation with respect to shares of the Funds
are reminded that, pursuant to Rule 153 under the Securities Act, a prospectus delivery obligation under Section 5(b)(2) of the Securities Act owed to an exchange member in connection with a sale on the Listing Exchange is satisfied by the fact that the prospectus is available at the Listing Exchange upon request. The prospectus delivery mechanism provided in Rule 153 is only available with respect to transactions on an exchange.

PORTFOLIO HOLDINGS

The Board has adopted a policy on disclosure of portfolio holdings, which it believes is in the best interest of the Funds’ shareholders. The policy provides that neither the Funds nor their Investment Adviser, Distributor or any agent, or any employee thereof (“Fund Representative”) will disclose a Fund’s portfolio holdings information to any person other than in accordance with the policy. For purposes of the policy, “portfolio holdings information” means a Fund’s actual portfolio holdings, as well as non-public information about its trading strategies or pending transactions including the portfolio holdings, trading strategies or pending transactions of any commingled fund portfolio which contains identical holdings as the Fund. Under the policy, neither a Fund nor any Fund Representative may solicit or accept any compensation or other consideration in connection with the disclosure of portfolio holdings information. A Fund Representative may provide portfolio holdings information to third parties if such information has been included in a Fund’s public filings with the SEC or is disclosed on the Fund’s publicly accessible website. Information posted on a Fund’s website may be separately provided to any person commencing the day after it is first published on the Fund’s website.

Under the policy, each business day each Fund’s portfolio holdings information will be provided to the Distributor or other agent for dissemination through the facilities of the National Securities Clearing Corporation (“NSCC”) and/or other fee based subscription services to NSCC members and/or subscribers to those other fee-based subscription services, including Authorized Participants (defined below) and to entities that publish and/or analyze such information in connection with the process of purchasing or redeeming Creation Units or trading shares of Funds in the secondary market. Additionally, under the policy, with respect to the FlexShares® US Quality Large Cap Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Quality Dividend Index Fund, FlexShares® Quality Dividend Defensive Index Fund, FlexShares® Quality Dividend Dynamic Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund, FlexShares® International Quality Dividend Dynamic Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and the FlexShares® High Yield Value-Scored Bond Index Fund, each business day before commencement of trading, the Trust will disclose on its website the identities and quantities of each Fund’s portfolio holdings that will form the basis for the Fund’s calculation of NAV at the end of the Business Day. The Distributor may also make available portfolio holdings information to other institutional market participants and entities that provide information services. This information typically reflects each Fund’s anticipated holdings on the following business day. The “Authorized Participants” are generally large institutional investors that have been authorized by the Distributor to purchase and redeem large blocks of shares (known as Creation Units) pursuant to legal requirements, including the exemptive order granted by the SEC, to which the Funds offer and redeem shares.

Other than portfolio holdings information made available in connection with the creation/redemption process, as discussed above, portfolio holdings information that is not filed with the SEC or posted on the publicly available website may be provided to third parties only in limited circumstances. Third-party recipients will be required to keep all portfolio holdings information confidential and are prohibited from trading on the information they receive. Disclosure to third parties must be approved in advance by the Trust’s Chief Compliance Officer (“CCO”). Disclosure to providers of auditing, custody, proxy voting and other similar services for the Funds, as well as rating and ranking organizations, will generally be permitted; however, information may be disclosed to other third parties (including, without limitation, individuals, institutional investors, and Authorized Participants that sell shares of a Fund) only upon approval by the CCO, who must first determine that the Fund has a legitimate business purpose for doing so. In general, each recipient of non-public portfolio holdings information must sign a confidentiality and non-trading agreement, although this requirement will not apply when the recipient is otherwise subject to a duty of confidentiality as determined by the CCO. In accordance with the policy, the recipients who receive non-public portfolio holdings information on an ongoing basis are as follows: the Investment Adviser and its affiliates, the Funds’ independent registered public accounting firm, the Funds’ distributor, administrator and custodian, the Funds’ legal counsel, Drinker Biddle & Reath LLP, the non-interested Trustees’ counsel, Ropes & Gray LLP, the Funds’ financial printer, R.R. Donnelley, and the Funds’ proxy voting service (Institutional Shareholder Services, Inc.). These entities are obligated to keep such information confidential. Third-party providers of custodial or accounting services to a Fund may release non-public portfolio holdings information of the Fund only with the permission of Fund Representatives.

Each Fund discloses its portfolio holdings and the percentages they represent of the Fund’s net assets each day the Fund is open for business, on the Fund’s website. More information about this disclosure is available at www.flexshares.com. A Fund may publish on the website complete portfolio holdings information more frequently if it has a legitimate business purpose for
doing so. Portfolio holdings will be disclosed through required filings with the SEC. Each Fund files its portfolio holdings with the SEC for each fiscal quarter on Form N-CSR (with respect to each annual period and semiannual period) and Form N-Q (or successor Form) (with respect to the first and third fiscal quarters of the Fund’s fiscal year). Shareholders may obtain a Fund’s Forms N-CSR and N-Q filings on the SEC’s website at www.sec.gov. You may call the SEC at 1-800-SEC-0330 for information about the SEC’s website.

Under the policy, the Board is to receive information, on a quarterly basis, regarding any other disclosures of non-public portfolio holdings information that were permitted during the preceding quarter.
TRUSTEES AND OFFICERS

The Board is responsible for the management and business and affairs of the Trust. Set forth below is information about the Trustees and Officers of the Trust as of the date of this SAI. A brief statement of their present positions and principal occupations during the past five years is also provided.

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<th>NAME, ADDRESS(1)</th>
<th>AGE, POSITIONS HELD WITH TRUST AND LENGTH OF SERVICE AS TRUSTEE(2)</th>
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<th>NUMBER OF FUNDS IN FUND COMPLEX(3) OVERSEEN BY TRUSTEE</th>
<th>OTHER DIRECTORSHIPS HELD BY TRUSTEE DURING THE PAST FIVE YEARS(4)</th>
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<td>NON-INTERESTED TRUSTEES</td>
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| Sarah N. Garvey | Age: 67 Trustee since July 2011 | • Chairman of the Board of Navy Pier from 2011 to 2013 and Member of the Board since 2011;  
• Member of the Board of Directors of The Civic Federation since 2004;  
• Member of the Executive Committee and Chairman of the Audit Committee since 2017 and Trustee of the Art Institute of Chicago since 2011. | 26 | NONE |
| Philip G. Hubbard | Age: 67 Trustee since July 2011 | • Managing Partner of Solidian Fund, LP and Solidian Management, LLC (a fund of hedge funds platform for family and friends investments) since 2001;  
• President of Hubbard Management Group, LLC (a personal investment vehicle) since 2001;  
• Chairman of the Board of Trustees of the Wheaton College Trust Company, N.A. since 2004;  
• Member of the Board of Trustees of Wheaton College since 1998;  
• Chairman of the Board of Directors of the English Language Institute/China (a nonprofit educational organization) since 1993; | 26 | NONE |
<table>
<thead>
<tr>
<th>NAME, ADDRESS, AGE, POSITIONS HELD WITH TRUST AND LENGTH OF SERVICE AS TRUSTEE</th>
<th>PRINCIPAL OCCUPATIONS DURING PAST FIVE YEARS</th>
<th>NUMBER OF FUNDS IN FUND COMPLEX OVERSEEN BY TRUSTEE</th>
<th>OTHER DIRECTORSHIPS HELD BY TRUSTEE DURING THE PAST FIVE YEARS</th>
</tr>
</thead>
</table>
| **Eric T. McKissack**  
Age: 65  
Trustee and Chairman since July 2011 |  
- Member of the Board of First Cup, LLC (restaurant franchising) since 2014.  
- Founder; CEO from 2004 to 2019 and CEO Emeritus since 2019 of Channing Capital Management, LLC (an SEC registered investment adviser);  
- Member of the Board of Trustees, the Investment Committee, and the Finance Committee of the Art Institute of Chicago since 2002;  
- Member of the Board of Grand Victoria Foundation since 2011;  
- Member of the Board of the Graham Foundation since 2014. | 26 |  
- Morgan Stanley Pathway Funds (formerly, Consulting Group Capital Markets Funds) (11 Portfolios) since April 2013 |
| **INTERESTED TRUSTEE**  
Darek Wojnar  
Age: 53  
Trustee since December 2018 |  
- Director and Executive Vice President, Head of Funds and Managed Accounts, Northern Trust Investments, Inc. since 2018;  
- Managing Member of the Wojnar Group LLC (a publishing industry consulting company) since 2013;  
- Head of Exchange-Traded Funds at Hartford Funds from 2016 to 2017 and Managing Director of Lattice Strategies LLC from 2014 to 2016; | 26 |  
- Northern Funds (43 Portfolios) since January 1, 2019 and Northern Institutional Funds (7 Portfolios) since January 1, 2019 |
NAME, ADDRESS, AGE, POSITIONS HELD WITH TRUST AND LENGTH OF SERVICE AS TRUSTEE

<table>
<thead>
<tr>
<th>NAME</th>
<th>ADDRESS</th>
<th>AGE</th>
<th>POSITIONS HELD WITH TRUST AND LENGTH OF SERVICE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Peter K. Ewing</td>
<td>50 South LaSalle St.</td>
<td>60</td>
<td>President since March 2017</td>
</tr>
<tr>
<td>Jose J. Del Real</td>
<td>50 South LaSalle St.</td>
<td>41</td>
<td>Secretary since December 2018</td>
</tr>
<tr>
<td>Brian Meikel</td>
<td>50 South LaSalle St.</td>
<td>51</td>
<td>Acting Chief Compliance Officer since October 2018</td>
</tr>
</tbody>
</table>

PRINCIPAL OCCUPATIONS DURING PAST FIVE YEARS

- Managing Director and Head of US iShares Product at BlackRock (including Barclays Global Investors acquired by BlackRock) from 2005 to 2013.

OFFICERS OF THE TRUST

NAME, ADDRESS, AGE, POSITIONS HELD WITH TRUST AND LENGTH OF SERVICE

<table>
<thead>
<tr>
<th>NAME</th>
<th>ADDRESS</th>
<th>AGE</th>
<th>POSITIONS HELD WITH TRUST AND LENGTH OF SERVICE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Peter K. Ewing</td>
<td>50 South LaSalle St.</td>
<td>60</td>
<td>President of Northern Funds and Northern Institutional Funds since March 2017; Vice President of the Trust from July 2011 to February 2017; Director of ETF Product Management, Northern Trust Investments, Inc. and Senior Vice President, The Northern Trust Company, since September 2010.</td>
</tr>
<tr>
<td>Jose J. Del Real</td>
<td>50 South LaSalle St.</td>
<td>41</td>
<td>Senior Legal Counsel and Senior Vice President, Asset Management Practice Group of the Legal Department of The Northern Trust Company since March 2017; Senior Legal Counsel and Vice President, Asset Management Practice Group of the Legal Department of The Northern Trust Company from August 2015 to March 2017; Assistant Secretary of Northern Trust Investments, Inc. since 2016; Legal Counsel and Vice President, Asset Management Practice Group of the Legal Department of The Northern Trust Company from 2014 until 2015; Secretary of Northern Funds and Northern Institutional Funds since November 2018; Assistant Secretary of Northern Funds and Northern Institutional Funds from 2011 to 2014, and from May 2015 to November 2018; Assistant Secretary of FlexShares® Trust from June 2015 to December 2018; Vice President and Regulatory Administration Senior Attorney of The Northern Trust Company from 2012 until 2014.</td>
</tr>
<tr>
<td>Brian Meikel</td>
<td>50 South LaSalle St.</td>
<td>51</td>
<td>Acting Chief Compliance Officer of Northern Funds and Northern Institutional Funds since August 2018; Vice President of Northern Trust Investments, Inc. since June 2014; Chief Compliance Officer of BMO Asset Management – Harris Investment Management from August 2006 to September 2013.</td>
</tr>
</tbody>
</table>
Randal E. Rein
Age: 48
50 South LaSalle Street
Chicago, IL 60603
Treasurer and Principal Financial Officer since July 2011

Senior Vice President of Northern Trust Investments, Inc. since 2010; Treasurer of Northern Funds and Northern Institutional Funds since 2008; Treasurer of Alpha Core Strategies Fund from 2008 to 2018; Treasurer of Equity Long/Short Opportunities Fund from 2011 to 2018.

Jeff Beeson
Age: 40
50 South LaSalle Street
Chicago, IL 60603
Vice President since December 2018

Senior ETF Product Manager, Northern Trust Investments, Inc. since 2018 and Vice President, The Northern Trust Company since April 2017; Product Development Manager of Invesco PowerShares from 2015 to 2017; Vice President of Guggenheim Investments from 2011 to 2015.

Peter J. Flood
Age: 61
50 South LaSalle Street
Chicago, IL 60603
Vice President since July 2011

Director of ETF Investment Strategy, Northern Trust Investments, Inc. since 2010; Portfolio Manager, Northern Trust Investments, Inc. from 2007 to 2014.

Darlene Chappell
Age: 56
50 South LaSalle Street
Chicago, IL 60603
Anti-Money Laundering Officer since July 2011

Anti-Money Laundering Compliance Officer for Northern Trust Investments, Inc., Northern Trust Securities, Inc., Northern Funds, Northern Institutional Funds and Alpha Core Strategies Fund (formerly NT Alpha Strategies Fund) since 2009, Equity Long/Short Opportunities Fund (formerly NT Equity Long/Short Strategies Fund) since 2011 and 50 South Capital Advisors, LLC since 2015; Vice President and Compliance Consultant for The Northern Trust Company since 2006; Anti-Money Laundering Compliance Officer for Northern Trust Company of Connecticut from 2009 to 2013.

Susan W. Yee
Age: 49
70 Fargo Street
Boston, MA 02110
Assistant Secretary since October 2014

Vice President, Regulatory Services Group, JPMorgan Chase Bank, N.A. since 1994, in various positions.
Trust. The scope of the Audit Committee’s responsibilities is oversight. It is management’s responsibility to maintain appropriate systems for accounting and internal control and the independent registered public accounting firm’s responsibility to plan and carry out an audit in accordance with the standards of the Public Company Accounting Oversight Board. The Audit Committee met three times during the last fiscal year ended October 31, 2018.

The Governance Committee consists of Ms. Garvey (chair), Mr. Hubbard and Mr. McKissack. The Board has determined that each member of the Governance Committee is an Independent Trustee. The functions performed by the Governance Committee include, among other things, selecting and nominating candidates to serve as Independent Trustees, reviewing and making recommendations regarding Trustee compensation and developing policies regarding Trustee education. In filling Board vacancies, the Governance Committee will consider nominees recommended by shareholders. Nominee recommendations (accompanied by resumes) should be submitted to the Trust at its mailing address stated in the Funds’ Prospectus and should be directed to the attention of the FlexShares® Trust Governance Committee, care of the Secretary of the Trust. The Governance Committee has not established specific qualifications that it believes must be met by a nominee. In evaluating nominees, the Governance Committee considers, among other things, candidates’ qualifications for Board membership and their independence from management and principal service providers. Persons selected must be independent in terms of both the letter and the spirit of the 1940 Act and the Rules and Regulations under the 1940 Act. The Committee will consider the effect of any relationships beyond those delineated in the 1940 Act that might impair independence, such as business, financial or family relationships with managers or service providers of the Trust. The Committee also considers whether the individual’s background, skills, and experience will complement the background, skills, and experience of other Trustees and will contribute to the Board’s diversity. The Governance Committee met three times during the last fiscal year ended October 31, 2018.

LEADERSHIP STRUCTURE AND QUALIFICATIONS OF THE BOARD OF TRUSTEES

The Board is responsible for oversight of the Trust. The Trust has engaged the Investment Adviser to manage the Funds of the Trust on a day-to-day basis. The Board oversees the Investment Adviser and certain other principal service providers in the operations of the Funds. The Board currently is composed of four Trustees, three of whom are Independent Trustees. The Board believes that having Mr. Wojnar serve as an interested Trustee brings management insight that is important to certain of the Board’s decisions and also in the best interest of shareholders. The Board meets in-person at regularly scheduled meetings currently anticipated to occur four times in a year. In addition, the Board members may meet in-person or by telephone at special meetings or on an informal basis at other times. The Independent Trustees also expect to meet separately in executive session, including with independent trustee counsel. The Trustees believe that these meetings will help mitigate conflicts of interest. The Trustees also believe that the executive sessions will allow the Independent Trustees to deliberate candidly and constructively, separately from management, in a manner that affords honest disagreement and critical questioning.

As stated above, the Board has established a standing Audit Committee and a Governance Committee to assist the Board in fulfilling its oversight responsibilities. The Board also may establish ad hoc committees or working groups from time to time to aid in its oversight. The Independent Trustees have engaged independent legal counsel to assist them in fulfilling their responsibilities.

The Board is chaired by Eric McKissack, an Independent Trustee. As Chair, this Independent Trustee leads the Board in its activities. Also, the Chair acts as a member of the Audit and Governance Committees (and may serve as a member of each subsequently established standing or ad hoc committee). The Trustees have determined that the Board’s leadership and committee structure is appropriate because the Board believes that it sets the proper tone to the relationships between the Trust, on the one hand, and the Investment Adviser and certain other principal service providers, on the other, and facilitates the exercise of the Board’s independent judgment in evaluating and managing the relationships.

The Board has concluded that, based on each Board member’s experience, qualifications, attributes or skills on an individual basis and in combination with those of the other Board members, each Board member should serve as a Board member. Among other attributes common to all Board members are their ability to review critically, evaluate, question and discuss information provided to them, to interact effectively with the various service providers to the Trust, and to exercise reasonable business judgment in the performance of their duties as Board members. In addition, the Board will take into account the actual service and commitment of the Board members during their tenure in determining whether each should continue to serve. A Board member’s ability to perform his or her duties effectively may have been attained through a Board member’s educational background or professional training; business, consulting, public service or academic positions; experience from service as a Board member of other funds, public companies, or non-profit entities or other organizations; or other experiences. Set forth below is a brief discussion of the specific experience, qualifications, attributes or skills of each Trustee that led the Board to conclude that he or she should serve as a Board member.
Non-Interested Trustees:

Ms. Garvey. Ms. Garvey is a former partner of Deloitte & Touche LLP and has more than 20 years experience in tax accounting. She previously served as Vice President of Corporate Relations and Vice President of State and Local Government Relations for The Boeing Company. She serves on the Executive Committee and is Chairman of the Audit Committee of the Board of Trustees of the Art Institute of Chicago. She previously served as Chairman of the Board of Chicago’s Navy Pier and of Chicago’s Shedd Aquarium. She is a Certified Public Accountant and holds bachelors and masters degrees in accounting.

Mr. Hubbard. Mr. Hubbard has served for 18 years as president of the Hubbard Management Group, LLC, and as managing partner for Solidian Fund, LP and Solidian Management, LLC. He previously served for 13 years on the Board of Harris Bank Winnetka, Illinois, and is a Certified Public Accountant. In addition, Mr. Hubbard serves on the Board of Trustees of Wheaton College and is the chairman of the Wheaton College Trust Company and of the English Language Institute/China. He holds a bachelors degree in economics and a masters degree in business administration.

Mr. McKissack. Mr. McKissack is the Chief Executive Officer Emeritus and Founder of Channing Capital Management, LLC, a registered investment adviser. He also serves as an independent trustee on the Board of Trustees of a group of mutual funds, the Morgan Stanley Pathway Funds (formerly, the Consulting Group Capital Markets Funds). Mr. McKissack also serves on the Board of the Art Institute of Chicago, the Board of the Grand Victoria Foundation, and the Board of the Graham Foundation. He also served on the Board of the ICMA Retirement Corporation, a non-profit provider of retirement administration services. He is a Chartered Financial Analyst.

Interested Trustee:

Mr. Darek Wojnar. Mr. Wojnar is Executive Vice President, Head of Funds and Managed Accounts of Northern Trust Asset Management. Prior to that, Mr. Wojnar was the Head of Exchange-Traded Funds of Hartford Funds and a Managing Director of Lattice Strategies LLC. He also served as a Managing Director and Head of US iShares Product at BlackRock (including Barclays Global Investors which was acquired by BlackRock). He also serves as a Trustee on the Boards of Northern Funds and Northern Institutional Funds. He also serves as a Managing Member of the Wojnar Group LLC. He holds a bachelor’s degree in Electrical Engineering and a masters degree in business administration.

RISK OVERSIGHT

Investing in general and the operation of exchange-traded funds involve a variety of risks, such as investment risk, compliance risk, and operational risk, among others. The Board oversees risk as part of its oversight of the Trust. Risk oversight is addressed as part of various regular Board and Audit Committee activities. The Board reviews reports from, among others, the Investment Adviser, the Trust’s Chief Compliance Officer, the Trust’s independent registered public accounting firm and counsel, as appropriate, regarding risks faced by the Trust and the risk management programs of the Investment Adviser and certain service providers. The actual day-to-day risk management with respect to the Trust resides with the Investment Adviser and other service providers to the Trust. The Investment Adviser has a dedicated risk management function that is headed by a chief risk officer. Although the risk management policies of the Investment Adviser and the service providers are designed to be effective, those policies and their implementation vary among service providers and over time, and there is no guarantee that they will be effective. Not all risks that may affect the Trust can be identified or processes and controls developed to eliminate or mitigate their occurrence or effects, and some risks are simply beyond any control of the Trust or the Investment Adviser, its affiliates or other service providers.

TRUSTEE OWNERSHIP OF FUND SHARES

The following table shows the dollar range of shares of the Funds owned by each Trustee.

<table>
<thead>
<tr>
<th>Name of Non-Interested Trustee</th>
<th>Fund</th>
<th>Dollar Range of Equity Securities in the Fund</th>
<th>Aggregate Dollar Range of Equity Securities in All Registered Investment Companies Overseen by Trustee in Family of Investment Companies1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sarah N. Garvey</td>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$10,001-$50,000</td>
<td>Over $100,000</td>
</tr>
</tbody>
</table>

- 60 -
**Information as of December 31, 2018**

<table>
<thead>
<tr>
<th>Name of Non-Interested Trustee</th>
<th>Fund</th>
<th>Dollar Range of Equity Securities in the Fund</th>
<th>Aggregate Dollar Range of Equity Securities in All Registered Investment Companies by Trustee in Family of Investment Companies¹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Philip G. Hubbard</td>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$50,001-$100,000</td>
<td>None</td>
</tr>
<tr>
<td></td>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$10,001-$50,000</td>
<td>None</td>
</tr>
<tr>
<td>Eric T. McKissack</td>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$1-$10,000</td>
<td>$10,001-$50,000</td>
</tr>
<tr>
<td></td>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$1-$10,000</td>
<td>None</td>
</tr>
<tr>
<td></td>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$10,001-$50,000</td>
<td>None</td>
</tr>
</tbody>
</table>

¹ The Family of Investment Companies consists only of the Funds of FlexShares® Trust. Messrs. Hubbard and McKissack each have an economic interest in the Trust valued at over $100,000 by virtue of their participation in the Trust’s deferred compensation plan (the “DC Plan”) for its non-interested Trustees. Under the DC Plan, a non-interested Trustee may elect to have his or her deferred compensation treated as if it had been invested by the Trust in shares of the FlexShares® Morningstar US Market Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Quality Dividend Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Ready Access Variable Income Fund and/or the FlexShares® Morningstar Global Upstream Natural Resources Index Fund. The amount paid to the Trustees under the DC Plan will be determined based upon the performance of these investments.

**TRUSTEE AND OFFICER COMPENSATION**

The Trust pays each Trustee who is not an officer, director or employee of Northern Trust Corporation or its subsidiaries annual fees for his or her services as a Trustee of the Trust and as a member of Board committees. In recognition of their services, the fees paid to the Board and Committee chairpersons may be larger than the fees paid to other members of the Trust’s Board and Committees. The Trustees also are reimbursed for travel expenses incurred in connection with attending such meetings. The Trust also may pay the incidental costs of a Trustee to attend training or other types of conferences relating to the investment company industry. The Trust does not provide pension or retirement benefits to its Trustees. Each non-interested Trustee is entitled to participate in the Trust’s DC Plan. Under the DC Plan, a non-interested Trustee may elect to defer all or a portion of his or her compensation and have the deferred compensation treated as if it had been invested by the Trust in shares of the FlexShares® Morningstar US Market Factor Tilt Index Fund, the FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, the FlexShares® Global Quality Real Estate Index Fund, the FlexShares® Quality Dividend Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Ready Access Variable Income Fund and/or the FlexShares® Morningstar Global Upstream Natural Resources Index Fund. The amount paid to the Trustees under the DC Plan will be determined based upon the performance of such investments.
The following table sets forth important information with respect to the compensation of each non-interested and interested Trustee of the Trust:

<table>
<thead>
<tr>
<th>Name of Trustee</th>
<th>Aggregate Compensation from Trust</th>
<th>FlexShares® Morningstar US Market Factor Tilt Index Fund</th>
<th>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</th>
<th>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</th>
<th>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Non-Interested Trustees:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sarah N. Garvey</td>
<td>$151,250</td>
<td>$11,575</td>
<td>$9,639</td>
<td>$5,998</td>
<td>$402</td>
</tr>
<tr>
<td>Philip G. Hubbard</td>
<td>$151,250</td>
<td>$11,575</td>
<td>$9,639</td>
<td>$5,998</td>
<td>$402</td>
</tr>
<tr>
<td>Eric T. McKissack</td>
<td>$151,250</td>
<td>$11,575</td>
<td>$9,639</td>
<td>$5,998</td>
<td>$402</td>
</tr>
<tr>
<td><strong>Interested Trustee:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Darek Wojnar</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>None</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Name of Trustee</th>
<th>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</th>
<th>FlexShares® US Quality Large Cap Index Fund</th>
<th>FlexShares® STOXX® US ESG Impact Index Fund</th>
<th>FlexShares® STOXX® Global ESG Impact Index Fund</th>
<th>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Non-Interested Trustees:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sarah N. Garvey</td>
<td>$513</td>
<td>$712</td>
<td>$489</td>
<td>$931</td>
<td>$48,337</td>
</tr>
<tr>
<td>Philip G. Hubbard</td>
<td>$513</td>
<td>$712</td>
<td>$489</td>
<td>$931</td>
<td>$48,337</td>
</tr>
<tr>
<td>Eric T. McKissack</td>
<td>$513</td>
<td>$712</td>
<td>$489</td>
<td>$931</td>
<td>$48,337</td>
</tr>
<tr>
<td><strong>Interested Trustee:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Darek Wojnar</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>None</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Name of Trustee</th>
<th>FlexShares® STOXX® Global Broad Infrastructure Index Fund</th>
<th>FlexShares® Global Quality Real Estate Index Fund</th>
<th>FlexShares® Real Assets Allocation Index Fund</th>
<th>FlexShares® Quality Dividend Index Fund</th>
<th>FlexShares® Quality Dividend Defensive Index Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Non-Interested Trustees:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sarah N. Garvey</td>
<td>$7,405</td>
<td>$2,685</td>
<td>$392</td>
<td>$16,668</td>
<td>$3,198</td>
</tr>
<tr>
<td>Philip G. Hubbard</td>
<td>$7,405</td>
<td>$2,685</td>
<td>$392</td>
<td>$16,668</td>
<td>$3,198</td>
</tr>
<tr>
<td>Eric T. McKissack</td>
<td>$7,405</td>
<td>$2,685</td>
<td>$392</td>
<td>$16,668</td>
<td>$3,198</td>
</tr>
<tr>
<td><strong>Interested Trustee:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Darek Wojnar</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>None</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Name of Trustee</th>
<th>FlexShares® International Quality Dividend Dynamic Index Fund</th>
<th>FlexShares® International Quality Dividend Defensive Index Fund</th>
<th>FlexShares® International Quality Dividend Dynamic Index Fund</th>
<th>FlexShares® International Quality Dividend Defensive Index Fund</th>
<th>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Non-Interested Trustees:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sarah N. Garvey</td>
<td>$847</td>
<td>$8,796</td>
<td>$1,124</td>
<td>$985</td>
<td>$17,571</td>
</tr>
<tr>
<td>Philip G. Hubbard</td>
<td>$847</td>
<td>$8,796</td>
<td>$1,124</td>
<td>$985</td>
<td>$17,571</td>
</tr>
<tr>
<td>Eric T. McKissack</td>
<td>$847</td>
<td>$8,796</td>
<td>$1,124</td>
<td>$985</td>
<td>$17,571</td>
</tr>
<tr>
<td><strong>Interested Trustee:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

- 62 -
The amounts represent the compensation received by the Trustees for the fiscal year ended October 31, 2018. Effective January 1, 2019, the non-interested Trustees receive an annual retainer of $130,000, and the chairs of the Board and each Committee receive an additional annual retainer of $25,000. Ms. Garvey did not defer any compensation during the fiscal year ended October 31, 2018. Mr. Hubbard elected to defer $75,625 of $151,250 in total compensation during the fiscal year ended October 31, 2018. Mr. McKissack elected to defer $75,625 of $151,250 in total compensation during the fiscal year ended October 31, 2018.

The Trust’s officers do not receive fees from the Trust for services in such capacities. NTI receives fees from the Trust as Investment Adviser. Messrs. Beeson, Del Real, Ewing, Flood, Rein, and Meikel and Ms. Chappell are officers of NTI and/or its affiliates.

CONTROL PERSONS AND PRINCIPAL HOLDERS OF SECURITIES

The Trustees and officers of the Trust collectively owned less than 1% of each Fund’s outstanding shares as of February 1, 2019.

Although the Trust does not have information concerning the beneficial ownership of shares nominally held by Depository Trust Company (“DTC”), as of February 1, 2019, the name and percentage ownership of each DTC participant that owned record 5% or more of the outstanding shares of each Fund were as follows:

**FlexShares® Morningstar US Market Factor Tilt Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>TD Ameritrade Clearing, Inc.</td>
<td>5.10%</td>
</tr>
<tr>
<td>P.O. Box 2553</td>
<td></td>
</tr>
<tr>
<td>Omaha, NE 68103-2533</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>79.17%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Morgan Stanley</td>
<td>5.10%</td>
</tr>
<tr>
<td>1300 Thames Street, 7th Floor</td>
<td></td>
</tr>
<tr>
<td>Baltimore, MD 21231</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>72.95%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>
### FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northern Trust Company</td>
<td>74.99%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
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</tbody>
</table>

### FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>JPMorgan Securities LLC</td>
<td>5.88%</td>
</tr>
<tr>
<td>P.O. Box 183211</td>
<td></td>
</tr>
<tr>
<td>Columbus, OH 43218</td>
<td></td>
</tr>
<tr>
<td>Merrill Lynch</td>
<td>7.84%</td>
</tr>
<tr>
<td>1600 Merrill Lynch Drive</td>
<td></td>
</tr>
<tr>
<td>Pennington, NJ 08534</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>33.55%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
<tr>
<td>National Financial Services LLC</td>
<td>45.17%</td>
</tr>
<tr>
<td>P.O. Box 673004</td>
<td></td>
</tr>
<tr>
<td>Dallas, TX 75267-3004</td>
<td></td>
</tr>
</tbody>
</table>

### FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund:

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Merrill Lynch</td>
<td>5.31%</td>
</tr>
<tr>
<td>1600 Merrill Lynch Drive</td>
<td></td>
</tr>
<tr>
<td>Pennington, NJ 08534</td>
<td></td>
</tr>
<tr>
<td>Charles Schwab &amp; Co., Inc.</td>
<td>5.92%</td>
</tr>
<tr>
<td>P.O. Box 64930</td>
<td></td>
</tr>
<tr>
<td>Phoenix, AZ 85082</td>
<td></td>
</tr>
<tr>
<td>TD Ameritrade Clearing, Inc.</td>
<td>6.17%</td>
</tr>
<tr>
<td>P.O. Box 2553</td>
<td></td>
</tr>
<tr>
<td>Omaha, NE 68103</td>
<td></td>
</tr>
<tr>
<td>JPMorgan Securities LLC</td>
<td>7.85%</td>
</tr>
<tr>
<td>P.O. Box 183211</td>
<td></td>
</tr>
<tr>
<td>Columbus, OH 43218</td>
<td></td>
</tr>
<tr>
<td>National Financial Services LLC</td>
<td>19.40%</td>
</tr>
<tr>
<td>P.O. Box 673004</td>
<td></td>
</tr>
<tr>
<td>Dallas, TX 75267</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>42.60%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
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### FlexShares® US Quality Large Cap Index Fund:

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pershing LLC</td>
<td>5.88%</td>
</tr>
<tr>
<td>1 Pershing Plaza, 7th Floor</td>
<td></td>
</tr>
<tr>
<td>Jersey City, NJ 07399</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>20.65%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
<tr>
<td>CNB Bank</td>
<td>27.85%</td>
</tr>
<tr>
<td>P.O. Box 42</td>
<td></td>
</tr>
<tr>
<td>Clearfield, PA 16830</td>
<td></td>
</tr>
<tr>
<td>Nominee Name/Address</td>
<td>Percentage Ownership</td>
</tr>
<tr>
<td>----------------------</td>
<td>----------------------</td>
</tr>
<tr>
<td>Fifth Third Bank</td>
<td>27.85%</td>
</tr>
<tr>
<td>5050 Kingsley Drive</td>
<td></td>
</tr>
<tr>
<td>Cincinnati, OH 45263</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® STOXX® US ESG Impact Index Fund:**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Charles Schwab &amp; Co., Inc.</td>
<td>6.64%</td>
</tr>
<tr>
<td>P.O. Box 64930</td>
<td></td>
</tr>
<tr>
<td>Phoenix, AZ 85082-4930</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>74.48%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® STOXX® Global ESG Impact Index Fund:**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northern Trust Company</td>
<td>80.53%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® Morningstar Global Upstream Natural Resources Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>National Financial Services LLC</td>
<td>11.49%</td>
</tr>
<tr>
<td>P.O. Box 673004</td>
<td></td>
</tr>
<tr>
<td>Dallas, TX 75267-3004</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>73.91%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
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**FlexShares® STOXX® Global Broad Infrastructure Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northern Trust Company</td>
<td>88.51%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
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</table>

**FlexShares® Global Quality Real Estate Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
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</thead>
<tbody>
<tr>
<td>Fifth Third Bank</td>
<td>5.20%</td>
</tr>
<tr>
<td>5050 Kingsley Drive</td>
<td></td>
</tr>
<tr>
<td>Cincinnati, OH 45263</td>
<td></td>
</tr>
<tr>
<td>Charles Schwab &amp; Co., Inc.</td>
<td>7.13%</td>
</tr>
<tr>
<td>P.O. Box 64930</td>
<td></td>
</tr>
<tr>
<td>Phoenix, AZ 85082</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>65.53%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
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**FlexShares® Real Assets Allocation Index Fund:**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>JPMorgan Securities LLC</td>
<td>6.64%</td>
</tr>
<tr>
<td>P.O. Box 183211</td>
<td></td>
</tr>
<tr>
<td>Columbus, OH 43218</td>
<td></td>
</tr>
<tr>
<td>Pershing LLC</td>
<td>7.22%</td>
</tr>
<tr>
<td>1 Pershing Plaza, 7th Floor</td>
<td></td>
</tr>
<tr>
<td>Jersey City, NJ 07399</td>
<td></td>
</tr>
</tbody>
</table>
### FlexShares® Quality Dividend Index Fund

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Charles Schwab &amp; Co., Inc.</td>
<td>5.09%</td>
</tr>
<tr>
<td>P.O. Box 64930</td>
<td></td>
</tr>
<tr>
<td>Phoenix, AZ 85082</td>
<td></td>
</tr>
<tr>
<td>Pershing LLC</td>
<td>15.33%</td>
</tr>
<tr>
<td>1 Pershing Plaza, 7th Floor</td>
<td></td>
</tr>
<tr>
<td>Jersey City, NJ 07399</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>55.34%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

### FlexShares® Quality Dividend Defensive Index Fund

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>National Financial Services LLC</td>
<td>7.40%</td>
</tr>
<tr>
<td>P.O. Box 673004</td>
<td></td>
</tr>
<tr>
<td>Dallas, TX 75267-3004</td>
<td></td>
</tr>
<tr>
<td>Charles Schwab &amp; Co., Inc.</td>
<td>16.18%</td>
</tr>
<tr>
<td>P.O. Box 64930</td>
<td></td>
</tr>
<tr>
<td>Phoenix, AZ 85082</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>54.32%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

### FlexShares® Quality Dividend Dynamic Index Fund

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goldman Sachs &amp; Co. Proxy Services</td>
<td>5.21%</td>
</tr>
<tr>
<td>Church Street Station</td>
<td></td>
</tr>
<tr>
<td>P.O. Box 3197</td>
<td></td>
</tr>
<tr>
<td>New York, NY 10008</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>70.83%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

### FlexShares® International Quality Dividend Index Fund

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>RBC Wealth Management</td>
<td>6.85%</td>
</tr>
<tr>
<td>60 South 6th Street</td>
<td></td>
</tr>
<tr>
<td>Minneapolis, MN 55402</td>
<td></td>
</tr>
<tr>
<td>Nominee Name/Address</td>
<td>Percentage Ownership</td>
</tr>
<tr>
<td>----------------------</td>
<td>----------------------</td>
</tr>
<tr>
<td>Charles Schwab &amp; Co., Inc.</td>
<td>8.07%</td>
</tr>
<tr>
<td>P.O. Box 64930</td>
<td></td>
</tr>
<tr>
<td>Phoenix, AZ 85082</td>
<td></td>
</tr>
<tr>
<td>TD Ameritrade Clearing, Inc.</td>
<td>8.28%</td>
</tr>
<tr>
<td>P.O. Box 2553</td>
<td></td>
</tr>
<tr>
<td>Omaha, NE 68103-2553</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>53.56%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
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</tbody>
</table>

**FlexShares® International Quality Dividend Defensive Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northern Trust Company</td>
<td>80.30%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® International Quality Dividend Dynamic Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Merrill Lynch</td>
<td>6.62%</td>
</tr>
<tr>
<td>1600 Merrill Lynch Dr.</td>
<td></td>
</tr>
<tr>
<td>Pennington, NJ 08534</td>
<td></td>
</tr>
<tr>
<td>US Bank</td>
<td>24.77%</td>
</tr>
<tr>
<td>Securities Control</td>
<td></td>
</tr>
<tr>
<td>1555 North Rivercenter Drive, Suite 302</td>
<td></td>
</tr>
<tr>
<td>Milwaukie, WI 53212</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>54.02%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Charles Schwab &amp; Co., Inc.</td>
<td>9.90%</td>
</tr>
<tr>
<td>P.O. Box 64930</td>
<td></td>
</tr>
<tr>
<td>Phoenix, AZ 85082</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>78.16%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Charles Schwab &amp; Co., Inc.</td>
<td>24.57%</td>
</tr>
<tr>
<td>P.O. Box 64930</td>
<td></td>
</tr>
<tr>
<td>Phoenix, AZ 85082</td>
<td></td>
</tr>
<tr>
<td>National Financial Services LLC</td>
<td>27.82%</td>
</tr>
<tr>
<td>P.O. Box 673004</td>
<td></td>
</tr>
<tr>
<td>Dallas, TX 75267-3004</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>38.03%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
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</tr>
</tbody>
</table>

**FlexShares® Disciplined Duration MBS Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Charles Schwab &amp; Co., Inc.</td>
<td>8.29%</td>
</tr>
<tr>
<td>P.O. Box 64930</td>
<td></td>
</tr>
<tr>
<td>Phoenix, AZ 85082-4930</td>
<td></td>
</tr>
<tr>
<td>Nominee Name/Address</td>
<td>Percentage Ownership</td>
</tr>
<tr>
<td>--------------------------------------</td>
<td>----------------------</td>
</tr>
<tr>
<td>JPMorgan</td>
<td>18.32%</td>
</tr>
<tr>
<td>500 Stanton Christiana Road</td>
<td></td>
</tr>
<tr>
<td>Newark, DE 19713-2107</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>57.77%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® Credit-Scored US Corporate Bond Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>JPMorgan</td>
<td>12.26%</td>
</tr>
<tr>
<td>500 Stanton Christiana Road</td>
<td></td>
</tr>
<tr>
<td>Newark, DE 19713-2107</td>
<td></td>
</tr>
<tr>
<td>JPMorgan Securities LLC</td>
<td>12.71%</td>
</tr>
<tr>
<td>P.O. Box 183211</td>
<td></td>
</tr>
<tr>
<td>Columbus, OH 43218</td>
<td>66.30%</td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td></td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® Credit-Scored US Long Corporate Bond Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wells Fargo</td>
<td>5.59%</td>
</tr>
<tr>
<td>P.O. Box 5268</td>
<td></td>
</tr>
<tr>
<td>Sioux Falls, SD 57117-5268</td>
<td></td>
</tr>
<tr>
<td>JPMorgan</td>
<td>14.32%</td>
</tr>
<tr>
<td>500 Stanton Christiana Road</td>
<td></td>
</tr>
<tr>
<td>Newark, DE 19713-2107</td>
<td></td>
</tr>
<tr>
<td>JPMorgan Securities LLC</td>
<td>16.05%</td>
</tr>
<tr>
<td>P.O. Box 183211</td>
<td></td>
</tr>
<tr>
<td>Columbus, OH 43218</td>
<td>54.19%</td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td></td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>

**FlexShares® High Yield Value-Scored Bond Index Fund**

<table>
<thead>
<tr>
<th>Nominee Name/Address</th>
<th>Percentage Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vanguard Brokerage Services</td>
<td>5.82%</td>
</tr>
<tr>
<td>P.O. Box 2600</td>
<td></td>
</tr>
<tr>
<td>Valley Forge, PA 19482</td>
<td></td>
</tr>
<tr>
<td>National Financial Services LLC</td>
<td>7.88%</td>
</tr>
<tr>
<td>P.O. Box 673004</td>
<td></td>
</tr>
<tr>
<td>Dallas, TX 75267-3004</td>
<td></td>
</tr>
<tr>
<td>JPMorgan Securities LLC</td>
<td>8.08%</td>
</tr>
<tr>
<td>P.O. Box 183211</td>
<td></td>
</tr>
<tr>
<td>Columbus, OH 43218</td>
<td></td>
</tr>
<tr>
<td>Pershing LLC</td>
<td>10.49%</td>
</tr>
<tr>
<td>1 Pershing Plaza, 7th Floor</td>
<td></td>
</tr>
<tr>
<td>Jersey City, NJ 07399</td>
<td></td>
</tr>
<tr>
<td>TD Ameritrade Clearing, Inc.</td>
<td>11.10%</td>
</tr>
<tr>
<td>P.O. Box 2553</td>
<td></td>
</tr>
<tr>
<td>Omaha, NE 68103-2533</td>
<td></td>
</tr>
<tr>
<td>Northern Trust Company</td>
<td>11.85%</td>
</tr>
<tr>
<td>801 S. Canal Street</td>
<td></td>
</tr>
<tr>
<td>Chicago, IL 60607</td>
<td></td>
</tr>
</tbody>
</table>
To the extent that any shareholder is the beneficial owner of more than 25% of the outstanding shares of any Fund, the shareholder may be deemed a “control person” of that Fund for purposes of the 1940 Act.

CODE OF ETHICS

The Trust and the Adviser have each adopted a code of ethics under Rule 17j-1 of the 1940 Act. These codes of ethics permit, subject to certain conditions, personnel of each of those entities to invest in securities that may be purchased or held by the Fund. The Distributor relies on the principal underwriters exception under Rule 17j-1(c)(3), specifically where the Distributor is not affiliated with the Trust or the Adviser, and no officer, director or general partner of the Distributor serves as an officer, director or general partner of the Trust or the Adviser.

INVESTMENT ADVISER

NTI, a subsidiary of TNTC and an indirect subsidiary of Northern Trust Corporation, serves as the Investment Adviser of the Funds. Northern Trust Corporation is regulated by the Board of Governors of the Federal Reserve System as a financial holding company under the U.S. Bank Holding Company Act of 1956, as amended. NTI is located at 50 South LaSalle Street, Chicago, Illinois 60603.

NTI is an Illinois State Banking Corporation and an investment adviser registered under the Investment Advisers Act of 1940, as amended. It primarily manages assets for institutional and individual separately managed accounts, investment companies and bank common and collective funds.

TNTC is the principal subsidiary of Northern Trust Corporation. TNTC is located at 50 South LaSalle Street, Chicago, Illinois 60603.

TNTC is a member of the Federal Reserve System. Since 1889, TNTC has administered and managed assets for individuals, institutions and corporations. Unless otherwise indicated, NTI and TNTC are referred to collectively in this SAI as “Northern Trust.”

As of December 31, 2018, Northern Trust Corporation, through its affiliates, had assets under investment management of $1.07 trillion and assets under custody of $7.59 trillion.

Investment Advisory and Ancillary Services Agreement

Under the Trust’s Investment Advisory and Ancillary Services Agreement with the Investment Adviser for the Funds (the “Advisory Agreement”), the Investment Adviser, subject to the general supervision of the Board, makes decisions with respect to, and places orders for, all purchases and sales of portfolio securities for each Fund and also provides certain ancillary services.

The Investment Adviser also is responsible for monitoring and preserving the records required to be maintained under the regulations of the SEC (with certain exceptions unrelated to its activities for the Trust). In making investment recommendations for the Funds, if any, investment advisory personnel may not inquire or take into consideration whether issuers of securities proposed for purchase or sale for the Funds’ accounts are customers of TNTC’s commercial banking department. These requirements are designed to prevent investment advisory personnel for the Funds from knowing which companies have commercial business with TNTC and from purchasing securities where they know the proceeds will be used to repay loans to the bank.

The Advisory Agreement has been approved by the Board, including the “non-interested” Trustees and the initial shareholder of each Fund prior to the initial offering of shares of the Fund.

The Advisory Agreement provides that generally in selecting brokers or dealers to place orders for transactions on: (i) common and preferred stocks, the Investment Adviser shall use its best judgment to obtain the best overall terms available; and (ii) on bonds and other fixed-income obligations, the Investment Adviser shall attempt to obtain best net price and execution or, use its best judgment to obtain the best overall terms available.
Transactions on U.S. stock exchanges, and increasingly equity securities traded over-the-counter, involve the payment of negotiated brokerage commissions. Over-the-counter transactions in equity securities also may involve the payment of negotiated commissions to brokers. Transactions on foreign stock exchanges involve payment for brokerage commissions, which generally are fixed by applicable regulatory bodies. Many over-the-counter issues, including corporate debt and government securities, are normally traded on a “net” basis (i.e., without commission) through dealers, or otherwise involve transactions directly with the issuer of an instrument. With respect to over-the-counter transactions, the Investment Adviser will often deal directly with dealers who make a market in the instruments involved except in those circumstances where more favorable prices and execution are available elsewhere. The cost of foreign and domestic securities purchased from underwriters includes an underwriting commission or concession, and the prices at which securities are purchased from and sold to dealers include a dealer’s mark-up or mark-down. On exchanges on which commissions are negotiated, the cost of transactions may vary among different brokers. In assessing the best overall terms available for any transaction, the Investment Adviser is to consider all factors it deems relevant, including the breadth of the market in the security, the price of the security, the financial condition and execution capability of the broker or dealer, and the reasonableness of the commission, if any, both for the specific transaction and on a continuing basis. In evaluating the best overall terms available and in selecting the broker or dealer to execute a particular transaction, the Investment Adviser may consider the brokerage and research services provided to the Funds and/or other accounts over which the Investment Adviser or an affiliate exercises investment discretion. A broker or dealer providing brokerage and/or research services may receive a higher commission than another broker or dealer would receive for the same transaction. These brokerage and research services may include but are not limited to, furnishing of advice, either directly or through publications or writings, as to the value of securities, the advisability of investing in securities and the availability of securities or purchasers or sellers of securities. The Investment Adviser also may obtain economic statistics, forecasting services, industry and company analyses, portfolio strategies, quantitative data, quotation services, order management systems for certain purposes, certain news services, credit rating services, testing services, execution services, market information systems, consulting services from economists and political analysts and computer software or on-line data feeds. These services and products may disproportionately benefit other accounts. For example, research or other services paid for through the Funds’ commissions may not be used in managing the Funds. In addition, other accounts may receive the benefit, including disproportionate benefits, of economies of scale or price discounts in connection with products or services that may be provided to the Funds and to such other accounts. To the extent that the Investment Adviser uses soft dollars, it will not have to pay for those products or services itself. The Investment Adviser may receive research that is bundled with the trade execution, clearing, and/or settlement services provided by a particular broker-dealer. In that event, the research will effectively be paid for by client commissions that will also be used to pay for execution, clearing and settlement services provided by the broker-dealer and will not be paid by the Investment Adviser.

The Investment Adviser and its affiliates also receive products and services that provide both research and non-research benefits to them (“mixed-use items”). The research portion of mixed-use items may be paid for with soft dollars. When paying for the research portion of mixed-use items with soft dollars, the Investment Adviser must make a good faith allocation between the cost of the research portion and the cost of the non-research portion of the mixed-use items. The Investment Adviser will pay for the non-research portion of the mixed-use items with hard dollars.

Supplemental research information so received is in addition to, and not in lieu of, services required to be performed by the Investment Adviser and does not reduce the advisory fees payable to the Investment Adviser by the Funds. The Trustees will periodically review the commissions paid by the Funds to consider whether the commissions paid over representative periods of time appear to be reasonable in relation to the benefits inuring to the Funds. It is possible that certain of the supplemental research or other services received will primarily benefit one or more other investment companies or other accounts. Conversely, a Fund may be the primary beneficiary of the research or services received as a result of portfolio transactions effected for such other account or investment company.

The Funds may participate, if and when practicable, in bidding for the purchase of portfolio securities directly from an issuer in order to take advantage of the lower purchase price available to members of a bidding group. The Funds will engage in this practice, however, only when the Investment Adviser believes such practice to be in the Funds’ interests.

On occasions when the Investment Adviser deems the purchase or sale of a security to be in the best interests of a Fund as well as other fiduciary or agency accounts (“other accounts”) managed by the Investment Adviser, the Advisory Agreement provides that the Investment Adviser, to the extent permitted by applicable laws and regulations, may aggregate the securities to be sold or purchased for the Funds with those to be sold or purchased for such other accounts in order to obtain the best net price and execution. In such an event, allocation of the securities so purchased or sold, as well as the expenses incurred in the transaction, will be made by the Investment Adviser in the manner it considers to be the most equitable and consistent with its fiduciary obligations to the Fund and its other accounts involved. In some instances, this procedure may adversely affect the size of the position obtainable for a Fund or the amount of the securities that are able to be sold for a Fund. To the extent that the
execution and price available from more than one broker or dealer are believed to be comparable, the Advisory Agreement permits
the Investment Adviser, at its discretion but subject to applicable law, to select the executing broker or dealer on the basis of the
Investment Adviser’s opinion of the reliability and quality of the broker or dealer.

The Advisory Agreement provides that the Investment Adviser may render similar services to others so long as its
services under the Advisory Agreement are not impaired thereby. The Advisory Agreement also provides that the Trust will
indemnify the Investment Adviser against certain liabilities (including liabilities under the federal securities laws relating to untrue
statements or omissions of material fact and actions that are in accordance with the terms of the Advisory Agreement) or, in lieu
thereof, contribute to resulting losses.

Pursuant to the Advisory Agreement, the Investment Adviser is responsible for most of the operating expenses of the
Funds, except: (i) its advisory fees payable under the Advisory Agreement; (ii) distribution fees and expenses paid by the Trust
under any distribution plan adopted pursuant to Rule 12b-1 under the 1940 Act; (iii) interest expenses; (iv) brokerage expenses and
other expenses (such as stamp taxes) in connection with the execution of portfolio transactions or in connection with creation and
redemption transactions; (v) compensation and expenses of the non-interested trustees; (vi) compensation and expenses of counsel
to the non-interested trustees; (vii) tax expenses; and (viii) extraordinary expenses, as determined under generally accepted
accounting principles. For its services to each Fund, the Investment Adviser is entitled to an advisory fee, computed daily and
payable monthly, at annual rates set forth in the table below (expressed as a percentage of each Fund’s respective average daily net
assets).

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>INVESTMENT ADVISORY FEE</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>0.25%</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>0.39%</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>0.59%</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>0.44%</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</td>
<td>0.64%</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>0.32%</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund</td>
<td>0.32%</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund</td>
<td>0.42%</td>
</tr>
<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>0.46%</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>0.47%</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>0.45%</td>
</tr>
<tr>
<td>FlexShares® Real Assets Allocation Index Fund</td>
<td>0.57%</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>0.37%</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>0.37%</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>0.37%</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
<td>0.47%</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>0.47%</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>0.47%</td>
</tr>
<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>0.18%</td>
</tr>
<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
<td>0.18%</td>
</tr>
<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund</td>
<td>0.20%</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>0.22%</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>0.22%</td>
</tr>
<tr>
<td>FlexShares® High Yield Value-Scored Bond Index Fund</td>
<td>0.37%</td>
</tr>
</tbody>
</table>

Unless sooner terminated, the Advisory Agreement will continue in effect with respect to a particular Fund until June 30,
2019, and thereafter for successive 12-month periods, provided that the continuance is approved at least annually: (i) by the vote
of a majority of the Trustees who are not parties to the agreement or “interested persons” (as such term is defined in the 1940 Act)
of any party thereto, cast in person at a meeting called for the purpose of voting on such approval; and (ii) by the Trustees or by
the vote of a majority of the outstanding shares of such Fund (as defined under “Description of Shares”). The Advisory Agreement
is terminable at any time without penalty by the Trust (by specified Trustee or shareholder action) or by the Investment Adviser on
60 days’ written notice.

The table below provides the aggregate advisory fees paid to the Investment Adviser by each Fund in existence during the
fiscal year ended October 31, 2016.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>ADVISORY FEES PAID</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$2,053,607</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$2,421,466</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$1,625,868</td>
</tr>
</tbody>
</table>
## NAME OF FUND ADVISORY FEES PAID

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>ADVISORY FEES PAID</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund(1)</td>
<td>$12,566</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund(1)</td>
<td>$148,320</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$12,446</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund(2)</td>
<td>$4,867</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund(2)</td>
<td>$9,646</td>
</tr>
<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$9,841,686</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>$2,773,245</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>$818,246</td>
</tr>
<tr>
<td>FlexShares® Real Assets Allocation Index Fund(3)</td>
<td>$7,905</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$4,225,938</td>
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<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>$783,024</td>
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<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$204,667</td>
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<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
<td>$1,893,837</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>$305,772</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>$118,899</td>
</tr>
<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>$3,683,245</td>
</tr>
<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
<td>$1,072,036</td>
</tr>
<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund(4)</td>
<td>$65,468</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>$57,804</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>$20,751</td>
</tr>
</tbody>
</table>

(1) The FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund and FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund commenced operations on November 9, 2015. For the fiscal year ended October 31, 2016, the Investment Adviser reimbursed $11,219 and $137,651 of the advisory fees paid by the FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund and FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, respectively.

(2) The FlexShares® STOXX® US ESG Impact Index Fund and FlexShares® STOXX® Global ESG Impact Index Fund commenced operations on July 13, 2016.

(3) The FlexShares® Real Assets Allocation Index Fund commenced operations on November 23, 2015. For the fiscal year ended October 31, 2016, the Investment Adviser reimbursed $6,424 of the advisory fees paid by the FlexShares® Real Assets Allocation Index Fund.

(4) For the fiscal year ended October 31, 2016, JPMorgan voluntarily reimbursed $65,468 of the advisory fees paid by the FlexShares® Disciplined Duration MBS Index Fund.

The table below provides the aggregate advisory fees paid to the Investment Adviser by each Fund in existence during the fiscal year ended October 31, 2017.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>ADVISORY FEES PAID</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$2,556,469</td>
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<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$3,125,302</td>
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<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$2,516,735</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund(1)</td>
<td>$77,667</td>
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<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund(1)</td>
<td>$250,394</td>
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<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$58,995</td>
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<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund</td>
<td>$28,091</td>
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<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund</td>
<td>$42,300</td>
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<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$18,946,757</td>
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<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>$3,862,256</td>
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<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>$955,626</td>
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<tr>
<td>FlexShares® Real Assets Allocation Index Fund(2)</td>
<td>$16,741</td>
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<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$6,247,478</td>
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<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>$1,103,099</td>
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<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$238,542</td>
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<td>$3,370,865</td>
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<td>$384,100</td>
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<td>$273,462</td>
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<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>$3,988,820</td>
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<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
<td>$1,497,416</td>
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<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund(4)</td>
<td>$271,406</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>$10,864</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>$20,751</td>
</tr>
</tbody>
</table>

The table below provides the aggregate advisory fees paid to the Investment Adviser by each Fund in existence during the fiscal year ended October 31, 2017.
The table below provides the aggregate advisory fees paid to the Investment Adviser by each Fund in existence during the fiscal year ended October 31, 2018.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>ADVISORY FEES PAID</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>$ 30,029</td>
</tr>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$ 3,140,692</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$ 4,136,301</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$ 3,785,424</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>$ 59,742</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</td>
<td>$ 200,191</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$ 146,955</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund</td>
<td>$ 70,771</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund</td>
<td>$ 274,617</td>
</tr>
<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$ 25,178,142</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>$ 3,936,524</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>$ 1,220,458</td>
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<tr>
<td>FlexShares® Real Assets Allocation Index Fund</td>
<td>$ 65,358</td>
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<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$ 6,909,085</td>
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<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>$ 1,180,847</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$ 1,933,751</td>
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<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>$ 4,691,660</td>
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<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>$ 457,995</td>
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<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>$ 3,612,754</td>
</tr>
<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
<td>$ 1,653,034</td>
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<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund</td>
<td>$ 99,481</td>
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<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>$ 123,978</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>$ 52,915</td>
</tr>
<tr>
<td>FlexShares® High Yield Value-Scored Bond Index Fund</td>
<td>$ 53,627</td>
</tr>
</tbody>
</table>

(1) For the fiscal year ended October 31, 2018, the Investment Adviser reimbursed $53,048 and $183,878 of the advisory fees paid by the FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund and the FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, respectively.

(2) For the fiscal year ended October 31, 2018, the Investment Adviser reimbursed $52,763 of the advisory fees paid by the FlexShares® Real Assets Allocation Index Fund.

(3) The FlexShares® High Yield Value-Scored Bond Index Fund commenced operations on July 17, 2018.

NTI has contractually agreed to reimburse each Fund its proportionate share of the expenses relating to the administration of the DC Plan for the Trust’s non-interested trustees allocated to such Fund until March 1, 2020. NTI also has contractually agreed until March 1, 2020 in the case of the FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund and FlexShares® Real Assets Allocation Index Fund to waive management fees or reimburse certain expenses in an amount equal to the acquired fund fees and expenses attributable to each Fund’s investments in their respective Underlying Fund(s). NTI and a Fund may mutually agree to extend the contractual arrangements. The Board may terminate the contractual arrangements at any time if it determines that it is in the best interest of a Fund and its shareholders.

The table below provides the reimbursements made by the Investment Adviser to each Fund in existence during the fiscal year ended October 31, 2016.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>EXPENSE REIMBURSEMENTS BY NTI</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$ 54,686</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$ 41,861</td>
</tr>
</tbody>
</table>
The table below provides the reimbursements made by the Investment Adviser to each Fund in existence during the fiscal year ended October 31, 2017.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>EXPENSE REIMBURSEMENTS BY NTI</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$ 19,858</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>$ 13,439</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund (1)</td>
<td>$141,100</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$ 2,341</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund (2)</td>
<td>$ 721</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund (2)</td>
<td>$ 770</td>
</tr>
<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$141,655</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>$ 40,807</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>$ 14,074</td>
</tr>
<tr>
<td>FlexShares® Real Assets Allocation Index Fund (3)</td>
<td>$ 8,496</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$ 79,249</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>$ 17,278</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$ 6,780</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
<td>$ 28,899</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>$ 6,625</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>$ 3,997</td>
</tr>
<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>$120,219</td>
</tr>
<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
<td>$ 46,192</td>
</tr>
<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund (4)</td>
<td>$ 4,263</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>$ 3,827</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>$ 2,757</td>
</tr>
</tbody>
</table>

(1) The FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund and FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund commenced operations on November 9, 2015.

(2) The FlexShares® STOXX® US ESG Impact Index Fund and FlexShares® STOXX® Global ESG Impact Index Fund commenced operations on July 13, 2016.

(3) The FlexShares® Real Assets Allocation Index Fund commenced operations on November 23, 2015.

(4) In addition, JPMorgan voluntarily reimbursed $65,468 of the advisory fees paid by the FlexShares® Disciplined Duration MBS Index Fund.
The table below provides the reimbursements made by the Investment Adviser to each Fund in existence during the fiscal year ended October 31, 2018.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>EXPENSE REIMBURSEMENTS BY NTI</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$ 57,157</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$ 47,595</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$ 29,618</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>$ 55,031</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</td>
<td>$186,410</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$ 3,516</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund</td>
<td>$ 2,416</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund</td>
<td>$ 4,598</td>
</tr>
<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$238,681</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>$ 36,564</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>$ 13,259</td>
</tr>
<tr>
<td>FlexShares® Real Assets Allocation Index Fund</td>
<td>$ 54,699</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$ 82,307</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>$ 15,791</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$ 4,180</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
<td>$ 43,435</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>$ 5,551</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>$ 4,864</td>
</tr>
<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>$ 86,761</td>
</tr>
<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
<td>$ 41,922</td>
</tr>
<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund</td>
<td>$ 3,680</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>$ 3,882</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>$ 2,481</td>
</tr>
<tr>
<td>FlexShares® High Yield Value-Scored Bond Index Fund (1)</td>
<td>$ 788</td>
</tr>
</tbody>
</table>

(1) The FlexShares® High Yield Value-Scored Bond Index Fund commenced operations on July 17, 2018.

Under the Advisory Agreement with the Trust, Northern Trust Corporation agrees that the name “FlexShares” may be used in connection with the Trust’s business on a royalty-free basis. Northern Trust Corporation has reserved to itself the right to grant the non-exclusive right to use the name “FlexShares” to any other person. The Advisory Agreement provides that at such time as the Agreement is no longer in effect, the Trust will cease using the name “FlexShares.”

**BROKERAGE TRANSACTIONS**

The table below shows the aggregate dollar amount of brokerage commissions paid by each Fund in existence during the fiscal year ended October 31, 2016.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>BROKERAGE COMMISSIONS</th>
<th>AMOUNT OF TRANSACTIONS INVOLVED</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$12,243.43</td>
<td>$246,165,355.42</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$40,009.06</td>
<td>$279,322,791.38</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$114,367.87</td>
<td>$235,318,862.65</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>$147.74</td>
<td>$625,286.35</td>
</tr>
</tbody>
</table>

(1) The FlexShares® High Yield Value-Scored Bond Index Fund commenced operations on July 17, 2018.
<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>BROKERAGE COMMISSIONS</th>
<th>AMOUNT OF TRANSACTIONS INVOLVED</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
<td>$161,166.22</td>
<td>$441,577,411.20</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>$ 32,477.82</td>
<td>81,858,297.37</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>$ 10,759.68</td>
<td>29,870,203.45</td>
</tr>
<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

(1) The FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund and FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund commenced operations on November 9, 2015.

(2) The FlexShares® STOXX® US ESG Impact Index Fund and FlexShares® STOXX® Global ESG Impact Index Fund commenced operations on July 13, 2016.

(3) The FlexShares® Real Assets Allocation Index Fund commenced operations on November 23, 2015.

The table below shows the aggregate dollar amount of brokerage commissions paid by each Fund in existence during the fiscal year ended October 31, 2017.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>BROKERAGE COMMISSIONS</th>
<th>AMOUNT OF TRANSACTIONS INVOLVED</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$ 99,753.10</td>
<td>$421,475,677.12</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$ 70,736.42</td>
<td>358,719,353.62</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$277,670.18</td>
<td>508,145,079.13</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>$ 545.57</td>
<td>3,115,898.85</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</td>
<td>$ 944.76</td>
<td>4,723,700.50</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$ 317.70</td>
<td>2,526,913.34</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund</td>
<td>$ 850.24</td>
<td>6,425,537.11</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund</td>
<td>$ 2,069.51</td>
<td>10,999,950.29</td>
</tr>
<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$404,141.43</td>
<td>52,086,994.751.53</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>$ 40,076.73</td>
<td>252,400,734.80</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>$ 12,909.72</td>
<td>85,018,619.55</td>
</tr>
<tr>
<td>FlexShares® Real Assets Allocation Index Fund</td>
<td>$ 128.73</td>
<td>644,733.26</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$260,013.65</td>
<td>966,369,741.24</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>$ 24,200.40</td>
<td>129,056,478.11</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$ 1,427.86</td>
<td>14,555,363.01</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
<td>$202,613.00</td>
<td>633,663,144.83</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>$ 19,761.00</td>
<td>68,495,739.24</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>$ 19,336.05</td>
<td>55,541,843.32</td>
</tr>
<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

The table below shows the aggregate dollar amount of brokerage commissions paid by each Fund in existence during the fiscal year ended October 31, 2018.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>BROKERAGE COMMISSIONS</th>
<th>AMOUNT OF TRANSACTIONS INVOLVED</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$ 5,219.69</td>
<td>$237,739,342.57</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$ 52,193.38</td>
<td>415,904,163.14</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$323,848.82</td>
<td>684,222,866.31</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>$ 398.62</td>
<td>3,345,954.76</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</td>
<td>$ 1,002.94</td>
<td>6,425,537.11</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$ 4,558.31</td>
<td>44,393,036.15</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund</td>
<td>$ 2,263.44</td>
<td>18,977,413.63</td>
</tr>
</tbody>
</table>
During the fiscal year ended October 31, 2018, the Trust directed brokerage transactions to brokers because of research services provided. The amounts of such transactions and related commissions are as follows:

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>AMOUNT OF RESEARCH COMMISSIONS (000's)</th>
<th>AMOUNT OF RESEARCH COMMISSIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$1,389.28</td>
<td>$2.94</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$15,339.86</td>
<td>$9.10</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$204,046.44</td>
<td>$1.58</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>$352.73</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</td>
<td>$536.01</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$3,842.40</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund</td>
<td>$2,187.49</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund</td>
<td>$257.16</td>
<td>$6.99</td>
</tr>
<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$179,435.98</td>
<td>$277.70</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>$7,657.44</td>
<td>$106.88</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>$19,544.21</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Real Assets Allocation Index Fund</td>
<td>$226.37</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$137,952.52</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>$31,552.89</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$3,243.94</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
<td>$175,411.17</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>$14,434.17</td>
<td>-</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>$16,906.44</td>
<td>-</td>
</tr>
</tbody>
</table>

The value of the FlexShares® Morningstar US Market Factor Tilt Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the fiscal year ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debit (D)/Equity (E)</th>
<th>Aggregate Holdings (000’s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America Corp.</td>
<td>E</td>
<td>$21,735,260</td>
</tr>
<tr>
<td>Bank of New York Mellon Corp.</td>
<td>E</td>
<td>$1,932,200</td>
</tr>
<tr>
<td>Citigroup, Inc.</td>
<td>D</td>
<td>$2,000,000</td>
</tr>
<tr>
<td>JPMorgan Chase Bank, N.A.</td>
<td>E</td>
<td>$19,698,170</td>
</tr>
</tbody>
</table>

(1) The FlexShares® High Yield Value-Scored Bond Index Fund commenced operations on July 17, 2018.
The value of the FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the fiscal year ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goldman Sachs &amp; Co.</td>
<td>E</td>
<td>$4,202,700</td>
</tr>
<tr>
<td>Investment Technology Group, Inc.</td>
<td>E</td>
<td>$193,899</td>
</tr>
</tbody>
</table>

The value of the FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the fiscal year ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Citigroup, Inc.</td>
<td>D</td>
<td>$2,511,881</td>
</tr>
<tr>
<td>Credit Suisse Securities (USA) LLC</td>
<td>E</td>
<td>$807,985</td>
</tr>
<tr>
<td>HSBC Holdings PLC</td>
<td>E</td>
<td>$4,917,823</td>
</tr>
<tr>
<td>Societe Generale S.A.</td>
<td>E</td>
<td>$1,311,604</td>
</tr>
</tbody>
</table>

The value of the FlexShares® US Quality Large Cap Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the fiscal year ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Macquarie Bank Limited</td>
<td>E</td>
<td>$87,638</td>
</tr>
</tbody>
</table>

The value of the FlexShares® STOXX® US ESG Impact Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America Corp.</td>
<td>E</td>
<td>$1,402,115</td>
</tr>
<tr>
<td>Citigroup Inc.</td>
<td>E</td>
<td>$1,181,946</td>
</tr>
</tbody>
</table>

The value of the FlexShares® STOXX® Global ESG Impact Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America Corp.</td>
<td>E</td>
<td>$1,294,920</td>
</tr>
<tr>
<td>Bank of New York Mellon Corp.</td>
<td>E</td>
<td>$178,718</td>
</tr>
<tr>
<td>Barclays Capital, Inc.</td>
<td>E</td>
<td>$24,686</td>
</tr>
<tr>
<td>Citigroup, Inc.</td>
<td>E</td>
<td>$741,531</td>
</tr>
<tr>
<td>Credit Suisse Securities (USA) LLC</td>
<td>E</td>
<td>$92,102</td>
</tr>
<tr>
<td>Goldman Sachs &amp; Co.</td>
<td>E</td>
<td>$263,232</td>
</tr>
<tr>
<td>HSBC Holdings PLC</td>
<td>E</td>
<td>$635,880</td>
</tr>
<tr>
<td>JPMorgan Chase &amp; Co.</td>
<td>E</td>
<td>$1,269,865</td>
</tr>
<tr>
<td>Morgan Stanley &amp; Co. Inc.</td>
<td>E</td>
<td>$157,801</td>
</tr>
<tr>
<td>Societe Generale S.A.</td>
<td>E</td>
<td>$15,309</td>
</tr>
<tr>
<td>UBS Securities LLC</td>
<td>E</td>
<td>$266,924</td>
</tr>
</tbody>
</table>
The value of the FlexShares® Morningstar Global Upstream Natural Resources Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000’s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America Corp</td>
<td>D</td>
<td>$11,000,000</td>
</tr>
<tr>
<td>Citigroup, Inc.</td>
<td>D</td>
<td>$16,500,398</td>
</tr>
<tr>
<td>Societe Generale S.A.</td>
<td>D</td>
<td>$ 2,500,201</td>
</tr>
</tbody>
</table>

The value of the FlexShares® STOXX® Global Broad Infrastructure Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000’s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America Corp</td>
<td>D</td>
<td>$2,000,000</td>
</tr>
<tr>
<td>Citigroup, Inc.</td>
<td>D</td>
<td>$6,664,782</td>
</tr>
<tr>
<td>Nomura Group</td>
<td>D</td>
<td>$6,000,000</td>
</tr>
</tbody>
</table>

The value of the FlexShares® Global Quality Real Estate Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000’s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Citigroup, Inc.</td>
<td>D</td>
<td>$5,335,740</td>
</tr>
<tr>
<td>Societe Generale S.A.</td>
<td>E</td>
<td>$ 115,282</td>
</tr>
</tbody>
</table>

The value of the FlexShares® Quality Dividend Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000’s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America Corp</td>
<td>E</td>
<td>$ 9,689,350</td>
</tr>
<tr>
<td>JPMorgan Chase Bank, NA</td>
<td>D</td>
<td>$10,000,000</td>
</tr>
<tr>
<td>Citigroup, Inc.</td>
<td>E</td>
<td>$ 5,067,913</td>
</tr>
<tr>
<td>Societe Generale S.A.</td>
<td>D</td>
<td>$ 75,695,656</td>
</tr>
</tbody>
</table>

The value of the FlexShares® Quality Dividend Defensive Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000’s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America Corp</td>
<td>E</td>
<td>$ 296,835</td>
</tr>
<tr>
<td>Citigroup, Inc.</td>
<td>E</td>
<td>$ 307,924</td>
</tr>
</tbody>
</table>

The value of the FlexShares® Quality Dividend Dynamic Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:
The value of the FlexShares® International Quality Dividend Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>JPMorgan Chase Bank, N.A.</td>
<td>D</td>
<td>$2,097,212</td>
</tr>
<tr>
<td></td>
<td>E</td>
<td>$1,785,748</td>
</tr>
</tbody>
</table>

The value of the FlexShares® International Quality Dividend Defensive Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Citigroup, Inc.</td>
<td>D</td>
<td>$12,511,607</td>
</tr>
<tr>
<td>HSBC Holdings PLC</td>
<td>E</td>
<td>$11,748,874</td>
</tr>
</tbody>
</table>

The value of the FlexShares® International Quality Dividend Dynamic Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Citigroup, Inc.</td>
<td>D</td>
<td>$53,581</td>
</tr>
<tr>
<td>HSBC Holdings PLC</td>
<td>E</td>
<td>$1,313,217</td>
</tr>
<tr>
<td>Societe Generale S.A.</td>
<td>E</td>
<td>$66,812</td>
</tr>
</tbody>
</table>

The value of the FlexShares® Credit-Scored US Corporate Bond Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America Corp.</td>
<td>D</td>
<td>$2,970,453</td>
</tr>
<tr>
<td>Bank of New York Mellon Corp.</td>
<td>D</td>
<td>$736,685</td>
</tr>
<tr>
<td>Citigroup, Inc.</td>
<td>D</td>
<td>$2,610,604</td>
</tr>
<tr>
<td>Credit Suisse Securities (USA) LLC</td>
<td>D</td>
<td>$735,496</td>
</tr>
<tr>
<td>Deutsche Bank AG</td>
<td>D</td>
<td>$135,509</td>
</tr>
<tr>
<td>JPMorgan Chase &amp; Co.</td>
<td>D</td>
<td>$2,963,459</td>
</tr>
<tr>
<td>Mitsubishi UFJ Holdings Securities Holdings Co.</td>
<td>D</td>
<td>$1,020,515</td>
</tr>
<tr>
<td>Morgan Stanley &amp; Co. Inc.</td>
<td>D</td>
<td>$2,169,363</td>
</tr>
<tr>
<td>US Bancorp</td>
<td>D</td>
<td>$141,543</td>
</tr>
<tr>
<td>Wells Fargo &amp; Co.</td>
<td>D</td>
<td>$1,297,813</td>
</tr>
</tbody>
</table>

The value of the FlexShares® Credit-Scored US Long Corporate Bond Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America Corp.</td>
<td>D</td>
<td>$619,726</td>
</tr>
<tr>
<td>Citigroup, Inc.</td>
<td>D</td>
<td>$772,040</td>
</tr>
<tr>
<td>Credit Suisse Securities (USA) LLC</td>
<td>D</td>
<td>$94,182</td>
</tr>
<tr>
<td>JPMorgan Chase &amp; Co.</td>
<td>D</td>
<td>$931,090</td>
</tr>
<tr>
<td>Morgan Stanley &amp; Co., Inc.</td>
<td>D</td>
<td>$173,692</td>
</tr>
</tbody>
</table>
The value of the FlexShares® High Yield Value-Scored Bond Index Fund’s aggregate holdings of the securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) as of October 31, 2018 if any portion of such holdings were purchased during the period ended October 31, 2018 are as follows:

<table>
<thead>
<tr>
<th>Regular Broker-Dealer</th>
<th>Debt (D)/Equity (E)</th>
<th>Aggregate Holdings (000's)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wells Fargo &amp; Co.</td>
<td>D</td>
<td>$324,559</td>
</tr>
<tr>
<td>Credit Suisse Securities (USA) LLC</td>
<td>D</td>
<td>$357,000</td>
</tr>
<tr>
<td>Jefferies &amp; Co., Inc.</td>
<td>D</td>
<td>$196,500</td>
</tr>
</tbody>
</table>

No other Fund held securities of its regular brokers or dealers (as defined in Rule 10b-1 under the 1940 Act) during the fiscal year ended October 31, 2018.

There were no brokerage commissions paid to any affiliated broker or dealer of NTI during the fiscal year ended October 31, 2018.

**PORTFOLIO MANAGERS**

**NAME OF FUND**

- FlexShares® Morningstar US Market Factor Tilt Index Fund
- FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund
- FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund
- FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund
- FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund
- FlexShares® US Quality Large Cap Index Fund
- FlexShares® STOXX® US ESG Impact Index Fund
- FlexShares® STOXX® Global ESG Impact Index Fund
- FlexShares® Morningstar Global Upstream Natural Resources Index Fund
- FlexShares® STOXX® Global Broad Infrastructure Index Fund
- FlexShares® Global Quality Real Estate Index Fund
- FlexShares® Real Assets Allocation Index Fund
- FlexShares® Quality Dividend Index Fund
- FlexShares® Quality Dividend Defensive Index Fund
- FlexShares® Quality Dividend Dynamic Index Fund
- FlexShares® International Quality Dividend Index Fund
- FlexShares® International Quality Dividend Defensive Index Fund
- FlexShares® International Quality Dividend Dynamic Index Fund
- FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund
- FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund
- FlexShares® Disciplined Duration MBS Index Fund
- FlexShares® Credit-Scored US Corporate Bond Index Fund
- FlexShares® Credit-Scored US Long Corporate Bond Index Fund
- FlexShares® High Yield Value-Scored Bond Index Fund

**Accounts Managed by Portfolio Managers**

The table below discloses accounts within each type of category listed below for which **Robert Anstine** was jointly and primarily responsible for day-to-day portfolio management as of October 31, 2018.

<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>Total # of Accounts Managed</th>
<th>Total Assets Managed</th>
<th># of Accounts Managed that Advisory Fee is Based on Performance</th>
<th>Total Assets that Advisory Fee is Based on Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Trust:</td>
<td>18</td>
<td>$12,561,327,609</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

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<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>Total # of Accounts Managed</th>
<th>Total Assets</th>
<th># of Accounts Managed that Advisory Fee is Based on Performance</th>
<th>Total Assets that Advisory Fee is Based on Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Other Registered Investment Companies:</td>
<td>0</td>
<td>-</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Pooled Investment Vehicles:</td>
<td>8</td>
<td>$5,557,000,000</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Accounts:</td>
<td>5</td>
<td>$920,000,000</td>
<td>0</td>
<td>$0</td>
</tr>
</tbody>
</table>

The table below discloses accounts within each type of category listed below for which **Brendan Sullivan** was jointly and primarily responsible for day-to-day portfolio management as of October 31, 2018.

<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>Total # of Accounts Managed</th>
<th>Total Assets</th>
<th># of Accounts Managed that Advisory Fee is Based on Performance</th>
<th>Total Assets that Advisory Fee is Based on Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Trust:</td>
<td>18</td>
<td>$12,561,327,609</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Registered Investment Companies:</td>
<td>1</td>
<td>$4,600,000,000</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Pooled Investment Vehicles:</td>
<td>3</td>
<td>$13,100,000,000</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Accounts:</td>
<td>9</td>
<td>$3,700,000,000</td>
<td>0</td>
<td>$0</td>
</tr>
</tbody>
</table>

The table below discloses accounts within each type of category listed below for which **Daniel J. Personette** was jointly and primarily responsible for day-to-day portfolio management as of October 31, 2018.

<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>Total # of Accounts Managed</th>
<th>Total Assets</th>
<th># of Accounts Managed that Advisory Fee is Based on Performance</th>
<th>Total Assets that Advisory Fee is Based on Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Trust:</td>
<td>3</td>
<td>$2,593,743,211.00</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Registered Investment Companies:</td>
<td>4</td>
<td>$1,574,505,000.00</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Pooled Investment Vehicles:</td>
<td>4</td>
<td>$6,147,269,000.00</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Accounts:</td>
<td>13</td>
<td>$2,741,497,000.00</td>
<td>0</td>
<td>$0</td>
</tr>
</tbody>
</table>

The table below discloses accounts within each type of category listed below for which **Michael R. Chico** was jointly and primarily responsible for day-to-day portfolio management as of October 31, 2018.

<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>Total # of Accounts Managed</th>
<th>Total Assets</th>
<th># of Accounts Managed that Advisory Fee is Based on Performance</th>
<th>Total Assets that Advisory Fee is Based on Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Trust:</td>
<td>2</td>
<td>$2,555,160,312.30</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Registered Investment Companies:</td>
<td>3</td>
<td>$170,844,732.07</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Pooled Investment Vehicles:</td>
<td>7</td>
<td>$16,270,301,412.27</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Accounts:</td>
<td>11</td>
<td>$4,688,279,014.86</td>
<td>0</td>
<td>$0</td>
</tr>
</tbody>
</table>

The table below discloses accounts within each type of category listed below for which **Brandon P. Ferguson** was jointly and primarily responsible for day-to-day portfolio management as of October 31, 2018.

<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>Total # of Accounts Managed</th>
<th>Total Assets</th>
<th># of Accounts Managed that Advisory Fee is Based on Performance</th>
<th>Total Assets that Advisory Fee is Based on Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Trust:</td>
<td>6</td>
<td>$2,729,771,789.98</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Registered Investment Companies:</td>
<td>0</td>
<td>-</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Pooled Investment Vehicles:</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Accounts:</td>
<td>9</td>
<td>$3,725,710,000.00</td>
<td>0</td>
<td>$0</td>
</tr>
</tbody>
</table>

The table below discloses accounts within each type of category listed below for which **Bradley Camden** was jointly and
primarily responsible for day-to-day portfolio management as of October 31, 2018.

<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>Total # of Accounts Managed</th>
<th>Total Assets</th>
<th># of Accounts Managed that Advisory Fee is Based on Performance</th>
<th>Total Assets that Advisory Fee is Based on Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Trust:</td>
<td>5</td>
<td>$246,239,061.61</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Registered Investment Companies:</td>
<td>4</td>
<td>$6,023,000,000.00</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Pooled Investment Vehicles:</td>
<td>74</td>
<td>$3,942,132,000.00</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Accounts:</td>
<td>0</td>
<td>-</td>
<td>0</td>
<td>$0</td>
</tr>
</tbody>
</table>

The table below discloses accounts within each type of category listed below for which **Kevin O’Shaughnessy** was jointly and primarily responsible for day-to-day portfolio management as of October 31, 2018.

<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>Total # of Accounts Managed</th>
<th>Total Assets</th>
<th># of Accounts Managed that Advisory Fee is Based on Performance</th>
<th>Total Assets that Advisory Fee is Based on Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Trust:</td>
<td>1</td>
<td>$71,627,583.93</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Registered Investment Companies:</td>
<td>4</td>
<td>$10,195,640,529.39</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Pooled Investment Vehicles:</td>
<td>12</td>
<td>$10,941,079,968.32</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Accounts:</td>
<td>1</td>
<td>$822,799,394.25</td>
<td>0</td>
<td>$0</td>
</tr>
</tbody>
</table>

The table below discloses accounts within each type of category listed below for which **Mike T. Doyle** was jointly and primarily responsible for day-to-day portfolio management as of October 31, 2018.

<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>Total # of Accounts Managed</th>
<th>Total Assets</th>
<th># of Accounts Managed that Advisory Fee is Based on Performance</th>
<th>Total Assets that Advisory Fee is Based on Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Trust:</td>
<td>2</td>
<td>$87,171,001.96</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Registered Investment Companies:</td>
<td>0</td>
<td>-</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Pooled Investment Vehicles:</td>
<td>9</td>
<td>$5,032,183,394.28</td>
<td>0</td>
<td>$0</td>
</tr>
<tr>
<td>Other Accounts:</td>
<td>49</td>
<td>$1,857,882,681.61</td>
<td>0</td>
<td>$0</td>
</tr>
</tbody>
</table>

**Material Conflicts of Interest**

NTI's portfolio managers are often responsible for managing one or more FlexShares® Funds, as well as other client accounts, including mutual funds, separate accounts and other pooled investment vehicles. A Fund’s portfolio managers may manage various client accounts that may have materially higher or lower fee arrangement than the Funds. The side-by-side management of these accounts may raise potential conflicts of interest relating to cross trading, the allocation of investment opportunities and the aggregation and allocation of trades. In addition, while portfolio managers generally only manage accounts with similar investment strategies, it is possible that due to varying investment restrictions among accounts that certain investments are made for some accounts and not others or conflicting investment positions could be taken among accounts. Some portfolio managers may be dual officers of one or more NTI affiliates and undertake investment advisory duties for the affiliates. The portfolio managers have a responsibility to manage all client accounts in a fair and equitable manner. NTI seeks to provide best execution of all securities transactions and aggregate and then allocate securities to client accounts in a fair and timely manner. To this end, NTI has developed policies and procedures designed to mitigate and manage the potential conflicts of interest that may arise from side-by-side management.

NTI may have a financial incentive to favor accounts with performance-based fees because there may be an opportunity to earn greater fees on such accounts compared to accounts without performance-based fees. As a result, NTI may have an incentive to direct its best investment ideas to or allocate the sequencing of trades in favor of the account that pays a performance fee. NTI may also have an incentive to recommend investments that may be riskier or more speculative than those that it would recommend under a different fee arrangement.
NTI may invest client accounts in affiliated investment pools. If appropriate and consistent with the client’s investment objectives and applicable law, NTI may recommend to clients investment pools in which it or an affiliate provides services for a fee. NTI has an incentive to allocate investments to these types of affiliated investment pools in order to generate additional fees for NTI or its affiliates. In addition, NTI could direct its best investment ideas to these investment products or investment pools to the potential disadvantage of the Funds.

As NTI becomes aware of additional potential or actual conflicts of interest, they will be reviewed on a case-by-case basis.

NTI manages its client accounts consistent with applicable law and follows its own policies and procedures that are reasonably designed to treat clients fairly and to prevent any client or group of clients from being systematically favored or disadvantaged.

NTI provides advice and makes investment decisions for client accounts that it believes are consistent with each client’s stated investment objectives and guidelines. Advice given to clients or investment decisions made for clients may differ from, or may conflict with, advice given or investment decisions made for clients of an affiliate. NTI’s affiliates may also affect NTI’s client accounts and investment decisions made for NTI’s affiliates may affect investment decisions of NTI’s client accounts. NTI may also invest in the same securities that it or its affiliates recommend to clients. Investment decisions taken by NTI's affiliates are generally unknown to NTI. When NTI or an affiliate currently holds for its own benefit the same securities as a client, it could be viewed as having a potential conflict of interest.

Generally, NTI will not, as principal for its own account, buy securities from or sell securities to any client. It is possible that an affiliate, will, as principal, purchase securities from or sell securities to its clients.

From time to time securities to be sold on behalf of a client may be suitable for purchase by another client. In such instances, if NTI determines in good faith that the transaction is in the best interest of each client, it may arrange for the securities to be crossed between client accounts at an independently determined fair market value and in compliance with the 1940 Act, if applicable. Cross-trades present conflicts of interest, as there may be an incentive for NTI to favor one client to the disadvantage of another. Cross-trades are only effected as permitted under applicable law and regulation and consistent with the client’s guidelines, with any restrictions. NTI does not receive fees or commissions for these transactions. In addition, NTI and the Trust have adopted policies on cross-trades that may be effected between the Funds and another client account. NTI conducts periodic reviews of trades for consistency with these policies.

NTI has established certain policies and procedures designed to address conflicts of interest that may arise between its employees and clients as well as between clients and NTI or its affiliates. NTI’s employees must act in the best interests of its clients and generally do not have knowledge of proprietary trading positions or certain other operations of affiliates.

Receipt of research from brokers who execute client transactions involve conflicts of interest. To the extent that NTI uses commissions to obtain research services for NTI or TNTC, NTI or TNTC will receive a benefit as it will not have to pay for the research, products or services itself. NTI may, therefore, have an incentive to select or recommend a broker-dealer based on its interest in receiving research rather than in obtaining the lowest commission rate on the transaction. NTI or TNTC may also obtain research services from brokerage commissions incurred by client accounts that may not directly benefit such client accounts. Similarly, clients may benefit from research even if trades placed on their behalf did not contribute to the compensation of the broker-dealer providing such research. NTI and TNTC do not seek to allocate research services to client accounts proportionately to the commissions that the client accounts generate.

Also, NTI and TNTC may receive products and services that are mixed use. In these cases, NTI or TNTC will use commissions to pay only for the eligible portion of the product or service that assists NTI or TNTC in the investment decision-making process. Any ineligible portion of the product will be paid directly by NTI or TNTC. NTI or TNTC make a good faith effort to reasonably allocate such items and keep records of such allocations although clients should be aware of the potential conflicts of interest.

NTI may provide investment advice to its affiliates and may provide investment advisory services to affiliates’ clients or as an investment adviser to the registered or unregistered investment pools in which these clients may invest. TNTC and NTI share a common trading desk and may have shared arrangements with investment research vendors. Also, these affiliates may provide marketing services to NTI, including the referral of certain clients.
NTI may have common management and officers with some of its affiliates. NTI shares facilities with affiliates and relies on TNTC and other affiliates for various administrative support, including information technology, human resources, business continuity, legal, compliance, finance, enterprise risk management, internal audit and general administrative support.

NTI’s affiliations may create potential conflicts of interest. NTI seeks to mitigate the potential conflicts of interest to ensure accounts are managed at all times in a client’s best interests and in accordance with client investment objectives and guidelines through regular account reviews attended by investment advisory, compliance and senior management staff. NTI also seeks to mitigate potential conflicts of interest through a governance structure and by maintaining policies and procedures that include, but are not limited to, personal trading, custody and trading.

Various non-affiliated investment advisers that may manage NTI client accounts, or may be recommended to NTI clients, may use an NTI affiliate for banking, trust, custody, administration, brokerage and related services for which NTI’s affiliate may receive fees. NTI does not recommend or utilize non-affiliated investment advisers based upon their use of NTI affiliates.

Given the interrelationships among NTI and its affiliates, there may be other or different potential conflicts of interest that arise in the future that are not included in this section.

NTI may develop, or own and operate indices that are based on investment and trading strategies developed by NTI, or assist unaffiliated entities by creating bespoke indices that are utilized by NTI for client-specific investment accounts. In addition, NTI may manage accounts that are based on the same, or substantially similar, strategies that are used in the operation of the indices or the Funds. The administration of the indices, and the portfolio management of the Funds and client accounts in this manner may give rise to potential conflicts of interest. These conflicts of interest may include, but are not limited to, the Funds engaging in the purchase or sale of securities relating to changes being implemented as part of an index reconstitution, while at the same time the client accounts engage in similar trading activity due to ongoing portfolio rebalancing. These differences may result in client account strategies outperforming vis-à-vis the index, the Funds, or vice versa. Other potential conflicts include the potential for unauthorized access to index information, allowing index changes that benefit NTI or other client accounts and not the investors in the Funds.

To the extent permitted by applicable law, the Investment Adviser may make payments to authorized dealers and other financial intermediaries (“Intermediaries”) from time to time to promote the Funds. These payments may be made out of the Investment Adviser’s assets, or amounts payable to the Investment Adviser rather than as a separately identifiable charge to the Funds. These payments may compensate Intermediaries for, among other things: marketing the Funds; access to the Intermediaries’ registered representatives or salespersons, including at conferences and other meetings; assistance in training and education of personnel; marketing support; and/or other specified services intended to assist in the distribution and marketing of the Funds. The payments may also, to the extent permitted by applicable regulations, contribute to various non-cash and cash incentive arrangements to promote certain products, as well as sponsor various educational programs, sales contests and/or administrative services.

Portfolio Manager Compensation Structure

The compensation for the portfolio managers of the Funds is based on the competitive marketplace and consists of a fixed base salary plus a variable annual cash incentive award. In addition, non-cash incentives, such as stock options or restricted stock of Northern Trust Corporation, may be awarded from time to time. The annual incentive award is discretionary and is based on a quantitative and qualitative evaluation of each portfolio manager’s investment performance and contribution to his or her respective team plus the financial performance of the investment business unit and Northern Trust Corporation as a whole. The annual incentive award is not based on performance of the Funds or the amount of assets held in the Funds. Moreover, no material differences exist between the compensation structure for Fund accounts and other types of accounts.

Disclosure of Securities Ownership

For the most recently completed fiscal year ended October 31, 2018, the table below provides beneficial ownership of shares of the portfolio managers of the Funds. Please note that the table provides a dollar range of each portfolio manager’s holdings in each Fund (None, $1-$10,000, $10,001-$50,000, $50,001-$100,000, $100,001-$500,000, $500,001-$1,000,000, or over $1,000,000).
<table>
<thead>
<tr>
<th>Shares Beneficially Owned by</th>
<th>Fund</th>
<th>Dollar ($) Range of Shares Beneficially Owned by Portfolio Manager Because of Direct or Indirect Pecuniary Interest</th>
</tr>
</thead>
<tbody>
<tr>
<td>Robert Anstine</td>
<td>FlexShares® Morningstar U.S. Market Factor Tilt Index Fund</td>
<td>$10,001-$50,000</td>
</tr>
<tr>
<td>Robert Anstine</td>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$10,001-$50,000</td>
</tr>
<tr>
<td>Robert Anstine</td>
<td>FlexShares® Real Assets Allocation Index Fund</td>
<td>$10,001-$50,000</td>
</tr>
<tr>
<td>Robert Anstine</td>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>$10,001-$50,000</td>
</tr>
<tr>
<td>Bradley Camden</td>
<td>FlexShares® Disciplined Duration MBS Index Fund</td>
<td>$10,001-$50,000</td>
</tr>
<tr>
<td>Bradley Camden</td>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>$1-$10,000</td>
</tr>
<tr>
<td>Bradley Camden</td>
<td>FlexShares® High Yield Value-Scored Bond Index Fund</td>
<td>$10,001-$50,000</td>
</tr>
</tbody>
</table>

**PROXY VOTING**

The Trust has delegated the voting of portfolio securities to its Investment Adviser. The Investment Adviser has adopted the Institutional Shareholder Services Inc. (“ISS”) United States SRI Proxy Voting Guidelines (“SRI US Guidelines”) for the voting of U.S. proxies on behalf of the FlexShares® STOXX® US ESG Impact Index Fund and FlexShares® STOXX® Global ESG Impact Index Fund and the ISS Internationally SRI Proxy Voting Guidelines (“SRI International Guidelines” and together with the SRI US Guidelines, the “SRI Guidelines”) for the voting of international proxies on behalf of the FlexShares® STOXX® Global ESG Impact Index Fund.

On matters of corporate governance, executive compensation and corporate structure, the SRI Guidelines, as developed by ISS, are based on a commitment to create and preserve economic value and to advance principles of good corporate governance consistent with responsibilities to society as a whole. The SRI Guidelines provide an overview of how ISS recommends that its clients vote. There may be cases in which the final vote recommendation on a particular company varies from the vote guideline due to the fact that ISS closely examines the merits of each proposal and consider relevant information and company specific circumstances in arriving at vote recommendations. The SRI Guidelines are updated on an annual basis to take into account emerging issues and trends on environmental, social, and corporate governance topics, in addition to evolving market standards, regulatory changes, and client feedback. The SRI Guidelines do not take into consideration any interest that the Investment Adviser or any affiliated person of the Funds or the Investment Adviser may have in the proposed proxy issue. See Appendix D to this SAI for a complete list of the SRI Guidelines.

Additionally, the Investment Adviser has adopted proxy voting policies and procedures applicable to Northern Trust Corporation and its affiliates (the “Northern Proxy Voting Policy”) for the voting of proxies on behalf of client accounts for which the Investment Adviser has voting discretion, including the FlexShares® Morningstar US Market Factor Tilt Index Fund, FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Heded Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Heded Morningstar EM Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Quality Dividend Index Fund, FlexShares® Quality Dividend Defensive Index Fund, FlexShares® Quality Dividend Dynamic Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund, FlexShares® International Quality Dividend Dynamic Index Fund, FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund. Under the Northern Proxy Voting Policy, shares are to be voted in the best interests of the above-referenced Funds and the value of the investment.

A Proxy Committee comprised of senior investment and compliance officers of Northern Trust Corporation, including officers of the Investment Adviser has adopted certain guidelines (the “Proxy Guidelines”) concerning various corporate governance issues. The Proxy Committee has the responsibility for the content, interpretation and application of the Proxy Guidelines and may apply these Proxy Guidelines with a measure of flexibility. The Investment Adviser has retained an independent third party proxy voting service (the “Service Firm”) to review proxy proposals and to make voting recommendations to the Proxy Committee in a manner consistent with the Proxy Guidelines. The Proxy Committee will apply the Proxy Guidelines as discussed below to any such recommendation.
The Proxy Guidelines provide that the Proxy Committee will generally vote for or against various proxy proposals, usually based upon certain specified criteria. As an example, the Proxy Guidelines provide that the Proxy Committee will generally vote in favor of:

- Shareholder proposals in support of the appointment of a lead independent director;
- Shareholder proposals requesting that the board of a company be comprised of a majority of independent directors;
- Proposals to repeal classified boards and to elect all directors annually;
- Shareholder proposals calling for directors in uncontested elections to be elected by an affirmative majority of votes cast where companies have not adopted a written majority voting (or majority withhold) policy;
- Shareholder proposals that ask a company to submit its poison pill for shareholder ratification;
- Shareholder proposals to lower supermajority shareholder vote requirements for charter and bylaw amendments;
- Shareholder proposals to lower supermajority shareholder vote requirements for mergers and other significant business combinations while taking into account ownership structure, quorum requirements, and vote requirements;
- Management proposals to reduce the par value of common stock while taking into account accompanying corporate governance concerns;
- Management proposals to implement a reverse stock split, provided that the reverse split does not result in an increase of authorized but unissued shares of more than 100% after giving effect to the shares needed for the reverse split;
- Proposals to approve an ESOP (employee stock ownership plan) or other broad based employee stock purchase or ownership plan, or to increase authorized shares for such existing plans, except in cases when the number of shares allocated to such plans is “excessive” (i.e., generally greater than ten percent (10%) of outstanding shares); and
- Proposals requesting that a company take reasonable steps to ensure that women and minority candidates are in the pool from which board nominees are chosen or that request that women and minority candidates are routinely sought as part of every board search the company undertakes.

The Proxy Guidelines also provide that the Proxy Committee will generally vote against:

- Shareholder proposals requesting that the board of a company be comprised of a supermajority of independent directors;
- Proposals to elect director nominees if it is a CEO who sits on more than two public boards or a non-CEO who sits on more than four public company boards;
- Proposals to classify the board of directors;
- Shareholder proposals requiring directors to own a minimum amount of company stock in order to qualify as a director or to remain on the board;
- Shareholder proposals to impose age and term limits unless the company is found to have poor board refreshment and director succession practices;
- Proposals for multi class exchange offers and multi class recapitalizations;
- Management proposal to require a supermajority shareholder vote to approve mergers and other significant business combinations, while taking into account ownership structure, quorum requirements, and vote requirements;
- Management proposals to require a supermajority shareholder vote to approve charter and bylaw amendments; and
- Shareholder proposals to eliminate, direct, or otherwise restrict charitable contributions.

For proxy proposals that under the Proxy Guidelines are to be voted on a case by case basis, the Proxy Committee provides supplementary instructions to the Service Firm to guide it in making vote recommendations.

Except as otherwise provided in the Northern Proxy Voting Policy, the Proxy Committee may vote proxies contrary to the recommendations of the Service Firm if it determines that such action is in the best interest of a Fund. In exercising its discretion, the Proxy Committee may take into account a wide array of factors relating to the matter under consideration, the
nature of the proposal and the company involved. As a result, the Proxy Committee may vote in one manner in the case of one company and in a different manner in the case of another where, for example, the past history of the company, the character and integrity of its management, the role of outside directors, and the company’s record of producing performance for investors justifies a high degree of confidence in the company and the effect of the proposal on the value of the investment. Similarly, poor past performance, uncertainties about management and future directions, and other factors may lead the Proxy Committee to conclude that particular proposals present unacceptable investment risks and should not be supported. In addition, the Proxy Committee also evaluates proposals in context. For example, a particular proposal may be acceptable standing alone, but objectionable when part of an existing or proposed package. Special circumstances may also justify casting different votes for different clients with respect to the same proxy vote.

The Investment Adviser or its affiliates may occasionally be subject to conflicts of interest in the voting of proxies due to business or personal relationships it maintains with persons having an interest in the outcome of certain votes. For example, the Investment Adviser or its affiliates may provide trust, custody, investment management, brokerage, underwriting, banking and related services to accounts owned or controlled by companies whose management is soliciting proxies. Occasionally, the Investment Adviser or its affiliates may also have business or personal relationships with other proponents of proxy proposals, participants in proxy contests, corporate directors or candidates for directorships. The Investment Adviser may also be required to vote proxies for securities issued by Northern Trust Corporation or its affiliates or on matters in which the Investment Adviser or its affiliates have a direct financial interest, such as shareholder approval of a change in the advisory fees paid by a Fund. The Investment Adviser seeks to address such conflicts of interest through various measures, including the establishment, composition and authority of the Proxy Committee and the retention of the Service Firm to perform proxy review and vote recommendation functions. The Proxy Committee has the responsibility to determine whether a proxy vote involves a conflict of interest and how the conflict should be addressed in conformance with the Northern Proxy Voting Policy. The Proxy Committee may resolve such conflicts in any of a variety of ways, including without limitation the following: (i) voting in accordance with the Proxy Guidelines based recommendation of the Service Firm; (ii) voting in accordance with the recommendation of an independent fiduciary appointed for that purpose; (iii) voting pursuant to client direction by seeking instructions from the Board; or (iv) by voting pursuant to a “mirror voting” arrangement under which shares are voted in the same manner and proportion as shares over which the Investment Adviser does not have voting discretion. The method selected by the Proxy Committee may vary depending upon the facts and circumstances of each situation.

The Investment Adviser may choose not to vote proxies in certain situations. This may occur, for example, in situations where the exercise of voting rights could restrict the ability to freely trade the security in question (as is the case, for example, in certain foreign jurisdictions known as “blocking markets”). In circumstances in which the Service Firm does not provide recommendations for a particular proxy, the Proxy Committee may obtain recommendations from analysts at the Investment Adviser who review the issuer in question or the industry in general. The Proxy Committee will apply the Proxy Guidelines as discussed above to any such recommendation.

This summary of the Northern Proxy Voting Policy and Proxy Guidelines, as adopted by the Investment Adviser, is posted on the Trust’s website. You may also obtain, upon request and without charge, a paper copy of the Northern Proxy Voting Policy and Proxy Guidelines or a Statement of Additional Information by calling 1-855-FLEXETF (1-855-353-9383).

Information regarding how the Funds voted proxies, if any, relating to portfolio securities for the most recent 12-month period ended June 30 will be made available, without charge, upon request, by contacting the Investment Adviser at 1-855-FLEXETF or by visiting the SEC’s website at www.sec.gov.

ADMINISTRATOR

JPMorgan (the “Administrator”), One Beacon Street, Boston, Massachusetts 02108, acts as Administrator for the Funds under a Fund Servicing Agreement with the Trust. Subject to the general supervision of the Board, the Administrator provides supervision of all aspects of the Trust’s non-investment advisory operations and performs various administration, compliance, accounting and regulatory services, including but not limited to: (i) providing office facilities and furnishing corporate officers for the Trust; (ii) coordination, preparation and review of financial statements; (iii) monitoring compliance with federal tax and securities laws; (iv) performing certain functions ordinarily performed by the office of a corporate treasurer, and furnishing the services and facilities ordinarily incident thereto, such as expense accrual monitoring and payment of the Trust’s bills, preparing monthly reconciliation of the Trust’s expense records, updating projections of annual expenses, preparing materials for review by the Board and compliance testing; (v) maintaining the Trust books and records in accordance with applicable statutes, rules and
regulations; (vi) preparing post-effective amendments to the Trust’s registration statement; (vii) calculating each Fund’s NAV; (viii) accounting for dividends and interest received and distributions made by the Trust; and (ix) preparing and filing the Trust’s federal and state tax returns (other than those required to be filed by the Trust’s Custodian and Transfer Agent) and providing shareholder tax information to the Trust’s Transfer Agent.

Subject to the limitations described below, as compensation for its administrative services and the assumption of related expenses, the Administrator is entitled to asset-based fees for accounting and administration services, subject to a certain minimum fee. The Administration Agreement will continue until August 31, 2019 unless sooner terminated pursuant to the agreement and renew each year thereafter unless at least sixty days’ notice is given prior to the end of a term. Under the Advisory Agreement, the Investment Adviser has contractually assumed the Trust’s obligation to pay the fees of the Administrator.

DISTRIBUTOR

Foreside Fund Services, LLC (“Foreside” or the “Distributor”), a Delaware limited liability company, serves as the distributor of Creation Units for the Funds on an agency basis. The Trust has entered into a Distribution Agreement under which Foreside, as agent, receives orders from Authorized Participants to create and redeem shares in Creation Unit Aggregations and transmits such orders to the Trust’s Custodian and Transfer Agent. The Distributor’s principal address is Three Canal Plaza, Portland, Maine 04101. The Distributor is a broker-dealer registered under the Securities Exchange Act of 1934, as amended (the “1934 Act”), and a member of the FINRA. Shares will be continuously offered for sale by the Trust through the Distributor only in whole Creation Units, as described in the section of this SAI entitled “Purchase and Redemption of Creation Units Aggregations.” The Distributor also acts as an agent for the Trust for those activities described within the Distribution Agreement. The Distributor will deliver a prospectus to Authorized Participants purchasing Shares in Creation Units and will maintain records of both orders placed with it and confirmations of acceptance furnished by it to Authorized Participants. The Distributor has no role in determining the investment policies of the Funds or which securities are to be purchased or sold by the Funds. No compensation is payable by the Trust to Foreside for such distribution services. However, the Investment Adviser has entered into an agreement with Foreside under which it makes payments to Foreside in consideration for its services under the Distribution Agreement. The payments made by the Investment Adviser to Foreside do not represent an additional expense to the Trust or its shareholders.

DISTRIBUTION AND SERVICE PLAN

As stated in the Funds’ Prospectus, the Trust has adopted a Distribution and Service Plan (the “Plan”) pursuant to Rule 12b-1 with respect to shares of the Funds. However, no 12b-1 fee is currently charged to the Funds, and the Funds do not expect to pay any 12b-1 fees during the current and next fiscal years. Pursuant to the Plan, the Funds may enter into agreements from time to time with financial intermediaries providing for support and/or distribution services to customers of the financial intermediaries who are the beneficial owners of Fund shares. Under the agreements, the Funds may pay financial intermediaries up to 0.25% (on an annualized basis) of the average daily NAV of the shares beneficially owned by their customers. Distribution services may include: (i) services in connection with distribution assistance; or (ii) payments to financial institutions and other financial intermediaries, such as broker-dealers and mutual fund “supermarkets,” as compensation for services or reimbursement of expenses incurred in connection with distribution assistance.

Any amendment to increase materially the costs under the Plan with respect to a Fund must be approved by the holders of a majority of the outstanding shares of the Fund. So long as the Plan is in effect, the selection and nomination of the members of the Board who are not “interested persons” (as defined in the 1940 Act) of the Trust will be committed to the discretion of such Non-Interested Trustees.

TRANSFER AGENT

JPMorgan (the “Transfer Agent”) acts as Transfer Agent for the Fund under an Agency Services Agreement with the Trust. The Transfer Agent has undertaken to perform some or all of the following services: (i) perform and facilitate the performance of purchases and redemptions of Creation Units; (ii) prepare and transmit payments for dividends and distributions; (iii) record the issuance of shares and maintain records of the number of authorized shares; (iv) prepare and transmit information regarding purchases and redemptions of shares; (v) communicate information regarding purchases and redemptions of shares and other relevant information to appropriate parties; (vi) maintain required books and records; and (vii) perform other customary services of a transfer agent and dividend disbursing agent for an ETF (exchange traded fund).
As compensation for the services rendered by the Transfer Agent under the Agency Services Agreement the Transfer Agent is entitled to reasonable out-of-pocket or incidental expenses as provided under the Agency Services Agreement. The Agency Services Agreement will continue until August 31, 2019 unless sooner terminated pursuant to the agreement and renew each year thereafter unless at least sixty days’ notice is given prior to the end of a term. Under the Advisory Agreement, the Investment Adviser has contractually assumed the Trust’s obligation to pay the expenses of the Transfer Agent.

CUSTODIAN

JPMorgan (the “Custodian”) acts as Custodian for the Funds under a Global Custody Agreement with the Trust. The Custodian: (i) holds each Fund’s cash and securities; (ii) maintains such cash and securities in separate accounts in the name of each Fund; (iii) receives, delivers and releases securities on behalf of each Fund; (iv) collects and receives all income, principal and other payments in respect of each Fund’s investments held by the Custodian; and (v) maintains a statement of account for each account of the Trust. The Custodian may employ one or more sub-custodians, provided that the Custodian shall be liable for direct losses due to the sub-custodian’s insolvency or the sub-custodian’s failure to use reasonable care, fraud or willful default in the provision of its services. The Custodian will enter into agreements with financial institutions and depositories located in foreign countries with respect to the custody of the Funds’ foreign securities.

As compensation for the services rendered under the Global Custody Agreement with respect to the Trust by the Custodian to each Fund, the Custodian is entitled to fees and reasonable out-of-pocket expenses. The Global Custody Agreement will continue until August 31, 2019 unless sooner terminated pursuant to the agreement and renew each year thereafter unless at least sixty days’ notice is given prior to the end of a term. Under the Advisory Agreement, the Investment Adviser has contractually assumed the Trust’s obligation to pay the fees and expenses of the Custodian.

JPMorgan also serves as securities lending agent for the Funds. For such services, JPMorgan receives a percentage of securities lending revenue generated for the Funds.

The following table sets forth the administration, custodian and transfer agency expenses of each Fund paid by the Investment Adviser to JPMorgan for the fiscal years noted:

<table>
<thead>
<tr>
<th>Fund</th>
<th>Inception Date</th>
<th>Administration, Custodian, Transfer Agency Expenses Paid During Fiscal Year Ended October 31, 2018</th>
<th>Administration, Custodian, Transfer Agency Expenses Paid During Fiscal Year Ended October 31, 2017</th>
<th>Administration, Custodian, Transfer Agency Expenses Paid During Fiscal Year Ended October 31, 2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>9/16/2011</td>
<td>$ 568,725</td>
<td>$ 509,231</td>
<td>$ 386,600</td>
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<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>9/25/2012</td>
<td>$ 501,602</td>
<td>$ 463,855</td>
<td>$ 424,059</td>
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<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>9/25/2012</td>
<td>$ 505,180</td>
<td>$ 717,293</td>
<td>$ 490,553</td>
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<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>11/9/2015</td>
<td>$ 8,502</td>
<td>$ 13,835</td>
<td>$ 3,701</td>
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<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</td>
<td>11/9/2015</td>
<td>$ 16,328</td>
<td>$ 24,610</td>
<td>$ 12,497</td>
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<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>9/23/2015</td>
<td>$ 19,398</td>
<td>$ 10,053</td>
<td>$ 5,142</td>
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<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund</td>
<td>7/13/2016</td>
<td>$ 14,349</td>
<td>$ 7,565</td>
<td>$ 2,667</td>
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<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund</td>
<td>7/13/2016</td>
<td>$ 65,824</td>
<td>$ 33,685</td>
<td>$ 13,251</td>
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<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>9/16/2011</td>
<td>$2,192,085</td>
<td>$2,218,099</td>
<td>$1,127,784</td>
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<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>10/8/2013</td>
<td>$ 339,276</td>
<td>$ 436,528</td>
<td>$ 324,038</td>
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<tr>
<td>Fund</td>
<td>Inception Date</td>
<td>Administration, Custodian, Transfer Agency Expenses Paid During Fiscal Year Ended October 31, 2018</td>
<td>Administration, Custodian, Transfer Agency Expenses Paid During Fiscal Year Ended October 31, 2017</td>
<td>Administration, Custodian, Transfer Agency Expenses Paid During Fiscal Year Ended October 31, 2016</td>
</tr>
<tr>
<td>------------------------------------------------</td>
<td>----------------</td>
<td>---------------------------------------------------------------------------------------------------</td>
<td>---------------------------------------------------------------------------------------------------</td>
<td>---------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>11/5/2013</td>
<td>$117,307</td>
<td>$116,363</td>
<td>$104,533</td>
</tr>
<tr>
<td>FlexShares® Real Assets Allocation Index Fund</td>
<td>11/23/2015</td>
<td>$ 7,363</td>
<td>$ 3,433</td>
<td>$ 2,711</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>12/14/2012</td>
<td>$699,592</td>
<td>$666,364</td>
<td>$465,960</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>12/14/2012</td>
<td>$123,291</td>
<td>$121,963</td>
<td>$ 88,004</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>12/14/2012</td>
<td>$ 22,435</td>
<td>$ 28,442</td>
<td>$ 26,614</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
<td>4/12/2013</td>
<td>$378,122</td>
<td>$526,260</td>
<td>$271,539</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>4/12/2013</td>
<td>$ 63,787</td>
<td>$ 83,102</td>
<td>$ 55,206</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>4/12/2013</td>
<td>$ 48,157</td>
<td>$ 51,912</td>
<td>$ 24,553</td>
</tr>
<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>9/19/2011</td>
<td>$782,121</td>
<td>$811,518</td>
<td>$786,877</td>
</tr>
<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund</td>
<td>9/19/2011</td>
<td>$365,379</td>
<td>$311,614</td>
<td>$236,215</td>
</tr>
<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund</td>
<td>9/3/2014</td>
<td>$ 20,605</td>
<td>$ 13,861</td>
<td>$ 11,766</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
<td>11/12/2014</td>
<td>$ 27,419</td>
<td>$ 17,195</td>
<td>$ 9,647</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>9/23/2015</td>
<td>$ 15,918</td>
<td>$ 7,642</td>
<td>$ 7,061</td>
</tr>
<tr>
<td>FlexShares® High Yield Value-Scored Bond Index Fund</td>
<td>7/17/2018</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

**SECURITIES LENDING AGENT**

JPMorgan (the “Securities Lending Agent”) acts as Securities Lending Agent for the Funds under a Securities Lending Agreement with the Trust. The Securities Lending Agent (i) arranges and administers the loan of securities when establishing a loan and the return of securities upon termination of a loan, (ii) collects from borrowers cash, securities or other instruments to serve as collateral for the loan, (iii) monitors the value of securities on loan and the value of the corresponding collateral, (iv) communicates to each borrower the minimum amount of collateral required for each loan and collects additional collateral as required on a daily basis to maintain such minimum, (v) collects or arranges for the collection of any interest, dividends or other distributions related to loaned securities, and (vi) performs other necessary services related to the establishment and maintenance of the Trust’s securities lending program. The Securities Lending Agreement will continue indefinitely and may be terminated by either party on sixty days’ notice to the other.
The following table sets forth the income and fees/compensation related to the securities lending activities of each Fund during the fiscal year ended October 31, 2018:

<table>
<thead>
<tr>
<th>Fund</th>
<th>Gross income from securities lending activities</th>
<th>Securities lending revenue paid to securities lending agent (“Revenue Split”)</th>
<th>Rebate (paid to borrower)</th>
<th>Aggregate fees/compensation for securities lending activities</th>
<th>Net income from securities lending activities</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$2,305,940</td>
<td>$154,048</td>
<td>$1,301,378</td>
<td>$0</td>
<td>$1,004,562</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$975,541</td>
<td>$133,049</td>
<td>(191,941)</td>
<td>$0</td>
<td>$1,167,482</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$291,343</td>
<td>$31,860</td>
<td>288</td>
<td>$0</td>
<td>291,055</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$4,814,202</td>
<td>$440,468</td>
<td>$1,483,613</td>
<td>$0</td>
<td>$3,330,589</td>
</tr>
<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>$672,005</td>
<td>$41,172</td>
<td>$377,409</td>
<td>$0</td>
<td>294,596</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>$123,611</td>
<td>$9,247</td>
<td>$59,481</td>
<td>$0</td>
<td>64,130</td>
</tr>
<tr>
<td>FlexShares® Real Assets Allocation Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$2,401,786</td>
<td>$114,740</td>
<td>$1,774,665</td>
<td>$0</td>
<td>627,121</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>$329,441</td>
<td>$12,010</td>
<td>$260,550</td>
<td>$0</td>
<td>68,891</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$33,986</td>
<td>$1,030</td>
<td>$28,326</td>
<td>$0</td>
<td>5,660</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
<td>$822,100</td>
<td>$103,576</td>
<td>(75,947)</td>
<td>$0</td>
<td>898,047</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>$85,270</td>
<td>$10,685</td>
<td>(9,267)</td>
<td>$0</td>
<td>94,537</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Dynamic Index Fund</td>
<td>$62,929</td>
<td>$7,566</td>
<td>(1,769)</td>
<td>$0</td>
<td>64,698</td>
</tr>
<tr>
<td>FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® Disciplined Duration MBS Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
<tr>
<td>FlexShares® High Yield Value-Scored Bond Index Fund (1)</td>
<td>$0</td>
<td>$0</td>
<td>0</td>
<td>$0</td>
<td>0</td>
</tr>
</tbody>
</table>

(1) As of October 31, 2018, the Fund did not lend any securities.
The Funds do not pay any separate cash collateral management fees, administrative fees, fees for indemnification or other fees not reflected above for securities lending activities. Earnings from cash collateral investments are included in the Revenue Split.

DESCRIPTION OF SHARES

The Declaration of Trust of the Trust (the “Declaration”) permits the Board to cause the Trust to issue an unlimited number of full and fractional shares of beneficial interest of one or more separate series representing interests in one or more investment portfolios. The Trustees or Trust may create additional series and each series may be divided into classes.

Under the terms of the Declaration, each share of each Fund has a par value of $0.0001, and represents a proportionate interest in the particular Fund with each other share of its class in the same Fund and is entitled to such dividends and distributions out of the assets belonging to the Fund as are authorized by the Trustees and declared by the Trust. Upon any liquidation of a Fund, shareholders of each class of a Fund are entitled to share pro rata in the net assets belonging to that class available for distribution. Shares do not have any preemptive or conversion rights. The right of redemption is described under “Shareholder Information” in the Prospectus. In addition, pursuant to the terms of the 1940 Act, the right of a shareholder to redeem shares and the date of payment by a Fund may be suspended for more than seven days: (i) for any period during which the New York Stock Exchange is closed, other than the customary weekends or holidays, or trading in the markets the Fund normally utilizes is closed or is restricted as determined by the SEC; (ii) during any emergency, as determined by the SEC, as a result of which it is not reasonably practicable for the Fund to dispose of instruments owned by it or fairly to determine the value of its net assets; or (iii) for such other period as the SEC may by order permit for the protection of the shareholders of the Fund. The Trust also may suspend or postpone the recording of the transfer of its shares upon the occurrence of any of the foregoing conditions. In addition, shares of each Fund are redeemable at the unilateral option of the Trust. The Declaration permits the Board to alter the number of shares constituting a Creation Unit or to specify that shares of beneficial interest of the Trust may be individually redeemable. Shares when issued as described in the Prospectus are validly issued, fully paid and nonassessable. In the interests of economy and convenience, certificates representing shares of the Funds are not issued.

Following the creation of the initial Creation Unit Aggregation(s) of a Fund and immediately prior to the commencement of trading in such Fund’s shares, a holder of shares may be a “control person” of the Fund, as defined in the 1940 Act. A Fund cannot predict the length of time for which one or more shareholders may remain a control person of the Fund.

The proceeds received by each Fund for each issue or sale of its shares, and all net investment income, realized and unrealized gain and proceeds thereof, subject only to the rights of creditors, will be specifically allocated to and constitute the underlying assets of that Fund. The underlying assets of each Fund will be segregated on the books of account, and will be charged with the liabilities in respect to that Fund and with a share of the general liabilities of the Trust. Expenses with respect to the Funds normally are allocated in proportion to the NAV of the respective Funds except where allocations of direct expenses can otherwise be fairly made.

Each Fund and other funds of the Trust entitled to vote on a matter will vote in the aggregate and not by fund, except as required by law or when the matter to be voted on affects only the interests of shareholders of a particular fund or funds.

Rule 18f-2 under the 1940 Act provides that any matter required by the provisions of the 1940 Act or applicable state law, or otherwise, to be submitted to the holders of the outstanding voting securities of an investment company such as the Trust shall not be deemed to have been effectively acted upon unless approved by the holders of a majority of the outstanding shares of each investment portfolio affected by such matter. Rule 18f-2 further provides that an investment portfolio shall be deemed to be affected by a matter unless the interests of each investment portfolio in the matter are substantially identical or the matter does not affect any interest of the investment portfolio. Under the Rule, the approval of an investment advisory agreement, a distribution plan subject to Rule 12b-1 under the 1940 Act or any change in a fundamental investment policy would be effectively acted upon with respect to an investment portfolio only if approved by a majority of the outstanding shares of such investment portfolio. However, the Rule also provides that the ratification of the appointment of independent accountants, the approval of principal underwriting contracts and the election of Trustees are exempt from the separate voting requirements stated above.

The Trust is not required to hold annual meetings of shareholders and does not intend to hold such meetings. In the event that a meeting of shareholders is held, each share of the Trust will be entitled, as determined by the Trustees without the vote or consent of shareholders, either to one vote for each share or to one vote for each dollar of NAV represented by such shares on all matters presented to shareholders, including the election of Trustees (this method of voting being referred to as “dollar-based voting”). However, to the extent required by the 1940 Act or otherwise determined by the Trustees, series and classes of the Trust will vote separately from each other. Shareholders of the Trust do not have cumulative voting rights in the election of Trustees and, accordingly, the holders of more than 50% of the aggregate voting power of the Trust may elect all of the Trustees,
irrespective of the vote of the other shareholders. Meetings of shareholders of the Trust, or any series or class thereof, may be called by the Trustees or upon the written request of holders of at least a majority of the shares entitled to vote at such meeting. The shareholders of the Trust will have voting rights only with respect to the limited number of matters specified in the Declaration and such other matters as the Trustees may determine or may be required by law.

The Declaration authorizes the Trustees, without shareholder approval (except as stated in the next paragraph), to cause the Trust, or any series thereof, to merge or consolidate with any corporation, association, trust or other organization or sell or exchange all or substantially all of the property belonging to the Trust, or any series thereof. In addition, the Trustees, without shareholder approval, may adopt a “master-feeder” structure by investing substantially all of the assets of a series of the Trust in the securities of another open-end investment company or pooled portfolio.

The Declaration also authorizes the Trustees, in connection with the termination or other reorganization of the Trust or any series or class by way of merger, consolidation, the sale of all or substantially all of the assets, or otherwise, to classify the shareholders of any class into one or more separate groups and to provide for the different treatment of shares held by the different groups, provided that such termination or reorganization is approved by a majority of the outstanding voting securities (as defined in the 1940 Act) of each group of shareholders that are so classified.

The Declaration permits the Trustees to amend the Declaration without a shareholder vote. However, shareholders of the Trust have the right to vote on any amendment: (i) that would adversely affect the voting rights of shareholders specified in the Declaration; (ii) that is required by law to be approved by shareholders; (iii) to the amendment section of the Declaration; or (iv) that the Trustees determine to submit to shareholders.

The Declaration permits the termination of the Trust or of any series or class of the Trust: (i) by a majority of the affected shareholders at a meeting of shareholders of the Trust, series or class; or (ii) by a majority of the Trustees without shareholder approval if the Trustees determine that such action is in the best interest of the Trust or its shareholders. The factors and events that the Trustees may take into account in making such determination include: (i) the inability of the Trust or any series or class to maintain its assets at an appropriate size; (ii) changes in laws or regulations governing the Trust, or any series or class thereof, or affecting assets of the type in which it invests; or (iii) economic developments or trends having a significant adverse impact on their business or operations.

In the event of a termination of the Trust or the Fund, the Board, in its sole discretion, could determine to permit the shares to be redeemable in aggregations smaller than Creation Unit Aggregations or to be individually redeemable. In such circumstance, the Trust may make redemptions in-kind, for cash, or for a combination of cash or securities.

Under the Maryland Statutory Trust Act (the “Maryland Act”), shareholders are not personally liable for obligations of the Trust. The Maryland Act entitles shareholders of the Trust to the same limitation of liability as is available to stockholders of corporations incorporated in the State of Maryland. However, no similar statutory or other authority limiting business trust shareholder liability exists in many other states. As a result, to the extent that the Trust or a shareholder is subject to the jurisdiction of courts in such other states, those courts may not apply Maryland law and may subject the shareholders to liability. To offset this risk, the Declaration: (i) contains an express disclaimer of shareholder liability for acts or obligations of the Trust and provides that notice of such disclaimer may be given in each agreement, obligation and instrument entered into or executed by the Trust or its Trustees; and (ii) provides for indemnification out of the property of the applicable series of the Trust of any shareholder held personally liable for the obligations of the Trust solely by reason of being or having been a shareholder and not because of the shareholder’s acts or omissions or for some other reason. Thus, the risk of a shareholder incurring financial loss beyond his or her investment because of shareholder liability is limited to circumstances in which all of the following factors are present: (i) a court refuses to apply Maryland law; (ii) the liability arises under tort law or, if not, no contractual limitation of liability is in effect; and (iii) the applicable series of the Trust is unable to meet its obligations.

The Declaration provides that the Trustees will not be liable to any person other than the Trust or a shareholder and that a Trustee will not be liable for any act as a Trustee. Additionally, subject to applicable federal law, no person who is or who has been a Trustee or officer of the Trust shall be liable to the Trust or to any shareholder for money damages except for liability resulting from: (a) actual receipt of an improper benefit or profit in money, property or services; or (b) active and deliberate dishonesty established by a final judgment and which is material to the cause of action. However, nothing in the Declaration protects a Trustee against any liability to which he or she would otherwise be subject by reason of willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of his or her office. The Declaration requires indemnification of Trustees and officers of the Trust unless the recipient is liable by reason of willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of such person’s office.
The Declaration provides that each shareholder, by virtue of becoming such, will be held to have expressly assented and agreed to the terms of the Declaration and the Bylaws of the Trust.

The Declaration provides that a shareholder of the Trust may bring a derivative action on behalf of the Trust only if the following conditions are met: (i) shareholders who hold at least 10% of the outstanding shares of the Trust, or 10% of the outstanding shares of the series or class to which such action relates, must join in the request for the Trustees to commence such action; and (ii) the Trustees must be afforded a reasonable amount of time to consider such shareholder request and to investigate the basis of such claim. The Declaration also provides that no person, other than the Trustees, who is not a shareholder of a particular series or class shall be entitled to bring any derivative action, suit or other proceeding on behalf of or with respect to such series or class. The Trustees will be entitled to retain counsel or other advisers in considering the merits of the request and may require an undertaking by the shareholders making such request to reimburse the Trust for the expense of any such advisers in the event that the Trustees determine not to bring such action.

The Trustees may appoint separate Trustees with respect to one or more series or classes of the Trust’s shares (the “Series Trustees”). To the extent provided by the Trustees in the appointment of Series Trustees, Series Trustees: (i) may, but are not required to, serve as Trustees of the Trust or any other series or class of the Trust; (ii) may have, to the exclusion of any other Trustee of the Trust, all the powers and authorities of Trustees under the Declaration with respect to such series or class; and/or (iii) may have no power or authority with respect to any other series or class.

The term “majority of the outstanding shares” of either the Trust or a particular Fund or another investment portfolio of the Trust means, with respect to the approval of an investment advisory agreement, a distribution plan or a change in a fundamental investment policy, the vote of the lesser of: (i) 67% or more of the shares of the Trust or such Fund or portfolio present at a meeting, if the holders of more than 50% of the outstanding shares of the Trust or such Fund or portfolio are present or represented by proxy; or (ii) more than 50% of the outstanding shares of the Trust or such Fund or portfolio.

Absent an applicable exemption or other relief from the SEC or its staff, beneficial owners of more than 5% of the shares of a Fund may be subject to the reporting provisions of Section 13 of the 1934 Act and the SEC’s rules promulgated thereunder. In addition, absent an applicable exemption or other relief from the SEC staff, Officers and Trustees of a Fund and beneficial owners of 10% of the shares of a Fund (“Insiders”) may be subject to the insider reporting, short-swng profit and short sale provisions of Section 16 of the 1934 Act and the SEC’s rules promulgated thereunder. Beneficial owners and Insiders should consult with their own legal counsel concerning their obligations under Sections 13 and 16 of the 1934 Act.

On September 24, 2015, the Board adopted an amendment to the Trust’s By-Laws to establish the state and federal courts sitting in the State of Maryland as the sole and exclusive forums for any shareholder (including a beneficial owner) to bring (i) any action or proceeding brought on behalf of the Trust, (ii) any action asserting a claim or breach of a fiduciary duty owed by any Trustee, officer or employee, if any, of the Trust to the Trust or the Trust’s shareholders, (iii) any action asserting a claim against the Trust, its Trustees, officers or employees, if any, arising pursuant to any provision of the Maryland Statutory Trust Act or the Trust’s Trust Instrument or bylaw; or (iv) any action asserting a claim against the Trust, its Trustees, officers or employees, if any, governed by the internal affairs doctrine.

BOOK-ENTRY ONLY SYSTEM

The following information supplements and should be read in conjunction with the Shareholder Information section in the Prospectus.

The Depository Trust Company (“DTC”) acts as Securities Depository for the Shares of the Trust. Shares of each Fund are represented by securities registered in the name of DTC or its nominee and deposited with, or on behalf of, DTC.

DTC, a limited-purpose trust company, was created to hold securities of its participants (the “DTC Participants”) and to facilitate the clearance and settlement of securities transactions among the DTC Participants in such securities through electronic book-entry changes in accounts of the DTC Participants, thereby eliminating the need for physical movement of securities certificates. DTC Participants include securities brokers and dealers, banks, trust companies, clearing corporations and certain other organizations, some of whom (and/or their representatives) own DTC. More specifically, DTC is a subsidiary of the Depository Trust and Clearing Corporation (“DTCC”), which is owned by its member firms including international broker/dealers, correspondent and clearing banks, mutual fund companies and investment banks. Access to the DTC system is also available to others such as banks, brokers, dealers and Trust companies that clear through or maintain a custodial relationship with a DTC Participant, either directly or indirectly (the “Indirect Participants”).

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Beneficial ownership of shares is limited to DTC Participants, Indirect Participants and persons holding interests through DTC Participants and Indirect Participants. Ownership of beneficial interests in Fund shares (owners of such beneficial interests are referred to herein as “Beneficial Owners”) is shown on, and the transfer of ownership is effected only through, records maintained by DTC (with respect to DTC Participants) and on the records of DTC Participants (with respect to Indirect Participants and Beneficial Owners that are not DTC Participants). Beneficial Owners will receive from or through the DTC Participant a written confirmation relating to their purchase of shares. The laws of some jurisdictions may require that certain purchasers of securities take physical delivery of such securities in definitive form. Such laws may impair the ability of certain investors to acquire beneficial interests in shares.

Beneficial Owners of shares are not entitled to have shares registered in their names, will not receive or be entitled to receive physical delivery of certificates in definitive form and are not considered the registered holder thereof. Accordingly, each Beneficial Owner must rely on the procedures of DTC, the DTC Participant and any Indirect Participant through which such Beneficial Owner holds its interests, to exercise any rights of a holder of shares. The Trust understands that under existing industry practice, in the event the Trust requests any action of holders of shares, or a Beneficial Owner desires to take any action that DTC, as the record owner of all outstanding shares, is entitled to take, DTC would authorize the DTC Participants to take such action and that the DTC Participants would authorize the Indirect Participants and Beneficial Owners acting through such DTC Participants to take such action and would otherwise act upon the instructions of Beneficial Owners owning through them. As described above, the Trust recognizes DTC or its nominee as the owner of all shares for all purposes.

Conveyance of all notices, statements and other communications to Beneficial Owners is effected as follows. Pursuant to the Depositary Agreement between the Trust and DTC, DTC is required to make available to the Trust upon request and for a fee to be charged to the Trust a listing of the share holdings of each DTC Participant. The Trust shall inquire of each such DTC Participant as to the number of Beneficial Owners holding shares of the Funds, directly or indirectly, through such DTC Participant. The Trust shall provide each such DTC Participant with copies of such notice, statement or other communication, in such form, number and at such place as such DTC Participant may reasonably request, in order that such notice, statement or communication may be transmitted by such DTC Participant, directly or indirectly, to such Beneficial Owners. In addition, the Trust shall pay to each such DTC Participant a fair and reasonable amount as reimbursement for the expenses attendant to such transmittal, all subject to applicable statutory and regulatory requirements.

Share distributions shall be made to DTC or its nominee, Cede & Co., as the registered holder of all shares of the Trust. DTC or its nominee, upon receipt of any such distributions, shall credit immediately DTC Participants’ accounts with payments in amounts proportionate to their respective beneficial interests in shares as shown on the records of DTC or its nominee. Payments by DTC Participants to Indirect Participants and Beneficial Owners of shares held through such DTC Participants will be governed by standing instructions and customary practices, as is now the case with securities held for the accounts of customers in bearer form or registered in a “street name,” and will be the responsibility of such DTC Participants. The Trust has no responsibility or liability for any aspects of the records relating to or notices to Beneficial Owners, or payments made on account of beneficial ownership interests in such shares, or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests or for any other aspect of the relationship between DTC and the DTC Participants or the relationship between such DTC Participants and the Indirect Participants and Beneficial Owners owning through such DTC Participants.

DTC may determine to discontinue providing its service with respect to shares of the Trust at any time by giving reasonable notice to the Trust and discharging its responsibilities with respect thereto under applicable law. Under such circumstances, the Trust shall take action either to find a replacement for DTC to perform its functions at a comparable cost or, if such a replacement is unavailable, to issue and deliver printed certificates representing ownership of shares, unless the Trust makes other arrangements with respect thereto satisfactory to the Listing Exchange on which shares are listed.

PURCHASE AND REDEMPTION OF CREATION UNIT AGGREGATIONS

CREATION UNIT AGGREGATIONS

The Trust issues and sells shares of each Fund only in Creation Unit Aggregations. The Board reserves the right to declare a split or a consolidation in the number of shares outstanding of any Fund of the Trust, and to make a corresponding change in the number of shares constituting a Creation Unit, in the event that the per share price in the secondary market rises (or declines) to an amount that falls outside the range deemed desirable by the Board.
PURCHASE AND ISSUANCE OF CREATION UNIT AGGREGATIONS

General. The Trust issues and sells shares of each Fund only in Creation Units on a continuous basis through the Distributor, without a sales load, at the Fund’s NAV next determined after receipt, on any Business Day (as defined herein), of an order in proper form. A “Business Day” with respect to each Fund is any day on which the Listing Exchange is open for business. As of the date of this SAI, each Listing Exchange observes the following holidays, as observed: New Year’s Day, Martin Luther King, Jr. Day, Presidents’ Day, Good Friday, Memorial Day, Independence Day, Labor Day, Thanksgiving Day and Christmas Day.

Portfolio Deposit. Unless cash purchases are specified for a Fund, the consideration for purchase of a Creation Unit of shares of a Fund generally consists of the in-kind deposit of a designated portfolio of securities and other instruments (the “Deposit Securities”) generally corresponding pro rata (except in certain circumstances) to the Fund’s portfolio positions and an amount of cash computed as described below (the “Cash Component”). Together, the Deposit Securities and the Cash Component constitute the “Portfolio Deposit,” which represents the minimum initial and subsequent investment amount for shares of a Fund. The Cash Component is an amount equal to the difference between (x) the NAV (per Creation Unit) of the Fund and (y) the “Deposit Amount”, which is the market value (per Creation Unit) of the securities deposited with the Trust. The Balancing Amount serves the function of compensating for any differences between the NAV per Creation Unit and the Deposit Amount. If the Balancing Amount is a positive number (i.e., the net asset value per Creation Unit is more than the Deposit Amount), the Authorized Participant will deliver the Balancing Amount. If the Balancing Amount is a negative number (i.e., the NAV per Creation Unit is less than the Deposit Amount), the Authorized Participant will receive the Balancing Amount. Payment of any stamp duty or other similar fees and expenses payable upon transfer of beneficial ownership of the Deposit Securities shall be the sole responsibility of the Authorized Participant that purchased the Creation Unit. The Authorized Participant must ensure that all Deposit Securities properly denote change in beneficial ownership.

NTI makes available through the National Securities Clearing Corporation (“NSCC”) on each Business Day, prior to the opening of business on the Listing Exchange (currently 9:30 a.m., Eastern time), the list of the names and the required quantity of each Deposit Security to be included in the current Portfolio Deposit (based on information at the end of the previous Business Day) for each Fund. Such Portfolio Deposit is applicable, subject to any adjustments as described below, in order to effect purchases of Creation Units of a given Fund until such time as the next-announced Portfolio Deposit composition is made available.

The identity and number of shares of the Deposit Securities required for a Portfolio Deposit for each Fund changes as rebalancing adjustments and corporate action events are reflected from time to time by NTI with a view to the investment objective of the Fund. The composition of the Deposit Securities may also change in response to adjustments to the weighting or composition of the securities constituting the relevant Underlying Index. The adjustments will reflect changes, known to NTI on the date of announcement to be in effect by the time of delivery of the Portfolio Deposit, in the composition of the relevant Fund’s Underlying Index, or resulting from stock splits and other corporate actions.

In addition, the Trust reserves the right to permit or require the substitution of an amount of cash (that is a “cash in lieu” amount) to be added to the Cash Component to replace any Deposit Security which may not be available in sufficient quantity for delivery or that may not be eligible for transfer through the systems of DTC, the Clearing Process (discussed below), the Federal Reserve System for U.S. Treasury Securities (discussed below) or for other similar reasons. The Trust also reserves the right to permit or require a “cash in lieu” amount where the delivery of Deposit Securities by the Authorized Participant (as described below) would be restricted under the securities laws or where delivery of Deposit Securities to the Authorized Participant would result in the disposition of Deposit Securities by the Authorized Participant becoming restricted under the securities laws, and in certain other situations.

On a given Business Day, the Trust may require all Authorized Participants purchasing Creation Units on that day to deposit an amount of cash (that is a “cash in lieu” amount) to replace any Deposit Security that may not be eligible for transfer through the systems of DTC or the Clearing Process (discussed below) or, in the case of a non-U.S. Deposit Security, the security or instrument is not eligible for trading due to local trading restrictions, local restrictions on securities transfers or other similar circumstances. The Trust also reserves the right to permit a “cash in lieu” to replace any Deposit Security which may not be available in sufficient quantity or which may not be eligible for trading by an Authorized Participant or the investor on whose behalf the Authorized Participant is acting. The Trust may in its discretion require an Authorized Participant to purchase Creation Units of a Fund in cash, rather than in-kind. On a given Business Day, the Trust may announce before the open of trading that all purchases of Creation Units of a Fund on that day will be made entirely in cash or, upon receiving a purchase order for Creation Units of a Fund from an Authorized Participant, the Trust may determine to require that purchase to be made entirely in cash.
In addition to the list of names and numbers of securities constituting the current Deposit Securities of a Portfolio Deposit, on each Business Day, the Cash Component effective through and including the previous Business Day, per outstanding Creation Unit of each Fund, will be made available.

**Procedures For Creation of Creation Units.** To be eligible to place orders with the Distributor and to create a Creation Unit of a Fund, an entity must be: (i) a “Participating Party,” i.e., a broker-dealer or other participant in the clearing process through the Continuous Net Settlement System of the NSCC (the “Clearing Process”), a clearing agency that is registered with the SEC; or (ii) a DTC Participant, and must have executed an agreement with the Distributor, with respect to creations and redemptions of Creation Units (“Participant Agreement”) (discussed below). A Participating Party or DTC Participant who has executed a Participant Agreement is referred to as an “Authorized Participant.” Investors should contact the Distributor for the names of Authorized Participants. All shares of a Fund, however created, will be entered on the records of DTC in the name of Cede & Co. for the account of a DTC Participant.

Except as described below, all creation orders must be placed for one or more Creation Units and, whether through a Participating Party or a DTC Participant, must be received by the Distributor in proper form no later than the closing time of the regular trading session of the Listing Exchange (normally 4:00 p.m., Eastern time), and with respect to the FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and the FlexShares® High Yield Value-Scored Bond Index Fund, no later than 2:00 p.m., Eastern time (“Closing Time”) on any Business Day in order for creation of Creation Units to be effected based on the NAV of shares of a Fund as next determined on such date. The FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund and FlexShares® International Quality Dividend Dynamic Index Fund are hereinafter referred to as the “Foreign Funds.” All other Funds discussed in this SAI are hereinafter referred to as “Domestic Funds.” The date on which an order to create Creation Units (or an order to redeem Creation Units, as discussed below) is timely received in proper form is referred to as the “Transmittal Date.” Orders must be transmitted by an Authorized Participant by telephone or other transmission method acceptable to the Distributor pursuant to procedures set forth in the Participant Agreement, as described below. Economic or market disruptions or changes, or telephone or other communication failure, may impede the ability to reach the Distributor or an Authorized Participant.

All orders to create Creation Units shall be placed with an Authorized Participant in the form required by such Authorized Participant. In addition, an Authorized Participant may request that an investor make certain representations or enter into agreements with respect to an order (e.g., to provide for payments of cash). Investors should be aware that their particular broker may not have executed a Participant Agreement and, therefore, orders to create Creation Units of a Fund will have to be placed by the investor’s broker through an Authorized Participant. In such cases, there may be additional charges to such investor. A limited number of broker-dealers have executed a Participant Agreement and only a small number of such Authorized Participants have international capabilities. Investors placing orders for Creation Units of Domestic Funds through the Clearing Process should afford sufficient time to permit proper submission of the order to the Distributor prior to the Closing Time on the Transmittal Date. Orders for Creation Units of Domestic Funds that are effected outside the Clearing Process are likely to require transmission by the DTC Participant earlier on the Transmittal Date than orders effected using the Clearing Process. Those persons placing orders outside the Clearing Process should ascertain the deadlines applicable to DTC and the Federal Reserve Bank wire system by contacting the operations department of the broker or depository institution effectuating such transfer of Deposit Securities and Cash Component.

Investors placing orders for Creation Units of the Domestic Funds should ascertain the applicable deadline for cash transfers by contacting the operations department of the broker or depository institution making the transfer of the Cash Component. This deadline is likely to be significantly earlier than the closing time of the regular trading session on the applicable Listing Exchange. Investors should be aware that the Authorized Participant may require orders for Creation Units placed with it to be in the form required by the individual Authorized Participant, which form may not be the same as the form of purchase order specified by the Trust that the Authorized Participant must deliver to the Distributor.

Investors placing orders for Creation Units of a Foreign Fund should ascertain the applicable deadline for cash transfers by contacting the operations department of the broker or depository institution making the transfer of the Cash Component. This deadline is likely to be significantly earlier than the closing time of the regular trading session on the applicable Listing Exchange. Investors should be aware that the Authorized Participant may require orders for Creation Units placed with it to be in the form required by the individual Authorized Participant, which form may not be the same as the form of purchase order specified by the Trust that the Authorized Participant must deliver to the Distributor.
Placement of Creation Orders For Domestic Funds Using The Clearing Process. The Clearing Process is the process of creating or redeeming Creation Units. Fund Deposits made through the Clearing Process must be delivered through a Participating Party that has executed a Participant Agreement. The Participant Agreement authorizes the Distributor to transmit through the Transfer Agent (also known as the Index Receipt Agent) to NSCC, on behalf of the Participating Party, such trade instructions as are necessary to effect the Participating Party’s creation order. Pursuant to such trade instructions to NSCC, the Participating Party agrees to deliver the requisite Deposit Securities and the Cash Component to the Trust, together with such additional information as may be required by the Distributor. An order to create Creation Units through the Clearing Process is deemed received by the Distributor on the Transmittal Date if: (i) such order is received by the Distributor not later than the Closing Time on such Transmittal Date; and (ii) all other procedures set forth in the Participant Agreement are properly followed.

Placement of Creation Orders For Domestic Funds Outside The Clearing Process. Fund Deposits made outside the Clearing Process must be delivered through a DTC Participant that has executed a Participant Agreement. A DTC Participant who wishes to place an order creating Creation Units to be effected outside the Clearing Process does not need to be a Participating Party, but such orders must state that the DTC Participant is not using the Clearing Process and that the creation of Creation Units will instead be effected through the transfer of securities (other than U.S. government securities) directly through DTC, or through a transfer of U.S. government securities and cash directly through the Federal Reserve System. The Fund Deposit transfer must be ordered by the DTC Participant on the Transmittal Date in a timely fashion so as to ensure the delivery of the requisite number of Deposit Securities through DTC to the account of the Fund by no later than 2:00 p.m., Eastern time, on the “Settlement Date.” The Settlement Date is typically the second Business Day following the Transmittal Date, except that the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund will generally settle transactions on a T+1 basis. In certain cases Authorized Participants will create and redeem Creation Units of the same Fund on the same trade date. In these instances, the Trust reserves the right to settle these transactions on a net basis. All questions as to the number of Deposit Securities to be delivered, and the validity, form and eligibility (including time of receipt) for the deposit of any tendered securities, will be determined by the Trust, whose determination shall be final and binding.

The amount of cash equal to the Cash Component must be transferred directly to the Custodian through the Federal Reserve Bank wire transfer system in a timely manner so as to be received by the Custodian no later than 2:00 p.m., Eastern time, on the Settlement Date. An order to create Creation Units outside the Clearing Process is deemed received by the Distributor on the Transmittal Date if: (i) such order is received by the Distributor not later than the Closing Time on such Transmittal Date; and (ii) all other procedures set forth in the Participant Agreement are properly followed. However, if the Custodian does not receive both the required Deposit Securities and the Cash Component by 2:00 p.m., Eastern time on the Settlement Date, such order may be canceled. Upon written notice to the Distributor, such canceled order may be resubmitted the following Business Day using a Fund Deposit as newly constituted to reflect the then current NAV of the Fund. The delivery of Creation Units so created generally will occur no later than the Settlement Date. Creation Units of Domestic Funds may be created in advance of receipt by the Trust of all or a portion of the applicable Deposit Securities as described below. In these circumstances, the initial deposit will have a value greater than the NAV of the shares on the date the order is placed in proper form since, in addition to available Deposit Securities, cash must be deposited in an amount equal to the sum of: (i) the Cash Component; plus (ii) at least 110%, which NTI may change from time to time, of the market value of the undelivered Deposit Securities (the “Additional Cash Deposit”) with the Fund pending delivery of any missing Deposit Securities.

If an Authorized Participant determines to post an additional cash deposit as collateral for any undelivered Deposit Securities, such Authorized Participant must deposit with the Custodian the appropriate amount of federal funds by 2:00 p.m., Eastern time, on the date of requested settlement. If the Authorized Participant does not place its purchase order by the closing time or the Custodian does not receive federal funds in the appropriate amount by such time, then the order may be deemed to be rejected and the Authorized Participant shall be liable to the Fund for any resulting losses. An additional amount of cash shall be required to be deposited with the Custodian, pending delivery of the missing Deposit Securities to the extent necessary to maintain the Additional Cash Deposit with the Trust in an amount at least equal to 110%, which NTI may change from time to time, of the daily marked to market value of the missing Deposit Securities. To the extent that missing Deposit Securities are not received by 2:00 p.m., Eastern time, on the Settlement Date or in the event a marked-to-market payment is not made within one Business Day following notification by the Distributor that such a payment is required, the Trust may use the cash on deposit to purchase the missing Deposit Securities. Authorized Participants will be liable to the Trust for the costs incurred by the Trust in connection with any such purchases. These costs will be deemed to include the amount by which the actual purchase price of the Deposit Securities exceeds the market value of such Deposit Securities on the transmittal date plus the brokerage and related transaction
costs associated with such purchases. The Trust will return any unused portion of the Additional Cash Deposit once all of the missing Deposit Securities have been properly received by the Custodian or purchased by the Trust and deposited into the Trust. In addition, a transaction fee, as listed below, will be charged. The delivery of Creation Units so created generally will occur no later than the Settlement Date.

**Placement of Creation Orders For Foreign Funds.** For the Foreign Funds, NTI shall cause the sub-custodians of the Fund to maintain an account into which the Authorized Participant shall deliver, on behalf of itself or the party on whose behalf it is acting, the securities included in the designated Portfolio Deposit (or the cash value of all or part of such securities, in the case of a permitted or required cash purchase or “cash in lieu” amount), with any appropriate adjustments as advised by the Trust. Deposit Securities must be delivered to an account maintained at the applicable local sub-custodian(s). Orders to purchase Creation Unit Aggregations must be received by the Distributor from an Authorized Participant on its own or the applicable Listing Exchange on the relevant Business Day. However, when a relevant local market is closed due to local market holidays, the local market settlement process will not commence until the end of the local holiday period. Settlement must occur by 2:00 p.m., Eastern time, on the contractual settlement date.

The Authorized Participant must also make available on or before the contractual settlement date, by means satisfactory to the Trust, immediately available or same day funds estimated by the Trust to be sufficient to pay the Cash Component next determined after acceptance of the purchase order, together with the applicable purchase transaction fee. Any excess funds will be returned following settlement of the issue of the Creation Unit.

**Acceptance of Purchase Order.** Subject to the conditions that: (i) an irrevocable purchase order has been submitted by the Authorized Participant (either on its own or another investor’s behalf); and (ii) arrangements satisfactory to the Trust are in place for payment of the Cash Component and any other cash amounts which may be due, the Trust will accept the order, subject to its right (and the right of the Distributor and NTI) to reject any order until acceptance.

Once the Trust has accepted an order, upon next determination of the NAV of the shares, the Trust will confirm the issuance of a Creation Unit of the Fund, against receipt of payment, at such NAV. The Distributor will then transmit a confirmation of acceptance to the Authorized Participant that placed the order.

The Trust reserves the absolute right to reject or revoke acceptance of a purchase order transmitted to it by the Distributor in respect of any Fund if: (a) the purchase order is not in proper form; (b) the purchaser or group of purchasers, upon obtaining the shares ordered, would own 80% or more of the currently outstanding shares of any Fund; (c) the Deposit Securities delivered are not as specified by NTI as described above; (d) acceptance of the Deposit Securities would have certain adverse tax consequences to the Fund; (e) the acceptance of the Portfolio Deposit would, in the opinion of counsel, be unlawful; (f) the acceptance of the Portfolio Deposit would otherwise, in the discretion of the Trust or NTI, have an adverse effect on the Trust or the rights of beneficial owners; or (g) in the event that circumstances outside the control of the Trust, the Distributor, Transfer Agent, Custodian, a sub-custodian or NTI make it for all practical purposes impossible to process purchase orders. Examples of such circumstances include acts of God; public service or utility problems; fires, floods or extreme weather conditions; power outages resulting in telephone, telecopy or computer failures; market conditions or activities causing trading halts; systems failures involving computer or other informational systems affecting the Trust, the Distributor, DTC, NSCC, NTI, Transfer Agent, Custodian, a sub-custodian or any other participant in the creation process; and similar extraordinary events. The Distributor shall notify a prospective creator of a Creation Unit and/or Authorized Participant acting on behalf of such creator of its rejection of the purchase order. The Trust, Transfer Agent, Custodian, any sub-custodian and the Distributor are under no duty, however, to give notification of any defects or irregularities in the delivery of Portfolio Deposits nor shall either of them incur any liability for the failure to give any such notification. The Trust reserves the right, in its sole discretion, to suspend the offering of Shares of a Fund or to reject purchase orders when, in its judgment, such suspension or rejection would be in the best interests of the Trust or the Fund.

**Issuance of a Creation Unit.** Except as provided herein, a Creation Unit of shares of a Fund will not be issued until the transfer of good title to the Trust of the Deposit Securities and the payment of the Cash Component, or transfer of cash, as applicable, have been completed. With respect to any non-U.S. Deposit Securities, when the applicable local sub-custodian(s) have confirmed to the Custodian that the required securities included in the Portfolio Deposit (or the cash value thereof) have been delivered to the account of the applicable local sub-custodian or sub-custodians, the Distributor and the Investment Adviser shall be notified of such delivery, and the Trust will issue, and cause the delivery of the Creation Unit. Creation Units typically are issued on a T+2 basis (two Business Days after trade date) except the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund will generally settle on a T+1 basis (one Business Day after trade date).
However, as discussed in Appendix A, each Fund reserves the right to settle Creation Unit transactions on a basis other than T+2 (T+1 basis for the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund) in order to accommodate foreign market holiday schedules, to account for different treatment among foreign and U.S. markets of dividend record dates or ex-dividend dates (the last day the holder of a security can sell the security and still receive dividends payable on the security), and in certain other circumstances.

To the extent contemplated by an Authorized Participant’s agreement with the Distributor, the Trust will issue Creation Units to such Authorized Participant notwithstanding the fact that the corresponding Portfolio Deposits have not been received in part or in whole, in reliance on the undertaking of the Authorized Participant to deliver the missing Deposit Securities as soon as possible, which undertaking shall be secured by such Authorized Participant’s delivery and maintenance of collateral having a value at least equal to 110%, which NTI may change from time to time, of the value of the missing Deposit Securities. Such cash collateral must be delivered no later than 2:00 p.m., Eastern time, on the contractual settlement date. The only collateral that is acceptable to the Trust is cash in U.S. Dollars. The cash collateral posted by the Authorized Participant may be invested at the risk of the Authorized Participant, and income, if any, on invested cash collateral will be paid to that Authorized Participant. Information concerning the Trust’s current procedures for collateralization of missing Deposit Securities is available from the Distributor. The Participant Agreement will permit the Trust to buy the missing Deposit Securities at any time and will subject the Authorized Participant to liability for any shortfall between the cost to the Trust of purchasing such securities and the cash collateral.

In certain cases, Authorized Participants will create and redeem Creation Units on the same trade date. In these instances, the Trust reserves the right to settle these transactions on a net basis. All questions as to the number of shares of each security in the Deposit Securities and the validity, form, eligibility and acceptance for deposit of any securities to be delivered shall be determined by the Trust, and the Trust’s determination shall be final and binding.

**Cash Purchase Method.** When cash purchases of Creation Units are available or specified for a Fund, they will be effected in essentially the same manner as in-kind purchases thereof. For the cash purchase portion, the investor must pay the cash equivalent of the designated subset of Deposit Securities it would otherwise be required to provide through an in-kind purchase, plus the same Cash Component required to be paid by an in-kind purchaser. In addition, to offset the Trust’s brokerage and other transaction costs associated with using the cash to purchase the requisite Deposit Securities, the investor may be required to pay a fixed purchase transaction fee, plus an additional variable charge for cash purchases, which is expressed as a percentage of the value of the Deposit Securities. The transaction fees for in-kind and cash purchases of Creation Units are described below.

**Purchase Transaction Fee.** Purchasers of Creation Units are responsible for the costs of transferring the securities constituting the Deposit Securities to the account of the Trust. Investors who use the services of a broker, or other such intermediary, may be charged a fee for such services. A fixed purchase transaction fee payable to the Trust is imposed to compensate the Trust for the transfer and other transaction costs of a Fund associated with the issuance of Creation Units. The standard purchase transaction fee will be the same regardless of the number of Creation Units purchased by the purchaser on the same day. The Authorized Participant may also be required to pay an additional variable charge to compensate the Fund for certain brokerage, tax, foreign exchange, execution, market impact and other costs and expenses related to the execution of trades resulting from cash purchases of Creation Units (up to the maximum amount shown below). Where the Trust permits an in-kind purchaser to substitute cash in lieu of depositing a portion of the Deposit Securities, the purchaser also will be assessed an additional variable transaction charge (up to the maximum amount shown below). To the extent the Fund cannot recoup the amount of transaction costs incurred in connection with a purchase, those transaction costs will be borne by the Fund’s shareholders and negatively affect the Fund’s performance. The purchase transaction fees for in-kind purchases and cash purchases (when available) are listed in the table below. This table is subject to revision from time to time.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>Fee for In-Kind and Cash Purchases</th>
<th>Maximum Additional Variable Charge for Cash Purchase*</th>
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<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
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<td>3.00%</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
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<td>3.00%</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$25,000</td>
<td>3.00%</td>
</tr>
<tr>
<td>NAME OF FUND</td>
<td>Fee for In-Kind and Cash Purchases</td>
<td>Maximum Additional Variable Charge for Cash Purchase*</td>
</tr>
<tr>
<td>----------------------------------------------------------------------------</td>
<td>-----------------------------------</td>
<td>-----------------------------------------------------</td>
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<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
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<tr>
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<tr>
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<td>FlexShares® Quality Dividend Index Fund</td>
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<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
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<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
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<tr>
<td>FlexShares® High Yield Value-Scored Bond Index Fund</td>
<td>$ 500</td>
<td>3.00%</td>
</tr>
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* As a percentage of the net asset value per Creation Unit.

**Redemption of Creation Units.** Shares of a Fund may be redeemed only in Creation Units at their NAV next determined after receipt of a redemption request in proper form by the Fund through the Distributor and only on a Business Day. The Trust will not redeem shares in amounts less than Creation Units. Beneficial owners also may sell shares in the secondary market, but must accumulate enough Fund shares to constitute a Creation Unit in order to have such shares redeemed by the Trust. There can be no assurance, however, that there will be sufficient liquidity in the public trading market at any time to permit assembly of a Creation Unit. Investors should expect to incur brokerage and other costs in connection with assembling a sufficient number of shares to constitute a redeemable Creation Unit.

With respect to each Fund, NTI makes available through the NSCC prior to the opening of business on the Listing Exchange (currently 9:30 a.m., Eastern time) on each Business Day, the portfolio securities that will be applicable (subject to possible amendment or correction) to redemption requests received in proper form (as defined below) on that day (“Fund Securities”). Fund Securities received on redemption may not be identical to Deposit Securities that are applicable to creations of Creation Units. Unless cash redemptions are available or specified for a Fund, the redemption proceeds for a Creation Unit generally consist of Fund Securities as announced by NTI through the NSCC on the Business Day of the request for redemption,
plus cash in an amount equal to the difference between the NAV of the shares being redeemed, as next determined after a receipt of a request in proper form, and the value of the Fund Securities, less the redemption transaction fee described below (“Cash Redemption Amount”). The redemption transaction fee described below is deducted from such redemption proceeds. In the event that the Fund Securities have a value greater than the NAV of the Fund shares, a compensating cash payment equal to such difference is required to be made by or through an Authorized Participant by the redeeming shareholder. On a given Business Day, the Trust may require all Authorized Participants redeeming Creation Units on that day to receive an amount of cash (that is a “cash in lieu” amount) to replace any Fund Security that may not be eligible for transfer through the systems of DTC or the Clearing Process (discussed above) or, in the case of a non-U.S. Fund Security, the security or instrument is not eligible for trading due to local trading restrictions, local restrictions on securities transfers or other similar circumstances. The Trust also reserves the right to permit a “cash in lieu” to replace any Fund Security which may not be eligible for trading by an Authorized Participant or the investor on whose behalf the Authorized Participant is acting or if a shareholder would be subject to unfavorable income tax treatment if the shareholder received redemption proceeds in-kind. On a given Business Day, the Trust may announce before the open of trading that all redemptions of Creation Units of a Fund on that day will be made entirely in cash or, upon receiving a redemption order for Creation Units of the Fund from an Authorized Participant, the Trust may determine to require that redemption to be made entirely in cash.

When cash redemptions of Creation Units are specified for a Fund, they will be effected in essentially the same manner as in-kind redemptions thereof. The investor will receive the cash equivalent of the designated Fund Securities it would otherwise have received through an in-kind redemption, plus the same Cash Redemption Amount required to be paid to an in-kind redeemer. In addition, to offset the Trust’s brokerage and other transaction costs associated with a cash redemption, the investor will be required to pay a fixed redemption transaction fee, plus an additional variable charge for cash redemptions, which is expressed as a percentage of the value per Creation Unit. The transaction fees for in-kind and cash redemptions of Creation Units are described below.

Investors will bear the costs of transferring the Fund Securities from the Trust to their account on their order. Investors who use the services of a broker or other such intermediary may be charged a fee for such services. A fixed redemption transaction fee payable to the Trust also is imposed to offset transfer and other transaction costs that may be incurred by the relevant Fund. The standard redemption transaction fee will be the same regardless of the number of Creation Units redeemed by an investor on the same day. The Authorized Participant may also be required to pay a variable transaction fee to compensate the relevant Fund for certain brokerage, tax, foreign exchange, execution, market impact and other costs and expenses related to the execution of trades resulting from cash redemptions of Creation Units (up to the maximum amount shown below). Where the Trust requires or permits an in-kind redeemer to substitute cash in lieu of receiving a portion of the Deposit Securities, the redeemer also will be assessed an additional variable transaction charge (up to the maximum amount shown below). To the extent the Fund cannot recoup the amount of transaction costs incurred in connection with a redemption, those transaction costs will be borne by the Fund’s remaining shareholders and negatively affect the Fund’s performance. The redemption transaction fee for redemptions in-kind and for cash and the additional variable charge for cash redemptions (when cash redemptions are available or specified) are listed in the table below.

<table>
<thead>
<tr>
<th>NAME OF FUND</th>
<th>Fee for In-Kind and Cash Redemptions</th>
<th>Maximum Additional Variable Charge for Cash Redemption*</th>
</tr>
</thead>
<tbody>
<tr>
<td>FlexShares® Morningstar US Market Factor Tilt Index Fund</td>
<td>$ 1,500</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund</td>
<td>$20,000</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund</td>
<td>$25,000</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund</td>
<td>$ 0</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</td>
<td>$ 0</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® US Quality Large Cap Index Fund</td>
<td>$ 500</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® STOXX® US ESG Impact Index Fund</td>
<td>$ 350</td>
<td>2.00%</td>
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<tr>
<td>FlexShares® STOXX® Global ESG Impact Index Fund</td>
<td>$ 7,500</td>
<td>2.00%</td>
</tr>
<tr>
<td>NAME OF FUND</td>
<td>Fee for In-Kind and Cash Redemptions</td>
<td>Maximum Additional Variable Charge for Cash Redemption*</td>
</tr>
<tr>
<td>--------------</td>
<td>-------------------------------------</td>
<td>--------------------------------------------------------</td>
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<tr>
<td>FlexShares® Morningstar Global Upstream Natural Resources Index Fund</td>
<td>$ 1,500</td>
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<tr>
<td>FlexShares® STOXX® Global Broad Infrastructure Index Fund</td>
<td>$ 2,000</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® Global Quality Real Estate Index Fund</td>
<td>$ 2,000</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® Real Assets Allocation Index Fund</td>
<td>$ 0</td>
<td>2.00%</td>
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<tr>
<td>FlexShares® Quality Dividend Index Fund</td>
<td>$ 750</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® Quality Dividend Defensive Index Fund</td>
<td>$ 750</td>
<td>2.00%</td>
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<tr>
<td>FlexShares® Quality Dividend Dynamic Index Fund</td>
<td>$ 750</td>
<td>2.00%</td>
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<tr>
<td>FlexShares® International Quality Dividend Index Fund</td>
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<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® International Quality Dividend Defensive Index Fund</td>
<td>$ 5,000</td>
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<tr>
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<tr>
<td>FlexShares® Credit-Scored US Corporate Bond Index Fund</td>
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<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® Credit-Scored US Long Corporate Bond Index Fund</td>
<td>$ 500</td>
<td>2.00%</td>
</tr>
<tr>
<td>FlexShares® High Yield Value-Scored Bond Index Fund</td>
<td>$ 500</td>
<td>2.00%</td>
</tr>
</tbody>
</table>

* As a percentage of the net asset value per Creation Unit, inclusive of the standard transaction fee.

Placement of Redemption Orders For Domestic Funds Using The Clearing Process. Orders to redeem Creation Units of Domestic Funds through the Clearing Process must be delivered through a Participating Party that has executed the Participant Agreement. An order to redeem Creation Units using the Clearing Process is deemed received by the Trust on the Transmittal Date if: (i) such order is received by the Transfer Agent not later than the Closing Time on such Transmittal Date; and (ii) all other procedures set forth in the Participant Agreement are properly followed. Such order will be effected based on the NAV of the Fund as next determined. An order to redeem Creation Units using the Clearing Process made in proper form but received by the Trust after the Closing Time, will be deemed received on the next Business Day immediately following the Transmittal Date and will be effected at the NAV next determined on such Business Day. The requisite Fund Securities and the Cash Redemption Amount will be transferred by the second NSCC Business Day following the date on which such request for redemption is deemed received.

Placement of Redemption Orders For Domestic Funds Outside The Clearing Process. Orders to redeem Creation Units of Domestic Funds outside the Clearing Process must be delivered through a DTC Participant that has executed the Participant Agreement. A DTC Participant who wishes to place an order for redemption of Creation Units to be effected outside the Clearing Process does not need to be a Participating Party, but such orders must state that the DTC Participant is not using the Clearing Process and that redemption of Creation Units will instead be effected through transfer of shares directly through DTC. An order in good form to redeem Creation Units outside the Clearing Process is deemed received by the Trust on the Transmittal Date if: (i) such order is received by the Transfer Agent no later than 10:00 a.m., Eastern time, on the contracted settlement date; (ii) such order is accompanied or followed by the requisite number of shares of the Fund specified in such order, which delivery must be made through DTC to the Transfer Agent no later than 10:00 a.m., Eastern time, on the contracted settlement date; and (iii) all other procedures set forth in the Participant Agreement are properly followed. After the Trust has deemed an order for redemption outside the Clearing Process received, the Trust will initiate procedures to transfer the requisite Fund Securities which are generally expected to be delivered within two Business Days and the Cash Redemption Amount to the Authorized Participant on behalf of the redeeming Beneficial Owner by the Settlement Date. Each of the FlexShares® iBoxx 3-Year Target Duration TIPS...
Placement of Redemption Orders For Foreign Funds. Orders to redeem Creation Units must be delivered through an Authorized Participant. An order in good form to redeem Creation Units is deemed received by the Trust on the Transmittal Date if: (i) a request in satisfactory form to the Trust is received by the Transfer Agent not later than the Closing Time on the Transmittal Date; (ii) such order is accompanied or followed by the requisite number of shares of the Fund specified in such order, which delivery must be made through DTC to the Transfer Agent no later than 10:00 a.m., Eastern time, on the next Business Day following the Transmittal Date; and (iii) all other procedures set forth in the Participant Agreement are properly followed. Deliveries of Fund Securities to redeeming investors generally will be made within two Business Days. Due to the schedule of holidays in certain countries, however, the delivery of in-kind redemption proceeds for a Foreign Fund may take longer than two Business Days after the Transmittal Date. In such cases, the local market settlement procedures will not commence until the end of local holiday periods. See Appendix A for a list of local holidays in the non-U.S. countries relevant to the Foreign Funds.

Investors should be aware that their particular broker may not have executed a Participant Agreement, and that, therefore, requests to redeem Creation Units may have to be placed by the investor’s broker through an Authorized Participant who has executed a Participant Agreement. At any given time there will be only a limited number of broker-dealers that have executed an Authorized Participant Agreement. Investors making a redemption request should be aware that such request must be in the form specified by such Authorized Participant. Investors making a request to redeem Creation Units should allow sufficient time to permit proper submission of the request by an Authorized Participant and transfer of the shares to the Trust’s Transfer Agent; such investors should allow for the additional time that may be required to effect redemptions through their banks, brokers or other financial intermediaries if such intermediaries are not Authorized Participants.

In connection with taking delivery of shares of non-U.S. Fund Securities upon redemption of shares of the Fund, a redeeming Beneficial Owner or Authorized Participant acting on behalf of such Beneficial Owner must maintain appropriate security arrangements with a qualified broker-dealer, bank or other custody providers in each jurisdiction in which any of the portfolio securities are customarily traded, to which account such portfolio securities will be delivered.

To the extent permitted by an Authorized Participant’s agreement with the Distributor, in the event the Authorized Participant that has submitted a Redemption Order in proper form is unable to transfer the Fund Shares to the Custodian, at or prior to 10:00 a.m., Eastern time, on the next Business Day following the Transmittal Date, the Fund at its discretion may, in reliance on the undertaking by the Participant to deliver the missing Fund Shares as soon as possible, allow the Participant to provide and maintain collateral to secure the Participant’s obligation to deliver Fund Shares. The collateral provided must be in US dollars, with an initial value at least equal to 110% of the value of the entire Redemption Order (marked-to-market daily). The collateral percentage required may change from time to time. Such cash collateral must be requested no later than 10:00 a.m. Eastern Time, and delivered no later than 2:00 p.m., Eastern Time, on the Listing Exchange business day after the date of submission of such redemption request. The Trust’s current procedures require, among other things, that any cash collateral shall be in the form of U.S. dollars in immediately available funds and shall be held by the Trust’s Custodian and marked to market daily, and that the fees of the Custodian and any sub-custodians in respect of the delivery, maintenance and redelivery of the cash collateral shall be payable by the Authorized Participant. The cash collateral posted by the Authorized Participant may be invested at the risk of the Authorized Participant, and income, if any, on invested cash collateral will be paid to that Authorized Participant. The Participant Agreement may permit the Trust to purchase the missing shares or acquire the portfolio securities and the Cash Component underlying such shares at any time and subject the Authorized Participant to liability for any shortfall between the cost to the Trust of purchasing such shares, portfolio securities or Cash Component and the cash collateral.

The calculation of the value of the Fund Securities and the Cash Redemption Amount to be delivered upon redemption will be made by the Trust according to the procedures set forth under “Determination of Net Asset Value” in the Funds’ Prospectus and “Net Asset Value” below computed on the Business Day on which a redemption order is deemed received in good form by the Trust. Therefore, if a redemption order in proper form is submitted to the Transfer Agent by a DTC Participant not later than Closing Time on the Transmittal Date, and the requisite number of shares of the relevant Fund are delivered to Transfer Agent prior to the DTC Cut-Off-Time, then the value of the Fund Securities and the Cash Redemption Amount to be delivered will be determined by Trust on such Transmittal Date. If, however, a redemption order is submitted to the Transfer Agent by a DTC Participant not later than the Closing Time on the Transmittal Date but either: (i) the requisite number of shares of the relevant Fund are not delivered by the DTC Cut-Off-Time, as described above, on such Transmittal Date; or (ii) the redemption order is not submitted in proper form, then the redemption order will not be deemed received as of the Transmittal Date. In such case, the
value of the Fund Securities and the Cash Redemption Amount to be delivered will be computed on the Business Day that such order is deemed received by the Trust, (i.e., the Business Day on which the shares of the relevant Fund are delivered through DTC to the Transfer Agent by the DTC Cut-Off-Time) on such Business Day pursuant to a properly submitted redemption order.

If it is not possible to effect deliveries of the portfolio securities, the Trust may in its discretion exercise its option to redeem such shares in cash, and the redeeming Beneficial Owner will be required to receive its redemption proceeds in cash. In addition, an investor may request a redemption in cash that the Fund may, in its sole discretion, permit. In either case, the investor will receive a cash payment equal to the net asset value of its shares based on the NAV of shares of the relevant Fund next determined after the redemption request is received in proper form (minus a redemption transaction fee and additional variable charge for cash redemptions specified above, to offset the Trust’s brokerage and other transaction costs associated with the disposition of portfolio securities of the Fund).

Redemptions of shares for Fund Securities will be subject to compliance with applicable U.S. federal and state securities laws and each Fund (whether or not it otherwise permits cash redemptions) reserves the right to redeem Creation Units for cash to the extent that the Fund could not lawfully deliver specific Fund Securities upon redemptions or could not do so without first registering the Fund Securities under such laws. An Authorized Participant or an investor for which it is acting subject to a legal restriction with respect to particular securities included in the Fund Securities applicable to the redemption of a Creation Unit may be paid an equivalent amount of cash. The Authorized Participant may request the redeeming Beneficial Owner of the shares to complete an order form or to enter into agreements with respect to such matters as compensating cash payment.

Because the portfolio securities of a Foreign Fund may trade on the relevant exchange(s) on days that the Listing Exchange is closed or are otherwise not Business Days for the Fund, shareholders may not be able to redeem their shares of the Fund, or to purchase or sell shares of the Fund on the Listing Exchange, on days when the NAV of the Fund could be significantly affected by events in the relevant foreign markets.

The right of redemption may be suspended or the date of payment postponed with respect to any Fund: (1) for any period during which the New York Stock Exchange is closed (other than customary weekend and holiday closings); (2) for any period during which trading on the New York Stock Exchange is suspended or restricted; (3) for any period during which an emergency exists as a result of which disposal of the shares of the Fund’s portfolio securities or determination of its NAV is not reasonably practicable; or (4) in such other circumstance as is permitted by the SEC.

TAXES

The following summarizes certain additional federal income tax considerations generally affecting the Funds and their shareholders that are not described in the Prospectus. No attempt is made to present a detailed explanation of the tax treatment of the Funds or their shareholders, and the discussions here and in the Prospectus are not intended as a substitute for careful tax planning. Potential investors should consult their tax advisers with specific reference to their own tax situations.

The discussions of the federal income tax consequences in the Prospectus and this SAI are based on the Code and the regulations issued under it, and court decisions and administrative interpretations, as in effect on the date of this SAI. Future legislative or administrative changes or court decisions may significantly alter the statements included herein, and any such changes or decisions may be retroactive.

FEDERAL - GENERAL INFORMATION

Each Fund intends to qualify as a regulated investment company under Subchapter M of Subtitle A, Chapter 1, of the Code. As a regulated investment company, each Fund generally will be exempt from federal income tax on its net investment income and realized capital gains that it distributes to shareholders. To qualify for treatment as a regulated investment company, it must meet three important tests each year.

First, each Fund must derive with respect to each taxable year at least 90% of its gross income from dividends, interest, certain payments with respect to securities loans, gains from the sale or other disposition of stock or securities or foreign currencies, other income derived with respect to the Fund’s business of investing in stock, securities or currencies, or net income derived from interests in qualified publicly traded partnerships.

Second, generally, at the close of each quarter of the Fund’s taxable year, at least 50% of the value of each Fund's assets must consist of cash and cash items, U.S. government securities, securities of other regulated investment companies, and securities of other issuers as to which: (a) the Fund has not invested more than 5% of the value of its total assets in securities of the issuer; and (b) the Fund does not hold more than 10% of the outstanding voting securities of the issuer, and no more than 25% of the
value of each Fund’s total assets may be invested in the securities of: (1) any one issuer (other than U.S. government securities and securities of other regulated investment companies); (2) two or more issuers that the Fund controls and which are engaged in the same or similar trades or businesses; or (3) one or more qualified publicly traded partnerships.

Third, each Fund must distribute an amount equal to at least the sum of 90% of its investment company taxable income (net investment income and the excess of net short-term capital gain over net long-term capital loss), before taking into account any deduction for dividends paid, and 90% of its tax-exempt income, if any, for the year.

Each Fund intends to comply with these requirements. If a Fund were to fail to make sufficient distributions, it could be liable for corporate income tax and for excise tax in respect of the shortfall or, if the shortfall is large enough, the Fund could be disqualified as a regulated investment company. If for any taxable year a Fund were not to qualify as a regulated investment company, all its taxable income would be subject to tax at regular corporate rates without any deduction for distributions to shareholders. In that event, taxable shareholders would recognize dividend income on distributions (including distributions attributable to tax-exempt income) to the extent of the Fund’s current and accumulated earnings and profits, and corporate shareholders could be eligible for the dividends-received deduction.

The Code imposes a nondeductible 4% excise tax on regulated investment companies that fail to currently distribute an amount equal to specified percentages of their ordinary taxable income and capital gain net income (excess of capital gains over capital losses) by the end of each calendar year. Each Fund intends to make sufficient distributions or deemed distributions of its ordinary taxable income and capital gain net income each calendar year to avoid liability for this excise tax.

Each Fund intends to distribute annually to their shareholders substantially all of their investment company taxable income, and any net realized long-term capital gains in excess of net realized short-term capital losses (including any capital loss carryovers). However, if a Fund retains for investment an amount equal to all or a portion of its net long-term capital gains in excess of its net short-term capital losses (including any capital loss carryovers), it will be subject to a corporate tax (currently at a maximum rate of 21%) on the amount retained. In that event, such Fund may designate such retained amounts as undistributed capital gains in a notice to its shareholders who, in such case, (a) will be required to include in income for U.S. federal income tax purposes, as long-term capital gains, their proportionate shares of the undistributed amount; (b) will be entitled to credit their proportionate shares of the tax paid by such Fund on the undistributed amount against their U.S. federal income tax liabilities, if any; and (c) will be entitled to increase their tax basis, for U.S. federal income tax purposes, in their shares by an amount equal to the amount of undistributed capital gains included in the shareholder’s income reduced by their proportionate share of the taxes paid. Organizations or persons not subject to U.S. federal income tax on such capital gains will be entitled to a refund of their pro rata share of such taxes paid by such Fund upon filing appropriate returns or claims for refund with the Internal Revenue Service.

Distributions of net realized long-term capital gains, if any, that a Fund designates as capital gains dividends are taxable as long-term capital gains, regardless of how long a shareholder has held shares of such Fund. All other dividends of a Fund (including dividends from short-term capital gains) from its current and accumulated earnings and profits (“regular dividends”) are generally subject to tax as ordinary income.

If an individual trust or estate receives a qualified dividend qualifying for the long-term capital gains rates and such dividend constitutes an “extraordinary dividend,” and the individual subsequently recognizes a loss on the sale or exchange of stock in respect of which the extraordinary dividend was paid, then the loss will be long-term capital loss to the extent of such extraordinary dividend. An “extraordinary dividend” on common stock for this purpose is generally a dividend: (i) in an amount greater than or equal to 10% of the taxpayer’s tax basis (or trading value) in a share of stock, aggregating dividends with ex-dividend dates within an 85-day period; or (ii) in an amount greater than 20% of the taxpayer’s tax basis (or trading value) in a share of stock, aggregating dividends with ex-dividend dates within a 365-day period.

Distributions in excess of a Fund’s current and accumulated earnings and profits will, as to each shareholder, be treated as a tax-free return of capital to the extent of a shareholder’s basis in his shares of such Fund, and as a capital gain thereafter (if the shareholder holds his shares of such Fund as capital assets). Shareholders receiving dividends or distributions in the form of additional shares should be treated for U.S. federal income tax purposes as receiving a distribution in an amount equal to the amount of money that the shareholders receiving cash dividends or distributions will receive, and should have a cost basis in the shares received equal to such amount. Dividends paid by a Fund that are attributable to dividends received by a Fund from domestic corporations may qualify for the federal dividends-received deduction for corporations.

Investors considering buying shares just prior to a dividend or capital gain distribution should be aware that, although the price of shares just purchased at that time may reflect the amount of the forthcoming distribution, such dividend or distribution may nevertheless be taxable to them. If a Fund is the holder of record of any stock on the record date for any dividends payable
with respect to such stock, such dividends will be included in such Fund’s gross income not as of the date received but as of the later of: (a) the date such stock became ex-dividend with respect to such dividends (that is, the date on which a buyer of the stock would not be entitled to receive the declared, but unpaid, dividends); or (b) the date such Fund acquired such stock. Accordingly, in order to satisfy its income distribution requirements, a Fund may be required to pay dividends based on anticipated earnings, and shareholders may receive dividends in an earlier year than would otherwise be the case.

**BACK-UP WITHHOLDING**

In certain cases, if a shareholder: (1) has failed to provide a correct taxpayer identification number; (2) is subject to backup withholding by the Internal Revenue Service; (3) has failed to certify to a Fund that such shareholder is not subject to backup withholding; or (4) has not certified that such shareholder is a U.S. person (including a U.S. resident alien), 24% of the dividends and distributions payable to such shareholder will be withheld and remitted to the U.S. Treasury.

**SECTIONS 351 AND 362**

The Trust on behalf of each Fund has the right to reject an order for a purchase of shares of a Fund if the purchaser (or group of purchasers) would, upon obtaining the shares so ordered, own 80% or more of the outstanding shares of a given Fund and if, pursuant to Sections 351 and 362 of the Code, that Fund would have a basis in the securities different from the market value of such securities on the date of deposit. If a Fund’s basis in such securities on the date of deposit was less than market value on such date, such Fund, upon disposition of the securities, would recognize more taxable gain or less taxable loss than if its basis in the securities had been equal to market value. It is not anticipated that the Trust will exercise the right of rejection except in a case where the Trust determines that accepting the order could result in material adverse tax consequences to a Fund or its shareholders. The Trust also has the right to require information necessary to determine beneficial share ownership for purposes of the 80% determination.

**QUALIFIED DIVIDEND INCOME**

Distributions by each Fund of investment company taxable income (excluding any short-term capital gains) whether received in cash or shares will be taxable either as ordinary income or as qualified dividend income, eligible for the reduced maximum rate to individuals of 20% to the extent each Fund receives qualified dividend income on the securities it holds and such Fund designates the distribution as qualified dividend income. Qualified dividend income is, in general, dividend income from taxable domestic corporations and certain foreign corporations (e.g., foreign corporations incorporated in a possession of the United States or in certain countries with a comprehensive tax treaty with the United States, or the stock of which is readily tradable on an established securities market in the United States). A dividend will not be treated as qualified dividend income to the extent that: (i) the shareholder has not held the shares on which the dividend was paid for more than 60 days during the 121-day period that begins on the date that is 60 days before the date on which the shares become ex dividend with respect to such dividend (and each Fund also satisfies those holding period requirements with respect to the securities it holds that paid the dividends distributed to the shareholder); (ii) the shareholder is under an obligation (whether pursuant to a short sale or otherwise) to make related payments with respect to substantially similar or related property; or (iii) the shareholder elects to treat such dividend as investment income under section 163(d)(4)(B) of the Code. Distributions by each Fund of its net short-term capital gains will be taxable as ordinary income. Capital gain distributions consisting of each Fund’s net capital gains will be taxable as long-term capital gains except to the extent of any “unrecaptured section 1250 gains” which are taxed at a maximum rate of 25%.

**CORPORATE DIVIDENDS RECEIVED DEDUCTION**

A Fund’s dividends that are paid to its corporate shareholders and are attributable to qualifying dividends it received from U.S. domestic corporations may be eligible, in the hands of such shareholders, for the corporate dividends received deduction, subject to certain holding period requirements and debt financing limitations.

**NET CAPITAL LOSS CARRYFORWARDS**

On December 22, 2010, the Regulated Investment Company Modernization Act of 2010 (the “Act”) was enacted, which changed various technical rules governing the tax treatment of regulated investment companies. The changes are generally effective for taxable years beginning after the date of enactment. Under the Act, a Fund is permitted to carry forward capital losses incurred in taxable years beginning after the date of enactment for an unlimited period. The Funds have no pre-enactment loss carry forwards since the Funds commenced operations after the effective date of the Act. Post-enactment capital loss carry forwards will retain their character as either short-term or long-term capital losses rather than being considered all short-term as permitted under previous law.
As of October 31, 2018, the following Funds had available post-enactment capital loss carry forwards as set forth below:

<table>
<thead>
<tr>
<th>Fund</th>
<th>Short-Term</th>
<th>Long-Term</th>
<th>Total</th>
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<tr>
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<td>$ -</td>
<td>$16,348,607</td>
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<tr>
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<td>$13,267,926</td>
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<tr>
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<td>$23,725,638</td>
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<td>$612,482</td>
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<td>FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund</td>
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**EXCESS INCLUSION INCOME**

Certain types of income received by a Fund from real estate investment Trusts (“REITs”), real estate mortgage investment conduits (“REMICs”), taxable mortgage pools or other investments may cause a Fund to designate some or all of its distributions as “excess inclusion income.” To Fund shareholders such excess inclusion income may: (1) constitute taxable income, as “unrelated business taxable income” (“UBTI”) for those shareholders who would otherwise be tax-exempt such as individual retirement accounts, 401(k) accounts, Keogh plans, pension plans and certain charitable entities; (2) as UBTI cause a charitable remainder Trust to be subject to a 100% excise tax on its UBTI; (3) not be offset against net operating losses for tax purposes; (4) not be eligible for reduced U.S. withholding for non-U.S. shareholders even from tax treaty countries; and (5) cause a Fund to be subject to tax if certain “disqualified organizations” as defined by the Code are Fund shareholders.

**TAXATION OF INCOME FROM CERTAIN FINANCIAL INSTRUMENTS, REITS AND PFICS**

The tax principles applicable to transactions in financial instruments and futures contracts and options that may be engaged in by a Fund including the effect of fluctuations in the value of foreign currencies, and investments in REITs and passive foreign investment companies (“PFICs”), are complex and, in some cases, uncertain. Such transactions and investments may cause a Fund to recognize taxable income prior to the receipt of cash, thereby requiring such Fund to liquidate other positions, or to borrow money, so as to make sufficient distributions to shareholders to avoid corporate-level tax. Moreover, some or all of the taxable income recognized may be ordinary income or short-term capital gain, so that the distributions may be taxable to shareholders as ordinary income.

In addition, in the case of any shares of a PFIC in which a Fund invests, such Fund may be liable for corporate-level tax on any ultimate gain or distributions on the shares if such Fund fails to make an election to recognize income annually during the period of its ownership of the shares.
Under the Tax Cuts and Jobs Act (the “2017 Tax Act”), “qualified REIT dividends” (i.e., ordinary REIT dividends other than capital gain dividends and portions of REIT dividends designated as qualified dividend income) are eligible for a 20% deduction by individuals and other non-corporate taxpayers. On January 18, 2019, the Treasury Department released proposed regulations, on which taxpayers may rely pending the issuance of final regulations, that allows a regulated investment company (such as a Fund) to pay and report “section 199A dividends” to its shareholders with respect to the regulated investment company’s qualified REIT dividends. Under the proposed regulations, the amount of section 199A dividends that a Fund may pay and report to its shareholders is limited to the excess of the “qualified REIT dividends” that the Fund receives from REITs for a taxable year over the Fund’s expenses allocable to such dividends. A shareholder may treat section 199A dividends received with respect to a share of a Fund as “qualified REIT dividends” if the shareholder has held the share for more than 45 days during the 91-day period beginning 45 days before the date on which the share becomes ex-dividend, but only to the extent that the shareholder is not under an obligation (under a short-sale or otherwise) to make related payments with respect to positions in substantially similar or related property. A shareholder may include 20% of the shareholder’s “qualified REIT dividends” in the computation of the shareholder’s “combined qualified business income amount” under Code Section 199A. Code Section 199A allows a taxpayer (other than a corporation) a deduction for a taxable year equal to the lesser of (A) the taxpayer’s “combined qualified business income amount” or (B) 20% of the excess of the taxpayer’s taxable income over the taxpayer’s net capital gain for the year.

SALES OF SHARES

Upon the sale or exchange of his shares, a shareholder will realize a taxable gain or loss equal to the difference between the amount realized and his basis in his shares. A redemption of shares by a Fund will be treated as a sale for this purpose. Except as provided below, such gain or loss will be treated as capital gain or loss if the shares are capital assets in the shareholder’s hands, and will be long-term capital gain or loss if the shares are held for more than one year and short-term capital gain or loss if the shares are held for one year or less. Any loss realized on a sale or exchange will be disallowed to the extent the shares disposed of are replaced, including replacement through the reinvesting of dividends and capital gains distributions in a Fund, within a 61-day period beginning 30 days before and ending 30 days after the disposition of the shares. In such a case, the basis of the shares acquired will be increased to reflect the disallowed loss. Any loss realized by a shareholder on the sale of a Fund share held by the shareholder for six months or less will be treated for U.S. federal income tax purposes as a long-term capital loss to the extent of any distributions or deemed distributions of long-term capital gains received by the shareholder with respect to such share.

OTHER TAXES

Dividends, distributions and redemption proceeds may also be subject to additional state, local and foreign taxes depending on each shareholder’s particular situation.

TAXATION OF NON-U.S. SHAREHOLDERS

Dividends paid by a Fund to non-U.S. shareholders are generally subject to withholding tax at a 30% rate or a reduced rate specified by an applicable income tax treaty to the extent derived from investment income and short-term capital gains. In order to obtain a reduced rate of withholding, a non-U.S. shareholder will be required to provide an IRS Form W-8BEN or W-8BEN-E, as applicable, certifying its entitlement to benefits under a treaty. Certain interest related dividends and short term capital gain dividends as designated by the Fund are not subject to this 30% withholding tax if the shareholder provides a properly completed Form W-8BEN or W-8BEN-E applicable. The withholding tax does not apply to regular dividends paid to a non-U.S. shareholder who provides a Form W-8ECI, certifying that the dividends are effectively connected with the non-U.S. shareholder’s conduct of a trade or business within the United States. Instead, the effectively connected dividends will be subject to regular U.S. income tax as if the non-U.S. shareholder were a U.S. shareholder. A non-U.S. corporation receiving effectively connected dividends may also be subject to additional “branch profits tax” imposed at a rate of 30% (or lower treaty rate). A non-U.S. shareholder who fails to provide an IRS Form W-8BEN, W-8BEN-E or other applicable form may be subject to backup withholding at the appropriate rate.

In general, United States federal withholding tax will not apply to any gain or income realized by a non-U.S. shareholder in respect of any distributions of net long-term capital gains over net short-term capital losses, exempt-interest dividends, or upon the sale or other disposition of shares of a Fund.

Certain dividends paid to a non-U.S. shareholder that fails to make certain required certifications, or that is a “foreign financial institution” as defined in Section 1471 of the Code and that does not meet the requirements imposed on foreign financial institutions by Section 1471, are generally subject to a U.S. withholding tax at a 30% rate. The extent, if any, to which such
withholding tax may be reduced or eliminated by an applicable tax treaty is unclear. A non-U.S. shareholder may be exempt from
the withholding described in this paragraph under an intergovernmental agreement between the U.S. and a foreign government,
provided that the shareholder and the applicable foreign government comply with the terms of such agreement.

REPORTING

If a shareholder recognizes a loss with respect to a Fund’s shares of $2 million or more for an individual shareholder or
$10 million or more for a corporate shareholder, the shareholder may be required to file with the Internal Revenue Service a
disclosure statement on Form 8886. Direct shareholders of portfolio securities are in many cases exempted from this reporting
requirement, but under current guidance, shareholders of a regulated investment company are not exempted. The fact that a loss is
reportable under these regulations does not affect the legal determination of whether the taxpayer’s treatment of the loss is proper.
Shareholders should consult their tax advisors to determine the applicability of these regulations in light of their individual
circumstances. Certain tax-exempt entities and their managers may be subject to excise tax if they are parties to certain reportable
transactions.

The foregoing discussion is a summary only and is not intended as a substitute for careful tax planning. Purchasers of
shares should consult their own tax advisers as to the tax consequences of investing in such shares, including under state, local and
foreign tax laws. Finally, the foregoing discussion is based on applicable provisions of the Code, regulations, judicial authority and
administrative interpretations in effect on the date of this Statement of Additional Information. Changes in applicable authority
could materially affect the conclusions discussed above, and such changes often occur.

NET ASSET VALUE

Net asset value is determined as indicated under “Determination of Net Asset Value” in the Funds’ Prospectus.

The time at which transactions and shares are priced and the time by which orders must be received may be changed in
case of an emergency or if regular trading on the New York Stock Exchange is stopped at a time other than 4:00 p.m. Eastern
Standard Time. On any business day when the Securities Industry and Financial Markets Association (“SIFMA”) recommends that
the bond markets close early, the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target
Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond
Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and the FlexShares® High Yield Value-Scored Bond
Index Fund reserve the right to close at or prior to the SIFMA recommended closing time and credit will be given on the next
business day. The Trust reserves the right to advance the time by which purchase and redemption orders must be received for same
business day credit as otherwise permitted by the SEC. In addition, each Fund may compute its NAV as of any time permitted
pursuant to any exemption, order or statement of the SEC or its staff. The Trust reserves the right to reprocess purchase and
redemption transactions that were processed at a NAV other than the Fund’s official closing NAV. For instance, if a pricing error is
discovered that impacts a Fund’s NAV, the corrected NAV would be the official closing NAV and the erroneous NAV would be a
NAV other than the Fund’s official closing NAV. Those transactions that were processed using the erroneous NAV may then be
reprocessed using the official closing NAV.

DIVIDENDS AND DISTRIBUTIONS

GENERAL POLICIES

Dividends from net investment income, including any net foreign currency gains, are generally declared and paid at least
quarterly (the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index
Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund,
FlexShares® Credit-Scored US Long Corporate Bond Index Fund and the FlexShares® High Yield Value-Scored Bond Index Fund
generally declare and pay any dividends monthly) and any net realized securities gains, if any, generally are distributed at least
annually. In order to improve tracking error or comply with the distribution requirements of the Code, dividends may be declared
and paid more frequently for certain Funds. Dividends and securities gains distributions are distributed in U.S. dollars and cannot
be automatically reinvested in additional shares of the Funds. The Trust reserves the right to declare special distributions if, in its
reasonable discretion, such action is necessary or advisable to preserve the status of the Fund as a RIC or to avoid imposition of
income or excise taxes on undistributed income.

Dividends and other distributions on Fund Shares are distributed, as described below, on a pro rata basis to Beneficial
Owners of such Shares. Dividend payments are made through DTC Participants and Indirect Participants to Beneficial Owners
then of record with proceeds received from the Fund.
DIVIDEND REINVESTMENT SERVICE

No dividend reinvestment service is provided by the Trust. Broker-dealers may make available the DTC book-entry Dividend Reinvestment Service for use by Beneficial Owners of Funds for reinvestment of their dividend distributions. Beneficial Owners should contact their broker to determine the availability and costs of the service and the details of participation therein. Brokers may require Beneficial Owners to adhere to specific procedures and timetables. If this service is available and used, dividend distributions of both income and realized gains will be automatically reinvested in additional whole shares of the same Fund purchased in the secondary market.

OTHER INFORMATION

COUNSEL

Drinker Biddle & Reath LLP, with offices at One Logan Square, Ste. 2000, Philadelphia, PA 19103-6996, is counsel to the Trust.

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Deloitte & Touche LLP, located at 111 South Wacker Drive, Chicago, Illinois 60606-4301, serves as the independent registered public accounting firm of the Trust, audits the Funds’ financial statements and may perform other services.

ADDITIONAL INFORMATION

The Prospectus and this SAI do not contain all the information included in the Registration Statement filed with the SEC under the Securities Act with respect to the securities offered by the Trust’s Prospectus. Certain portions of the Registration Statement have been omitted from the Prospectus and this SAI pursuant to the rules and regulations of the SEC. The Registration Statement, including the exhibits filed therewith, may be examined at the office of the SEC in Washington, D.C.

Statements contained in the Prospectus or in this SAI as to the contents of any contract or other documents referred to are not necessarily complete, and in each instance reference is made to the copy of such contract or other document filed as an exhibit to the Registration Statement of which the Prospectus and this SAI form a part, each such statement being qualified in all respects by such reference.

FINANCIAL STATEMENTS

The audited financial statements of the FlexShares® Morningstar US Market Factor Tilt Index Fund, FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar DM ex-US Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® US Quality Large Cap Index Fund, FlexShares® STOXX® US ESG Impact Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® STOXX® Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® Quality Dividend Index Fund, FlexShares® Quality Dividend Defensive Index Fund, FlexShares® Quality Dividend Dynamic Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund, FlexShares® International Quality Dividend Dynamic Index Fund, FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Bond Index Fund and related report of Deloitte & Touche LLP, an independent registered public accounting firm, contained in the annual report to the Funds’ shareholders for the fiscal year or period ended October 31, 2018 (the “Annual Report”) are hereby incorporated by reference herein. No other parts of the Annual Report are incorporated by reference herein. Copies of the Trust’s Annual Report may be obtained upon request and without charge, by writing to FlexShares ETFs, c/o Foreside Fund Services, LLC, 3 Canal Plaza, Suite 100, Portland, ME 04101 or by calling 1-855-FLEXETF (1-855-353-9383).
APPENDIX A

Each Fund generally intends to effect deliveries of Creation Units and portfolio securities on a basis of “T” plus two business days (except that the FlexShares® iBoxx 3-Year Target Duration TIPS Index Fund, FlexShares® iBoxx 5-Year Target Duration TIPS Index Fund, FlexShares® Disciplined Duration MBS Index Fund, FlexShares® Credit-Scored US Corporate Bond Index Fund, FlexShares® Credit-Scored US Long Corporate Bond Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund will generally settle transactions on a T plus one business day basis). Each Fund may effect deliveries of Creation Units and portfolio securities on a basis other as noted above in order to accommodate local holiday schedules, to account for different treatment among foreign and U.S. markets of dividend record dates and ex-dividend dates, or under certain other circumstances. The ability of the Trust to effect in-kind creations and redemptions within one or two business days, as applicable of receipt of an order in good form is subject, among other things, to the condition that, within the time period from the date of the order to the date of delivery of the securities, there are no days that are holidays in the applicable foreign market. For every occurrence of one or more intervening holidays in the applicable foreign market that are not holidays observed in the U.S. equity market, the redemption settlement cycle may be extended by the number of such intervening holidays. In addition to holidays, other unforeseeable closings in a foreign market due to emergencies may also prevent the Trust from delivering securities within the normal settlement period.

The securities delivery cycles currently practicable for transferring portfolio securities to redeeming investors, coupled with foreign market holiday schedules, may require a delivery process longer than seven calendar days for the FlexShares® Morningstar Developed Markets ex-US Factor Tilt Index Fund, FlexShares® Morningstar Emerging Markets Factor Tilt Index Fund, FlexShares® Currency Hedged Morningstar EM Factor Tilt Index Fund, FlexShares® STOXX® Global ESG Impact Index Fund, FlexShares® Morningstar Global Upstream Natural Resources Index Fund, FlexShares® STOXX® Global Broad Infrastructure Index Fund, FlexShares® Global Quality Real Estate Index Fund, FlexShares® Real Assets Allocation Index Fund, FlexShares® International Quality Dividend Index Fund, FlexShares® International Quality Dividend Defensive Index Fund, FlexShares® International Quality Dividend Dynamic Index Fund and FlexShares® High Yield Value-Scored Bond Index Fund in certain circumstances. The holidays applicable to these Funds through December 31, 2020 are listed below, as are instances where more than seven days may be needed to deliver redemption proceeds. Although certain holidays may occur on different dates in subsequent years, the number of days required to deliver redemption proceeds in any given year is not expected to exceed the maximum number of days listed below. The proclamation of new holidays, the treatment by market participants of certain days as “informal holidays” (e.g., days on which no or limited securities transactions occur, as a result of substantially shortened trading hours), the elimination of existing holidays, or changes in local securities delivery practices, could affect the information set forth herein at some time in the future.

### Regular Holidays through December 31, 2019.

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The Israeli market is closed every Friday.

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**South Africa**

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**Sweden**

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April 8, 2019 May 6, 2019 August 12, 2019 December 31, 2019
April 15, 2019 May 20, 2019 October 23, 2019 January 1, 2020

Turkey
January 1, 2019 June 5, 2019 August 12, 2019 October 28, 2019
April 23, 2019 June 6, 2019 August 13, 2019 October 29, 2019
May 1, 2019 June 7, 2019 August 14, 2019 January 1, 2020
June 4, 2019 July 15, 2019 August 30, 2019

United Arab Emirates
January 1, 2019 June 5, 2019 August 31, 2019 November 29, 2019
February 18, 2019 June 6, 2019 September 1, 2019 November 30, 2019
April 2, 2019 July 4, 2019 September 2, 2019 December 2, 2019
April 3, 2019 August 10, 2019 October 14, 2019 December 3, 2019
April 19, 2019 August 11, 2019 November 9, 2019 December 10, 2019
May 27, 2019 August 12, 2019 November 11, 2019 December 24, 2019
June 4, 2019 August 13, 2019 November 28, 2019 December 25, 2019

United States
January 1, 2019 April 19, 2019 September 2, 2019 November 28, 2019
January 21, 2019 May 27, 2019 October 14, 2019 December 25, 2019
February 18, 2019 July 4, 2019 November 11, 2019 January 1, 2020
Regular Holidays through December 31, 2020.

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<th>Austria</th>
<th>Belgium</th>
<th>Brazil</th>
<th>Britain</th>
<th>Canada</th>
<th>Chilé</th>
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<td>January 1, 2020 - May 25, 2020</td>
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<td>The Czech Republic</td>
<td>September 28, 2020</td>
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<td>The Egyptian market is closed every Friday.</td>
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<td>November 11, 2020</td>
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<td>Hungary</td>
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<td>India</td>
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<td>Ireland</td>
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<td>April 13, 2020</td>
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<td>December 25, 2020</td>
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<td>March 17, 2020</td>
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<td>June 1, 2020</td>
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<td>October 26, 2020</td>
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<td>December 29, 2020</td>
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<td>Israel</td>
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<td>April 15, 2020</td>
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<td>September 28, 2020</td>
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-A- 12
April 2, 2020        April 9, 2020        April 29, 2020
April 3, 2020        April 14, 2020        July 30, 2020

The Israeli market is closed every Friday.

Italy

January 1, 2020        April 10, 2020        May 1, 2020        December 25, 2020
January 6, 2020        April 13, 2020        December 8, 2020

Japan

January 3, 2020        May 6, 2020        September 21, 2020        December 31, 2020
January 13, 2020        July 20, 2020        September 22, 2020
March 20, 2020        July 23, 2020        October 12, 2020
April 29, 2020        July 24, 2020        November 3, 2020

Luxembourg

January 1, 2020        April 13, 2020        May 21, 2020        December 25, 2020
April 10, 2020        May 1, 2020

Malaysia

May 1, 2020        June 1, 2020        August 31, 2020        November 16, 2020
May 7, 2020        July 31, 2020        September 16, 2020        December 25, 2020
May 25, 2020        August 20, 2020        October 29, 2020

Mexico

April 9, 2020        May 1, 2020        November 2, 2020        December 25, 2020
April 10, 2020        September 16, 2020        November 16, 2020

Morocco

January 1, 2020        April 9, 2020        August 21, 2020        November 21, 2020
May 1, 2020        July 31, 2020        October 29, 2020        November 18, 2020
July 30, 2020        August 20, 2020        October 30, 2020

Netherlands

January 1, 2020        April 27, 2020        May 5, 2020        December 25, 2020
April 10, 2020        April 30, 2020        May 21, 2020
April 13, 2020        May 1, 2020        June 1, 2020
<table>
<thead>
<tr>
<th>Country</th>
<th>Dates</th>
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<td>New Zealand</td>
<td>April 10, 2020 - April 27, 2020, June 1, 2020, April 13, 2020, June 1, 2020, December 25, 2020, December 28, 2020</td>
</tr>
<tr>
<td>Norway</td>
<td>January 1, 2020 - April 13, 2020, June 1, 2020, April 9, 2020, May 1, 2020, December 24, 2020, December 25, 2020</td>
</tr>
<tr>
<td>Pakistan</td>
<td>January 1, 2020 - May 1, 2020, May 24, 2020, October 29, 2020</td>
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<td>Palestine</td>
<td>January 1, 2020 - May 24, 2020, May 25, 2020, October 29, 2020</td>
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<td>January 1, 2020 - April 10, 2020, April 9, 2020, May 1, 2020, October 8, 2020, December 25, 2020</td>
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<td>January 1, 2020 - June 12, 2020, August 31, 2020, December 30, 2020</td>
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<td>Poland</td>
<td>January 1, 2020 - April 10, 2020, April 13, 2020, June 11, 2020</td>
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<tr>
<td>Qatar</td>
<td>January 1, 2020 - March 1, 2020, August 2, 2020, August 3, 2020</td>
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<td>Russia</td>
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<tr>
<td></td>
<td>January 2, 2020 - March 9, 2020, May 25, 2020, November 11, 2020</td>
</tr>
</tbody>
</table>
January 6, 2020  May 1, 2020  September 7, 2020  December 25, 2020
January 7, 2020  

May 24, 2020  July 29, 2020  July 30, 2020  September 23, 2020

Saudi Arabia

January 1, 2020  April 3, 2020  May 25, 2020  October 9, 2020
January 24, 2020  April 6, 2020  July 31, 2020  December 25, 2020
January 27, 2020  April 10, 2020  August 10, 2020  
January 28, 2020  May 1, 2020  October 1, 2020  
January 29, 2020  May 7, 2020  October 2, 2020  

Singapore

January 1, 2020  April 27, 2020  September 24, 2020  
April 10, 2020  June 16, 2020  December 16, 2020  
April 13, 2020  August 10, 2020  December 25, 2020  

South Africa

January 1, 2020  April 30, 2020  October 1, 2020  December 25, 2020
January 24, 2020  May 1, 2020  October 2, 2020  December 31, 2020
April 15, 2020  May 5, 2020  October 9, 2020  

South Korea

March 19, 2020  May 1, 2020  June 24, 2020  November 9, 2020
April 9, 2020  May 15, 2020  September 11, 2020  December 8, 2020
April 10, 2020  June 1, 2020  September 24, 2020  December 25, 2020
April 13, 2020  June 11, 2020  October 12, 2020  

Spain

Sweden

January 1, 2020  April 13, 2020  June 19, 2020  December 25, 2020
January 6, 2020  May 1, 2020  June 26, 2020  December 31, 2020
April 10, 2020  May 21, 2020  December 24, 2020  

Switzerland

January 1, 2020  April 13, 2020  June 1, 2020  December 31, 2020
January 2, 2020  May 1, 2020  December 24, 2020  
April 10, 2020  May 21, 2020  December 25, 2020  

-A- 15
Redemption. The longest redemption cycle for a Fund is a function of the longest redemption cycles among the countries whose securities comprise a Fund. Through December 31, 2019, the dates of regular holidays affecting the following securities markets present the worst-case redemption cycles* for a Fund as follows:

<table>
<thead>
<tr>
<th>Country</th>
<th>Trade Date</th>
<th>Settlement Date</th>
<th>Number of Days to Settle</th>
</tr>
</thead>
<tbody>
<tr>
<td>Britain</td>
<td>12/20/2019</td>
<td>1/3/2020</td>
<td>14</td>
</tr>
<tr>
<td></td>
<td>12/23/2019</td>
<td>1/6/2020</td>
<td>14</td>
</tr>
<tr>
<td>China</td>
<td>1/31/2019</td>
<td>2/11/2019</td>
<td>11</td>
</tr>
<tr>
<td></td>
<td>1/31/2019</td>
<td>2/11/2019</td>
<td>11</td>
</tr>
<tr>
<td></td>
<td>2/1/2019</td>
<td>2/12/2019</td>
<td>11</td>
</tr>
<tr>
<td></td>
<td>9/30/2019</td>
<td>10/9/2019</td>
<td>9</td>
</tr>
<tr>
<td>Egypt</td>
<td>4/24/2019</td>
<td>5/2/2019</td>
<td>8</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>1/31/2019</td>
<td>2/11/2019</td>
<td>11</td>
</tr>
<tr>
<td></td>
<td>2/1/2019</td>
<td>2/12/2019</td>
<td>11</td>
</tr>
<tr>
<td></td>
<td>9/30/2019</td>
<td>10/9/2019</td>
<td>9</td>
</tr>
<tr>
<td>Hungary</td>
<td>12/23/2019</td>
<td>12/31/2019</td>
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<tr>
<td></td>
<td>12/20/2019</td>
<td>12/30/2019</td>
<td>10</td>
</tr>
<tr>
<td>Israel</td>
<td>10/3/2019</td>
<td>10/15/2019</td>
<td>12</td>
</tr>
<tr>
<td>Country</td>
<td>Trade Date</td>
<td>Settlement Date</td>
<td>Number of Days to Settle</td>
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<tr>
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<td>--------------------------</td>
</tr>
<tr>
<td>Qatar</td>
<td>10/7/2019</td>
<td>10/16/2019</td>
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</tr>
<tr>
<td></td>
<td>8/8/2019</td>
<td>8/19/2019</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>8/7/2019</td>
<td>8/15/2019</td>
<td>8</td>
</tr>
<tr>
<td>Russia</td>
<td>12/28/2018</td>
<td>1/8/2019</td>
<td>11</td>
</tr>
<tr>
<td></td>
<td>12/31/2018</td>
<td>1/9/2019</td>
<td>9</td>
</tr>
<tr>
<td>Singapore</td>
<td>1/31/2019</td>
<td>2/8/2019</td>
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<tr>
<td></td>
<td>2/1/2019</td>
<td>2/11/2019</td>
<td>10</td>
</tr>
<tr>
<td>Taiwan</td>
<td>1/31/2019</td>
<td>2/8/2019</td>
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<td>2/1/2019</td>
<td>2/11/2019</td>
<td>10</td>
</tr>
<tr>
<td>Turkey</td>
<td>5/31/2019</td>
<td>6/10/2019</td>
<td>10</td>
</tr>
</tbody>
</table>

* These worst-case redemption cycles are based on information regarding regular holidays, which may be out of date. Based on changes in holidays, longer (worse) redemption cycles are possible.

**Redemption.** The longest redemption cycle for a Fund is a function of the longest redemption cycles among the countries whose securities comprise a Fund. Through December 31, 2020, the dates of regular holidays affecting the following securities markets present the worst-case redemption cycles* for a Fund as follows:

<table>
<thead>
<tr>
<th>Country</th>
<th>Trade Date</th>
<th>Settlement Date</th>
<th>Number of Days to Settle</th>
</tr>
</thead>
<tbody>
<tr>
<td>Britain</td>
<td>12/22/2020</td>
<td>1/1/2021</td>
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<tr>
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<td>12/23/2020</td>
<td>1/4/2021</td>
<td>12</td>
</tr>
<tr>
<td>China</td>
<td>1/23/2020</td>
<td>1/31/2020</td>
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<tr>
<td></td>
<td>1/24/2020</td>
<td>2/3/2020</td>
<td>10</td>
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<td>2/3/2020</td>
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<td>12/30/2019</td>
<td>1/8/2020</td>
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<td></td>
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<td>1/9/2020</td>
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<tr>
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<td>1/23/2020</td>
<td>1/31/2020</td>
<td>8</td>
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</tbody>
</table>

* These worst-case redemption cycles are based on information regarding regular holidays, which may be out of date. Based on changes in holidays, longer (worse) redemption cycles are possible.
APPENDIX B

As stated in the Prospectus, the Funds may enter into certain futures transactions. Some of these transactions are described in this Appendix. The Funds may also enter into other futures transactions or other securities and instruments that are available in the markets from time to time.

I. Index and Security Futures Contracts

A stock index assigns relative values to the stocks included in the index, which fluctuates with changes in the market values of the stocks included. Some stock index futures contracts are based on broad market indexes, such as the S&P 500 or the New York Stock Exchange Composite Index. In contrast, certain futures contracts relate to narrower market indexes, such as the S&P 100® or indexes based on an industry or market segment, such as oil and gas stocks. Since 2001, trading has been permitted in futures based on a single stock and on narrow-based security indexes (as defined in the Commodity Futures Modernization Act of 2000) (together “security futures”; broader-based index futures are referred to as “index futures”). Some futures contracts are traded on organized exchanges regulated by the CFTC. These exchanges may be either designated by the CFTC as a contract market or registered with the CFTC as a Derivatives Transaction Execution Facility (DTEF). Transactions on such exchanges are cleared through a clearing corporation, which guarantees the performance of the parties to each contract. Futures contracts also may be traded on electronic trading facilities or over-the-counter. These various trading facilities are licensed and/or regulated by varying degrees by the CFTC. To the extent consistent with its investment objective, a Fund may also engage in transactions, from time to time, in foreign stock index futures such as the ALL-ORDS (Australia), CAC40 (France), TOPIX (Japan) and the FTSE-100 (United Kingdom).

II. Futures Contracts on Foreign Currencies

A futures contract on foreign currency creates a binding obligation on one party to deliver, and a corresponding obligation on another party to accept delivery of, a stated quantity of foreign currency for an amount fixed in U.S. dollars. Foreign currency futures may be used by a Fund to help the Fund track the price and yield performance of its Underlying Index.

III. Margin Payments

Unlike purchases or sales of portfolio securities, no price is paid or received by a Fund upon the purchase or sale of a futures contract. Initially, the Funds will be required to deposit with the broker or in a segregated account with a custodian or sub-custodian an amount of liquid assets, known as initial margin, based on the value of the contract. The nature of initial margin in futures transactions is different from that of margin in security transactions in that futures contract margin does not involve the borrowing of funds by the customer to finance the transactions. Rather, the initial margin is in the nature of a performance bond or good faith deposit on the contract, which is returned to the Funds upon termination of the futures contract assuming all contractual obligations have been satisfied. Subsequent payments, called variation margin, to and from the broker, will be made on a daily basis as the price of the underlying instruments fluctuates making the long and short positions in the futures contract more or less valuable, a process known as “marking-to-market.” For example, when a Fund has purchased a futures contract and the price of the contract has risen in response to a rise in the underlying instruments, that position will have increased in value and the Fund will be entitled to receive from the broker a variation margin payment equal to that increase in value. Conversely, where a Fund has purchased a futures contract and the price of the future contract has declined in response to a decrease in the underlying instruments, the position would be less valuable and the Fund would be required to make a variation margin payment to the broker. Prior to expiration of the futures contract, the Investment Adviser may elect to close the position by taking an opposite position, subject to the availability of a secondary market, which will operate to terminate a Fund’s position in the futures contract. A final determination of variation margin is then made, additional cash is required to be paid by or released to the Fund, and the Fund realizes a loss or gain.

IV. Risks of Transactions in Futures Contracts

There are several risks in connection with the use of futures by the Funds, even for futures that are used for hedging (non-speculative) purposes. One risk arises because of the imperfect correlation between movements in the price of the futures and movements in the price of the instruments which are the subject of the hedge. The price of the future may move more than or less than the price of the instruments being hedged. If the price of the futures moves less than the price of the instruments which are the subject of the hedge, the hedge will not be fully effective but, if the price of the instruments being hedged has moved in an unfavorable direction, a Fund would be in a better position than if it had not hedged at all. If the price of the instruments being hedged has moved in a favorable direction, this advantage will be partially offset by the loss on the futures. If the price of the
futures moves more than the price of the hedged instruments, the Fund involved will experience either a loss or gain on the futures which will not be completely offset by movements in the price of the instruments that are the subject of the hedge. To compensate for the imperfect correlation of movements in the price of instruments being hedged and movements in the price of futures contracts, the Funds may buy or sell futures contracts in a greater dollar amount than the dollar amount of instruments being hedged if the volatility over a particular time period of the prices of such instruments has been greater than the volatility over such time period of the futures, or if otherwise deemed to be appropriate by the Investment Adviser. Conversely, a Fund may buy or sell fewer futures contracts if the volatility over a particular time period of the prices of the instruments being hedged is less than the volatility over such time period of the futures contract being used, or if otherwise deemed to be appropriate by the Investment Adviser.

In addition to the possibility that there may be an imperfect correlation, or no correlation at all, between movements in the futures and the instruments being hedged, the price of futures may not correlate perfectly with movement in the cash market due to certain market distortions. Rather than meeting additional margin deposit requirements, investors may close futures contracts through off-setting transactions which could distort the normal relationship between the cash and futures markets. Second, with respect to financial futures contracts, the liquidity of the futures market depends on participants entering into off-setting transactions rather than making or taking delivery. To the extent participants decide to make or take delivery, liquidity in the futures market could be reduced thus producing distortions. Third, from the point of view of speculators, the deposit requirements in the futures market are less onerous than margin requirements in the securities market. Therefore, increased participation by speculators in the futures market may also cause temporary price distortions. Due to the possibility of price distortion in the futures market, and because of the imperfect correlation between the movements in the cash market and movements in the price of futures, a correct forecast of general market trends or interest rate movements by the Investment Adviser may still not result in a successful hedging transaction over a short time frame.

In general, positions in futures may be closed out only on an exchange, board of trade or other trading facility, which provides a secondary market for such futures. Although the Funds intend to purchase or sell futures only on trading facilities where there appear to be active secondary markets, there is no assurance that a liquid secondary market on any trading facility will exist for any particular contract or at any particular time. In such an event, it may not be possible to close a futures investment position, and in the event of adverse price movements, the Funds would continue to be required to make daily cash payments of variation margin. However, in the event futures contracts have been used to hedge portfolio securities, such securities will not be sold until the futures contract can be terminated. In such circumstances, an increase in the price of the securities, if any, may partially or completely offset losses on the futures contract. However, as described above, there is no guarantee that the price of the securities will in fact correlate with the price movements in the futures contract and thus provide an offset on a futures contract.

Further, it should be noted that the liquidity of a secondary market in a futures contract may be adversely affected by “daily price fluctuation limits” established by commodity exchanges which limit the amount of fluctuation in a futures contract price during a single trading day. Once the daily limit has been reached in the contract, no trades may be entered into at a price beyond the limit, thus preventing the liquidation of open futures positions. The trading of futures contracts is also subject to the risk of trading halts, suspensions, exchange or clearing house equipment failures, government intervention, insolvency of a brokerage firm or clearing house or other disruptions of normal trading activity, which could at times make it difficult or impossible to liquidate existing positions or to recover excess variation margin payments.

Successful use of futures by Funds is also subject to the Investment Adviser’s ability to predict correctly movements in the direction of the market. In addition, in such situations, if a Fund has insufficient cash, it may have to sell securities to meet daily variation margin requirements. Such sales of securities may be, but will not necessarily be, at increased prices which reflect the rising market. The Fund may have to sell securities at a time when it may be disadvantageous to do so.

Futures purchased or sold by a Fund (and related options) may be traded on foreign exchanges. Participation in foreign futures and foreign options transactions involves the execution and clearing of trades on or subject to the rules of a foreign board of trade. Neither the National Futures Association nor any domestic exchange regulates activities of any foreign boards of trade, including the execution, delivery and clearing of transactions, or has the power to compel enforcement of the rules of a foreign board of trade or any applicable foreign law. This is true even if the exchange is formally linked to a domestic market so that a position taken on the market may be liquidated by a transaction on another market. Moreover, such laws or regulations will vary depending on the foreign country in which the foreign futures or foreign options transaction occurs. For these reasons, customers who trade foreign futures or foreign options contracts may not be afforded certain of the protective measures provided by the Commodity Exchange Act, the CFTC regulations and the rules of the National Futures Association and any domestic exchange or other trading facility (including the right to use reparations proceedings before the CFTC and arbitration proceedings provided by
the National Futures Association or any domestic futures exchange), nor the protective measures provided by the Securities and Exchange Commission’s rules relating to security futures. In particular, the investments of the Funds in foreign futures, or foreign options transactions may not be provided the same protections in respect to transactions on United States futures trading facilities. In addition, the price of any foreign futures or foreign options contract may be affected by any variance in the foreign exchange rate between the time an order is placed and the time it is liquidated, offset or exercised.

V. Options on Futures Contracts

The Funds may purchase and write options on the futures contracts described above. A futures option gives the holder, in return for the premium paid, the right to buy (call) from or sell (put) to the writer of the option of a futures contract at a specified price at any time during the period of the option. Upon exercise, the writer of the option is obligated to pay the difference between the cash value of the futures contract and the exercise price. Like the buyer or seller of a futures contract, the holder, or writer, of an option has the right to terminate its position prior to the scheduled expiration of the option by selling, or purchasing an option of the same series, at which time the person entering into the closing transaction will realize a gain or loss. A Fund will be required to deposit initial margin and variation margin with respect to put and call options on futures contracts written by it pursuant to brokers’ requirements similar to those described above. Net option premiums received will be included as initial margin deposits.

Investments in futures options involve some of the same considerations that are involved in connection with investments in futures contracts (for example, the existence of a liquid secondary market). See “Risks of Transactions in Futures Contracts” above. In addition, the purchase or sale of an option also entails the risk that changes in the value of the underlying futures contract will not correspond to changes in the value of the option purchased. Depending on the pricing of the option compared to either the futures contract upon which it is based, or upon the price of the securities being hedged, an option may or may not be less risky than ownership of the futures contract or such securities. In general, the market prices of options can be expected to be more volatile than the market prices on the underlying futures contract. Compared to the purchase or sale of futures contracts, however, the purchase of call or put options on futures contracts may frequently involve less potential risk to the Fund because the maximum amount at risk is the premium paid for the options (plus transaction costs). The writing of an option on a futures contract involves risks similar to those risks relating to the sale of futures contracts.

VI. Other Matters

The Funds intend to comply with the regulations of the CFTC exempting it from registration as a “Commodity Pool Operator”. The Funds are operated by persons who have claimed an exclusion from the definition of the term “Commodity Pool Operator” with respect to the Funds under the Commodity Exchange Act and, therefore, are not subject to registration or regulations as a pool operator with respect to the Funds under such Act. In order to continue to claim exclusion from registration as a “commodity pool operator” with respect to the Funds, each Fund is limited in its ability to use futures, options and swaps subject to regulation under the CEA for purposes other than bona fide hedging, which is narrowly defined. With respect to transactions other than for bona fide hedging purposes, either: (1) the aggregate initial margin and premiums required to establish the Fund’s positions in such investments may not exceed 5% of the liquidation value of the Fund’s assets (after accounting for unrealized profits and unrealized losses on any such investments), or (2) the aggregate net notional value of such instruments may not exceed 100% of the liquidation value of the Fund’s assets (after accounting for unrealized profits and unrealized losses on any such positions). In addition to meeting one of the foregoing trading limitations, a Fund may not market itself as a commodity pool or otherwise as a vehicle for trading in the futures, options or swaps markets. Accounting for futures contracts will be in accordance with generally accepted accounting principles.
APPENDIX C

DESCRIPTION OF SECURITIES RATINGS

Short-Term Credit Ratings

An S&P Global Ratings short-term issue credit rating is generally assigned to those obligations considered short-term in the relevant market. The following summarizes the rating categories used by S&P Global Ratings for short-term issues:

“A-1” – A short-term obligation rated “A-1” is rated in the highest category by S&P Global Ratings. The obligor’s capacity to meet its financial commitments on the obligation is strong. Within this category, certain obligations are designated with a plus sign (+). This indicates that the obligor’s capacity to meet its financial commitment on these obligations is extremely strong.

“A-2” – A short-term obligation rated “A-2” is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligations in higher rating categories. However, the obligor’s capacity to meet its financial commitments on the obligation is satisfactory.

“A-3” – A short-term obligation rated “A-3” exhibits adequate protection parameters. However, adverse economic conditions or changing circumstances are more likely to weaken an obligor’s capacity to meet its financial commitments on the obligation.

“B” – A short-term obligation rated “B” is regarded as vulnerable and has significant speculative characteristics. The obligor currently has the capacity to meet its financial commitments; however, it faces major ongoing uncertainties that could lead to the obligor’s inadequate capacity to meet its financial commitments.

“C” – A short-term obligation rated “C” is currently vulnerable to nonpayment and is dependent upon favorable business, financial, and economic conditions for the obligor to meet its financial commitments on the obligation.

“D” – A short-term obligation rated “D” is in default or in breach of an imputed promise. For non-hybrid capital instruments, the “D” rating category is used when payments on an obligation are not made on the date due, unless S&P Global Ratings believes that such payments will be made within any stated grace period. However, any stated grace period longer than five business days will be treated as five business days. The “D” rating also will be used upon the filing of a bankruptcy petition or the taking of a similar action and where default on an obligation is a virtual certainty, for example due to automatic stay provisions. An obligation’s rating is lowered to “D” if it is subject to a distressed exchange offer.

Local Currency and Foreign Currency Ratings – S&P Global Ratings’ issuer credit ratings make a distinction between foreign currency ratings and local currency ratings. A foreign currency rating on an issuer will differ from the local currency rating on it when the obligor has a different capacity to meet its obligations denominated in its local currency, vs. obligations denominated in a foreign currency.

Moody’s Investors Service (“Moody’s”) short-term ratings are forward-looking opinions of the relative credit risks of financial obligations with an original maturity of thirteen months or less and reflect both on the likelihood of a default or impairment on contractual financial obligations and the expected financial loss suffered in the event of default or impairment.

Moody’s employs the following designations to indicate the relative repayment ability of rated issuers:

“P-1” – Issuers (or supporting institutions) rated Prime-1 have a superior ability to repay short-term debt obligations.

“P-2” – Issuers (or supporting institutions) rated Prime-2 have a strong ability to repay short-term debt obligations.

“P-3” – Issuers (or supporting institutions) rated Prime-3 have an acceptable ability to repay short-term obligations.

“NP” – Issuers (or supporting institutions) rated Not Prime do not fall within any of the Prime rating categories.

“NR” – Is assigned to an unrated issuer.

Fitch, Inc. / Fitch Ratings Ltd. (“Fitch”) short-term issuer or obligation rating is based in all cases on the short-term vulnerability to default of the rated entity and relates to the capacity to meet financial obligations in accordance with the documentation governing the relevant obligation. Short-term deposit ratings may be adjusted for loss severity. Short-term ratings are assigned to obligations whose initial maturity is viewed as “short-term” based on market convention. Typically, this means up to 13 months for corporate, sovereign, and structured obligations and up to 36 months for obligations in U.S. public finance.
markets. The following summarizes the rating categories used by Fitch for short-term obligations:

“F1” – Securities possess the highest short-term credit quality. This designation indicates the strongest intrinsic capacity for timely payment of financial commitments; may have an added “+” to denote any exceptionally strong credit feature.

“F2” – Securities possess good short-term credit quality. This designation indicates good intrinsic capacity for timely payment of financial commitments.

“F3” – Securities possess fair short-term credit quality. This designation indicates that the intrinsic capacity for timely payment of financial commitments is adequate.

“B” – Securities possess speculative short-term credit quality. This designation indicates minimal capacity for timely payment of financial commitments, plus heightened vulnerability to near term adverse changes in financial and economic conditions.

“C” – Securities possess high short-term default risk. Default is a real possibility.

“RD” – Restricted default. Indicates an entity that has defaulted on one or more of its financial commitments, although it continues to meet other financial obligations. Typically applicable to entity ratings only.

“D” – Default. Indicates a broad-based default event for an entity, or the default of a short-term obligation.

Plus (+) or minus (-) – The “F1” rating may be modified by the addition of a plus (+) or minus (-) sign to show the relative status within that major rating category.

“NR” – Is assigned to an unrated issue of a rated issuer.

The DBRS® Ratings Limited (“DBRS”) short-term debt rating scale provides an opinion on the risk that an issuer will not meet its short-term financial obligations in a timely manner. Ratings are based on quantitative and qualitative considerations relevant to the issuer and the relative ranking of claims. The R-1 and R-2 rating categories are further denoted by the sub-categories “(high)”, “(middle)”, and “(low)”.

The following summarizes the ratings used by DBRS for commercial paper and short-term debt:

“R-1 (high)” - Short-term debt rated “R-1 (high)” is of the highest credit quality. The capacity for the payment of short-term financial obligations as they fall due is exceptionally high. Unlikely to be adversely affected by future events.

“R-1 (middle)” – Short-term debt rated “R-1 (middle)” is of superior credit quality. The capacity for the payment of short-term financial obligations as they fall due is very high. Differs from “R-1 (high)” by a relatively modest degree. Unlikely to be significantly vulnerable to future events.

“R-1 (low)” – Short-term debt rated “R-1 (low)” is of good credit quality. The capacity for the payment of short-term financial obligations as they fall due is substantial. Overall strength is not as favorable as higher rating categories. May be vulnerable to future events, but qualifying negative factors are considered manageable.

“R-2 (high)” – Short-term debt rated “R-2 (high)” is considered to be at the upper end of adequate credit quality. The capacity for the payment of short-term financial obligations as they fall due is acceptable. May be vulnerable to future events.

“R-2 (middle)” – Short-term debt rated “R-2 (middle)” is considered to be of adequate credit quality. The capacity for the payment of short-term financial obligations as they fall due is acceptable. May be vulnerable to future events or may be exposed to other factors that could reduce credit quality.

“R-2 (low)” – Short-term debt rated “R-2 (low)” is considered to be at the lower end of adequate credit quality. The capacity for the payment of short-term financial obligations as they fall due is acceptable. May be vulnerable to future events. A number of challenges are present that could affect the issuer’s ability to meet such obligations.

“R-3” – Short-term debt rated “R-3” is considered to be at the lowest end of adequate credit quality. There is a capacity for the payment of short-term financial obligations as they fall due. May be vulnerable to future events and the certainty of meeting such obligations could be impacted by a variety of developments.
“R-4” – Short-term debt rated “R-4” is considered to be of speculative credit quality. The capacity for the payment of short-term financial obligations as they fall due is uncertain.

“R-5” – Short-term debt rated “R-5” is considered to be of highly speculative credit quality. There is a high level of uncertainty as to the capacity to meet short-term financial obligations as they fall due.

“D” – Short-term debt rated “D” is assigned when the issuer has filed under any applicable bankruptcy, insolvency or winding up statute or there is a failure to satisfy an obligation after the exhaustion of grace periods, a downgrade to “D” may occur. DBRS may also use “SD” (Selective Default) in cases where only some securities are impacted, such as the case of a “distressed exchange”.

**Long-Term Credit Ratings**

The following summarizes the ratings used by S&P Global Ratings for long-term issues:

“AAA” – An obligation rated “AAA” has the highest rating assigned by S&P Global Ratings. The obligor’s capacity to meet its financial commitments on the obligation is extremely strong.

“AA” – An obligation rated “AA” differs from the highest-rated obligations only to a small degree. The obligor’s capacity to meet its financial commitments on the obligation is very strong.

“A” – An obligation rated “A” is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligations in higher-rated categories. However, the obligor’s capacity to meet its financial commitments on the obligation is still strong.

“BBB” – An obligation rated “BBB” exhibits adequate protection parameters. However, adverse economic conditions or changing circumstances are more likely to weaken the obligor’s capacity to meet its financial commitments on the obligation.

“BB,” “B,” “CCC,” “CC” and “C” – Obligations rated “BB,” “B,” “CCC,” “CC” and “C” are regarded as having significant speculative characteristics. “BB” indicates the least degree of speculation and “C” the highest. While such obligations will likely have some quality and protective characteristics, these may be outweighed by large uncertainties or major exposure to adverse conditions.

“BB” – An obligation rated “BB” is less vulnerable to nonpayment than other speculative issues. However, it faces major ongoing uncertainties or exposure to adverse business, financial, or economic conditions that could lead to the obligor’s inadequate capacity to meet its financial commitments on the obligation.

“B” – An obligation rated “B” is more vulnerable to nonpayment than obligations rated “BB”, but the obligor currently has the capacity to meet its financial commitments on the obligation. Adverse business, financial, or economic conditions will likely impair the obligor’s capacity or willingness to meet its financial commitments on the obligation.

“CCC” – An obligation rated “CCC” is currently vulnerable to nonpayment and is dependent upon favorable business, financial, and economic conditions for the obligor to meet its financial commitments on the obligation. In the event of adverse business, financial, or economic conditions, the obligor is not likely to have the capacity to meet its financial commitments on the obligation.

“CC” – An obligation rated “CC” is currently highly vulnerable to nonpayment. The “CC” rating is used when a default has not yet occurred but S&P Global Ratings expects default to be a virtual certainty, regardless of the anticipated time to default.

“C” – An obligation rated “C” is currently highly vulnerable to nonpayment, and the obligation is expected to have lower relative seniority or lower ultimate recovery compared with obligations that are rated higher.

“D” – An obligation rated “D” is in default or in breach of an imputed promise. For non-hybrid capital instruments, the “D” rating category is used when payments on an obligation are not made on the date due, unless S&P Global Ratings believes that such payments will be made within five business days in the absence of a stated grace period or within the earlier of the stated grace period or 30 calendar days. The “D” rating also will be used upon the filing of a bankruptcy petition or the taking of similar action and where default on an obligation is a virtual certainty, for example due to automatic stay provisions. An obligation’s rating is lowered to “D” if it is subject to a distressed exchange offer.
Plus (+) or minus (-) – The ratings from “AA” to “CCC” may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.

“NR” – This indicates that a rating has not been assigned, or is no longer assigned.

Local Currency and Foreign Currency Risks - S&P Global Ratings’ issuer credit ratings make a distinction between foreign currency ratings and local currency ratings. An issuer’s foreign currency rating will differ from its local currency rating when the obligor has a different capacity to meet its obligations denominated in its local currency, vs. obligations denominated in a foreign currency.

Moody’s long-term ratings are forward-looking opinions of the relative credit risks of financial obligations with an original maturity of one year or more. Such ratings reflect both on the likelihood of default or impairment on contractual financial obligations and the expected financial loss suffered in the event of default or impairment. The following summarizes the ratings used by Moody’s for long-term debt:

“Aaa” – Obligations rated “Aaa” are judged to be of the highest quality, subject to the lowest level of credit risk.

“Aa” – Obligations rated “Aa” are judged to be of high quality and are subject to very low credit risk.

“A” – Obligations rated “A” are judged to be upper-medium grade and are subject to low credit risk.

“Baa” – Obligations rated “Baa” are judged to be medium-grade and subject to moderate credit risk and as such may possess certain speculative characteristics.

“Ba” – Obligations rated “Ba” are judged to be speculative and are subject to substantial credit risk.

“B” – Obligations rated “B” are considered speculative and are subject to high credit risk.

“Caa” – Obligations rated “Caa” are judged to be speculative of poor standing and are subject to very high credit risk.

“Ca” – Obligations rated “Ca” are highly speculative and are likely in, or very near, default, with some prospect of recovery of principal and interest.

“C” – Obligations rated “C” are the lowest rated and are typically in default, with little prospect for recovery of principal or interest.

Note: Moody’s appends numerical modifiers 1, 2, and 3 to each generic rating classification from “Aa” through “Caa.” The modifier 1 indicates that the obligation ranks in the higher end of its generic rating category; the modifier 2 indicates a mid-range ranking; and the modifier 3 indicates a ranking in the lower end of that generic rating category.

“NR” – Is assigned to unrated obligations.

The following summarizes long-term ratings used by Fitch:

“AAA” – Securities considered to be of the highest credit quality. “AAA” ratings denote the lowest expectation of credit risk. They are assigned only in cases of exceptionally strong capacity for payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.

“AA” – Securities considered to be of very high credit quality. “AA” ratings denote expectations of very low credit risk. They indicate very strong capacity for payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.

“A” – Securities considered to be of high credit quality. “A” ratings denote expectations of low credit risk. The capacity for payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to adverse business or economic conditions than is the case for higher ratings.

“BBB” – Securities considered to be of good credit quality. “BBB” ratings indicate that expectations of credit risk are currently low. The capacity for payment of financial commitments is considered adequate, but adverse business or economic conditions are more likely to impair this capacity.
“BB” – Securities considered to be speculative. “BB” ratings indicate that there is an elevated vulnerability to credit risk, particularly in the event of adverse changes in business or economic conditions over time; however, business or financial alternatives may be available to allow financial commitments to be met.

“B” – Securities considered to be highly speculative. “B” ratings indicate that material credit risk is present.

“CCC” – A “CCC” rating indicates that substantial credit risk is present.

“CC” – A “CC” rating indicates very high levels of credit risk.

“C” – A “C” rating indicates exceptionally high levels of credit risk.

Defaulted obligations typically are not assigned “RD” or “D” ratings but are instead rated in the “CCC” to “C” rating categories, depending on their recovery prospects and other relevant characteristics. Fitch believes that this approach better aligns obligations that have comparable overall expected loss but varying vulnerability to default and loss.

Plus (+) or minus (-) may be appended to a rating to denote relative status within major rating categories. Such suffixes are not added to the “AAA” obligation rating category, or to corporate finance obligation ratings in the categories below “CCC”.

“NR” – Is assigned to an unrated issue of a rated issuer.

The DBRS long-term rating scale provides an opinion on the risk of default. That is, the risk that an issuer will fail to satisfy its financial obligations in accordance with the terms under which an obligation has been issued. Ratings are based on quantitative and qualitative considerations relevant to the issuer, and the relative ranking of claims. All rating categories other than AAA and D also contain subcategories “(high)” and “(low)”. The absence of either a “(high)” or “(low)” designation indicates the rating is in the middle of the category. The following summarizes the ratings used by DBRS for long-term debt:

“AAA” – Long-term debt rated “AAA” is of the highest credit quality. The capacity for the payment of financial obligations is exceptionally high and unlikely to be adversely affected by future events.

“AA” – Long-term debt rated “AA” is of superior credit quality. The capacity for the payment of financial obligations is considered high. Credit quality differs from “AAA” only to a small degree. Unlikely to be significantly vulnerable to future events.

“A” – Long-term debt rated “A” is of good credit quality. The capacity for the payment of financial obligations is substantial, but of lesser credit quality than “AA.” May be vulnerable to future events, but qualifying negative factors are considered manageable.

“BBB” – Long-term debt rated “BBB” is of adequate credit quality. The capacity for the payment of financial obligations is considered acceptable. May be vulnerable to future events.

“BB” – Long-term debt rated “BB” is of speculative, non-investment grade credit quality. The capacity for the payment of financial obligations is uncertain. Vulnerable to future events.

“B” – Long-term debt rated “B” is of highly speculative credit quality. There is a high level of uncertainty as to the capacity to meet financial obligations.

“CCC”, “CC” and “C” – Long-term debt rated in any of these categories is of very highly speculative credit quality. In danger of defaulting on financial obligations. There is little difference between these three categories, although “CC” and “C” ratings are normally applied to obligations that are seen as highly likely to default, or subordinated to obligations rated in the “CCC” to “B” range. Obligations in respect of which default has not technically taken place but is considered inevitable may be rated in the “C” category.

“D” – A security rated “D” is assigned when the issuer has filed under any applicable bankruptcy, insolvency or winding up statute or there is a failure to satisfy an obligation after the exhaustion of grace periods, a downgrade to “D” may occur. DBRS may also use “SD” (Selective Default) in cases where only some securities are impacted, such as the case of a “distressed exchange”.

**Municipal Note Ratings**

An S&P Global Ratings U.S. municipal note rating reflects S&P Global Ratings’ opinion about the liquidity factors and market access risks unique to the notes. Notes due in three years or less will likely receive a note rating. Notes with an original
maturity of more than three years will most likely receive a long-term debt rating. In determining which type of rating, if any, to assign, S&P Global Ratings’ analysis will review the following considerations:

- Amortization schedule - the larger the final maturity relative to other maturities, the more likely it will be treated as a note; and
- Source of payment - the more dependent the issue is on the market for its refinancing, the more likely it will be treated as a note.

Municipal Short-Term Note rating symbols are as follows:

“SP-1” – A municipal note rated “SP-1” exhibits a strong capacity to pay principal and interest. An issue determined to possess a very strong capacity to pay debt service is given a plus (+) designation.

“SP-2” – A municipal note rated “SP-2” exhibits a satisfactory capacity to pay principal and interest, with some vulnerability to adverse financial and economic changes over the term of the notes.

“SP-3” – A municipal note rated “SP-3” exhibits a speculative capacity to pay principal and interest.

“D” – This rating is assigned upon failure to pay the note when due, completion of a distressed exchange offer, or the filing of a bankruptcy petition or the taking of similar action and where default on an obligation is a virtual certainty, for example due to automatic stay provisions.

Moody’s uses the Municipal Investment Grade (“MIG”) scale to rate U.S. municipal bond anticipation notes of up to five years maturity. Municipal notes rated on the MIG scale may be secured by either pledged revenues or proceeds of a take-out financing received prior to note maturity. MIG ratings expire at the maturity of the obligation, and the issuer’s long-term rating is only one consideration in assigning the MIG rating. MIG ratings are divided into three levels – “MIG-1” through “MIG-3” while speculative grade short-term obligations are designated “SG”. The following summarizes the ratings used by Moody’s for short-term municipal obligations:

“MIG-1” – This designation denotes superior credit quality. Excellent protection is afforded by established cash flows, highly reliable liquidity support, or demonstrated broad-based access to the market for refinancing.

“MIG-2” – This designation denotes strong credit quality. Margins of protection are ample, although not as large as in the preceding group.

“MIG-3” – This designation denotes acceptable credit quality. Liquidity and cash-flow protection may be narrow, and market access for refinancing is likely to be less well-established.

“SG” – This designation denotes speculative-grade credit quality. Debt instruments in this category may lack sufficient margins of protection.

“NR” – Is assigned to an unrated obligation.

In the case of variable rate demand obligations (“VRDOs”), a two-component rating is assigned: a long or short-term debt rating and a demand obligation rating. The first element represents Moody’s evaluation of risk associated with scheduled principal and interest payments. The second element represents Moody’s evaluation of risk associated with the ability to receive purchase price upon demand (“demand feature”). The second element uses a rating from a variation of the MIG scale called the Variable Municipal Investment Grade or “VMIG” scale. The rating transitions on the VMIG scale differ from those on the Prime scale to reflect the risk that external liquidity support generally will terminate if the issuer’s long-term rating drops below investment grade.

“VMIG-1” – This designation denotes superior credit quality. Excellent protection is afforded by the superior short-term credit strength of the liquidity provider and structural and legal protections that ensure the timely payment of purchase price upon demand.

“VMIG-2” – This designation denotes strong credit quality. Good protection is afforded by the strong short-term credit strength of the liquidity provider and structural and legal protections that ensure the timely payment of purchase price upon demand.
“VMIG-3” – This designation denotes acceptable credit quality. Adequate protection is afforded by the satisfactory short-term credit strength of the liquidity provider and structural and legal protections that ensure the timely payment of purchase price upon demand.

“SG” – This designation denotes speculative-grade credit quality. Demand features rated in this category may be supported by a liquidity provider that does not have an investment grade short-term rating or may lack the structural and/or legal protections necessary to ensure the timely payment of purchase price upon demand.

“NR” – Is assigned to an unrated obligation.

**About Credit Ratings**

An **S&P Global Ratings** issue credit rating is a forward-looking opinion about the creditworthiness of an obligor with respect to a specific financial obligation, a specific class of financial obligations, or a specific financial program (including ratings on medium-term note programs and commercial paper programs). It takes into consideration the creditworthiness of guarantors, insurers, or other forms of credit enhancement on the obligation and takes into account the currency in which the obligation is denominated. The opinion reflects S&P Global Ratings’ view of the obligor’s capacity and willingness to meet its financial commitments as they come due, and this opinion may assess terms, such as collateral security and subordination, which could affect ultimate payment in the event of default.

Ratings assigned on **Moody’s** global long-term and short-term rating scales are forward-looking opinions of the relative credit risks of financial obligations issued by non-financial corporates, financial institutions, structured finance vehicles, project finance vehicles, and public sector entities.

**Fitch’s** credit ratings provide an opinion on the relative ability of an entity to meet financial commitments, such as interest, preferred dividends, repayment of principal, insurance claims or counterparty obligations. Fitch credit ratings are used by investors as indications of the likelihood of receiving the money owed to them in accordance with the terms on which they invested. Fitch’s credit ratings cover the global spectrum of corporate, sovereign financial, bank, insurance, and public finance entities (including supranational and sub-national entities) and the securities or other obligations they issue, as well as structured finance securities backed by receivables or other financial assets.

Credit ratings provided by **DBRS** are forward-looking opinions about credit risk which reflect the creditworthiness of an issuer, rated entity, and/or security. Credit ratings are not statements of fact. While historical statistics and performance can be important considerations, credit ratings are not based solely on such; they include subjective considerations and involve expectations for future performance that cannot be guaranteed. To the extent that future events and economic conditions do not match expectations, credit ratings assigned to issuers and/or securities can change. Credit ratings are also based on approved and applicable Methodologies (“Methodologies”), which are periodically updated and when material changes are deemed necessary, this may also lead to rating changes.

Credit ratings typically provide an opinion on the risk that investors may not be repaid in accordance with the terms under which the obligation was issued. In some cases, credit ratings may also include consideration for the relative ranking of claims and recovery, should default occur. Credit ratings are meant to provide opinions on relative measures of risk and are not based on expectations of any specific default probability, nor are they meant to predict such.

The data and information on which DBRS bases its opinions is not audited or verified by DBRS, although, DBRS conducts a reasonableness review of information received and relied upon in accordance with its Methodologies and policies.

DBRS uses rating symbols as a concise method of expressing its opinion to the market, but there are a limited number of rating categories for the possible slight risk differentials that exist across the rating spectrum and DBRS does not assert that credit ratings in the same category are of “exactly” the same quality.
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INTRODUCTION

ISS’ Social Advisory Services division recognizes that socially responsible investors have dual objectives: financial and social. Socially responsible investors invest for economic gain, as do all investors, but they also require that the companies in which they invest conduct their business in a socially and environmentally responsible manner.

These dual objectives carry through to socially responsible investors’ proxy voting activity once the security selection process is completed. In voting their shares, socially responsible institutional shareholders are concerned not only with sustainable economic returns to shareholders and good corporate governance but also with the ethical behavior of corporations and the social and environmental impact of their actions.

Social Advisory Services has, therefore, developed proxy voting guidelines that are consistent with the dual objectives of socially responsible shareholders. On matters of social and environmental import, the guidelines seek to reflect a broad consensus of the socially responsible investing community. Generally, we take as our frame of reference policies that have been developed by groups such as the Interfaith Center on Corporate Responsibility, the General Board of Pension and Health Benefits of the United Methodist Church, Domini Social Investments, and other leading church shareholders and socially responsible mutual fund companies. Additionally, we incorporate the active ownership and investment philosophies of leading globally recognized initiatives such as the United Nations Environment Programme Finance Initiative (UNEP FI), the United Nations Principles for Responsible Investment (UNPRI), the United Nations Global Compact, and environmental and social European Union Directives.

On matters of corporate governance, executive compensation, and corporate structure, Social Advisory Services guidelines are based on a commitment to create and preserve economic value and to advance principles of good corporate governance consistent with responsibilities to society as a whole.

The guidelines provide an overview of how Social Advisory Services recommends that its clients vote. We note that there may be cases in which the final vote recommendation on a particular company varies from the vote guideline due to the fact that we closely examine the merits of each proposal and consider relevant information and company-specific circumstances in arriving at our decisions. Where Social Advisory Services acts as voting agent for its clients, it follows each client’s voting policy, which may differ in some cases from the policies outlined in this document. Social Advisory Services updates its guidelines on an annual basis to take into account emerging issues and trends on environmental, social, and corporate governance topics, in addition to evolving market standards, regulatory changes, and client feedback.
1. BOARD OF DIRECTORS

A corporation’s board of directors sits at the apogee of the corporate governance system. Though they normally delegate responsibility for the management of the business to the senior executives they select and oversee, directors bear ultimate responsibility for the conduct of the corporation’s business. The role of directors in publicly held corporations has undergone considerable change in recent years. Once derided as rubber stamps for management, directors of public corporations today are expected to serve as effective guardians of shareholders’ interests.

Voting on directors and board-related issues is the most important use of the shareholder franchise, not simply a routine proxy item. Although uncontested director elections do not present alternative nominees from whom to choose, a high percentage of opposition votes is an expression of shareholder dissatisfaction and should be sufficient to elicit a meaningful response from management.

The role and responsibilities of directors has increasingly been the subject of much discussion and debate, given the current economic climate and the difficulties many companies now face in their respective markets. Influential organizations, including the American Law Institute, the American Bar Association, the National Association of Corporate Directors, and the Business Roundtable have issued reports and recommendations regarding the duties and accountability of corporate boards. Both mainstream and alternative media outlets have highlighted the numerous gaps within risk oversight of company boards and individual directors, and many institutional investors, in response, have capitalized on their rights as stakeholders to prompt changes. Corporations have taken notice, implementing many of the reforms championed by their shareholders.

Although differences of opinion remain, a fairly strong consensus has emerged on a number of key issues. It is widely agreed that the board’s most important responsibility is to ensure that the corporation is managed in the shareholders’ best long-term economic interest. This will often require boards to consider the impact of their actions on other constituencies, including employees, customers, local communities, and the environment.

› The board’s principal functions are widely agreed to consist of the following:
› To select, evaluate, and if necessary replace management, including the chief executive officer;
› To review and approve major strategies and financial objectives;
› To advise management on significant issues;
› To assure that effective controls are in place to safeguard corporate assets, manage risk, and comply with the law; and
› To nominate directors and otherwise ensure that the board functions effectively.

Boards are expected to have a majority of directors independent of management. The independent directors are expected to organize much of the board’s work, even if the chief executive officer also serves as Chairman of the board. Key committees of the board are expected to be entirely independent of management. It is expected that boards will engage in critical self-evaluation of themselves and of individual members. Individual directors, in turn, are expected to devote significant amounts of time to their duties, to limit the number of directorships they accept, and to own a meaningful amount of stock in companies on whose boards they serve. Directors are ultimately responsible to the corporation’s shareholders. The most direct expression of this responsibility is the requirement that directors be elected to their positions by the shareholders. Shareholders are also asked to vote on a number of other matters regarding the role, structure, and composition of the board. Social Advisory Services classifies directors as either inside directors, affiliated directors, or independent directors.
Uncontested Election of Directors

Social Advisory Services Recommendation: Vote on director nominees on a case-by-case basis.

Four broad principles apply when determining votes on director nominees:

1. **Board Accountability**: Accountability refers to the promotion of transparency into a company’s governance practices and annual board elections and the provision to shareholders the ability to remove problematic directors and to vote on takeover defenses or other charter/bylaw amendments. These practices help reduce the opportunity for management entrenchment.

2. **Board Responsiveness**: Directors should be responsive to shareholders, particularly in regard to shareholder proposals that receive a majority vote or management proposals that receive significant opposition and to tender offers where a majority of shares are tendered. Furthermore, shareholders should expect directors to devote sufficient time and resources to oversight of the company.

3. **Director Independence**: Without independence from management, the board may be unwilling or unable to effectively set company strategy and scrutinize performance or executive compensation.

4. **Director Diversity/Competence**: Companies should seek a diverse board of directors who can add value to the board through their specific skills or expertise and who can devote sufficient time and commitment to serve effectively. Boards should be of a size appropriate to accommodate diversity, expertise, and independence, while ensuring active and collaborative participation by all members. Boards should be sufficiently diverse to ensure consideration of a wide range of perspectives.

**Board Accountability**

Vote against\(^1\) or withhold from the entire board of directors (except new nominees\(^2\), who should be considered case-by-case) for the following:

*Problematic Takeover Defenses*

**Classified Board Structure**: The board is classified, and a continuing director responsible for a problematic governance issue at the board/committee level that would warrant an against/withhold recommendation is not up for election. All appropriate nominees (except new) may be held accountable.

**Removal of Shareholder Discretion on Classified Boards**: The company has opted into, or failed to opt out of, state laws requiring a classified board structure.

**Director Performance Evaluation**: The board lacks mechanisms to promote accountability and oversight, coupled with sustained poor performance relative to peers. Sustained poor performance is measured by one-, three-, and five-year

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\(^1\) In general, companies with a plurality vote standard use “Withhold” as the contrary vote option in director elections; companies with a majority vote standard use “Against”. However, it will vary by company and the proxy must be checked to determine the valid contrary vote option for the particular company.

\(^2\) A “new nominee” is any current nominee who has not already been elected by shareholders and who joined the board after the problematic action in question transpired. If Social Advisory Services cannot determine whether the nominee joined the board before or after the problematic action transpired, the nominee will be considered a “new nominee” if he or she joined the board within the 12 months prior to the upcoming shareholder meeting.
total shareholder returns in the bottom half of a company’s four-digit GICS industry group (Russell 3000 companies only). Take into consideration the company’s operational metrics and other factors as warranted. Problematic provisions include but are not limited to a classified board structure, supermajority vote requirements, a majority vote standard for director elections with no carve out for contested elections, inability for shareholders to call special meetings or act by written consent, a multi-class capital structure, and/or a non-shareholder approved poison pill.

**Poison Pills:** Vote against/withhold from all nominees if:
› The company has a poison pill that was not approved by shareholders. However, vote case-by-case on nominees if the board adopts an initial pill with a term of one year or less, depending on the disclosed rationale for the adoption, and other factors as relevant (such as a commitment to put any renewal to a shareholder vote).
› The board makes a material adverse modification to an existing pill, including, but not limited to, extension, renewal, or lowering the trigger, without shareholder approval.

**Problematic Audit-Related Practices**

Vote against/withhold from the members of the audit committee if:
› The non-audit fees paid to the auditor are excessive (see discussion under “Auditor Ratification”);
› The company receives an adverse opinion on the company’s financial statements from its auditor; or
› There is persuasive evidence that the audit committee entered into an inappropriate indemnification agreement with its auditor that limits the ability of the company, or its shareholders, to pursue legitimate legal recourse against the audit firm.

Vote case-by-case on members of the audit committee and potentially the full board if:
› Poor accounting practices are identified that rise to a level of serious concern, such as: fraud; misapplication of GAAP; and material weaknesses identified in Section 404 disclosures. Examine the severity, breadth, chronological sequence, and duration, as well as the company’s efforts at remediation or corrective actions, in determining whether withhold/against votes are warranted.

**Problematic Compensation Practices**

In the absence of an Advisory Vote on Executive Compensation (Say on Pay) ballot item, or, in egregious situations, vote against/withhold from members of the compensation committee and potentially the full board if:
› There is a significant misalignment between CEO pay and company performance (pay-for-performance);
› The company maintains significant problematic pay practices including options backdating, excessive perks and overly generous employment contracts etc.;
› The board exhibits a significant level of poor communication and responsiveness to shareholders;
› The company reprices underwater options for stock, cash, or other consideration without prior shareholder approval, even if allowed in the firm’s equity plan;
› The company fails to include a Say on Pay ballot item when required under SEC provisions, or under the company’s declared frequency of say on pay; or
› The company fails to include a Frequency of Say on Pay ballot item when required under SEC provisions.

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3 Public shareholders only, approval prior to a company’s becoming public is insufficient.
Generally vote against members of the board committee responsible for approving/setting non-employee director compensation if there is a pattern (i.e. two or more years) of awarding excessive non-employee director compensation without disclosing a compelling rationale or other mitigating factors.

**Problematic Pledging of Company Stock**

Vote against the members of the committee that oversees risks related to pledging, or the full board, where a significant level of pledged company stock by executives or directors raises concerns. The following factors will be considered:

- The presence of an anti-pledging policy, disclosed in the proxy statement, that prohibits future pledging activity;
- The magnitude of aggregate pledged shares in terms of total common shares outstanding, market value, and trading volume;
- Disclosure of progress or lack thereof in reducing the magnitude of aggregate pledged shares over time;
- Disclosure in the proxy statement that shares subject to stock ownership and holding requirements do not include pledged company stock; and
- Any other relevant factors.

**Environmental, Social and Governance (ESG) Failures**

Vote against/withhold from directors individually, committee members, or potentially the entire board, due to:

- Material failures of governance, stewardship, risk oversight, or fiduciary responsibilities at the company, including failure to adequately guard against or manage ESG risks;
- A lack of sustainability reporting in the company's public documents and/or website in conjunction with a failure to adequately manage or mitigate environmental, social and governance (ESG) risks;
- Failure to replace management as appropriate; or
- Egregious actions related to the director(s)’ service on other boards that raise substantial doubt about his or her ability to effectively oversee management and serve the best interests of shareholders at any company.

**Unilateral Bylaw/Charter Amendments and Problematic Capital Structures**

Generally vote against or withhold from directors individually, committee members, or the entire board (except new nominees, who should be considered case-by-case) if the board amends the company's bylaws or charter without shareholder approval in a manner that materially diminishes shareholders' rights or that could adversely impact shareholders. Considering the following factors:

- The board's rationale for adopting the bylaw/charter amendment without shareholder ratification;
- Disclosure by the company of any significant engagement with shareholders regarding the amendment;
- The level of impairment of shareholders' rights caused by the board's unilateral amendment to the bylaws/charter;
- The board's track record with regard to unilateral board action on bylaw/charter amendments or other entrenchment provisions;
- The company's ownership structure;
- The company's existing governance provisions;
- The timing of the board's amendment to the bylaws/charter in connection with a significant business development; and

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4 Examples of failure of risk oversight include but are not limited to: bribery; large or serial fines or sanctions from regulatory bodies; significant environmental incidents including spills and pollution; large scale or repeat workplace fatalities or injuries; significant adverse legal judgments or settlements; or hedging of company stock.
Other factors, as deemed appropriate, that may be relevant to determine the impact of the amendment on shareholders.

Unless the adverse amendment is reversed or submitted to a binding shareholder vote, in subsequent years vote case-by-case on director nominees. Generally vote against (except new nominees, who should be considered case-by-case) if the directors:
› Classified the board;
› Adopted supermajority vote requirements to amend the bylaws or charter; or
› Eliminated shareholders’ ability to amend bylaws.

Problematic Governance Structure – Newly public companies

For newly public companies, generally vote against or withheld from directors individually, committee members, or the entire board (except new nominees, who should be considered case-by-case) if, prior to or in connection with the company’s public offering, the company or its board adopted bylaw or charter provisions materially adverse to shareholder rights, or implemented a multi-class capital structure in which the classes have unequal voting rights considering the following factors:
› The level of impairment of shareholders’ rights caused by the provision;
› The disclosed rationale;
› The ability to change the governance structure (e.g., limitations on shareholders’ right to amend the bylaws or charter, or supermajority vote requirements to amend the bylaws or charter);
› The ability of shareholders to hold directors accountable through annual director elections, or whether the company has a classified board structure;
› Any reasonable sunset provision; and
› Other relevant factors.

Unless the adverse provision and/or problematic capital structure is reversed or removed, vote case-by-case on director nominees in subsequent years.

Management Proposals to Ratify Existing Charter or Bylaw Provisions:

Vote against/withhold from individual directors, members of the governance committee, or the full board, where boards ask shareholders to ratify existing charter or bylaw provisions considering the following factors:
› The presence of a shareholder proposal addressing the same issue on the same ballot;
› The board’s rationale for seeking ratification;
› Disclosure of actions to be taken by the board should the ratification proposal fail;
› Disclosure of shareholder engagement regarding the board’s ratification request;
› The level of impairment to shareholders’ rights caused by the existing provision;
› The history of management and shareholder proposals on the provision at the company’s past meetings;
› Whether the current provision was adopted in response to the shareholder proposal;
› The company’s ownership structure; and
› Previous use of ratification proposals to exclude shareholder proposals.

Restrictions on Shareholders’ Rights: Restricting Binding Shareholder Proposals

Generally vote against or withhold from members of the governance committee if:
› The company’s governing documents impose undue restrictions on shareholders’ ability to amend the bylaws. Such restrictions include, but are not limited to: outright prohibition on the submission of binding shareholder
proposals, or share ownership requirements or time holding requirements in excess of SEC Rule 14a-8. Vote against on an ongoing basis.

**Board Responsiveness**

Vote case-by-case on individual directors, committee members, or the entire board of directors as appropriate if:

› The board failed to act on a shareholder proposal that received the support of a majority of the shares cast in the previous year or failed to act on a management proposal seeking to ratify an existing charter/bylaw provision that received opposition of a majority of the shares cast in the previous year. Factors that will be considered are:
  ‣ Disclosed outreach efforts by the board to shareholders in the wake of the vote;
  ‣ Rationale provided in the proxy statement for the level of implementation;
  ‣ The subject matter of the proposal;
  ‣ The level of support for and opposition to the resolution in past meetings;
  ‣ Actions taken by the board in response to the majority vote and its engagement with shareholders;
  ‣ The continuation of the underlying issue as a voting item on the ballot (as either shareholder or management proposals); and
  ‣ Other factors as appropriate.
› The board failed to act on takeover offers where the majority of shares are tendered;
› At the previous board election, any director received more than 50 percent withhold/against votes of the shares cast and the company has failed to address the issue(s) that caused the high withhold/against vote.

Vote case-by-case on compensation Committee members (or, in exceptional cases, the full board) and the Say on Pay proposal if:

› The company’s previous say-on-pay received the support of less than 70 percent of votes cast. Factors that will be considered are:
  ‣ The company’s response, including:
    ‣ Disclosure of engagement efforts with major institutional investors regarding the issues that contributed to the low level of support (including the timing and frequency of engagements and whether independent directors participated);
    ‣ Disclosure of the specific concerns voiced by dissenting shareholders that led to the say-on-pay opposition;
    ‣ Disclosure of specific and meaningful actions taken to address shareholders’ concerns;
  ‣ Other recent compensation actions taken by the company;
  ‣ Whether the issues raised are recurring or isolated;
  ‣ The company’s ownership structure; and
  ‣ Whether the support level was less than 50 percent, which would warrant the highest degree of responsiveness.
  ‣ The board implements an advisory vote on executive compensation on a less frequent basis than the frequency that received the plurality of votes cast.

**Director Independence**

Vote against/withhold from the entire board if the full board is less than majority independent.

Vote against/withhold from non-independent directors (executive directors and non-independent non-executive directors per the Categorization of Directors) when:

› The non-independent director serves on the audit, compensation, or nominating committee;
› The company lacks an audit, compensation, or nominating committee so that the full board functions as that committee; or
› The company lacks a formal nominating committee, even if the board attests that the independent directors fulfill the functions of such a committee.

**Director Diversity/Competence**

**Board Diversity**

Vote against/withhold from individual directors (except new nominees) who:

› Serve as members of the nominating committee and the board lacks at least one woman and one racially diverse director, and the board is not at least 30 percent diverse. If the company does not have a formal nominating committee, vote against/withhold votes from the entire board of directors.

**Competence**

**Attendance at Board and Committee Meetings**

› Generally vote against or withhold from directors (except new nominees,\(^5\)) who attend less than 75 percent of the aggregate of their board and committee meetings for the period for which they served, unless an acceptable reason for absences is disclosed in the proxy or another SEC filing. Acceptable reasons for director absences are generally limited to the following:
  › Medical issues/illness;
  › Family emergencies; and
  › If the director’s total service was three meetings or fewer and the director missed only one meeting.

› In cases of chronic poor attendance without reasonable justification, in addition to voting against the director(s) with poor attendance, generally vote against or withhold from appropriate members of the nominating/governance committees or the full board.

› If the proxy disclosure is unclear and insufficient to determine whether a director attended at least 75 percent of the aggregate of his/her board and committee meetings during his/her period of service, vote against or withhold from the director(s) in question.

**Overboarded Directors**

Vote against or withhold from individual directors who:

› Sit on more than five public company boards; or
› Are CEOs of public companies who sit on the boards of more than two public companies besides their own — withhold only at their outside boards\(^6\).

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\(^5\) New nominees who served for only part of the fiscal year are generally exempted from the attendance policy.

\(^6\) Although all of a CEO’s subsidiary boards will be counted as separate boards, Social Advisory Services will not recommend a withhold vote for the CEO of a parent company board or any of the controlled (>50 percent ownership) subsidiaries of that parent, but may do so at subsidiaries that are less than 50 percent controlled and boards outside the parent/subsidiary relationships.
# 2019 Classification of Directors – U.S.

<table>
<thead>
<tr>
<th>1. <strong>Executive Director</strong></th>
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<tbody>
<tr>
<td>1.1. Current employee or current officer(^i) of the company or one of its affiliates(^ii).</td>
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<table>
<thead>
<tr>
<th>2. <strong>Non-Independent Non-Executive Director</strong></th>
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<tbody>
<tr>
<td><strong>Board Identification</strong></td>
<td></td>
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<tr>
<td>2.1. Director identified as not independent by board.</td>
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<tr>
<td><strong>Controlling/Significant Shareholder</strong></td>
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<tr>
<td>2.2. Beneficial owner of more than 50 percent of the company's voting power (this may be aggregated if voting power is distributed among more than one member of a group).</td>
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<tr>
<td><strong>Former CEO/Interim Officer</strong></td>
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<tr>
<td>2.3. Former CEO of the company(^iii,iv).</td>
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<tr>
<td>2.4. Former CEO of an acquired company within the past five years(^v).</td>
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<tr>
<td>2.5. Former interim officer if the service was longer than 18 months. If the service was between 12 and 18 months an assessment of the interim officer’s employment agreement will be made(^v).</td>
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<tr>
<td><strong>Non-CEO Executives</strong></td>
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<tr>
<td>2.6. Former officer(^i) of the company, an affiliate(^d) or an acquired firm within the past five years.</td>
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<tr>
<td>2.7. Officer(^i) of a former parent or predecessor firm at the time the company was sold or split off from the parent/predecessor within the past five years.</td>
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<tr>
<td>2.8. Officer(^i), former officer, or general or limited partner of a joint venture or partnership with the company.</td>
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<tr>
<td><strong>Family Members</strong></td>
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<tr>
<td>2.9. Immediate family member(^vi) of a current or former officer(^i) of the company or its affiliates(^ii) within the last five years.</td>
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<tr>
<td>2.10. Immediate family member(^vi) of a current employee of company or its affiliates(^ii) where additional factors raise concern (which may include, but are not limited to, the following: a director related to numerous employees; the company or its affiliates employ relatives of numerous board members; or a non-Section 16 officer in a key strategic role).</td>
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<tr>
<td><strong>Transaction, Professional, Financial, and Charitable Relationships</strong></td>
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<tr>
<td>2.11. Currently provides (or an immediate family member(^vi) provides) professional services(^vii) to the company, to an affiliate(^d) of the company or an individual officer of the company or one of its affiliates in excess of $10,000 per year.</td>
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<tr>
<td>2.12. Is (or an immediate family member(^vi) is) a partner in, or a controlling shareholder or an employee of, an organization which provides professional services(^vii) to the company, to an affiliate(^d) of the company, or an individual officer of the company or one of its affiliates in excess of $10,000 per year.</td>
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<tr>
<td>2.13. Has (or an immediate family member(^vi) has) any material transactional relationship(^viii) with the company or its affiliates(^d) (excluding investments in the company through a private placement).</td>
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<tr>
<td>2.14. Is (or an immediate family member(^vi) is) a partner in, or a controlling shareholder or an executive officer of, an organization which has any material transactional relationship(^viii) with the company or its affiliates(^d) (excluding investments in the company through a private placement).</td>
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<tr>
<td>2.15. Is (or an immediate family member(^vi) is) a trustee, director, or employee of a charitable or non-profit organization that receives material grants or endowments(^viii) from the company or its affiliates(^d).</td>
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<tr>
<td><strong>Other Relationships</strong></td>
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<tr>
<td>2.16. Party to a voting agreement(^x) to vote in line with management on proposals being brought to shareholder vote.</td>
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<tr>
<td>2.17. Has (or an immediate family member(^x) has) an interlocking relationship as defined by the SEC involving members of the board of directors or its compensation committee(^x).</td>
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<tr>
<td>2.18. Founder(^x) of the company but not currently an employee.</td>
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<tr>
<td>2.19. Any material(^x) relationship with the company.</td>
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<tr>
<th>3. <strong>Independent Director</strong></th>
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<tbody>
<tr>
<td>3.1. No material(^x) connection to the company other than a board seat.</td>
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**Footnotes:**
The definition of officer will generally follow that of a “Section 16 officer” (officers subject to Section 16 of the Securities and Exchange Act of 1934) and includes the chief executive, operating, financial, legal, technology, and accounting officers of a company (including the president, treasurer, secretary, controller, or any vice president in charge of a principal business unit, division, or policy function). Current interim officers are included in this category. For private companies, the equivalent positions are applicable. A non-employee director serving as an officer due to statutory requirements (e.g. corporate secretary) will be classified as an Affiliated Outsider under 2.18: “Any material relationship with the company.” However, if the company provides explicit disclosure that the director is not receiving additional compensation in excess of $10,000 per year for serving in that capacity, then the director will be classified as an Independent Outsider.

“Affiliate” includes a subsidiary, sibling company, or parent company. Social Advisory Services uses 50 percent control ownership by the parent company as the standard for applying its affiliate designation.

“Immediate family member” follows the SEC’s definition of such and covers spouses, parents, children, step-parents, step-children, siblings, in-laws, and any person (other than a tenant or employee) sharing the household of any director, nominee for director, executive officer, or significant shareholder of the company.

Professional services can be characterized as advisory in nature, generally involve access to sensitive company information or to strategic decision-making, and typically have a commission- or fee-based payment structure. Professional services generally include, but are not limited to the following: investment banking/financial advisory services; commercial banking (beyond deposit services); investment services; insurance services; accounting/audit services; consulting services; marketing services; legal services; property management services; realtor services; lobbying services; executive search services; and IT consulting services. The following would generally be considered transactional relationships and not professional services: deposit services; IT tech support services; educational services; and construction services. The case of participation in a banking syndicate by a non-lead bank should be considered a transactional (and hence subject to the associated materiality test) rather than a professional relationship. “Of Counsel” relationships are only considered immaterial if the individual does not receive any form of compensation (in excess of $10,000 per year) from, or is a retired partner of, the firm providing the professional service. The case of a company providing a professional service to one of its directors or to an entity with which one of its directors is affiliated, will be considered a transactional rather than a professional relationship. Insurance services and marketing services are assumed to be professional services unless the company explains why such services are not advisory.

A material transactional relationship, including grants to non-profit organizations, exists if the company makes annual payments to, or receives annual payments from, another entity exceeding the greater of $200,000 or 5 percent of the recipient’s gross revenues, in the case of a company which follows NYSE listing standards; or the greater of $1,000,000 or 2 percent of the recipient’s gross revenues, in the case of a company which follows NASDAQ listing standards. In the case of a company which follows neither of the preceding standards, Social Advisory Services will apply the NASDAQ-based materiality test. (The recipient is the party receiving the financial proceeds from the transaction).

Dissident directors who are parties to a voting agreement pursuant to a settlement or similar arrangement may be classified as independent outsiders if an analysis of the following factors indicates that the voting agreement
does not compromise their alignment with all shareholders’ interests: the terms of the agreement; the duration of the standstill provision in the agreement; the limitations and requirements of actions that are agreed upon; if the dissident director nominee(s) is subject to the standstill; and if there any conflicting relationships or related party transactions.

* Interlocks include: executive officers serving as directors on each other’s compensation or similar committees (or, in the absence of such a committee, on the board); or executive officers sitting on each other’s boards and at least one serves on the other’s compensation or similar committees (or, in the absence of such a committee, on the board).

** The operating involvement of the founder with the company will be considered; if the founder was never employed by the company, Social Advisory Services may deem him or her an independent outsider.

*** For purposes of Social Advisory Services' director independence classification, “material” will be defined as a standard of relationship (financial, personal or otherwise) that a reasonable person might conclude could potentially influence one’s objectivity in the boardroom in a manner that would have a meaningful impact on an individual's ability to satisfy requisite fiduciary standards on behalf of shareholders.

Board-Related Management Proposals

**Classification/Declassification of the Board**

Under a classified board structure only one class of directors would stand for election each year, and the directors in each class would generally serve three-year terms. Although staggered boards can provide continuity for companies at the board level, there are also a number of downsides to the structure. First, a classified board can also be used to entrench management and effectively preclude most takeover bids or proxy contests. Board classification forces dissidents and would-be acquirers to negotiate with the incumbent board, which has the authority to decide on offers without a shareholder vote. In addition, when a board is classified, it is difficult to remove individual members for either poor attendance or poor performance; shareholders would only have the chance to vote on a given director every third year when he or she comes up for election. The classified board structure can also limit shareholders’ ability to withhold votes from inside directors that sit on key board committee, or to withhold votes from an entire board slate to protest the lack of board diversity. According to ISS’ 2012 Board Practices study, the number of S&P 500 companies with classified boards has continued to fall. In 2015, only 17 percent of S&P 500 companies maintained staggered boards, compared to 25 percent in 2014, 30 percent in 2013, and 39 percent in 2010. While we recognize that there are some advantages to classified boards, based on the latest studies on classified boards, the fact that classified boards can make it more difficult for shareholders to remove individual directors, and the fact that classified boards can be used as an antitakeover device, Social Advisory Services recommends against the adoption of classified boards.

**Social Advisory Services Recommendation:**

› Vote for proposals to repeal classified boards and to elect all directors annually.
› Vote against proposals to classify (stagger) the board of directors.

**Majority Vote Threshold for Director Elections**

**Social Advisory Services Recommendation:** Generally vote for management proposals to adopt a majority of votes cast standard for directors in uncontested elections.

Vote against if no carve-out for plurality in contested elections is included.
Cumulative Voting

Most corporations provide that shareholders are entitled to cast one vote for each share owned. Under a cumulative voting scheme the shareholder is permitted to have one vote per share for each director to be elected. Shareholders are permitted to apportion those votes in any manner they wish among the director candidates. Shareholders have the opportunity to elect a minority representative to a board through cumulative voting, thereby ensuring representation for all sizes of shareholders. For example, if there is a company with a ten-member board and 500 shares outstanding—the total number of votes that may be cast is 5,000. In this case a shareholder with 51 shares (10.2 percent of the outstanding shares) would be guaranteed one board seat because all votes may be cast for one candidate.

Social Advisory Services Recommendation: Generally vote against management proposals to eliminate cumulative voting, and for shareholder proposals to restore or provide for cumulative voting unless:

- The company has proxy access, thereby allowing shareholders to nominate directors to the company’s ballot; and
- The company has adopted a majority vote standard, with a carve-out for plurality voting in situations where there are more nominees than seats, and a director resignation policy to address failed elections.

Vote for proposals for cumulative voting at controlled companies (insider voting power > 50%).

Director and Officer Liability Protection

Management proposals typically seek shareholder approval to adopt an amendment to the company’s charter to eliminate or limit the personal liability of directors to the company and its shareholders for monetary damages for any breach of fiduciary duty to the fullest extent permitted by state law. In contrast, shareholder proposals seek to provide for personal monetary liability for fiduciary breaches arising from gross negligence. While Social Advisory Services recognizes that a company may have a more difficult time attracting and retaining directors if they are subject to personal monetary liability, Social Advisory Services believes the great responsibility and authority of directors justifies holding them accountable for their actions. Each proposal addressing director liability will be evaluated on a case-by-case basis consistent with this philosophy using Delaware law as the standard. Social Advisory Services may support these proposals when the company persuasively argues that such action is necessary to attract and retain directors, but may oppose management proposals and support shareholder proposals in light of promoting director accountability.

Social Advisory Services Recommendation: Vote against proposals to limit or eliminate entirely director and officer liability for monetary damages for: (i) a breach of the duty of care; (ii) acts or omissions not in good faith or involving intentional misconduct or knowing violations of the law; (iii) acts involving the unlawful purchases or redemptions of stock; (iv) the payment of unlawful dividends; or (v) the receipt of improper personal benefits.

Director and Officer Indemnification

Indemnification is the payment by a company of the expenses of directors who become involved in litigation as a result of their service to a company. Proposals to indemnify a company’s directors differ from those to eliminate or reduce their liability because with indemnification, directors may still be liable for an act or omission, but the company will bear the expense. Social Advisory Services may support these proposals when the company persuasively argues that such action is necessary to attract and retain directors, but will generally oppose indemnification when it is being proposed to insulate directors from actions they have already taken.

7 A proxy access right that meets the recommended guidelines.
Social Advisory Services Recommendation:

› Vote against indemnification proposals that would expand coverage beyond just legal expenses to acts, such as negligence, that are more serious violations of fiduciary obligations than mere carelessness.
› Vote against proposals that would expand the scope of indemnification to provide for mandatory indemnification of company officials in connection with acts that previously the company was permitted to provide indemnification for at the discretion of the company’s board (i.e., "permissive indemnification") but that previously the company was not required to indemnify.
› Vote for only those proposals that provide such expanded coverage in cases when a director’s or officer’s legal defense was unsuccessful if: (i) the director was found to have acted in good faith and in a manner that the director reasonably believed was in the best interests of the company; and (ii) only if the director’s legal expenses would be covered.

Shareholder Ability to Remove Directors/Fill Vacancies

Shareholder ability to remove directors, with or without cause, is either prescribed by a state’s business corporation law, an individual company’s articles of incorporation, or its bylaws. Many companies have sought shareholder approval for charter or bylaw amendments that would prohibit the removal of directors except for cause, thus ensuring that directors would retain their directorship for their full-term unless found guilty of self-dealing. By requiring cause to be demonstrated through due process, management insulates the directors from removal even if a director has been performing poorly, not attending meetings, or not acting in the best interests of shareholders.

Social Advisory Services Recommendation:

› Vote against proposals that provide that directors may be removed only for cause.
› Vote against proposals that provide that only continuing directors may elect replacements to fill board vacancies.
› Vote for proposals that permit shareholders to elect directors to fill board vacancies.

Board Size

Proposals which would allow management to increase or decrease the size of the board at its own discretion are often used by companies as a takeover defense. Social Advisory Services supports management proposals to fix the size of the board at a specific number, thus preventing management, when facing a proxy contest, from increasing the board size without shareholder approval. By increasing the size of the board, management can make it more difficult for dissidents to gain control of the board. Fixing the size of the board also prevents a reduction in the size of the board as a strategy to oust independent directors. Fixing board size also prevents management from increasing the number of directors in order to dilute the effects of cumulative voting.

Social Advisory Services Recommendation:

› Vote for proposals that seek to fix the size of the board.
› Vote against proposals that seek to change the size or range of the board.
› Vote against proposals that give management the ability to alter the size of the board outside of a specific range without shareholder approval.

Establish/Amend Nominee Qualifications

Social Advisory Services Recommendation: Vote case-by-case on proposals that establish or amend director qualifications. Votes should be based on how reasonable the criteria are and to what degree they may preclude dissident nominees from joining the board.
Term Limits

Social Advisory Services Recommendation: Vote against management proposals to limit the tenure of outside directors through term limits. However, scrutinize boards where the average tenure of all directors exceeds 15 years for independence from management and for sufficient turnover to ensure that new perspectives are being added to the board.

Age Limits

Social Advisory Services Recommendation: Vote against management proposal to limit the tenure of outside directors through mandatory retirement ages.

Board-Related Shareholder Proposals/Initiatives

Proxy Contests/Proxy Access- Voting for Director Nominees in Contested Elections

Contested elections of directors frequently occur when a board candidate or slate runs for the purpose of seeking a significant change in corporate policy or control. Competing slates will be evaluated based upon the personal qualifications of the candidates, the economic impact of the policies that they advance, and their expressed and demonstrated commitment to the interests of all shareholders.

Social Advisory Services Recommendation: Votes in a contested election of directors are evaluated on a case-by-case basis, considering the following factors:
› Long-term financial performance of the target company relative to its industry;
› Management’s track record;
› Background to the proxy contest;
› Qualifications of director nominees (both slates);
› Strategic plan of dissident slate and quality of critique against management;
› Likelihood that the proposed goals and objectives can be achieved (both slates);
› Stock ownership positions; and
› Impact on stakeholders, such as job loss, community lending, equal opportunity, impact on environment.

In the case of candidates nominated pursuant to proxy access, vote case-by-case considering any applicable factors listed above or additional factors which may be relevant, including those that are specific to the company, to the nominee(s) and/or to the nature of the election (such as whether or not there are more candidates than board seats).

Annual Election (Declassification) of the Board

Social Advisory Services Recommendation: Vote for shareholder proposals to repeal classified (staggered) boards and to elect all directors annually.

Vote against proposals to classify the board.

Majority Threshold Voting Shareholder Proposals

A majority vote standard requires that for directors to be elected (or re-elected) to serve on the company's board they must receive support from holders of a majority of shares voted. Shareholders have expressed strong support for shareholder proposals on majority threshold voting. Social Advisory Services believes shareholders should have a greater voice in the election of directors and believes majority threshold voting represents a viable alternative to the plurality system in the U.S. Companies are strongly encouraged to also adopt a post-election policy (also known as a
director resignation policy) that will provide guidelines so that the company will promptly address the situation of a holdover director.

**Social Advisory Services Recommendation:** Vote for precatory and binding resolutions requesting that the board change the company’s bylaws to stipulate that directors need to be elected with an affirmative majority of votes cast, provided it does not conflict with the state law where the company is incorporated. Binding resolutions need to allow for a carve-out for a plurality vote standard when there are more nominees than board seats.

**Majority of Independent Directors**

Social Advisory Services believes that a board independent from management is of vital importance to a company and its shareholders. Accordingly, Social Advisory Services will cast votes in a manner that shall encourage the independence of boards.

**Social Advisory Services Recommendation:**

› Vote for shareholder proposals asking that a majority or more of directors be independent unless the board composition already meets the proposed threshold by Social Advisory Services’ definition of independence.

› Vote for shareholder proposals to strengthen the definition of independence for board directors.

**Establishment of Independent Committees**

Most corporate governance experts agree that the key board committees (audit, compensation, and nominating/corporate governance) of a corporation should include only independent directors. The independence of key committees has been encouraged by regulation. Social Advisory Services believes that initiatives to increase the independent representation of these committees or to require that these committees be independent should be supported.

**Social Advisory Services Recommendation:** Vote for shareholder proposals asking that board audit, compensation, and/or nominating committees be composed exclusively of independent directors.

**Independent Board Chair**

One of the principle functions of the board is to monitor and evaluate the performance of the CEO. The chairperson’s duty to oversee management is obviously compromised when he or she is required to monitor himself or herself. Generally Social Advisory Services recommends a vote for shareholder proposals that would require that the position of board chair be held by an individual with no materials ties to the company other than their board seat.

**Social Advisory Services Recommendation:** Vote for shareholder proposals that would require the board chair to be independent of management.

**Establishment of Board Committees**

**Social Advisory Services Recommendation:** Generally vote for shareholder proposals to establish a new board committee to address broad corporate policy topics or to provide a forum for ongoing dialogue on issues such as the environment, human or labor rights, shareholder relations, occupational health and safety etc. when the formation of such committees appears to be a potentially effective method of protecting or enhancing shareholder value. In evaluating such proposals, the following factors will be considered:
Establish/Amend Nominee Qualifications

Social Advisory Services Recommendation: Vote case-by-case on proposals that establish or amend director qualifications. Votes should be based on the reasonableness of the criteria and to what degree they may preclude dissident nominees from joining the board.

Vote case-by-case on proposals that establish or amend director qualifications. Votes should be based on the reasonableness of the criteria and to what degree they may preclude dissident nominees from joining the board.

Vote case-by-case on shareholder resolutions seeking a director nominee candidate who possesses a particular subject matter expertise, considering:

› The company’s board committee structure, existing subject matter expertise, and board nomination provisions relative to that of its peers;
› The company’s existing board and management oversight mechanisms regarding the issue for which board oversight is sought;
› The company’s disclosure and performance relating to the issue for which board oversight is sought and any significant related controversies; and
› The scope and structure of the proposal.

Board Policy on Shareholder Engagement

Social Advisory Services Recommendation: Vote for shareholders proposals requesting that the board establish an internal mechanism/process, which may include a committee, in order to improve communications between directors and shareholders, unless the company has the following features, as appropriate:

› Established a communication structure that goes beyond the exchange requirements to facilitate the exchange of information between shareholders and members of the board;
› Effectively disclosed information with respect to this structure to its shareholders;
› The company has not ignored majority-supported shareholder proposals or a majority withhold vote on a director nominee; and
› The company has an independent chairman or a lead director (according to Social Advisory Services’ definition). This individual must be made available for periodic consultation and direct communication with major shareholders.

Proxy Access

Social Advisory Services supports proxy access as an important shareholder right, one that is complementary to other best-practice corporate governance features. However, in the absence of a uniform standard, proposals to enact proxy access may vary widely; as such, a case-by-case approach will be undertaken in evaluating these proposals.
Social Advisory Services Recommendation: Generally vote for management and shareholder proposals for proxy access with the following provisions:

› Ownership threshold: maximum requirement not more than three percent (3%) of the voting power;
› Ownership duration: maximum requirement not longer than three (3) years of continuous ownership for each member of the nominating group;
› Aggregation: minimal or no limits on the number of shareholders permitted to form a nominating group;
› Cap: cap on nominees of generally twenty-five percent (25%) of the board.

Review for reasonableness any other restrictions on the right of proxy access.

Generally vote against proposals that are more restrictive than these guidelines.

Term Limits

Supporters of term limits argue that this requirement would bring new ideas and approaches to a board. However, we prefer to look at directors and their contributions to the board individually rather than impose a strict rule.

Social Advisory Services Recommendation: Vote against shareholder proposals to limit the tenure of outside directors. However, scrutinize boards where the average tenure of all directors exceeds 15 years for independence from management and for sufficient turnover to ensure that new perspectives are being added to the board.

Age Limits

Social Advisory Services Recommendation: Vote against shareholder proposals to limit the tenure of outside directors through mandatory retirement ages.

CEO Succession Planning

Social Advisory Services Recommendation: Generally vote for proposals seeking disclosure on a CEO succession planning policy, considering at a minimum, the following factors:

› The reasonableness/scope of the request; and
› The company’s existing disclosure on its current CEO succession planning process.

Vote No Campaigns

Social Advisory Services Recommendation: In cases where companies are targeted in connection with public “vote no” campaigns, evaluate director nominees under the existing governance policies for voting on director nominees in uncontested elections. Take into consideration the arguments submitted by shareholders and other publicly available information.
2. RATIFICATION OF AUDITORS

Annual election of the outside accountants is best practice standard. While it is recognized that the company is in the best position to evaluate the competence of the outside accountants, we believe that outside accountants must ultimately be accountable to shareholders. A Blue Ribbon Commission report concluded that audit committees must improve their current level of oversight of independent accountants. Given the rash of accounting misdeeds that were not detected by audit panels or auditors, shareholder ratification is an essential step in restoring investor confidence. Shareholders should have the right to weigh in on the choice of the audit firm, and all companies should put ratification on the ballot of their annual meeting. Special consideration will be given when non-audit fees exceed audit fees, as high non-audit fees can compromise the independence of the auditor. Social Advisory Services will also monitor both auditor tenure and whether auditor ratification has been pulled from the ballot.

Social Advisory Services Recommendation: Vote for proposals to ratify auditors, unless any of the following apply:

› The non-audit fees paid represent 25 percent or more of the total fees paid to the auditor;
› An auditor has a financial interest in or association with the company, and is therefore not independent;
› There is reason to believe that the independent auditor has rendered an opinion that is neither accurate nor indicative of the company’s financial position; or
› Poor accounting practices are identified that rise to a serious level of concern, such as: fraud; misapplication of GAAP; and material weaknesses identified in Section 404 disclosures.

Auditor-Related Shareholder Proposals

Ratify Auditors/Ensure Auditor Independence

These shareholder proposals request that the board allow shareholders to ratify the company’s auditor at each annual meeting. Annual ratification of the outside accountants is standard practice. While it is recognized that the company is in the best position to evaluate the competence of the outside accountants, we believe that outside accountants must ultimately be accountable to shareholders.

Given the rash of accounting irregularities that were not detected by audit panels or auditors, shareholder ratification is an essential step in restoring investor confidence. Social Advisory Services believes that shareholders should have the ability to ratify the auditor on an annual basis.

Social Advisory Services Recommendation:
› Vote for shareholder proposals to allow shareholders to vote on auditor ratification.
› Vote for proposals that ask a company to adopt a policy on auditor independence.
› Vote for proposals that seek to limit the non-audit services provided by the company’s auditor.

Auditor Rotation

To minimize any conflict of interest that may rise between the company and its auditor, Social Advisory Services supports the rotation of auditors. Currently, SEC rules provide that partners should be rotated every five years. However, Social Advisory Services also believes that the long tenure of audit firms at U.S. companies can be problematic.

Social Advisory Services Recommendation: Vote for shareholder proposals to rotate company’s auditor every five years or more. Social Advisory Services believes that proposing a rotation period less than five years is unreasonably restrictive and may negatively affect audit quality and service while increasing expense.
3. TAKEOVER DEFENSES / SHAREHOLDER RIGHTS

Corporate takeover attempts come in various guises. Usually, a would-be acquirer makes a direct offer to the board of directors of a targeted corporation. The bidder may offer to purchase the company for cash and/or stock. If the board approves the offer, a friendly transaction is completed and presented to shareholders for approval. If, however, the board of directors rejects the bid, the acquirer can make a tender offer for the shares directly to the targeted corporation’s shareholders. Such offers are referred to as hostile tender bids.

Not wishing to wait until they are subjects of hostile takeover attempts, many corporations have adopted antitakeover measures designed to deter unfriendly bids or buy time. The most common defenses are the shareholders rights protection plan, also known as the poison pill, and charter amendments that create barriers to acceptance of hostile bids. In the U.S., poison pills do not require shareholder approval. However, shareholders must approve charter amendments, such as classified boards or supermajority vote requirements. In brief, the very existence of defensive measures can foreclose the possibility of tenders and hence, opportunities to premium prices for shareholders.

Anti-takeover statutes generally increase management’s potential for insulating itself and warding off hostile takeovers that may be beneficial to shareholders. While it may be true that some boards use such devices to obtain higher bids and to enhance shareholder value, it is more likely that such provisions are used to entrench management. The majority of historical evidence on individual corporate anti-takeover measures indicates that heavily insulated companies generally realize lower returns than those having managements that are more accountable to shareholders and the market. The evidence also suggests that when states adopt their own anti-takeover devices, or endorse those employed by firms, shareholder returns are harmed. Moreover, the body of evidence appears to indicate that companies in states with the strongest anti-takeover laws experience lower returns than they would absent such statutes.

Takeover Defenses and Shareholder Rights-Related Management Proposals

Poison Pills (Shareholder Rights Plans)

Poison pills are corporate-sponsored financial devices that, when triggered by potential acquirers, do one or more of the following: 1) dilute the acquirer’s equity holdings in the target company; 2) dilute the acquirer’s voting interests in the target company; or 3) dilute the acquirer’s equity holdings in the post-merger company. Poison pills generally allow shareholders to purchase shares from, or sell shares back to, the target company (flip-in pill) and/or the potential acquirer (flip-out pill) at a price far out of line with fair market value. Depending on the type of pill, the triggering event can either transfer wealth from the target company or dilute the equity holdings of current shareholders. Poison pills insulate management from the threat of a change in control and provide the target board with veto power over takeover bids. Because poison pills greatly alter the balance of power between shareholders and management, shareholders should be allowed to make their own evaluation of such plans.

Social Advisory Services Recommendation: Vote case-by-case on management proposals on poison pill ratification, focusing on the features of the shareholder rights plan. Rights plans should contain the following attributes:

- No lower than a 20 percent trigger, flip-in or flip-over provision;
- A term of no more than three years;
- No dead-hand, slow-hand, no-hand or similar feature that limits the ability of a future board to redeem the pill;
- Shareholder redemption feature (qualifying offer clause); if the board refuses to redeem the pill 90 days after a qualifying offer is announced, 10 percent of the shares may call a special meeting or seek a written consent to vote on rescinding the pill. In addition, the rationale for adopting the pill should be thoroughly explained by the company. In examining the request for the pill, take into consideration the company’s existing governance structure, including: board independence, existing takeover defenses, and any problematic governance concerns.
Net Operating Loss (NOL) Poison Pills/Protective Amendments

The financial crisis has prompted widespread losses in certain industries. This has resulted in previously profitable companies considering the adoption of a poison pill and/or NOL protective amendment to protect their NOL tax assets, which may be lost upon an acquisition of 5 percent of a company's shares.

When evaluating management proposals seeking to adopt NOL pills or protective amendments, the purpose behind the proposal, its terms, and the company's existing governance structure should be taken into account to assess whether the structure actively promotes board entrenchment or adequately protects shareholder rights. While Social Advisory Services acknowledges the high estimated tax value of NOLs, which benefit shareholders, the ownership acquisition limitations contained in an NOL pill/protective amendment coupled with a company's problematic governance structure could serve as an antitakeover device.

Given the fact that shareholders will want to ensure that such an amendment does not remain in effect permanently, Social Advisory Services will also closely review whether the pill/amendment contains a sunset provision or a commitment to cause the expiration of the NOL pill/protective amendment upon exhaustion or expiration of the NOLs.

Social Advisory Services Recommendation: Vote against proposals to adopt a poison pill for the stated purpose of protecting a company's net operating losses (“NOLs”) if the term of the pill would exceed the shorter of three years and the exhaustion of the NOL.

Vote case-by-case on management proposals for poison pill ratification, considering the following factors, if the term of the pill would be the shorter of three years (or less) and the exhaustion of the NOL:

› The ownership threshold to transfer (NOL pills generally have a trigger slightly below 5%);
› The value of the NOLs;
› Shareholder protection mechanisms (sunset provision, or commitment to cause expiration of the pill upon exhaustion or expiration of NOLs);
› The company's existing governance structure including: board independence, existing takeover defenses, track record of responsiveness to shareholders, and any other problematic governance concerns; and
› Any other factors that may be applicable.

Vote against proposals to adopt a protective amendment for the stated purpose of protecting a company's net operating losses (“NOLs”) if the effective term of the protective amendment would exceed the shorter of three years and the exhaustion of the NOL.

Vote case-by-case, considering the following factors, for management proposals to adopt an NOL protective amendment that would remain in effect for the shorter of three years (or less) and the exhaustion of the NOL:

› The ownership threshold (NOL protective amendments generally prohibit stock ownership transfers that would result in a new 5-percent holder or increase the stock ownership percentage of an existing five-percent holder);
› The value of the NOLs;
› Shareholder protection mechanisms (sunset provision or commitment to cause expiration of the protective amendment upon exhaustion or expiration of the NOL);
› The company's existing governance structure including; board independence, existing takeover defenses, track record of responsiveness to shareholders, and any other problematic governance concerns;
› Any other factors that may be applicable.

Ratification Proposals: Management Proposals to Ratify Existing Charter or Bylaw Provisions
Social Advisory Services Recommendation: Generally vote against management proposals to ratify provisions of the company’s existing charter or bylaws, unless these governance provisions align with best practice.

In addition, voting against/withhold from individual directors, members of the governance committee, or the full board may be warranted, considering:

› The presence of a shareholder proposal addressing the same issue on the same ballot;
› The board’s rationale for seeking ratification;
› Disclosure of actions to be taken by the board should the ratification proposal fail;
› Disclosure of shareholder engagement regarding the board’s ratification request;
› The level of impairment to shareholders’ rights caused by the existing provision;
› The history of management and shareholder proposals on the provision at the company’s past meetings;
› Whether the current provision was adopted in response to the shareholder proposal;
› The company’s ownership structure; and
› Previous use of ratification proposals to exclude shareholder proposals.

Supermajority Shareholder Vote Requirements

Supermajority provisions violate the principle that a simple majority of voting shares should be all that is necessary to effect change at a company.

Social Advisory Services Recommendation:

› Vote for proposals to reduce supermajority shareholder vote requirements for charter amendments, mergers and other significant business combinations. For companies with shareholder(s) who own a significant amount of company stock, vote case-by-case, taking into account: a) ownership structure; b) quorum requirements; and c) supermajority vote requirements.
› Vote against proposals to require a supermajority shareholder vote for charter amendments, mergers and other significant business combinations.

Shareholder Ability to Call a Special Meeting

Most state corporation statutes allow shareholders to call a special meeting when they want to take action on certain matters that arise between regularly scheduled annual meetings. Sometimes this right applies only if a shareholder or a group of shareholders own a specified percentage of shares, with 10 percent being the most common. Shareholders may lose the ability to remove directors, initiate a shareholder resolution, or respond to a beneficial offer without having to wait for the next scheduled meeting if they are unable to act at a special meeting of their own calling.

Social Advisory Services Recommendation:

› Vote for proposals that provide shareholders with the ability to call special meetings taking into account: a) shareholders’ current right to call special meetings; b) minimum ownership threshold necessary to call special meetings (10% preferred); c) the inclusion of exclusionary or prohibitive language; d) investor ownership structure; and e) shareholder support of and management’s response to previous shareholder proposals.
› Vote against proposals to restrict or prohibit shareholders’ ability to call special meetings.

Shareholder Ability to Act by Written Consent

Consent solicitations allow shareholders to vote on and respond to shareholder and management proposals by mail without having to act at a physical meeting. A consent card is sent by mail for shareholder approval and only requires a signature for action. Some corporate bylaws require supermajority votes for consents while at others, standard annual
meeting rules apply. Shareholders may lose the ability to remove directors, initiate a shareholder resolution, or respond to a beneficial offer without having to wait for the next scheduled meeting if they are unable to act at a special meeting of their own calling.

Social Advisory Service Recommendation:
› Generally vote against proposals to restrict or prohibit shareholders’ ability to take action by written consent.
› Vote for proposals to allow or facilitate shareholder action by written consent, taking into consideration: a) shareholders’ current right to act by written consent; b) consent threshold; c) the inclusion of exclusionary or prohibitive language; d) Investor ownership structure; and e) shareholder support of and management’s response to previous shareholder proposals.
› Vote case-by-case on shareholder proposals if, in addition to the considerations above, the company has the following governance and antitakeover provisions; a) an unfettered8 right for shareholders to call special meetings at a 10 percent threshold; b) a majority vote standard in uncontested director elections; c) no non-shareholder-approved pill, and; d) an annually elected board.

Advance Notice Requirements for Shareholder Proposals/Nominations

In 2008, the Delaware courts handed down two decisions, which, read together, indicate a judicial move toward a narrower interpretation of companies’ advance notice bylaws. These recent court decisions have encouraged companies to take a closer look at their bylaw provisions to ensure that broad language does not provide loopholes for activist investors. Specifically, companies are including language designed to provide more detailed advance notice provisions and to ensure full disclosure of economic and voting interests in a shareholder’s notice of proposals, including derivatives and hedged positions.

Social Advisory Services Recommendation: Vote case-by-case basis on advance notice proposals, giving support to those proposals which allow shareholders to submit proposals/nominations as close to the meeting date as reasonably possible and within the broadest window possible, recognizing the need to allow sufficient notice for company, regulatory and shareholder review.

To be reasonable, the company’s deadline for shareholder notice of a proposal/nomination must not be more than 60 days prior to the meeting, with a submittal window of at least 30 days prior to the deadline. The submittal window is the period under which a shareholder must file his proposal/nominations prior to the deadline. In general, support additional efforts by companies to ensure full disclosure in regard to a proponent’s economic and voting position in the company so long as the informational requirements are reasonable and aimed at providing shareholders with the necessary information to review such proposals.

Fair Price Provisions

Fair price provisions were originally designed to specifically defend against the most coercive of takeover devises, the two-tiered, front-end loaded tender offer. In such a hostile takeover, the bidder offers cash for enough shares to gain control of the target. At the same time the acquirer states that once control has been obtained, the target’s remaining shares will be purchased with cash, cash and securities or only securities. Since the payment offered for the remaining stock is, by design less valuable than the original offer for the controlling shares, shareholders are forced to sell out early to maximize their value. Standard fair price provisions require that, absent board or shareholder approval of the acquisition, the bidder must pay the remaining shareholders the same price for their shares that brought control.

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8 “Unfettered” means no restrictions on agenda items, no restrictions on the number of shareholders who can group together to reach the 10 percent threshold, and only reasonable limits on when a meeting can be called: no greater than 30 days after the last annual meeting and no greater than 90 prior to the next annual meeting.
Social Advisory Services Recommendation:
› Vote case-by-case on proposals to adopt fair price provisions evaluating factors such as the vote required to approve the proposed acquisition, the vote required to repeal the fair price provision, and the mechanism for determining the fair price.
› Generally, vote against fair price provisions with shareholder vote requirements greater than a majority of disinterested shares.

Greenmail

Greenmail payments are targeted share repurchases by management of company stock from individuals or groups seeking control of the company. Since only the hostile party receives payment, usually at a substantial premium over the market value of shares, the practice discriminates against most shareholders. This transferred cash, absent the greenmail payment, could be put to much better use for reinvestment in the company, payment of dividends, or to fund a public share repurchase program.

Social Advisory Services Recommendation:
› Vote for proposals to adopt antigreenmail charter or bylaw amendments or otherwise restrict a company’s ability to make greenmail payments.
› Review on a case-by-case basis antigreenmail proposals when they are bundled with other charter or bylaw amendments.

Confidential Voting

Confidential voting, or voting by secret ballot, is one of the key structural issues in the proxy system. It ensures that all votes are based on the merits of proposals and cast in the best interests of fiduciary clients and pension plan beneficiaries. In a confidential voting system, only vote tabulators and inspectors of election may examine individual proxies and ballots; management and shareholders are given only vote totals. In an open voting system, management can determine who has voted against its nominees or proposals and then re-solicit those votes before the final vote count. As a result, shareholders can be pressured to vote with management at companies with which they maintain, or would like to establish, a business relationship. Confidential voting also protects employee shareholders from retaliation. Shares held by employee stock ownership plans, for example, are important votes that are typically voted by employees.

Social Advisory Services Recommendation: Vote for management proposals to adopt confidential voting.

Control Share Acquisition Provisions

Control share acquisition statutes function by denying shares their voting rights when they contribute to ownership in excess of certain thresholds. Voting rights for those shares exceeding ownership limits may only be restored by approval of either a majority or supermajority of disinterested shares. Thus, control share acquisition statutes effectively require a hostile bidder to put its offer to a shareholder vote or risk voting disenfranchisement if the bidder continues buying up a large block of shares.

Social Advisory Services Recommendation:
› Vote for proposals to opt out of control share acquisition statutes unless doing so would enable the completion of a takeover that would be detrimental to shareholders.
› Vote against proposals to amend the charter to include control share acquisition provisions.
› Vote for proposals to restore voting rights to the control shares.
Control Share Cash-Out Provisions

Control share cash-out statutes give dissident shareholders the right to "cash-out" of their position in a company at the expense of the shareholder who has taken a control position. In other words, when an investor crosses a preset threshold level, remaining shareholders are given the right to sell their shares to the acquirer, who must buy them at the highest acquiring price.

Social Advisory Services Recommendation: Vote for proposals to opt out of control share cash-out statutes.

Disgorgement Provisions

Disgorgement provisions require an acquirer or potential acquirer of more than a certain percentage of a company’s stock to disgorge, or pay back, to the company any profits realized from the sale of that company’s stock purchased 24 months before achieving control status. All sales of company stock by the acquirer occurring within a certain period of time (between 18 months and 24 months) prior to the investor’s gaining control status are subject to these recapture-of-profits provisions.

Social Advisory Services Recommendation: Vote for proposals to opt out of state disgorgement provisions.

State Takeover Statutes

Social Advisory Services Recommendation: Vote case-by-case on proposals to opt in or out of state takeover statutes (including control share acquisition statutes, control share cash-out statutes, freezeout provisions, fair price provisions, stakeholder laws, poison pill endorsements, severance pay and labor contract provisions, antigreenmail provisions, and disgorgement provisions).

Vote for opting into stakeholder protection statutes if they provide comprehensive protections for employees and community stakeholders. Social Advisory Services would be less supportive of takeover statutes that only serve to protect incumbent management from accountability to shareholders and which negatively influence shareholder value.

Freeze-Out Provisions

Freeze-out provisions force an investor who surpasses a certain ownership threshold in a company to wait a specified period of time before gaining control of the company.

Social Advisory Services Recommendation: Vote for proposals to opt out of state freeze-out provisions.

Reincorporation Proposals

Social Advisory Services Recommendation: Vote case-by-case on proposals to change a company’s state of incorporation giving consideration to both financial and corporate governance concerns including the following:

› Reasons for reincorporation;
› Comparison of company’s governance practices and provisions prior to and following the reincorporation;
› Comparison of corporation laws of original state and destination state.

Reincorporations into "tax havens" will be given special consideration.
While a firm’s country of incorporation will remain the primary basis for evaluating companies, Social Advisory Services will generally apply U.S. policies to the extent possible with respect to issuers that file DEF 14As, 10-K annual reports, and 10-Q quarterly reports, and are thus considered domestic issuers by the U.S. Securities and Exchange Commission (SEC). Corporations that have reincorporated outside the U.S. have found themselves subject to a combination of governance regulations and best practice standards that may not be entirely compatible with an evaluation framework based solely on country of incorporation.

Amend Bylaws without Shareholder Consent

Social Advisory Services Recommendation: Vote against proposals giving the board exclusive authority to amend the bylaws.

Vote for proposals giving the board the ability to amend the bylaws in addition to shareholders.

Litigation Rights (including Exclusive Venue and Fee-Shifting Bylaw Provisions)

Beginning in 2011, companies began to adopt bylaw provisions intended to limit the venue for shareholder lawsuits to the jurisdiction of incorporation. More recently, companies and their advisers have proposed other types of bylaws intended to limit shareholders’ litigation rights. Most notably, a May 2014 Delaware Supreme Court decision opened the door to the adoption by companies of bylaws that would require a shareholder plaintiff who sues the company unsuccessfully to pay the defendant company’s litigation expenses. Although the Delaware legislature was widely expected to enact legislation limiting the applicability of the Supreme Court’s decision to non-stock corporations, the legislature has not yet done so, and several publicly traded Delaware corporations have already adopted fee-shifting bylaws by way of a board resolution.

Bylaw provisions impacting shareholders’ ability to bring suit against the company may include exclusive venue provisions, which provide that the state of incorporation shall be the sole venue for certain types of litigation, and fee-shifting provisions that require a shareholder who sues a company unsuccessfully to pay all litigation expenses of the defendant corporation.

Social Advisory Services Recommendation: Vote case-by-case on bylaws which impact shareholders’ litigation rights, taking into account factors such as:

› The company’s stated rationale for adopting such a provision;
› Disclosure of past harm from shareholder lawsuits in which plaintiffs were unsuccessful or shareholder lawsuits outside the jurisdiction of incorporation;
› The breadth of application of the bylaw, including the types of lawsuits to which it would apply and the definition of key terms; and
› Governance features such as shareholders’ ability to repeal the provision at a later date (including the vote standard applied when shareholders attempt to amend the bylaws) and their ability to hold directors accountable through annual director elections and a majority vote standard in uncontested elections.

Generally vote against bylaws that mandate fee-shifting whenever plaintiffs are not completely successful on the merits (i.e., in cases where the plaintiffs are partially successful).

Unilateral adoption by the board of bylaw provisions which affect shareholders’ litigation rights will be evaluated under SRI’s policy on Unilateral Bylaw/Charter Amendments and Problematic Capital Structures.
Takeover Defenses and Shareholder Rights-Related Shareholder Proposals

Shareholder Proposals to put Pill to a Vote and/or Adopt a Pill Policy

**Social Advisory Services Recommendation:** Vote for shareholder proposals requesting that the company submit its poison pill to a shareholder vote or redeem it unless the company has: (1) a shareholder approved poison pill in place; or (2) The company has adopted a policy concerning the adoption of a pill in the future specifying that the board will only adopt a shareholder rights plan if either:

- Shareholders have approved the adoption of the plan; or
- The board, in its exercise of its fiduciary responsibilities, determines that it is in the best interest of shareholders under the circumstances to adopt a pill without the delay in adoption that would result from seeking stockholder approval (i.e., the “fiduciary out” provision). A poison pill adopted under this fiduciary out will be put to a shareholder ratification vote within 12 months of adoption or expire. If the pill is not approved by a majority of the votes cast on this issue, the plan will immediately terminate.

If the shareholder proposal calls for a time period of less than 12 months for shareholder ratification after adoption, vote for the proposal, but add the caveat that a vote within 12 months would be considered sufficient implementation.

Reduce Supermajority Vote Requirements

Supermajority provisions violate the principle that a simple majority of voting shares should be all that is necessary to effect change regarding a company.

**Social Advisory Services Recommendation:**
- Vote for shareholder proposals to lower supermajority shareholder vote requirements for charter and bylaw amendments.
- Vote for shareholder proposals to lower supermajority shareholder vote requirements for mergers and other significant business combinations.

Remove Antitakeover Provisions

There are numerous antitakeover mechanisms available to corporations that can make takeovers prohibitively expensive for a bidder or at least guarantee that all shareholders are treated equally. The debate over antitakeover devices centers on whether these devices enhance or detract from shareholder value. One theory argues that a company’s board, when armed with these takeover protections, may use them as negotiating tools to obtain a higher premium for shareholders. The opposing view maintains that management protections afforded such protection are more likely to become entrenched than to actively pursue the best interests of shareholders. Such takeover defenses also serve as obstacles to the normal functioning of the marketplace which, when operating efficiently, should replace incapable and poorly performing managements.

**Social Advisory Services Recommendation:** Vote for shareholder proposals that seek to remove antitakeover provisions.

Reimburse Proxy Solicitation Expenses

**Social Advisory Services Recommendation:** Vote case-by-case on proposals to reimburse proxy solicitation expenses. When voting in conjunction with support of a dissident slate, vote for the reimbursement of all appropriate proxy solicitation expenses associated with the election.
Vote for shareholder proposals calling for the reimbursement of reasonable costs incurred in connection with nominating one or more candidates in a contested election where the following apply:

- The election of fewer than 50 percent of the directors to be elected is contested in the election;
- One or more of the dissident’s candidates is elected;
- Shareholders are not permitted to cumulate their votes for directors;
- The election occurred, and the expenses were incurred, after the adoption of this bylaw.
4. MISCELLANEOUS GOVERNANCE PROVISIONS

**Bundled Proposals**

**Social Advisory Services Recommendation**: Review on a case-by-case basis bundled or “conditional” proxy proposals. In the case of items that are conditioned upon each other, examine the benefits and costs of the packaged items. In instances where the joint effect of the conditioned items is not in shareholders’ best interests, vote against the proposals. If the combined effect is positive, support such proposals.

**Adjourn Meeting**

Companies may ask shareholders to adjourn a meeting in order to solicit more votes. Generally, shareholders already have enough information to make their vote decisions. Once their votes have been cast, there is no justification for spending more money to continue pressing shareholders for more votes.

**Social Advisory Services Recommendation**:

› Generally vote against proposals to provide management with the authority to adjourn an annual or special meeting absent compelling reasons to support the proposal.
› Vote for proposals that relate specifically to soliciting votes for a merger or transaction if supporting that merger or transaction. Vote against proposals if the wording is too vague or if the proposal includes "other business."

**Changing Corporate Name**

Proposals to change a company’s name are generally routine matters. Generally, the name change reflects a change in corporate direction or the result of a merger agreement.

**Social Advisory Services Recommendation**: Vote for changing the corporate name unless there is compelling evidence that the change would adversely affect shareholder value.

**Amend Quorum Requirements**

**Social Advisory Services Recommendation**: Vote against proposals to reduce quorum requirements for shareholder meetings below a majority of the shares outstanding unless there are compelling reasons to support the proposal.

**Amend Minor Bylaws**

**Social Advisory Services Recommendation**: Vote for bylaw or charter changes that are of a housekeeping nature (updates or corrections).

**Other Business**

Other business proposals are routine items to allow shareholders to raise other issues and discuss them at the meeting. Only issues that may be legally discussed at meetings may be raised under this authority. However, shareholders cannot know the content of these issues so they are generally not supported.

**Social Advisory Services Recommendation**: Generally vote against other business proposals.
5. CAPITAL STRUCTURE

The equity in a corporate enterprise (that is, the residual value of the company’s assets after the payment of all debts) belongs to the shareholders. Equity securities may be employed, or manipulated, in a manner that will ultimately enhance or detract from shareholder value. As such, certain actions undertaken by management in relation to a company’s capital structure can be of considerable significance to shareholders. Changes in capitalization usually require shareholder approval or ratification.

**Common Stock Authorization**

State statutes and stock exchanges require shareholder approval for increases in the number of common shares. Corporations increase their supply of common stock for a variety of ordinary business purposes: raising new capital, funding stock compensation programs, business acquisitions, and implementation of stock splits or payment of stock dividends.

**Social Advisory Services Recommendation:** Proposals to increase authorized common stock are evaluated on a case-by-case basis, taking into account the size of the increase, the company’s rationale for additional shares, the company’s use of authorized shares during the last three years, and the risk to shareholders if the request is not approved. A company’s need for additional shares is gauged by measuring shares outstanding and reserved as a percentage of the total number of shares currently authorized for issuance.

If, within the past three years, the board adopted a poison pill without shareholder approval, repriced or exchanged underwater stock options without shareholder approval, or placed a substantial amount of stock with insiders at prices substantially below market value without shareholder approval, Social Advisory Services will generally vote against the requested increase in authorized capital on the basis of imprudent past use of shares.

- Vote for proposals to increase the number of authorized common shares where the primary purpose of the increase is to issue shares in connection with a transaction on the same ballot that warrants support.
- Vote against proposals at companies with more than one class of common stock to increase the number of authorized shares of the class of common stock that has superior voting rights.
- Vote against proposals to increase the number of authorized common shares if a vote for a reverse stock split on the same ballot is warranted despite the fact that the authorized shares would not be reduced proportionally.
- Review on a case-by-case basis all other proposals to increase the number of shares of common stock authorized for issue, considering company-specific factors that include:
  - Past Board Performance;
  - The company’s use of authorized shares during the last three years.
  - The Current Request;
  - Disclosure in the proxy statement of the specific purposes of the proposed increase;
  - Disclosure in the proxy statement of specific and severe risks to shareholders of not approving the request; and
  - The dilutive impact of the request as determined relative to an allowable increase calculated by Social Advisory Services (typically 100 percent of existing authorized shares) that reflects the company’s need for shares and total shareholder returns.
Social Advisory Services will apply the relevant allowable increase below to requests to increase common stock that are for general corporate purposes (or to the general corporate purposes portion of a request that also includes a specific need):

A. Most companies: **100 percent** of existing authorized shares.
B. Companies with less than 50 percent of existing authorized shares either outstanding or reserved for issuance: **50 percent** of existing authorized shares.
C. Companies with one- and three-year total shareholder returns (TSRs) in the bottom 10 percent of the U.S. market as of the end of the calendar quarter that is closest to their most recent fiscal year end: **50 percent** of existing authorized shares.
D. Companies at which both conditions (B and C) above are both present: **25 percent** of existing authorized shares.

If there is an acquisition, private placement, or similar transaction on the ballot (not including equity incentive plans) that Social Advisory Services is recommending FOR, the allowable increase will be the greater of (i) twice the amount needed to support the transactions on the ballot, and (ii) the allowable increase as calculated above.

**Issue Stock for Use with Rights Plan**

**Social Advisory Services Recommendation:** Vote against proposals that increase authorized common stock for the explicit purpose of implementing a non-shareholder approved shareholder rights plan (poison pill).

**Stock Distributions: Splits and Dividends**

**Social Advisory Services Recommendation:** Generally vote for management proposals to increase the common share authorization for stock split or stock dividend, provided that the effective increase in authorized shares is equal to or is less than the allowable increase calculated in accordance with Social Advisory Services' Common Stock Authorization policy.

**Reverse Stock Splits**

Reverse splits exchange multiple shares for a lesser amount to increase share price. Increasing share price is sometimes necessary to restore a company’s share price to a level that will allow it to be traded on the national stock exchanges. In addition, some brokerage houses have a policy of not monitoring or investing in very low priced shares. Reverse stock splits help maintain stock liquidity.

**Social Advisory Services Recommendation:** Vote for management proposals to implement a reverse stock split if:

- The number of authorized shares will be proportionately reduced; or
- The effective increase in authorized shares is equal to or less than the allowable increase calculated in accordance with Social Advisory Services' Common Stock Authorization policy.

Vote case-by-case on proposals that do not meet either of the above conditions, taking into consideration the following factors:

- Stock exchange notification to the company of a potential delisting;
- Disclosure of substantial doubt about the company's ability to continue as a going concern without additional financing;
- The company's rationale; or
- Other factors as applicable.
Preferred Stock Authorization

Preferred stock is an equity security which has certain features similar to debt instruments, such as fixed dividend payments, seniority of claims to common stock, and in most cases no voting rights. The terms of blank check preferred stock give the board of directors the power to issue shares of preferred stock at their discretion—with voting rights, conversion, distribution and other rights to be determined by the board at time of issue. Blank check preferred stock can be used for sound corporate purposes but could be used as a device to thwart hostile takeovers without shareholder approval.

Social Advisory Services Recommendation:
- Vote for proposals to increase the number of authorized preferred shares where the primary purpose of the increase is to issue shares in connection with a transaction on the same ballot that warrants support.
- Vote against proposals at companies with more than one class or series of preferred stock to increase the number of authorized shares of the class or series of preferred stock that has superior voting rights.
- Vote on a case-by-case basis all other proposals to increase the number of shares of preferred stock authorized for issuance, considering company-specific factors that include:
  - Past Board Performance;
  - The company’s use of authorized preferred shares during the last three years.
  - The Current Request;
  - Disclosure in the proxy statement of specific reasons for the proposed increase;
  - Disclosure in the proxy statement of specific and severe risks to shareholders for not approving the request;
  - In instances where the company has existing authorized preferred stock, the dilutive impact of the request as determined by an allowable cap generated by Social Advisory Services' quantitative model (typically 100 percent of existing authorized shares) that reflects the company’s need for shares and total shareholder returns;
  - Whether the shares requested are blank check preferred shares that can be used for antitakeover purposes.

Blank Check Preferred Stock

Social Advisory Services Recommendation:
- Vote against proposals that would authorize the creation of new classes of preferred stock with unspecified voting, conversion, dividend distribution, and other rights ("blank check" preferred stock).
- Vote against proposals to increase the number of blank check preferred stock authorized for issuance when no shares have been issued or reserved for a specific purpose.
- Vote for proposals to create "declawed" blank check preferred stock (stock that cannot be used as a takeover defense).
- Vote for requests to require shareholder approval for blank check authorizations.

Adjustments to Par Value of Common Stock

Stock that has a fixed per share value that is on its certificate is called par value stock. The purpose of par value stock is to establish the maximum responsibility of a stockholder in the event that a corporation becomes insolvent. Proposals to reduce par value come from certain state level requirements for regulated industries such as banks, and other legal requirements relating to the payment of dividends.

Social Advisory Services Recommendation:
- Vote for management proposals to reduce the par value of common stock unless the action is being taken to facilitate an anti-takeover device or some other negative corporate governance action.
Vote for management proposals to eliminate par value.

**Unequal Voting Rights/Dual Class Structure**

Incumbent managers use unequal voting rights with the voting rights of their common shares superior to other shareholders in order to concentrate their power and insulate themselves from the wishes of the majority of shareholders. Dual class exchange offers involve a transfer of voting rights from one group of shareholders to another group of shareholders typically through the payment of a preferential dividend. A dual class recapitalization also establishes two classes of common stock with unequal voting rights, but initially involves an equal distribution of preferential and inferior voting shares to current shareholders.

**Social Advisory Services Recommendation:** Generally vote against proposals to create a new class of common stock unless:

- The company discloses a compelling rationale for the dual-class capital structure, including: a) the company's auditor has concluded that there is substantial doubt about the company's ability to continue as a going concern; or b) the new class of shares will be transitory;
- The new class is intended for financing purposes with minimal or no dilution to current shareholders in both the short term and long term;
- The new class is not designed to preserve or increase the voting power of an insider or significant shareholder.

**Preemptive Rights**

Preemptive rights permit shareholders to share proportionately in any new issues of stock of the same class. These rights guarantee existing shareholders the first opportunity to purchase shares of new issues of stock in the same class as their own and in the same proportion. The absence of these rights could cause stockholders' interest in a company to be reduced by the sale of additional shares without their knowledge and at prices unfavorable to them. Preemptive rights, however, can make it difficult for corporations to issue large blocks of stock for general corporate purposes. Both corporations and shareholders benefit when corporations are able to arrange issues without preemptive rights that do not result in a substantial transfer of control.

**Social Advisory Services Recommendation:** Review on a case-by-case basis proposals to create or abolish preemptive rights. In evaluating proposals on preemptive rights, we look at the size of a company, the characteristics of its shareholder base and the liquidity of the stock.

**Debt Restructurings**

Proposals to increase common and/or preferred shares and to issue shares as part of a debt-restructuring plan will be analyzed considering the following issues:

- **Dilution**—How much will the ownership interest of existing shareholders be reduced, and how extreme will dilution to any future earnings be?
- **Change in Control**—Will the transaction result in a change in control/management at the company? Are board and committee seats guaranteed? Do standstill provisions and voting agreements exist? Is veto power over certain corporate actions in place?
- **Financial Issues**—company's financial situation, degree of need for capital, use of proceeds, and effect of the financing on the company's cost of capital;
- **Terms of the offer**—discount/premium in purchase price to investor including any fairness opinion, termination penalties and exit strategy;
- **Conflict of interest**—arm's length transactions and managerial incentives;
› *Management’s efforts to pursue other alternatives.*

**Social Advisory Services Recommendation:**
› Review on a case-by-case basis proposals regarding debt restructurings.
› Vote for the debt restructuring if it is expected that the company will file for bankruptcy if the transaction is not approved.

**Share Repurchase Programs**

**Social Advisory Services Recommendation:** Vote for management proposals to institute open-market share repurchase plans in which all shareholders may participate on equal terms.

**Conversion of Securities**

**Social Advisory Services Recommendation:** Vote case-by-case on proposals regarding conversion of securities, taking into account the dilution to existing shareholders, the conversion price relative to market value, financial issues, control issues, termination penalties, and conflicts of interest.

Vote for the conversion if it is expected that the company will be subject to onerous penalties or will be forced to file for bankruptcy if the transaction is not approved.

**Recapitalization**

**Social Advisory Services Recommendation:** Vote case-by-case on recapitalizations (reclassifications of securities), taking into account:
› Whether the capital structure is simplified;
› Liquidity is enhanced;
› Fairness of conversion terms;
› Impact on voting power and dividends;
› Reasons for the reclassification;
› Conflicts of interest;
› Other alternatives considered.

**Tracking Stock**

**Social Advisory Services Recommendation:** Vote case-by-case on the creation of tracking stock, weighing the strategic value of the transaction against such factors as:
› Adverse governance changes;
› Excessive increases in authorized capital stock;
› Unfair method of distribution;
› Diminution of voting rights;
› Adverse conversion features;
› Negative impact on stock option plans;
› Alternatives such as spin-offs.
6. EXECUTIVE AND DIRECTOR COMPENSATION

The global financial crisis resulted in significant erosion of shareholder value and highlighted the need for greater assurance that executive compensation is principally performance-based, fair, reasonable, and not designed in a manner that would incentivize excessive risk-taking by managements. The financial crisis raised questions about the role of pay incentives in influencing executive behavior and motivating inappropriate or excessive risk-taking that could threaten a corporation’s long-term viability. The safety lapses that led to the disastrous explosions at BP’s Deepwater Horizon oil rig and Massey Energy’s Upper Big Branch mine, and the resulting unprecedented losses in shareholder value; a) underscore the importance of incorporating meaningful economic incentives around social and environmental considerations in compensation program design, and b) exemplify the costly liabilities of failing to do so.

Evolving disclosure requirements have opened a wider window into compensation practices and processes, giving shareholders more opportunity and responsibility to ensure that pay is designed to create and sustain value. Companies in the U.S. are now required to evaluate and discuss potential risks arising from misguided or misaligned compensation programs. The Dodd-Frank Wall Street Reform and Consumer Protection Act requires advisory shareholder votes on executive compensation (management “say on pay”), an advisory vote on the frequency of say on pay, as well as a shareholder advisory vote on golden parachute compensation. The advent of “say on pay” votes for shareholders in the U.S. has provided a new communication mechanism and impetus for constructive engagement between shareholders and managers/directors on pay issues.

The socially responsible investing community contends that corporations should be held accountable for their actions and decisions, including those around executive compensation. Social Advisory Services believes that executive pay programs should be fair, competitive, reasonable, and create appropriate incentives, and that pay for performance should be a central tenet in executive compensation philosophy. Most investors expect corporations to adhere to certain best practice pay considerations in designing and administering executive and director compensation programs, including:

- **Appropriate pay-for-performance alignment with emphasis on long-term shareholder value:** executive pay practices must be designed to attract, retain, and appropriately motivate the key employees who drive shareholder value creation over the long term. Evaluating appropriate alignment of pay incentives with shareholder value creation includes taking into consideration, among other factors, the link between pay and performance, the mix between fixed and variable pay, equity-based plan costs, and performance goals - including goals tied to social and environmental considerations.

- **Avoiding arrangements that risk “pay for failure”:** this includes assessing the appropriateness of long or indefinite contracts, excessive severance packages, guaranteed compensation, and practices or policies that fail to adequately mitigate against or address environmental, social and governance failures.

- **Independent and effective compensation committees:** oversight of executive pay programs by directors with appropriate skills, knowledge, experience, and a sound process for compensation decision-making (e.g., including access to independent expertise and advice when needed) should be promoted.

- **Clear and comprehensive compensation disclosures:** shareholders expect companies to provide informative and timely disclosures that enable shareholders to evaluate executive pay practices fully and fairly.

- **Avoiding inappropriate pay to non-executive directors:** compensation to outside directors should not compromise their independence and ability to make appropriate judgments in overseeing managers’ pay and performance. At the market level, this may incorporate a variety of generally accepted best practices.

A non-exhaustive list of best pay practices includes:

- **Employment contracts:** Companies should enter into employment contracts under limited circumstances for a short time period (e.g., new executive hires for a three-year contract) for limited executives. The contracts should not have automatic renewal feature and should have a specified termination date.
 › Severance agreements: Severance provisions should not be so appealing that it becomes an incentive for the executive to be terminated. Severance provisions should exclude excise tax gross-up. The severance formula should be reasonable and not overly generous to the executive (e.g., severance multiples of 1X, 2X, or 3X and use pro-rated target/average historical bonus and not maximum bonus). Failure to renew employment contract, termination under questionable events, or poor performance should not be considered as appropriate reasons for severance payments.

 › Change-in-control payments: Change-in-control payments should only be made when there is a significant change in company ownership structure, and when there is a loss of employment or substantial change in job duties associated with the change in company ownership structure ("double-triggered"). Change-in-control provisions should exclude excise tax gross-up and eliminate the acceleration of vesting of equity awards upon a change in control unless provided under a double-trigger scenario. Similarly, change in control provisions in equity plans should be double-triggered. A change in control event should not result in an acceleration of vesting of all unvested stock options or removal of vesting/performance requirements on restricted stock/performance shares, unless there is a loss of employment or substantial change in job duties.

 › Supplemental executive retirement plans (SERPs): SERPS should not include sweeteners that can increase the SERP value significantly or even exponentially, such as additional years of service credited for pension calculation, inclusion of variable pay (e.g. bonuses and equity awards) into the formula. Pension formula should not include extraordinary annual bonuses paid close to retirement years, and should be based on the average, not the maximum level of compensation earned.

 › Deferred compensation: Above-market returns or guaranteed minimum returns should not be applied on deferred compensation.

 › Disclosure practices: The Compensation Discussion & Analysis should be written in plain English, with as little “legalese” as possible and formatted using section headers, bulleted lists, tables, and charts where possible to ease reader comprehension. Ultimately, the document should provide detail and rationale regarding compensation, strategy, pay mix, goals/metrics, challenges, competition and pay for performance linkage, etc. in a narrative fashion.

 › Responsible use of company stock: Companies should adopt policies that prohibit executives from speculating in company’s stock or using company stock in hedging activities, such as “cashless” collars, forward sales, equity swaps or other similar arrangements. Such behavior undermines the ultimate alignment with long-term shareholders’ interests. In addition, the policy should prohibit or discourage the use of company stock as collateral for margin loans, to avoid any potential sudden stock sales (required upon margin calls), that could have a negative impact on the company’s stock price.

 › Long-term focus: Executive compensation programs should be designed to support companies’ long-term strategic goals. A short-term focus on performance does not necessarily create sustainable shareholder value, since long-term goals may be sacrificed to achieve short-term expectations. Compensation programs embedding a long-term focus with respect to company goals better align with the long-term interests of shareholders. Granting stock options and restricted stock to executives that vest in five years do not necessarily provide a long-term focus, as executives can sell the company shares once they vest. However, requiring senior executives to hold company stock until they retire can encourage a long-term focus on company performance.

Criteria for Evaluating Executive Pay

Pay-for-Performance Evaluation

Social Advisory Services conducts a five-part pay analysis to evaluate the degree of alignment between the CEO’s pay with the company’s performance over a sustained period. From a shareholders’ perspective, performance is predominantly gauged by the company’s stock performance over time. Even when financial, non-financial or operational measures are utilized in incentive awards, the achievement related to these measures should ultimately
translate into superior shareholder returns in the long-term. With respect to companies in the Russell 3000 or Russell 3000E Indices, this analysis considers the following:

Pay-for-Performance Elements:

› The degree of alignment between the company’s annualized TSR rank and the CEO’s annualized total pay rank within a peer group, each measured over a three-year period, and the rankings of CEO total pay and company financial performance within a peer group, each measured over a three-year period.
› Absolute Alignment: The absolute alignment between the trend in CEO pay and company TSR over the prior five fiscal years — i.e., the difference between the trend in annual pay changes and the trend in annualized TSR during the period.
› Equity Pay Mix: The ratio of the CEO’s performance- vs. time-based equity awards.

Pay Equity (Quantum) Elements:

› Multiple of Median: The multiple of the CEO’s total pay relative to the peer group median in the most recent fiscal year.
› Internal Pay Disparity: The multiple of the CEO’s total pay relative to other named executive officers (NEOs) — i.e., an excessive differential between CEO total pay and that of the next highest-paid NEO as well as CEO total pay relative to the average NEO pay.

If the above pay-for-performance analysis demonstrates unsatisfactory long-term pay-for-performance alignment or, in the case of non-Russell 3000 index companies, misaligned pay and performance are otherwise suggested, the following qualitative factors will be evaluated to determine how various pay elements may work to encourage or to undermine long-term value creation and alignment with shareholder interests:

› The ratio of performance-based compensation to overall compensation, including whether any relevant social or environmental factors are a component of performance-contingent pay elements;
› The presence of significant environmental, social or governance (ESG) controversies that have the potential to pose material risks to the company and its shareholders;
› Any downward discretion applied to executive compensation on the basis of a failure to achieve performance goals, including ESG performance objectives;
› The completeness of disclosure and rigor of performance goals;
› The company’s peer group benchmarking practices;
› Actual results of financial/non-financial and operational metrics, such as growth in revenue, profit, cash flow, workplace safety, environmental performance, etc., both absolute and relative to peers;
› Special circumstances related to, for example, a new CEO in the prior FY or anomalous equity grant practices (e.g., bi-annual awards);
› Realizable pay compared to grant pay; and
› Any other factors deemed relevant.

Problematic Pay Practices

The focus is on executive compensation practices that contravene best practice compensation considerations,
including:

› Problematic practices related to non-performance-based compensation elements;
› Incentives that may motivate excessive risk-taking; and
› Options backdating.

**Non-Performance based Compensation Elements** Pay elements that are not directly based on performance are generally evaluated on a case-by-case basis considering the context of a company’s overall pay program and demonstrated pay-for-performance philosophy. While not exhaustive, the following list represents certain adverse practices that are contrary to a performance-based pay philosophy and executive pay best practices, and may lead to negative vote recommendations:

› Egregious employment contracts:
  › Contracts containing multi-year guarantees for salary increases, non-performance based bonuses, and equity compensation.
› New CEO with overly generous new-hire package:
  › Excessive “make whole” provisions without sufficient rationale;
  › Any of the problematic pay practices listed under this policy.
› Abnormally large bonus payouts without justifiable performance linkage or proper disclosure:
  › Includes performance metrics that are changed, canceled, or replaced during the performance period without adequate explanation of the action and the link to performance.
› Egregious pension/SERP (supplemental executive retirement plan) payouts:
  › Inclusion of additional years of service not worked that result in significant benefits provided in new arrangements;
  › Inclusion of performance-based equity or other long-term awards in the pension calculation.
› Excessive Perquisites:
  › Perquisites for former and/or retired executives, such as lifetime benefits, car allowances, personal use of corporate aircraft, or other inappropriate arrangements;
  › Extraordinary relocation benefits (including home buyouts);
  › Excessive amounts of perquisites compensation.
› Excessive severance and/or change in control provisions:
  › Change in control cash payments exceeding 3 times base salary plus target/average/last paid bonus;
  › New or extended arrangements that provide for change-in-control payments without involuntary job loss or substantial diminution of job duties (single-triggered or modified single-triggered, where an executive may voluntarily leave for any reason and still receive the change-in-control severance package);
  › New or extended employment or severance agreements that provide for excise tax gross-ups. Modified gross-ups would be treated in the same manner as full gross-ups;
  › Excessive payments upon an executive’s termination in connection with performance failure;
  › Liberal change-in-control definition in individual contracts or equity plans which could result in payments to executives without an actual change in control occurring.
› Tax Reimbursements/Gross-ups: Excessive reimbursement of income taxes on executive perquisites or other payments (e.g., related to personal use of corporate aircraft, executive life insurance, bonus, restricted stock vesting, secular trusts, etc; see also excise tax gross-ups above).
› Dividends or dividend equivalents paid on unvested performance shares or units.
› Executives using company stock in hedging activities, such as “cashless” collars, forward sales, equity swaps, or other similar arrangements.
› Internal pay disparity: Excessive differential between CEO total pay and that of next highest-paid named executive officer (NEO).
› Repricing or replacing of underwater stock options/stock appreciation rights (SARs) without prior shareholder approval (including cash buyouts, option exchanges, and certain voluntary surrender of underwater options where shares surrendered may subsequently be re-granted).
Insufficient executive compensation disclosure by externally-managed issuers (EMIs) such that a reasonable assessment of pay programs and practices applicable to the EMI’s executives is not possible.

Other pay practices that may be deemed problematic in a given circumstance but are not covered in the above categories.

**Incentives that may Motivate Excessive Risk-Taking**

Assess company policies and disclosure related to compensation that could incentivize excessive risk-taking, for example:

- Multi-year guaranteed bonuses;
- A single or common performance metric used for short- and long-term plans;
- Lucrative severance packages;
- High pay opportunities relative to industry peers;
- Disproportionate supplemental pensions;
- Mega annual equity grants that provide unlimited upside with no downside risk.

Factors that potentially mitigate the impact of risky incentives include rigorous claw-back provisions and robust stock ownership/holding guidelines.

**Options Backdating**

The following factors should be examined on a case-by-case basis to allow for distinctions to be made between “sloppy” plan administration versus deliberate action or fraud, as well as those instances in which companies that subsequently took corrective action. Cases where companies have committed fraud are considered most egregious.

- Reason and motive for the options backdating issue, such as inadvertent vs. deliberate grant date changes;
- Duration of options backdating;
- Size of restatement due to options backdating;
- Corrective actions taken by the board or compensation committee, such as canceling or re-pricing backdated options, the recouping of option gains on backdated grants;
- Adoption of a grant policy that prohibits backdating, and creates a fixed grant schedule or window period for equity grants in the future.

**Board Communications and Responsiveness**

Consider the following factors case-by-case when evaluating ballot items related to executive pay on the board’s responsiveness to investor input and engagement on compensation issues:

- Failure to respond to majority-supported shareholder proposals on executive pay topics; or
- Failure to adequately respond to the company’s previous say-on-pay proposal that received the support of less than 70 percent of votes cast, taking into account:
  - The company’s response, including:
    - Disclosure of engagement efforts with major institutional investors regarding the issues that contributed to the low level of support (including the timing and frequency of engagements and whether independent directors participated);
    - Disclosure of the specific concerns voiced by dissenting shareholders that led to the say-on-pay opposition;
> Disclosure of specific and meaningful actions taken to address shareholders' concerns;
> Other recent compensation actions taken by the company;
> Whether the issues raised are recurring or isolated;
> The company's ownership structure; and
> Whether the support level was less than 50 percent, which would warrant the highest degree of responsiveness.

### Advisory Votes on Executive Compensation – Management Say-on-Pay Proposals

The Dodd-Frank Act mandates advisory votes on executive compensation (Say on Pay or "SOP") for a proxy or consent or authorization for an annual or other meeting of the shareholders that includes required SEC compensation disclosures. This non-binding shareholder vote on compensation must be included in a proxy or consent or authorization at least once every three years.

In general, the SOP ballot item is the primary focus of voting on executive pay practices – dissatisfaction with compensation practices can be expressed by voting against the SOP proposal rather than voting against or withhold from the compensation committee. However, if there is no SOP on the ballot, then the negative vote will apply to members of the compensation committee. In addition, in egregious cases, or if the board fails to respond to concerns raised by a prior SOP proposal, then Social Advisory Services will recommend a vote against or withhold votes from compensation committee members (or, if the full board is deemed accountable, all directors). If the negative factors involve equity-based compensation, then a vote against an equity-based plan proposal presented for shareholder approval may be appropriate. In evaluating SOP proposals, Social Advisory Services will also assess to what degree social and environmental considerations are incorporated into compensation programs and executive pay decision-making – to the extent that proxy statement Compensation Discussion and Analysis (CD&A) disclosures permit.

**Social Advisory Services Recommendation:** Evaluate executive pay and practices, as well as certain aspects of outside director compensation on a case-by-case basis.

- **Vote against management Say on Pay proposals if:**
  - There is a misalignment between CEO pay and company performance (pay-for-performance);
  - The company maintains problematic pay practices;
  - The board exhibits a significant level of poor communication and responsiveness to shareholders.
- **Vote against or withhold from the members of the compensation committee and potentially the full board if:**
  - There is no SOP on the ballot, and an against vote on an SOP is warranted due to pay-for-performance misalignment, problematic pay practices, or the lack of adequate responsiveness on compensation issues raised previously, or a combination thereof;
  - The board fails to respond adequately to a previous SOP proposal that received less than 70 percent support of votes cast;
  - The company has recently practiced or approved problematic pay practices, including option repricing or option backdating; or
  - The situation is egregious.
- **Vote against an equity plan on the ballot if:**
  - A pay-for-performance misalignment exists, and a significant portion of the CEO’s misaligned pay is attributed to non-performance-based equity awards, taking into consideration:
    - Magnitude of pay misalignment;
    - Contribution of non-performance-based equity grants to overall pay; and
    - The proportion of equity awards granted in the last three fiscal years concentrated at the named executive officer (NEO) level.
Frequency of Advisory Vote on Executive Compensation – Management Say on Pay

The Dodd-Frank Act, in addition to requiring advisory votes on compensation (SOP), requires that each proxy for the first annual or other meeting of the shareholders (that includes required SEC compensation disclosures) occurring after Jan. 21, 2011, include an advisory voting item to determine whether, going forward, the "say on pay" vote by shareholders to approve compensation should occur every one, two, or three years.

Social Advisory Services will recommend a vote for annual advisory votes on compensation. The SOP is at its essence a communication vehicle, and communication is most useful when it is received in a consistent and timely manner. Social Advisory Services supports an annual SOP vote for many of the same reasons it supports annual director elections rather than a classified board structure: because this provides the highest level of accountability and direct communication by enabling the MSOP vote to correspond to the majority of the information presented in the accompanying proxy statement for the applicable shareholders' meeting. Having SOP votes every two or three years, covering all actions occurring between the votes, would make it difficult to create the meaningful and coherent communication that the votes are intended to provide. Under triennial elections, for example, a company would not know whether the shareholder vote references the compensation year being discussed or a previous year, making it more difficult to understand the implications of the vote.

Social Advisory Services Recommendation: Vote for annual advisory votes on compensation, which provide the most consistent and clear communication channel for shareholder concerns about companies' executive pay programs.

Advisory Vote on Golden Parachutes in an Acquisition, Merger, Consolidation, or Proposed Sale

This is a proxy item regarding specific advisory votes on "golden parachute" arrangements for Named Executive Officers (NEOs) that is required under The Dodd-Frank Wall Street Reform and Consumer Protection Act. Social Advisory Services places particular focus on severance packages that provide inappropriate windfalls and cover certain tax liabilities of executives.

Social Advisory Services Recommendation: Vote case-by-case on say on Golden Parachute proposals, including consideration of existing change-in-control arrangements maintained with named executive officers rather than focusing primarily on new or extended arrangements.

Features that may result in an against recommendation include one or more of the following, depending on the number, magnitude, and/or timing of issue(s):

› Single- or modified-single-trigger cash severance;
› Single-trigger acceleration of unvested equity awards;
› Excessive cash severance (>3x base salary and bonus);
› Excise tax gross-ups triggered and payable (as opposed to a provision to provide excise tax gross-ups);
› Excessive golden parachute payments (on an absolute basis or as a percentage of transaction equity value); or
› Recent amendments that incorporate any problematic features (such as those above) or recent actions (such as extraordinary equity grants) that may make packages so attractive as to influence merger agreements that may not be in the best interests of shareholders; or
› The company's assertion that a proposed transaction is conditioned on shareholder approval of the golden parachute advisory vote.
Recent amendment(s) that incorporate problematic features will tend to carry more weight on the overall analysis. However, the presence of multiple legacy problematic features will also be closely scrutinized.

In cases where the golden parachute vote is incorporated into a company’s advisory vote on compensation (“management "say on pay"”), Social Advisory Services will evaluate the "say on pay" proposal in accordance with these guidelines, which may give higher weight to that component of the overall evaluation.

**Equity-Based Incentive Plans**

As executive pay levels continue to soar, non-salary compensation remains one of the most sensitive and visible corporate governance issues. The financial crisis raised questions about the role of pay incentives in influencing executive behavior, including their appetite for risk-taking. Although shareholders may have little say about how much the CEO is paid in salary and bonus, they do have a major voice in approving stock incentive plans.

Stock-based plans can transfer significant amounts of wealth from shareholders to executives and directors and are among the most economically significant issues that shareholders are entitled to vote on. Rightly, the cost of these plans must be in line with the anticipated benefits to shareholders. Clearly, reasonable limits must be set on dilution as well as administrative authority. In addition, shareholders must consider the necessity of the various pay programs and examine the appropriateness of award types. Consequently, the pros and cons of these proposals necessitate a case-by-case evaluation.

Factors that increase the cost (or have the potential to increase the cost) of plans to shareholders include: excessive dilution, options awarded at below-market discounts, permissive policies on pyramiding, restricted stock giveaways that reward tenure rather than results, sales of shares on concessionary terms, blank-check authority for administering committees, option repricing or option replacements, accelerated vesting of awards in the event of defined changes in corporate control, stand-alone stock appreciation rights, loans or other forms of assistance, or evidence of improvident award policies.

Positive plan features that can offset costly features include: plans with modest dilution potential (i.e. appreciably below double-digit levels), bars to pyramiding and related safeguards for investor interests. Also favorable are performance programs with a duration of two or more years, bonus schemes that pay off in non-dilutive, fully deductible cash, 401K and other thrift or profit sharing plans, and tax-favored employee stock purchase plans. In general, we believe that stock plans should afford incentives, not sure-fire, risk-free rewards.

**Social Advisory Services Recommendation:** Vote case-by-case on equity-based compensation plans depending on a combination of certain plan features and equity grant practices, where positive factors may counterbalance negative factors, and vice versa, as evaluated using an "equity plan scorecard" (EPSC) approach with three pillars:

- **Plan Cost:** The total estimated cost of the company’s equity plans relative to industry/market cap peers, measured by the company’s estimated Shareholder Value Transfer (SVT) in relation to peers and considering both:
  - SVT based on new shares requested plus shares remaining for future grants, plus outstanding unvested/unexercised grants; and
  - SVT based only on new shares requested plus shares remaining for future grants.

- **Plan Features:**
  - Automatic single-triggered award vesting upon a change in control (CIC);
  - Discretionary vesting authority;

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12 Proposals evaluated under the EPSC policy generally include those to approve or amend (1) stock option plans for employees and/or employees and directors, (2) restricted stock plans for employees and/or employees and directors, and (3) omnibus stock incentive plans for employees and/or employees and directors.
› Liberal share recycling on various award types;
› Lack of minimum vesting period for grants made under the plan;
› Dividends payable prior to award vesting.

› **Grant Practices:**
  › The company’s three-year burn rate relative to its industry/market cap peers;
  › Vesting requirements in most recent CEO equity grants (3-year look-back);
  › The estimated duration of the plan (based on the sum of shares remaining available and the new shares requested, divided by the average annual shares granted in the prior three years);
  › The proportion of the CEO’s most recent equity grants/awards subject to performance conditions;
  › Whether the company maintains a claw-back policy;
  › Whether the company has established post exercise/vesting share-holding requirements.

Generally vote against the plan proposal if the combination of above factors indicates that the plan is not, overall, in shareholders’ interests, or if any of the following apply:

› Awards may vest in connection with a liberal change-of-control definition;
› The plan would permit repricing or cash buyout of underwater options without shareholder approval (either by expressly permitting it – for NYSE and Nasdaq listed companies -- or by not prohibiting it when the company has a history of repricing – for non-listed companies);
› The plan is a vehicle for problematic pay practices or a pay-for-performance disconnect; or
› Any other plan features are determined to have a significant negative impact on shareholder interests.

Each of these factors is described below.

**Plan Cost**

Generally vote against equity plans if the cost is unreasonable. For non-employee director plans, vote for the plan if certain factors are met.

**Shareholder Value Transfer (SVT)**

The cost of the equity plans is expressed as Shareholder Value Transfer (SVT), which is measured using a binomial option pricing model that assesses the amount of shareholders’ equity flowing out of the company to employees and directors. SVT is expressed as both a dollar amount and as a percentage of market value, and includes the new shares proposed, shares available under existing plans, and shares granted but unexercised (using two measures, in the case of plans subject to the Equity Plan Scorecard evaluation, as noted above). All award types are valued. For omnibus plans, unless limitations are placed on the most expensive types of awards (for example, full value awards), the assumption is made that all awards to be granted will be the most expensive types. See discussion of specific types of awards.

Except for proposals subject to Equity Plan Scorecard evaluation, Shareholder Value Transfer is reasonable if it falls below a company-specific benchmark. The benchmark is determined as follows: The top quartile performers in each industry group (using the Global Industry Classification Standard: GICS) are identified. Benchmark SVT levels for each industry are established based on these top performers’ historic SVT. Regression analyses are run on each industry group to identify the variables most strongly correlated to SVT. The benchmark industry SVT level is then adjusted upwards or downwards for the specific company by plugging the company-specific performance measures, size and cash compensation into the industry cap equations to arrive at the company’s benchmark.\(^{13}\)

\(^{13}\) For plans evaluated under the Equity Plan Scorecard policy, the company’s SVT benchmark is considered along with other factors.
Repricing Provisions

Vote against plans that expressly permit the repricing or exchange of underwater stock options/stock appreciate rights (SARs) without prior shareholder approval. "Repricing" includes the ability to do any of the following:

› Amend the terms of outstanding options or SARs to reduce the exercise price of such outstanding options or SARs;
› Cancel outstanding options or SARs in exchange for options or SARs with an exercise price that is less than the exercise price of the original options or SARs.
› The cancellation of underwater options in exchange for stock awards; or
› Cash buyouts of underwater options.

While the above cover most types of repricing, Social Advisory Services may view other provisions as akin to repricing depending on the facts and circumstances.

Also, vote against or withheld from members of the compensation committee who approved repricing (as defined above or otherwise determined by Social Advisory Services), without prior shareholder approval, even if such repricings are allowed in their equity plan.

Vote against plans if the company has a history of repricing without shareholder approval, and the applicable listing standards would not preclude them from doing so.

Pay-for-Performance Misalignment – Application to Equity Plans

If the equity plan on the ballot is a vehicle for problematic pay practices, vote against the plan.

Social Advisory Services may recommend a vote against the equity plan if the plan is determined to be a vehicle for pay-for-performance misalignment. Considerations in voting against the equity plan may include, but are not limited to:

› Severity of the pay-for-performance misalignment;
› Whether problematic equity grant practices are driving the misalignment; and/or
› Whether equity plan awards have been heavily concentrated to the CEO and/or the other NEOs.

Grant Practices

Three-Year Burn Rate

Burn rate benchmarks (utilized in Equity Plan Scorecard evaluations) are calculated as the greater of: (1) the mean (μ) plus one standard deviation (σ) of the company’s GICS group segmented by S&P 500, Russell 3000 index (less the S&P500) and non-Russell 3000 index; and (2) two percent of weighted common shares outstanding. In addition, year-over-year burn-rate benchmark changes will be limited to a maximum of two (2) percentage points plus or minus the prior year’s burn-rate benchmark. See the U.S. Equity Compensation Plans FAQ for the benchmarks.

Liberal Definition of Change-in-Control

Generally vote against equity plans if the plan provides for the acceleration of vesting of equity awards even though an actual change in control may not occur. Examples of such a definition could include, but are not limited to, announcement or commencement of a tender offer, provisions for acceleration upon a “potential” takeover, shareholder approval of a merger or other transactions, or similar language.
Other Compensation Plans

Amending Cash and Equity Plans (including Approval for Tax Deductibility (162(m))

Cash bonus plans can be an important part of an executive’s overall pay package, along with stock-based plans tied to long-term total shareholder returns. Over the long term, stock prices are an excellent indicator of management performance. However, other factors, such as economic conditions and investor reaction to the stock market in general and certain industries in particular, can greatly impact the company’s stock price. As a result, a cash bonus plan can effectively reward individual performance and the achievement of business unit objectives that are independent of short-term market share price fluctuations.

Social Advisory Services Recommendation: Vote case-by-case on amendments to cash and equity incentive plans.

Generally vote for proposals to amend executive cash, stock, or cash and stock incentive plans if the proposal:

› Addresses administrative features only; or
› Seeks approval for Section 162(m) purposes only, and the plan administering committee consists entirely of independent outsiders, per Social Advisory Services’ Categorization of Directors. Note that if the company is presenting the plan to shareholders for the first time after the company’s initial public offering (IPO), or if the proposal is bundled with other material plan amendments, then the recommendation will be case-by-case (see below).

Vote against such proposals to amend executive cash, stock, or cash and stock incentive plans if the proposal:

› Seeks approval for Section 162(m) purposes only, and the plan administering committee does not consist entirely of independent outsiders, per Social Advisory Services’ Categorization of Directors.

Vote case-by-case on all other proposals to amend cash incentive plans. This includes plans presented to shareholders for the first time after the company’s IPO and/or proposals that bundle material amendment(s) other than those for Section 162(m) purposes

Vote case-by-case on all other proposals to amend equity incentive plans, considering the following:

› If the proposal requests additional shares and/or the amendments may potentially increase the transfer of shareholder value to employees, the recommendation will be based on the Equity Plan Scorecard evaluation as well as an analysis of the overall impact of the amendments.
› If the plan is being presented to shareholders for the first time (including after the company's IPO), whether or not additional shares are being requested, the recommendation will be based on the Equity Plan Scorecard evaluation as well as an analysis of the overall impact of any amendments.
› If there is no request for additional shares and the amendments are not deemed to potentially increase the transfer of shareholder value to employees, then the recommendation will be based entirely on an analysis of the overall impact of the amendments, and the EPSC evaluation will be shown for informational purposes.

In the first two case-by-case evaluation scenarios, the EPSC evaluation/score is the more heavily weighted consideration.
Employee Stock Purchase Plans (ESPPs)

Employee stock purchase plans enable employees to become shareholders, which gives them a stake in the company’s growth. However, purchase plans are beneficial only when they are well balanced and in the best interests of all shareholders. From a shareholder’s perspective, plans with offering periods of 27 months or less are preferable. Plans with longer offering periods remove too much of the market risk and could give participants excessive discounts on their stock purchases that are not offered to other shareholders.

Qualified Plans

Qualified employee stock purchase plans qualify for favorable tax treatment under Section 423 of the Internal Revenue Code. Such plans must be broad-based, permitting all full-time employees to participate. Some companies also permit part-time staff to participate. Qualified ESPPs must be expensed under SFAS 123 unless the plan meets the following conditions; a) purchase discount is 5 percent or below; b) all employees can participate in the program; and 3) no look-back feature in the program. Therefore, some companies offer nonqualified ESPPs.

Social Advisory Services Recommendation: Vote case-by-case on qualified employee stock purchase plans. Vote for employee stock purchase plans where all of the following apply:

› Purchase price is at least 85 percent of fair market value;
› Offering period is 27 months or less; and
› The number of shares allocated to the plan is ten percent or less of the outstanding shares.

Vote against qualified employee stock purchase plans where any of the following apply:

› Purchase price is less than 85 percent of fair market value; or
› Offering period is greater than 27 months; or
› The number of shares allocated to the plan is more than ten percent of the outstanding shares.

Non-Qualified Plans

For nonqualified ESPPs, companies provide a match to employees’ contributions instead of a discount in stock price. Also, limits are placed on employees’ contributions. Some companies provide a maximum dollar value for the year and others specify the limits in terms of a percent of base salary, excluding bonus or commissions. For plans that do not qualify under Section 423 of the Internal Revenue Code, a plan participant will not recognize income by participating in the plan, but will recognize ordinary compensation income for federal income tax purposes at the time of the purchase.

Social Advisory Services Recommendation: Vote case-by-case on nonqualified employee stock purchase plans. Vote for nonqualified employee stock purchase plans with all the following features:

› Broad-based participation (i.e., all employees of the company with the exclusion of individuals with 5 percent or more of beneficial ownership of the company);
› Limits on employee contribution, which may be a fixed dollar amount or expressed as a percent of base salary;
› Company matching contribution up to 25 percent of employee’s contribution, which is effectively a discount of 20 percent from market value;
› No discount on the stock price on the date of purchase since there is a company matching contribution.
Vote against nonqualified employee stock purchase plans when any of the plan features do not meet the above criteria. If the company matching contribution exceeds 25 percent of employee’s contribution, evaluate the cost of the plan against its allowable cap.

**Employee Stock Ownership Plans (ESOPs)**

An Employee Stock Ownership Plan (ESOP) is an employee benefit plan that makes the employees of a company also owners of stock in that company. The plans are designed to defer a portion of current employee income for retirement purposes.

The primary difference between ESOPs and other employee benefit plans is that ESOPs invest primarily in the securities of the employee's company. In addition, an ESOP must be created for the benefit of non-management level employees and administered by a trust that cannot discriminate in favor of highly paid personnel.

Academic research of the performance of ESOPs in closely held companies found that ESOPs appear to increase overall sales, employment, and sales per employee over what would have been expected absent an ESOP. Studies have also found that companies with an ESOP are also more likely to still be in business several years later, and are more likely to have other retirement oriented benefit plans than comparable non-ESOP companies.

**Social Advisory Services Recommendation:** Vote for proposals to implement an ESOP or increase authorized shares for existing ESOPs, unless the number of shares allocated to the ESOP is excessive (more than five percent of outstanding shares).

**Option Exchange Programs/Repricing Options**

**Social Advisory Services Recommendation:** Vote case-by-case on management proposals seeking approval to exchange/reprice options taking into consideration:

- Historic trading patterns — the stock price should not be so volatile that the options are likely to be back “in-the-money” over the near term;
- Rationale for the re-pricing — was the stock price decline beyond management’s control?
- Is this a value-for-value exchange?
- Are surrendered stock options added back to the plan reserve?
- Option vesting — does the new option vest immediately or is there a black-out period?
- Term of the option — the term should remain the same as that of the replaced option;
- Exercise price — should be set at fair market or a premium to market;
- Participants — executive officers and directors should be excluded.

If the surrendered options are added back to the equity plans for re-issuance, then also take into consideration the company’s total cost of equity plans and its three-year average burn rate.

In addition to the above considerations, evaluate the intent, rationale, and timing of the repricing proposal. The proposal should clearly articulate why the board is choosing to conduct an exchange program at this point in time. Repricing underwater options after a recent precipitous drop in the company’s stock price demonstrates poor timing. Repricing after a recent decline in stock price triggers additional scrutiny and a potential vote against the proposal. At a minimum, the decline should not have happened within the past year. Also, consider the terms of the surrendered options, such as the grant date, exercise price and vesting schedule. Grant dates of surrendered options should be far enough back (two to three years) so as not to suggest that repricings are being done to take advantage of short-term downward price movements. Similarly, the exercise price of surrendered options should be above the 52-week high for the stock price.
Vote for shareholder proposals to put option repricings to a shareholder vote.

**Stock Plans in Lieu of Cash**

**Social Advisory Services Recommendation:**

› Vote case-by-case on plans that provide participants with the option of taking all or a portion of their cash compensation in the form of stock.
› Vote for non-employee director-only equity plans that provide a dollar-for-dollar cash-for-stock exchange.
› Vote case-by-case on plans which do not provide a dollar-for-dollar cash for stock exchange. In cases where the exchange is not dollar-for-dollar, the request for new or additional shares for such equity program will be considered using the binomial option pricing model. In an effort to capture the total cost of total compensation, Social Advisory Services will not make any adjustments to carve out the in-lieu-of cash compensation.

**Transfer Stock Option (TSO) Programs**

**Social Advisory Services Recommendation:** One-time Transfers: Vote against or withhold from compensation committee members if they fail to submit one-time transfers to shareholders for approval.

Vote case-by-case on one-time transfers. Vote for if:

› Executive officers and non-employee directors are excluded from participating;
› Stock options are purchased by third-party financial institutions at a discount to their fair value using option pricing models such as Black-Scholes or a Binomial Option Valuation or other appropriate financial models;
› There is a two-year minimum holding period for sale proceeds (cash or stock) for all participants.

Additionally, management should provide a clear explanation of why options are being transferred to a third-party institution and whether the events leading up to a decline in stock price were beyond management’s control. A review of the company’s historic stock price volatility should indicate if the options are likely to be back “in-the-money” over the near term.

**Ongoing TSO program:** Vote against equity plan proposals if the details of ongoing TSO programs are not provided to shareholders. Since TSOs will be one of the award types under a stock plan, the ongoing TSO program, structure and mechanics must be disclosed to shareholders. The specific criteria to be considered in evaluating these proposals include, but not limited, to the following:

› Eligibility;
› Vesting;
› Bid-price;
› Term of options;
› Cost of the program and impact of the TSOs on company’s total option expense; and
› Option repricing policy.

Amendments to existing plans that allow for introduction of transferability of stock options should make clear that only options granted post-amendment shall be transferable.
401(k) Employee Benefit Plans

The 401(k) plan is one of the most popular employee benefit plans among U.S. companies. A 401(k) plan is any qualified plan under Section 401(k) of the Internal Revenue Code that contains a cash or deferred arrangement. In its simplest form, an employee can elect to have a portion of his salary invested in a 401(k) plan before any income taxes are assessed. The money can only be withdrawn before retirement under penalty. However, because the money contributed to the plan is withdrawn before taxes (reducing the employee's income tax), a properly planned 401(k) plan will enable an employee to make larger contributions to a 401(k) plan than to a savings plan, and still take the same amount home.

Social Advisory Services Recommendation: Vote for proposals to implement a 401(k) savings plan for employees.

Severance Agreements for Executives/Golden Parachutes

Social Advisory Services Recommendation: Vote on a case-by-case basis on proposals to ratify or cancel golden parachutes. An acceptable parachute should include, but is not limited to, the following:

› The triggering mechanism should be beyond the control of management;
› The amount should not exceed three times base amount (defined as the average annual taxable W-2 compensation during the five years prior to the year in which the change of control occurs;
› Change-in-control payments should be double-triggered, i.e., (1) after a change in control has taken place, and (2) termination of the executive as a result of the change in control. Change in control is defined as a change in the company ownership structure.

Director Compensation

The board’s legal charge of fulfilling its fiduciary obligations of loyalty and care is put to the ultimate test through the task of the board setting its own compensation. Directors themselves oversee the process for evaluating board performance and establishing pay packages for board members.

Shareholders provide limited oversight of directors by electing individuals who are primarily selected by the board, or a board nominating committee, and by voting on stock-based plans for directors designed by the board compensation committee. Additionally, shareholders may submit and vote on their own resolutions seeking to limit or restructure director pay. While the cost of compensating non-employee directors is small in absolute terms, compared to the cost of compensating executives, it is still a critical aspect of a company’s overall corporate governance structure.

Overall, director pay levels are rising in part because of the new forms of pay in use at many companies, as well as because of the increased responsibilities arising from the 2002 Sarbanes-Oxley Act requirements. In addition to an annual retainer fee, many companies also pay fees for attending board and committee meetings, fees for chairing a committee, or a retainer fee for chairing a committee.

Director compensation packages should be designed to provide value to directors for their contribution. Given that many directors are high-level executives whose personal income levels are generally high, cash compensation may hold little appeal. Stock-based incentives on the other hand reinforce the directors’ role of protecting and enhancing shareholder value. The stock-based component of director compensation should be large enough to ensure that when faced with a situation in which the interests of shareholders and management differ, the board will have a financial incentive to think as a shareholder. Additionally, many companies have instituted equity ownership programs for directors. Social Advisory Services recommends that directors receive stock grants equal to three times of their annual
retainer, as it is a reasonable starting point for companies of all sizes and industries. A vesting schedule for director grants helps directors to meet the stock ownership guidelines and maintains their long-term interests in the firm.

Director compensation packages should also be designed to attract and retain competent directors who are willing to risk becoming a defendant in a lawsuit and suffer potentially adverse publicity if the company runs into financial difficulties or is mismanaged.

Shareholder Ratification of Director Pay Programs

Social Advisory Services Recommendation: Vote case-by-case on management proposals seeking ratification of non-employee director compensation, based on the following factors:
› If the equity plan under which non-employee director grants are made is on the ballot, whether or not it warrants support; and
› An assessment of the following qualitative factors:
   › The relative magnitude of director compensation as compared to companies of a similar profile;
   › The presence of problematic pay practices relating to director compensation;
   › Director stock ownership guidelines and holding requirements;
   › Equity award vesting schedules;
   › The mix of cash and equity-based compensation;
   › Meaningful limits on director compensation;
   › The availability of retirement benefits or perquisites; and
   › The quality of disclosure surrounding director compensation.

Equity Plans for Non-Employee Directors

Stock-based plans may take on a variety of forms including: grants of stock or options, including: discretionary grants, formula based grants, and one-time awards; stock-based awards in lieu of all or some portion of the cash retainer and/or other fees; and deferred stock plans allowing payment of retainer and/or meeting fees to be taken in stock, the payment of which is postponed to some future time, typically retirement or termination of directorship.

Social Advisory Services Recommendation: Vote case-by-case on compensation plans for non-employee directors, based on:
› The total estimated cost of the company’s equity plans relative to industry/market cap peers, measured by the company’s estimated Shareholder Value Transfer (SVT) based on new shares requested plus shares remaining for future grants, plus outstanding unvested/unexercised grants;
› The company’s three year burn rate relative to its industry/market cap peers; and
› The presence of any egregious plan features (such as an option repricing provision or liberal CIC vesting risk).

On occasion, director stock plans that set aside a relatively small number of shares will exceed the plan cost or burn rate benchmark when combined with employee or executive stock compensation plans. In such cases, vote for the plan if all of the following qualitative factors in the board’s compensation are met and disclosed in the proxy statement:
› The relative magnitude of director compensation as compared to companies of a similar profile;
› The presence of problematic pay practices relating to director compensation;
› Director stock ownership guidelines and holding requirement;
› Equity award vesting schedules;
› The mix of cash and equity-based compensation;
› Meaningful limits on director compensation;
› The availability of retirement benefits or perquisites;
› The quality of disclosure surrounding director compensation.
**Outside Director Stock Awards/Options in Lieu of Cash**

These proposals seek to pay outside directors a portion of their compensation in stock rather than cash. By doing this, a director’s interest may be more closely aligned with those of shareholders.

**Social Advisory Services Recommendation:** Vote for proposals that seek to pay outside directors a portion of their compensation in stock rather than cash.

**Director Retirement Plans**

**Social Advisory Services Recommendation:**

› Vote against retirement plans for non-employee directors.
› Vote for shareholder proposals to eliminate retirement plans for non-employee directors.

**Shareholder Proposals on Compensation**

**Increase Disclosure of Executive Compensation**

The SEC requires that companies disclose, in their proxy statements, the salaries of the top five corporate executives (who make at least $100,000 a year). Companies also disclose their compensation practices and details of their stock-based compensation plans. While this level of disclosure is helpful, it does not always provide a comprehensive picture of the company’s compensation practices. For shareholders to make informed decisions on compensation levels, they need to have clear, concise information at their disposal. Increased disclosure will help ensure that management: (1) has legitimate reasons for setting specific pay levels; and (2) is held accountable for its actions.

**Social Advisory Services Recommendation:** Vote for shareholder proposals seeking increased disclosure on executive compensation issues including the preparation of a formal report on executive compensation practices and policies.

**Limit Executive Compensation**

Proposals that seek to limit executive or director compensation usually focus on the absolute dollar figure of the compensation or focus on the ratio of compensation between the executives and the average worker of a specific company. Proponents argue that the exponential growth of executive salaries is not in the best interests of shareholders, especially when that pay is exorbitant when compared to the compensation of other workers.

**Social Advisory Services Recommendation:**

› Vote for proposals to prepare reports seeking to compare the wages of a company’s lowest paid worker to the highest paid workers.
› Vote case-by-case on proposals that seek to establish a fixed ratio between the company’s lowest paid workers and the highest paid workers.

**Stock Ownership Requirements**

Corporate directors should own some amount of stock of the companies on which they serve as board members. Stock ownership is a simple method to align the interests of directors with company shareholders. Nevertheless, many highly qualified individuals such as academics and clergy who can offer valuable perspectives in boardrooms may be unable to...
purchase individual shares of stock. In such a circumstance, the preferred solution is to look at the board nominees individually and take stock ownership into consideration when voting on the merits of each candidate.

**Social Advisory Services Recommendation:** Generally vote against shareholder proposals that mandate a minimum amount of stock that directors must own in order to qualify as a director or to remain on the board.

### Prohibit/Require Shareholder Approval for Option Repricing

Repricing involves the reduction of the original exercise price of a stock option after the fall in share price. Social Advisory Services does not support repricing since it undermines the incentive purpose of the plan. The use of options as an incentive means that employees must bear the same risks as shareholders in holding these options. Shareholder resolutions calling on companies to abandon the practice of repricing or to submit repricings to a shareholder vote will be supported.

**Social Advisory Services Recommendation:**
- Vote for shareholder proposals seeking to limit repricing.
- Vote for shareholder proposals asking the company to have option repricings submitted for shareholder ratification.

### Severance Agreements/Golden Parachutes

Golden parachutes are designed to protect the employees of a corporation in the event of a change in control. With Golden Parachutes senior level management employees receive a payout during a change in control at usually two to three times base salary.

**Social Advisory Services Recommendation:** Vote for shareholder proposals requiring that golden parachutes or executive severance agreements be submitted for shareholder ratification, unless the proposal requires shareholder approval prior to entering into employment contracts.

### Cash Balance Plans

A cash balance plan is a defined benefit plan that treats an earned retirement benefit as if it was a credit from a defined contribution plan, but which provides a stated benefit at the end of its term. Because employer contributions to these plans are credited evenly over the life of a plan, and not based on a seniority formula they may reduce payouts to long-term employees who are currently vested in plans.

Cash-balance pension conversions have undergone congressional and federal agency scrutiny following high-profile EEOC complaints on age discrimination and employee anger at companies like IBM. While significant change is unlikely in the short-term, business interests were concerned enough that the National Association of Manufacturers and other business lobbies formed a Capitol Hill coalition to preserve the essential features of the plans and to overturn an IRS ruling. Driving the push behind conversions from traditional pension plans to cash-balance plans are the substantial savings that companies generate in the process. Critics point out that these savings are gained at the expense of the most senior employees. Resolutions call on corporate boards to establish a committee of outside directors to prepare a report to shareholders on the potential impact of pension-related proposals now being considered by national policymakers in reaction to the controversy spawned by the plans.

**Social Advisory Services Recommendation:**
- Vote for shareholder proposals calling for non-discrimination in retirement benefits.
Vote for shareholder proposals asking a company to give employees the option of electing to participate in either a cash balance plan or in a defined benefit plan.

**Performance-Based Equity Awards**

Social Advisory Services supports compensating executives at a reasonable rate and believes that executive compensation should be strongly correlated to performance. Social Advisory Services supports equity awards that provide challenging performance objectives and serve to motivate executives to superior performance and as performance-contingent stock options as a significant component of compensation.

**Social Advisory Services Recommendation:** Vote case-by-case on shareholder proposal requesting that a significant amount of future long-term incentive compensation awarded to senior executives shall be performance-based and requesting that the board adopt and disclose challenging performance metrics to shareholders, based on the following analytical steps:

- First, vote for shareholder proposals advocating the use of performance-based equity awards, such as performance contingent options or restricted stock, indexed options or premium-priced options, unless the proposal is overly restrictive or if the company has demonstrated that it is using a “substantial” portion of performance-based awards for its top executives. Standard stock options and performance-accelerated awards do not meet the criteria to be considered as performance-based awards. Further, premium-priced options should have a meaningful premium to be considered performance-based awards.

- Second, assess the rigor of the company’s performance-based equity program. If the bar set for the performance-based program is too low based on the company’s historical or peer group comparison, generally vote for the proposal. Furthermore, if target performance results in an above target payout, vote for the shareholder proposal due to program’s poor design. If the company does not disclose the performance metric of the performance-based equity program, vote for the shareholder proposal regardless of the outcome of the first step to the test.

In general, vote for the shareholder proposal if the company does not meet both of the above two steps.

**Pay for Superior Performance**

**Social Advisory Services Recommendation:** Generally vote for shareholder proposals based on a case-by-case analysis that requests the board establish a pay-for-superior performance standard in the company’s executive compensation plan for senior executives. The proposal has the following principles:

- Sets compensation targets for the Plan’s annual and long-term incentive pay components at or below the peer group median;
- Delivers a majority of the Plan’s target long-term compensation through performance-vested, not simply time-vested, equity awards;
- Provides the strategic rationale and relative weightings of the financial and non-financial performance metrics or criteria used in the annual and performance-vested long-term incentive components of the plan;
- Establishes performance targets for each plan financial metric relative to the performance of the company’s peer companies;
- Limits payment under the annual and performance-vested long-term incentive components of the plan to when the company’s performance on its selected financial performance metrics exceeds peer group median performance.

Consider the following factors in evaluating this proposal:

- What aspects of the company’s annual and long-term equity incentive programs are performance driven?
If the annual and long-term equity incentive programs are performance driven, are the performance criteria and hurdle rates disclosed to shareholders or are they benchmarked against a disclosed peer group?

Can shareholders assess the correlation between pay and performance based on the current disclosure?

What type of industry and stage of business cycle does the company belong to?

**Link Compensation to Non-Financial Factors**

Proponents of these proposals feel that social and environmental criteria should be factored into the formulas used in determining executive compensation packages. The shareholder sponsors of the resolutions look to companies to review current compensation practices and to include social or environmental performance criteria such as accounting for “poor corporate citizenship” and meeting environmental or workplace safety objectives and metrics when evaluating executive compensation. Some of the non-financial criteria that proponents of these resolutions seek to be incorporated in compensation program design include workplace safety, environmental stewardship, or diversity and customer/employee satisfaction – as part of a written policy used to align compensation with performance on non-financial factors alongside financial criteria.

Proponents believe that factors such as poor environmental performance, workplace lawsuits, etc. could have a significant adverse impact on a company’s financial performance if not proactively and adequately addressed, and that these factors *should* be considered along with traditional financial considerations when determining executive pay. The significant stock price declines and massive losses in shareholder value stemming from the BP Deepwater Horizon oil rig disaster and the tragic explosion at Massey Energy’s Upper Big Branch mine that killed 29 employees is a sobering reminder of the need to have the right management incentives in place to ensure that social and environmental risks are actively managed and mitigated against. Given the proliferation of derivative lawsuits targeted at firms such as Halliburton, Transocean and Cameron International that were suppliers to or partners with BP in a capacity that ignored safety considerations or that contributed to the economic and ecological disaster, investors are increasingly mindful of the far-reaching implications that exposure to social or environmental risks could have on shareholder value at portfolio companies.

**Social Advisory Services Recommendation:**

› Vote for shareholder proposals calling for linkage of executive pay to non-financial factors including performance against social and environmental goals, customer/employee satisfaction, corporate downsizing, community involvement, human rights, or predatory lending.

› Vote for shareholder proposals seeking reports on linking executive pay to non-financial factors.

**Advisory Vote on Executive Compensation (Say-on-Pay) Shareholder Proposals**

**Social Advisory Services Recommendation:** Generally, vote for shareholder proposals that call for non-binding shareholder ratification of the compensation of the Named Executive Officers and the accompanying narrative disclosure of material factors provided to understand the Summary Compensation Table.

**Termination of Employment Prior to Severance Payment and Eliminating Accelerated Vesting of Unvested Equity**

**Social Advisory Services Recommendation:** Generally vote for proposals seeking a policy that prohibits acceleration of the vesting of equity awards to senior executives in the event of a change in control (except for pro rata vesting considering the time elapsed and attainment of any related performance goals between the award date and the change in control).
Vote on a case-by-case on shareholder proposals seeking a policy requiring termination of employment prior to severance payment, and eliminating accelerated vesting of unvested equity. The following factors will be taken into regarding this policy:

› The company’s current treatment of equity in change-of-control situations (i.e. is it double triggered, does it allow for the assumption of equity by acquiring company, the treatment of performance shares;
› Current employment agreements, including potential problematic pay practices such as gross-ups embedded in those agreements.

Tax Gross-up Proposals

Social Advisory Services Recommendation: Generally vote for proposals calling for companies to adopt a policy of not providing tax gross-up payments to executives, except in situations where gross-ups are provided pursuant to a plan, policy, or arrangement applicable to management employees of the company, such as a relocation or expatriate tax equalization policy.

Compensation Consultants - Disclosure of Board or Company’s Utilization

Social Advisory Services Recommendation: Generally vote for shareholder proposals seeking disclosure regarding the company, board, or compensation committee’s use of compensation consultants, such as company name, business relationship(s) and fees paid.

Golden Coffins/Executive Death Benefits

Social Advisory Services Recommendation: Generally vote for proposals calling companies to adopt a policy of obtaining shareholder approval for any future agreements and corporate policies that could oblige the company to make payments or awards following the death of a senior executive in the form of unearned salary or bonuses, accelerated vesting or the continuation in force of unvested equity grants, perquisites and other payments or awards made in lieu of compensation. This would not apply to any benefit programs or equity plan proposals that the broad-based employee population is eligible.

Recoup Bonuses

Social Advisory Services Recommendation: Vote on a case-by-case on proposals to recoup unearned incentive bonuses or other incentive payments made to senior executives if it is later determined that the figures upon which incentive compensation is earned later turn out to have been in error. This is line with the clawback provision in the Troubled Asset Relief Program. Many companies have adopted policies that permit recoupment in cases where fraud, misconduct, or negligence significantly contributed to a restatement of financial results that led to the awarding of unearned incentive compensation. The following will be taken into consideration:

› If the company has adopted a formal recoupment bonus policy;
› If the company has chronic restatement history or material financial problems;
› If the company’s policy substantially addresses the concerns raised by the proponent.

Adopt Anti-Hedging/Pledging/Speculative Investments Policy

Social Advisory Services Recommendation: Generally vote for proposals seeking a policy that prohibits named executive officers from engaging in derivative or speculative transactions involving company stock, including hedging, holding stock in a margin account, or pledging stock as collateral for a loan. However, the company’s existing policies regarding responsible use of company stock will be considered.

Bonus Banking

Enabling the financial community to manage governance risk for the benefit of shareholders.
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Social Advisory Services Recommendation: Vote case-by-case on proposals seeking deferral of a portion of annual bonus pay, with ultimate payout linked to sustained results for the performance metrics on which the bonus was earned (whether for the named executive officers or a wider group of employees), taking into account the following factors:
› The company’s past practices regarding equity and cash compensation;
› Whether the company has a holding period or stock ownership requirements in place, such as a meaningful retention ratio (at least 50 percent for full tenure); and
› Whether the company has a rigorous claw-back policy in place.

Hold Equity Past Retirement or for a Significant Period of Time
Social Advisory Services Recommendation: Vote case-by-case on shareholder proposals asking companies to adopt policies requiring senior executive officers to retain a portion of net shares acquired through compensation plans. The following factors will be taken into account:
› The percentage/ratio of net shares required to be retained;
› The time period required to retain the shares;
› Whether the company has equity retention, holding period, and/or stock ownership requirements in place and the robustness of such requirements;
› Whether the company has any other policies aimed at mitigating risk taking by executives;
› Executives' actual stock ownership and the degree to which it meets or exceeds the proponent’s suggested holding period/retention ratio or the company’s existing requirements; and
› Problematic pay practices, current and past, which may demonstrate a short-term versus long-term focus.

Non-Deductible Compensation
Social Advisory Services Recommendation: Generally vote for proposals seeking disclosure of the extent to which the company paid non-deductible compensation to senior executives due to Internal Revenue Code Section 162(m), while considering the company’s existing disclosure practices.

Pre-Arranged Trading Plans (10b5-1 Plans)
Social Advisory Services Recommendation: Generally vote for shareholder proposals calling for certain principles regarding the use of prearranged trading plans (10b5-1 plans) for executives. These principles include:
› Adoption, amendment, or termination of a 10b5-1 Plan must be disclosed within two business days in a Form 8-K;
› Amendment or early termination of a 10b5-1 Plan is allowed only under extraordinary circumstances, as determined by the board;
› Ninety days must elapse between adoption or amendment of a 10b5-1 Plan and initial trading under the plan;
› Reports on Form 4 must identify transactions made pursuant to a 10b5-1 Plan;
› An executive may not trade in company stock outside the 10b5-1 Plan;
› Trades under a 10b5-1 Plan must be handled by a broker who does not handle other securities transactions for the executive.
7. MERGERS AND CORPORATE RESTRUCTURINGS

A merger occurs when one corporation is absorbed into another and ceases to exist. The surviving company gains all the rights, privileges, powers, duties, obligations and liabilities of the merged corporation. The shareholders of the absorbed company receive stock or securities of the surviving company or other consideration as provided by the plan of merger. Mergers, consolidations, share exchanges, and sale of assets are friendly in nature, which is to say that both sides have agreed to the combination or acquisition of assets.

Shareholder approval for an acquiring company is generally not required under state law or stock exchange regulations unless the acquisition is in the form of a stock transaction which would result in the issue of 20 percent or more of the acquirer’s outstanding shares or voting power, or unless the two entities involved require that shareholders approve the deal. Under most state laws, however, a target company must submit merger agreements to a shareholder vote. Shareholder approval is required in the formation of a consolidated corporation.

Mergers and Acquisitions

M&A analyses are inherently a balance of competing factors. Bright line rules are difficult if not impossible to apply to a world where every deal is different. Ultimately, the question for shareholders (both of the acquirer and the target) is the following: Is the valuation fair? Shareholders of the acquirer may be concerned that the deal values the target too highly. Shareholders of the target may be concerned that the deal undervalues their interests.

Vote recommendation will be based on primarily an analysis of shareholder value, which itself can be affected by ancillary factors such as the negotiation process. The importance of other factors, including corporate governance and social and environmental considerations however, should not fail to be recognized.

Social Advisory Services Recommendation: Votes on mergers and acquisitions are considered on a case-by-case basis. A review and evaluation of the merits and drawbacks of the proposed transaction is conducted, balancing various and sometimes countervailing factors including:

- **Valuation** - is the value to be received by the target shareholders (or paid by the acquirer) reasonable? While the fairness opinion may provide an initial starting point for assessing valuation reasonableness, emphasis is placed on the offer premium, market reaction and strategic rationale;
- **Market reaction** - how has the market responded to the proposed deal? A negative market reaction should cause closer scrutiny of a deal;
- **Strategic rationale** - does the deal make sense strategically? From where is the value derived? Cost and revenue synergies should not be overly aggressive or optimistic, but reasonably achievable. Management should also have a favorable track record of successful integration of historical acquisitions;
- **Negotiations and process** - were the terms of the transaction negotiated at arm's-length? Was the process fair and equitable?
- **Conflicts of interest** - are insiders benefiting from the transaction disproportionately and inappropriately as compared to non-insider shareholders?
- **Governance** - will the combined company have a better or worse governance profile than the current governance profiles of the respective parties to the transaction?
- **Stakeholder impact** - impact on community stakeholders and workforce including impact on stakeholders, such as job loss, community lending, equal opportunity, impact on environment etc.

Corporate Reorganization/Restructuring Plans (Bankruptcy)

The recent financial crisis has placed Chapter 11 bankruptcy reorganizations as a potential alternative for distressed companies. While the number of bankruptcies has risen over the past year as evidenced by many firms, including
General Motors and Lehman Brothers, the prevalence of these reorganizations can vary year over year due to, among other things, market conditions and a company's ability to sustain its operations. Additionally, the amount of time that lapses between a particular company's entrance into Chapter 11 and its submission of a plan of reorganization varies significantly depending on the complexity, timing, and jurisdiction of the particular case. These plans are often put to a vote of shareholders (in addition to other interested parties), as required by the Bankruptcy Code.

Social Advisory Services Recommendation: Vote case-by-case on proposals to common shareholders on bankruptcy plans of reorganization, considering the following factors including, but not limited to:

› Estimated value and financial prospects of the reorganized company;
› Percentage ownership of current shareholders in the reorganized company;
› Whether shareholders are adequately represented in the reorganization process (particularly through the existence of an official equity committee);
› The cause(s) of the bankruptcy filing, and the extent to which the plan of reorganization addresses the cause(s);
› Existence of a superior alternative to the plan of reorganization;
› Governance of the reorganized company.

Special Purpose Acquisition Corporations (SPACs)

Social Advisory Services Recommendation: Vote case-by-case on SPAC mergers and acquisitions taking into account the following:

› Valuation - Is the value being paid by the SPAC reasonable? SPACs generally lack an independent fairness opinion and the financials on the target may be limited. Compare the conversion price with the intrinsic value of the target company provided in the fairness opinion. Also, evaluate the proportionate value of the combined entity attributable to the SPAC IPO shareholders versus the pre-merger value of SPAC. Additionally, a private company discount may be applied to the target, if it is a private entity.
› Market reaction - How has the market responded to the proposed deal? A negative market reaction may be a cause for concern. Market reaction may be addressed by analyzing the one-day impact on the unaffected stock price.
› Deal timing - A main driver for most transactions is that the SPAC charter typically requires the deal to be complete within 18 to 24 months, or the SPAC is to be liquidated. Evaluate the valuation, market reaction, and potential conflicts of interest for deals that are announced close to the liquidation date.
› Negotiations and process - What was the process undertaken to identify potential target companies within specified industry or location specified in charter? Consider the background of the sponsors.
› Conflicts of interest - How are sponsors benefiting from the transaction compared to IPO shareholders? Potential conflicts could arise if a fairness opinion is issued by the insiders to qualify the deal rather than a third party or if management is encouraged to pay a higher price for the target because of an 80 percent rule (the charter requires that the fair market value of the target is at least equal to 80 percent of net assets of the SPAC). Also, there may be sense of urgency by the management team of the SPAC to close the deal since its charter typically requires a transaction to be completed within the 18-24 month timeframe.
› Voting agreements - Are the sponsors entering into enter into any voting agreements/tender offers with shareholders who are likely to vote against the proposed merger or exercise conversion rights?
› Governance - What is the impact of having the SPAC CEO or founder on key committees following the proposed merger?
› Stakeholder Impact - impact on community stakeholders and workforce including impact on stakeholders, such as job loss, community lending, equal opportunity, impact on environment etc.
Special Purpose Acquisition Corporations (SPACs) - Proposals for Extensions

Social Advisory Services Recommendation: Vote case-by-case on SPAC extension proposals taking into account the length of the requested extension, the status of any pending transaction(s) or progression of the acquisition process, any added incentive for non-redeeming shareholders, and any prior extension requests.

› **Length of request:** Typically, extension requests range from two to six months, depending on the progression of the SPAC’s acquisition process.

› **Pending transaction(s) or progression of the acquisition process:** Sometimes an initial business combination was already put to a shareholder vote, but, for varying reasons, the transaction could not be consummated by the termination date and the SPAC is requesting an extension. Other times, the SPAC has entered into a definitive transaction agreement, but needs additional time to consummate or hold the shareholder meeting.

› **Added incentive for non-redeeming shareholders:** Sometimes the SPAC sponsor (or other insiders) will contribute, typically as a loan to the company, additional funds that will be added to the redemption value of each public share as long as such shares are not redeemed in connection with the extension request. The purpose of the “equity kicker” is to incentivize shareholders to hold their shares through the end of the requested extension or until the time the transaction is put to a shareholder vote, rather than electing redemption at the extension proposal meeting.

› **Prior extension requests:** Some SPACs request additional time beyond the extension period sought in prior extension requests.

Spin-offs

Social Advisory Services Recommendation: Votes on spin-offs should be considered on a case-by-case basis depending on the tax and regulatory advantages, planned use of sale proceeds, valuation of spinoff, fairness opinion, benefits to the parent company, conflicts of interest, managerial incentives, corporate governance changes, changes in the capital structure.

Asset Purchases

Social Advisory Services Recommendation: Votes on asset purchase proposals should be made on a case-by-case after considering the purchase price, fairness opinion, financial and strategic benefits, how the deal was negotiated, conflicts of interest, other alternatives for the business, non-completion risk.

Asset Sales

Social Advisory Services Recommendation: Votes on asset sales should be made on a case-by-case basis after considering the impact on the balance sheet/working capital, value received for the asset, potential elimination of diseconomies, anticipated financial and operating benefits, anticipated use of funds, fairness opinion, how the deal was negotiated, and conflicts of interest.

Liquidations

Social Advisory Services Recommendation: Votes on liquidations should be made on a case-by-case basis after reviewing management’s efforts to pursue other alternatives, appraisal value of assets, and the compensation plan for executives managing the liquidation. Vote for the liquidation if the company will file for bankruptcy if the proposal is not approved.
Joint Ventures

**Social Advisory Services Recommendation:** Vote case-by-case on proposals to form joint ventures, taking into account percentage of assets/business contributed, percentage ownership, financial and strategic benefits, governance structure, conflicts of interest, other alternatives and non-completion risk.

Appraisal Rights

Rights of appraisal provide shareholders who do not approve of the terms of certain corporate transactions the right to demand a judicial review in order to determine the fair value for their shares. The right of appraisal generally applies to mergers, sales of essentially all assets of the corporation, and charter amendments that may have a materially adverse effect on the rights of dissenting shareholders.

**Social Advisory Services Recommendation:** Vote for proposals to restore, or provide shareholders with, rights of appraisal.

Going Private/Dark Transactions (Leveraged buyouts and Minority Squeeze-outs)

**Social Advisory Services Recommendation:** Vote case-by-case on going private transactions, taking into account the following: offer price/premium, fairness opinion, how the deal was negotiated, conflicts of interest, other alternatives/offers considered, and non-completion risk.

Vote case-by-case on “going dark” transactions, determining whether the transaction enhances shareholder value by taking into consideration:

- Whether the company has attained benefits from being publicly-traded (examination of trading volume, liquidity, and market research of the stock);
- Balanced interests of continuing vs. cashed-out shareholders, taking into account the following:
  - Are all shareholders able to participate in the transaction?
  - Will there be a liquid market for remaining shareholders following the transaction?
  - Does the company have strong corporate governance?
  - Will insiders reap the gains of control following the proposed transaction?
  - Does the state of incorporation have laws requiring continued reporting that may benefit shareholders?

Private Placements/Warrants/Convertible Debentures

**Social Advisory Services Recommendation:** Vote case-by-case on proposals regarding private placements taking into consideration:

- Dilution to existing shareholders’ position.
  - The amount and timing of shareholder ownership dilution should be weighed against the needs and proposed shareholder benefits of the capital infusion.
- Terms of the offer - discount/premium in purchase price to investor, including any fairness opinion; conversion features; termination penalties; exit strategy.
  - The terms of the offer should be weighed against the alternatives of the company and in light of company’s financial issues.
  - When evaluating the magnitude of a private placement discount or premium, Social Advisory Services will consider whether it is affected by liquidity, due diligence, control and monitoring issues, capital scarcity, information asymmetry and anticipation of future performance.
- Financial issues include but are not limited to examining the following: a) company’s financial situation; b) degree of need for capital; c) use of proceeds; d) effect of the financing on the company’s cost of capital; e) current and proposed cash burn rate; and f) going concern viability and the state of the capital and credit markets.
Management's efforts to pursue alternatives and whether the company engaged in a process to evaluate alternatives. A fair, unconstrained process helps to ensure the best price for shareholders. Financing alternatives can include joint ventures, partnership, merger or sale of part or all of the company.

Control issues including: a) Change in management; b) change in control; c) guaranteed board and committee seats; d) standstill provisions; e) voting agreements; f) veto power over certain corporate actions.

Minority versus majority ownership and corresponding minority discount or majority control premium

Conflicts of interest

Were the terms of the transaction negotiated at arm's-length? Are managerial incentives aligned with shareholder interests?

Market reaction

The market’s response to the proposed deal. A negative market reaction is a cause for concern. Market reaction may be addressed by analyzing the one day impact on the unaffected stock price.

Vote for the private placement if it is expected that the company will file for bankruptcy if the transaction is not approved.

Formation of Holding Company

Social Advisory Services Recommendation:

Vote case-by-case on proposals regarding the formation of a holding company, taking into consideration: a) the reasons for the change; b) any financial or tax benefits; c) regulatory benefits; d) increases in capital structure; and e) changes to the articles of incorporation or bylaws of the company.

Vote against the formation of a holding company, absent compelling financial reasons to support the transaction, if the transaction would include either: a) increases in common or preferred stock in excess of the allowable maximum; or b) adverse changes in shareholder rights.

Value Maximization Shareholder Proposals

Social Advisory Services Recommendation: Vote case-by-case on shareholder proposals seeking to maximize shareholder value by hiring a financial advisor to explore strategic alternatives, selling the company or liquidating the company and distributing the proceeds to shareholders. These proposals should be evaluated based on the following factors:

Prolonged poor performance with no turnaround in sight;
Signs of entrenched board and management;
Strategic plan in place for improving value;
Likelihood of receiving reasonable value in a sale or dissolution;
Whether company is actively exploring its strategic options, including retaining a financial advisor.
8. SOCIAL AND ENVIRONMENTAL PROPOSALS

Socially responsible shareholder resolutions are receiving a great deal more attention from institutional shareholders today than they have in the past. In addition to the moral and ethical considerations intrinsic to many of these proposals, there is a growing recognition of their potential impact on the economic performance of the company. Among the reasons for this change are:

› The number and variety of shareholder resolutions on social and environmental issues has increased;
› Many of the sponsors and supporters of these resolutions are large institutional shareholders with significant holdings, and therefore, greater direct influence on the outcomes;
› The proposals are more sophisticated – better written, more focused, and more sensitive to the feasibility of implementation;
› Investors now understand that a company’s response to social and environmental issues can have serious economic consequences for the company and its shareholders.

Social Advisory Services Recommendation: Generally vote for social and environmental shareholder proposals that promote good corporate citizens while enhancing long-term shareholder and stakeholder value. Vote for disclosure reports that seek additional information particularly when it appears companies have not adequately addressed shareholders’ social, workforce, and environmental concerns. In determining vote recommendations on shareholder social, workforce, and environmental proposals, Social Advisory Services will analyze the following factors:

› Whether the proposal itself is well framed and reasonable;
› Whether adoption of the proposal would have either a positive or negative impact on the company’s short-term or long-term share value;
› Whether the company’s analysis and voting recommendation to shareholders is persuasive;
› The degree to which the company’s stated position on the issues could affect its reputation or sales, or leave it vulnerable to boycott or selective purchasing;
› Whether the subject of the proposal is best left to the discretion of the board;
› Whether the issues presented in the proposal are best dealt with through legislation, government regulation, or company-specific action;
› The company’s approach compared with its peers or any industry standard practices for addressing the issue(s) raised by the proposal;
› Whether the company has already responded in an appropriate or sufficient manner to the issue(s) raised in the proposal;
› Whether there are significant controversies, fines, penalties, or litigation associated with the company’s environmental or social practices;
› If the proposal requests increased disclosure or greater transparency, whether sufficient information is publically available to shareholders and whether it would be unduly burdensome for the company to compile and avail the requested information to shareholders in a more comprehensive or amalgamated fashion;
› Whether implementation of the proposal would achieve the objectives sought in the proposal.

In general, Social Advisory Services supports proposals that request the company to furnish information helpful to shareholders in evaluating the company’s operations. In order to be able to intelligently monitor their investments shareholders often need information best provided by the company in which they have invested. Requests to report such information will merit support. Requests to establish special committees of the board to address broad corporate policy and provide forums for ongoing dialogue on issues including, but not limited to shareholder relations, the environment, human rights, occupational health and safety, and executive compensation, will generally be supported, particularly when they appear to offer a potentially effective method for enhancing shareholder value. We will closely evaluate proposals that ask the company to cease certain actions that the proponent believes are harmful to society or some segment of society with special attention to the company’s legal and ethical obligations, its ability to remain...
profitable, and potential negative publicity if the company fails to honor the request. Social Advisory Services supports shareholder proposals that improve the company’s public image, and reduce exposure to liabilities.

Diversity and Equality

Significant progress has been made in recent years in the advancement of women and racial minorities in the workplace and the establishment of greater protections against discriminatory practices in the workplace. In the U.S, there are many civil rights laws that are enforced by the Equal Employment Opportunity Commission. The Civil Rights Act of 1964 prohibits discrimination based on race, color, religion, sex and nationality. However, discrimination on the basis of race, gender, religion, nationality, and sexual preference continues. The SEC’s revised disclosure rules now require information on how boards factor diversity into the director nomination process, as well as disclosure on how the board assesses the effectiveness of its diversity policy. Shareholder proposals on diversity may target a company’s board nomination procedures or seek greater disclosure on a company’s programs and procedures on increasing the diversity of its workforce, and make reference to one or more of the following points:

› Violations of workplace anti-discrimination laws lead to expensive litigation and damaged corporate reputations that are not in the best interests of shareholders;
› Employers already prepare employee diversity reports for the EEOC, so preparing a similar report to shareholders can be done at minimal cost;
› The presence of women, ethnic minorities and union members in workforce and customer pools gives companies with diversified boards a practical advantage over their competitors as a result of their unique perspectives;
› Efforts to include women, minorities and union representatives on corporate boards can be made at reasonable costs;
› Reports can be prepared “at reasonable expense” describing efforts to encourage diversified representation on their boards;
› Board diversification increases the pool of the company’s potential investors because more and more investors are favoring companies with diverse boards;
› A commitment to diversity in the workforce can lead to superior financial returns.

Add Women and Minorities to the Board

Board diversification proposals ask companies to put systems in place to increase the representation of women, racial minorities, union members or other underrepresented minority groups on boards of directors. In prior years, board diversification proposals requested that companies nominate board members from certain constituencies, appoint special committees to recommend underrepresented classes of board members, establish board positions reserved for representatives of certain groups, or simply “make greater efforts” to nominate women and ethnic minorities to their boards.

Social Advisory Services Recommendation:
› Vote for shareholder proposals that ask the company to take steps to nominate more women and racial minorities to the board.
› Vote for shareholder proposals asking for reports on board diversity.
› Vote for shareholder proposals asking companies to adopt nomination charters or amend existing charters to include reasonable language addressing diversity.

Report on the Distribution of Stock Options by Gender and Race

Companies have received requests from shareholders to prepare reports documenting the distribution of the stock options and restricted stock awards by race and gender of the recipient. Proponents of these proposals argue that, in the future, there will be a shift toward basing racial and gender discrimination suits on the distribution of corporate
wealth through stock options. The appearance of these proposals is also in response to the nationwide wage gap and under representation of minorities and women at the highest levels of compensation.

**Social Advisory Services Recommendation:** Vote for shareholder proposals asking companies to report on the distribution of stock options by race and gender of the recipient.

**Prepare Report/Promote EEOC-Related Activities**

Filers of proposals on this issue generally ask a company to make available, at reasonable cost and omitting proprietary information, data the company includes in its annual report to the Equal Employment Opportunity Commission (EEOC) outlining the make-up of its workforce by race, gender and position. Shareholders also ask companies to report on any efforts they are making to advance the representation of women and ethnic minorities in jobs in which they have been historically underrepresented, such as sales and management. The costs of violating federal laws that prohibit discrimination by corporations are high and can affect corporate earnings. The Equal Opportunities Employment Commission does not release the companies’ filings to the public, unless it is involved in litigation, and this information is difficult to obtain from other sources. Companies need to be sensitive to minority employment issues as the new evolving work force becomes increasingly diverse. This information can be provided with little cost to the company and does not create an unreasonable burden on management.

**Social Advisory Services Recommendation:**

› Vote for shareholder proposals that ask the company to report on its diversity and/or affirmative action programs.
› Vote for shareholder proposals calling for legal and regulatory compliance and public reporting related to non-discrimination, affirmative action, workplace health and safety, and labor policies and practices that effect long-term corporate performance.
› Vote for shareholder proposals requesting nondiscrimination in salary, wages and all benefits.
› Vote for shareholder proposals calling for action on equal employment opportunity and antidiscrimination.

**Report on Progress Towards Glass Ceiling Commission Recommendations**

In November 1995, the Glass Ceiling Commission (Commission), a bipartisan panel of leaders from business and government, issued a report describing “an unseen yet unbreachable barrier that keeps women and minorities from rising to the upper rungs of the corporate ladder.” The Commission recommended that companies take practical steps to rectify this disparity, such as including diversity goals in business plans, committing to affirmative action for qualified employees and initiating family-friendly labor policies. Shareholders have submitted proposals asking companies to report on progress made toward the Commission’s recommendations.

**Social Advisory Services Recommendation:**

› Vote for shareholder proposals that ask the company to report on its progress against the Glass Ceiling Commission’s recommendations.
› Vote for shareholder proposals seeking to eliminate the “glass ceiling” for women and minority employees.

**Prohibit Discrimination on the Basis of Sexual Orientation or Gender Identity**

Federal law does not ban workplace discrimination against gay and lesbian employees, and only some states have enacted workplace protections for these employees. Although an increasing number of US companies have explicitly banned discrimination on the basis of sexual orientation or gender identity in their equal employment opportunity (EEO) statements, many still do not. Shareholder proponents and other activist groups concerned with gay and lesbian rights, such as the Human Rights Campaign (HRC) and the Pride Foundation, have targeted U.S. companies that do not specifically restrict discrimination on the basis of sexual orientation in their EEO statements. Shareholder proposals on
this topic ask companies to change the language of their EEO statements in order to put in place anti-discrimination protection for their gay and lesbian employees. In addition, proposals may seek disclosure on a company’s general initiatives to create a workplace free of discrimination on the basis of sexual orientation, including reference to such items as support of gay and lesbian employee groups, diversity training that addresses sexual orientation, and non-medical benefits to domestic partners of gay and lesbian employees.

Social Advisory Services Recommendation:
› Vote for shareholder proposals to include language in EEO statements specifically barring discrimination on the basis of sexual orientation or gender identity.
› Vote for shareholder proposals seeking reports on a company’s initiatives to create a workplace free of discrimination on the basis of sexual orientation or gender identity.
› Vote against shareholder proposals that seek to eliminate protection already afforded to gay and lesbian employees.

Report on/Eliminate Use of Racial Stereotypes in Advertising

Many companies continue to use racial stereotypes or images perceived as racially insensitive in their advertising campaigns. Filers of shareholder proposals on this topic often request companies to give more careful consideration to the symbols and images that are used to promote the company.

Social Advisory Services Recommendation: Vote for shareholder proposals seeking more careful consideration of using racial stereotypes in advertising campaigns, including preparation of a report on this issue.

Gender Pay Gap

Over the past three years shareholders have filed resolutions requesting that companies report whether a gender pay gap exists, and if so, what measures are being taken to eliminate the gap. While primarily filed at technology firms, in 2017, the resolutions were also filed at firms in the financial services, insurance, healthcare, and telecommunication sectors. Proponents are expected to continue this campaign by engaging companies and filing shareholder proposals on this issue.

Social Advisory Services Recommendation: Vote for requests for reports on a company’s pay data by gender, or a report on a company’s policies and goals to reduce any gender pay gap.

Labor and Human Rights

Investors, international human rights groups, and labor advocacy groups have long been making attempts to safeguard worker rights in the international marketplace. In instances where companies themselves operate factories in developing countries for example, these advocates have asked that the companies adopt global corporate standards that guarantee sustainable wages and safe working conditions for their workers abroad. Companies that contract out portions of their manufacturing operations to foreign companies have been asked to ensure that the products they receive from those contractors have not been made using forced labor, child labor, or sweatshop labor. These companies are asked to adopt formal vendor standards that, among other things, include some sort of monitoring mechanism. Globalization, relocation of production overseas, and widespread use of subcontractors and vendors, often make it difficult to obtain a complete picture of a company’s labor practices in global markets. Recent deadly accidents at factories, notably in Bangladesh and in Pakistan, have continued to intensify these concerns. Many investors believe that companies would benefit from adopting a human rights policy based on the Universal Declaration of Human Rights and the International Labour Organization’s Core Labor Standards. Efforts that seek greater disclosure on a company’s global labor practices, including its supply chain, and that seek to establish minimum standards for a company’s
operations will be supported. In addition, requests for independent monitoring of overseas operations will be supported.

Social Advisory Services generally supports proposals that call for the adoption and/or enforcement of principles or codes relating to countries in which there are systematic violations of human rights; such as the use of slave, child, or prison labor; a government that is illegitimate; or there is a call by human rights advocates, pro-democracy organizations, or legitimately-elected representatives for economic sanctions. The use of child, sweatshop, or forced labor is unethical and can damage corporate reputations. Poor labor practices can lead to litigation against the company, which can be costly and time consuming.

**Codes of Conduct and Vendor Standards**

In recent years, an increasing number of shareholder proposals have been submitted that pertain to the adoption of codes of conduct or provision, greater disclosure on a company’s international workplace standards, or that request human rights risk assessment. Companies have been asked to adopt a number of different types of codes, including a workplace code of conduct, standards for international business operations, human rights standards, International Labour Organization (ILO) standards and the SA 8000 principles. The ILO is an independent agency of the United Nations which consists of 187 member nations represented by workers, employers, and governments. The ILO’s general mandate is to promote a decent workplace for all individuals. The ILO sets international labor standards in the form of its conventions and then monitors compliance with the standards. The seven conventions of the ILO fall under four broad categories: Right to organize and bargain collectively, Nondiscrimination in employment, Abolition of forced labor, and End of child labor. Each of the 187 member-nations of the ILO is bound to respect and promote these rights to the best of their abilities. SA 8000 is a set of labor standards, based on the principles of the ILO conventions and other human rights conventions, and covers eight workplace conditions, including: child labor, forced labor, health and safety, freedom of association and the right to collective bargaining, discrimination, disciplinary practices, working hours and compensation. The Global Sullivan Principles are a set of guidelines that support economic, social and political justice by companies where they do business; to support human rights and to encourage equal opportunity at all levels of employment.

**Social Advisory Services Recommendation:**

› Vote for shareholder proposals to implement human rights standards and workplace codes of conduct.
› Vote for shareholder proposals calling for the implementation and reporting on ILO codes of conduct, SA 8000 Standards, or the Global Sullivan Principles.
› Vote for shareholder proposals that call for the adoption of principles or codes of conduct relating to company investments in countries with patterns of human rights abuses (e.g. Northern Ireland, Burma, former Soviet Union, and China).
› Vote for shareholder proposals that call for independent monitoring programs in conjunction with local and respected religious and human rights groups to monitor supplier and licensee compliance with codes.
› Vote for shareholder proposals that seek publication of a “Code of Conduct” by the company’s foreign suppliers and licensees, requiring that they satisfy all applicable standards and laws protecting employees’ wages, benefits, working conditions, freedom of association, and other rights.
› Vote for proposals requesting that a company conduct an assessment of the human rights risks in its operations or in its supply chain, or report on its human rights risk assessment process.
› Vote for shareholder proposals seeking reports on, or the adoption of, vendor standards including: reporting on incentives to encourage suppliers to raise standards rather than terminate contracts and providing public disclosure of contract supplier reviews on a regular basis.
› Vote for shareholder proposals to adopt labor standards for foreign and domestic suppliers to ensure that the company will not do business with foreign suppliers that manufacture products for sale in the U.S. using forced labor, child labor, or that fail to comply with applicable laws protecting employee’s wages and working conditions.
Adopt/Report on MacBride Principles

These resolutions have called for the adoption of the MacBride Principles for operations located in Northern Ireland. They request companies operating abroad to support the equal employment opportunity policies that apply in facilities they operate domestically. The principles were established to address the sectarian hiring problems between Protestants and Catholics in Northern Ireland. It is well documented that Northern Ireland’s Catholic community faced much higher unemployment figures than the Protestant community. In response to this problem, the U.K. government instituted the New Fair Employment Act of 1989 (and subsequent amendments) to address the sectarian hiring problems.

Many companies believe that the Act adequately addresses the problems and that further action, including adoption of the MacBride Principles, only duplicates the efforts already underway. In evaluating a proposal to adopt the MacBride Principles, shareholders must decide whether the principles will cause companies to divest, and therefore worsen the unemployment problem, or whether the principles will promote equal hiring practices. Proponents believe that the Fair Employment Act does not sufficiently address the sectarian hiring problems. They argue that the MacBride Principles serve to stabilize the situation and promote further investment.

Social Advisory Services Recommendation: Vote for shareholder proposals to report on or implement the MacBride Principles.

Community Impact Assessment/Indigenous Peoples’ Rights

In recent years, a number of U.S. public companies have found their operations or expansion plans in conflict with local indigenous groups. In order to improve their standing with indigenous groups and decrease any negative publicity companies may face, some concerned shareholders have sought reports requesting that companies review their obligations, actions and presence on these groups. Some have also requested these companies adopt policies based on the Draft UN Declaration on the Rights of Indigenous Peoples and the Organization of American States’ (OAS) American Declaration on rights of Indigenous Peoples. Some companies such as Starbucks have reached agreements with local governments to ensure better business practices for products produced by indigenous groups. Shareholders, concerned with the negative impact that the company’s operations may have on the indigenous people’s land and community, have sought reports detailing the impact of the company’s actions and presence on these groups.

Social Advisory Services Recommendation: Vote for shareholder proposals asking to prepare reports on a company’s environmental and health impact on communities.

Report on Risks of Outsourcing

Consumer interest in keeping costs low through comparison shopping, coupled with breakthroughs in productivity have prompted companies to look for methods of increasing profit margins while keeping prices competitive. Through a practice known as off-shoring, the outsourcing or moving of manufacturing and service operations to foreign markets with lower labor costs, companies have found one method where the perceived savings potential is quite substantial. Shareholder opponents of outsourcing argue that there may be long-term consequences to offshore outsourcing that outweigh short-term benefits such as backlash from a public already sensitive to off-shoring, security risks from information technology development overseas, and diminished employee morale. Shareholder proposals addressing
outsourcing ask that companies prepare a report to shareholders evaluating the risk to the company’s brand name and reputation in the U.S. from outsourcing and off-shoring of manufacturing and service work to other countries.

**Social Advisory Services Recommendation:** Vote for shareholders proposals asking companies to report on the risks associated with outsourcing or off-shoring.


Sub-Saharan Africa is the most affected region in the world with regard to the HIV/AIDS pandemic. With limited access to antiretroviral treatment for HIV/AIDS, the increasing death toll is expected to have profound social, political and economic impact on that region and the companies or industries with operations in Sub-Saharan Africa. In the past, shareholder proposals asked companies to develop policies to provide affordable HIV/AIDS, malaria, and tuberculosis drugs in third-world countries. However, in recent years, shareholders have changed their tactic, asking instead for reports on the impact of these pandemics on company operations, including both pharmaceutical and non-pharmaceutical companies operating in high-risk areas. This change is consistent with the general shift in shareholder proposals towards risk assessment and mitigation.

**Social Advisory Services Recommendation:** Vote for shareholder proposals asking for companies to report on the impact of pandemics, such as HIV/AIDS, malaria, and tuberculosis, on their business strategies.

**Operations in High Risk Markets**

In recent years, shareholder advocates and human rights organizations have highlighted concerns associated with companies operating in regions that are politically unstable, including state sponsors of terror. The U.S. government has active trade sanction regimes in place against a number of countries, including Cuba, Iran, North Korea, Sudan, and Syria, among others. These sanctions are enforced by the Office of Foreign Assets Control, which is part of the U.S. Department of the Treasury. However, these countries do not comprise an exhaustive list of countries considered to be high-risk markets.

Shareholder proponents have filed resolutions addressing a variety of concerns around how investments and operations in high-risk regions may support, or be perceived to support, potentially oppressive governments. Proponents contend that operations in these countries may lead to potential reputational, regulatory, and/or supply chain risks as a result of operational disruptions. Concerned shareholders have requested investment withdrawals or cessation of operations in high-risk markets as well as reports on operations in high-risk markets. Such reports may seek additional disclosure from companies on criteria employed for investing in, continuing to operate in, and withdrawing from specific countries.

Depending on the country’s human rights record, investors have also asked companies to refrain from commencing new projects in the country of concern until improvements are made. In addition, investors have sought greater disclosure on the nature of a company’s involvement in the country and on the impact of their involvement or operations.

**Social Advisory Services Recommendation:** Vote for requests for a review of and a report outlining the company’s potential financial and reputation risks associated with operations in “high-risk” markets, such as a terrorism-sponsoring state or otherwise, taking into account:

› The nature, purpose, and scope of the operations and business involved that could be affected by social or political disruption;
› Current disclosure of applicable risk assessment(s) and risk management procedures;
› Compliance with U.S. sanctions and laws;
Consideration of other international policies, standards, and laws;
Whether the company has been recently involved in significant controversies or violations in "high-risk" markets.

Reports on Operations in Burma/Myanmar

Since the early 1960s, Burma (also known as Myanmar) has been ruled by a military dictatorship that has been condemned for human rights abuses, including slave labor, torture, rape and murder. Many companies have pulled out of Burma over the past decade given the controversy surrounding involvement in the country. Oil companies continue to be the largest investors in Burma and therefore are the usual targets of shareholder proposals on this topic. However, proposals have also been filed at other companies, including financial companies, for their involvement in the country.

Social Advisory Services Recommendation:
› Vote for shareholder proposals to adopt labor standards in connection with involvement in Burma.
› Vote for shareholder proposals seeking reports on Burmese operations and reports on costs of continued involvement in the country.
› Vote shareholder proposals to pull out of Burma on a case-by-case basis.

Reports on Operations in China

Documented human rights abuses in China continue to raise concerns among investors, specifically with respect to alleged use of prison and child labor in manufacturing. Reports have identified U.S. companies with direct or indirect ties to companies controlled by the Chinese military, the People’s Liberation Army (PLA), and hence links to prison labor. The U.S. Business Principles for Human Rights of Workers in China may help a company with operations in China avoid being blacklisted by U.S. states and municipalities, many of whom have limited their contracts with companies that fail to adopt similar principles in other countries recognized for committing gross human rights violations.

Social Advisory Services Recommendation:
› Vote for shareholder proposals requesting more disclosure on a company’s involvement in China
› Vote case-by-case on shareholder proposals that ask a company to terminate a project or investment in China.

Product Sales to Repressive Regimes

Certain Internet technology companies have been accused of assisting repressive governments in violating human rights through the knowing misuse of their hardware and software. Human rights groups have accused companies such as Yahoo!, Cisco, Google, and Microsoft of allowing the Chinese government to censor and track down dissenting voices on the internet.

Social Advisory Services Recommendation:
› Vote case-by-case on shareholder proposals requesting that companies cease product sales to repressive regimes that can be used to violate human rights.
› Vote for proposals to report on company efforts to reduce the likelihood of product abuses in this manner.

Internet Privacy/Censorship and Data Security
Information technology sector companies have been at the center of shareholder advocacy campaigns regarding concerns over Internet service companies and technology providers’ alleged cooperation with potentially repressive regimes, notably the Chinese government. Shareholder proposals, submitted at Yahoo!, Google, Microsoft, and Cisco, among others, asked companies to take steps to stop abetting repression and censorship of the Internet and/or review their human rights policies taking this issue into consideration. Resolution sponsors generally argue that the Chinese government is using IT company technologies to track, monitor, identify, and, ultimately, suppress political dissent. In the view of proponents, this process of surveillance and associated suppression violates internationally accepted norms outlined in the U.N. Universal Declaration of Human Rights.

While early shareholder resolutions on Internet issues focused on censorship by repressive regimes and net neutrality, proponents have recently raised concerns regarding privacy and data security in the wake of increased breaches that result in the misuse of personal information. On Oct. 13, 2011, the Securities and Exchange Commission (SEC) issued a guidance document about the disclosure obligations relating to cybersecurity risks and cyber incidents. In the document, the SEC references the negative consequences that are associated with cyber-attacks, such as: remediation costs, including those required to repair relationships with customers and clients; increased cyber-security protection costs; lost revenues from unauthorized use of the information or missed opportunities to attract clients; litigation; and reputational damage. The document says that while the federal securities laws do not explicitly require disclosure of cybersecurity risks and incidents, some disclosure requirements may impose an obligation on the company to disclose such information and provides scenarios where disclosure may be required. A 2013 study by the Ponemon Institute found that the median annualized cost of cyber-attacks for the 60 organizations studied was $11.6 million. The study also found that the number of successful cyber-attacks among the 60 companies increased by 18 percent between 2012 and 2013, from 102 successful attacks on average per week to 122.

More recently, data security has been the focus of media outlets and a public concern. During the 2013 holiday shopping season, Target, Neiman Marcus, and other retailers were the targets of hackers looking to steal credit card numbers. It is estimated that as many as 40 million customer credit and debit card accounts were stolen at Target alone. These incidents preceded what many people consider the largest data security breach in the United States. In June 2013, major media outlets began releasing information about leaked classified documents disclosed by Edward Snowden, an NSA contractor. The documents revealed a government-run Internet and telephone surveillance program aimed at collecting metadata. As part of this operation, the government is said to have obtained from major U.S. telecommunications companies the call records of their customers.

Social Advisory Services Recommendation: Vote for resolutions requesting the disclosure and implementation of Internet privacy and censorship policies and procedures considering:

› The level of disclosure of policies and procedures relating to privacy, freedom of speech, Internet censorship, and government monitoring of the Internet;
› Engagement in dialogue with governments and/or relevant groups with respect to the Internet and the free flow of information;
› The scope of business involvement and of investment in markets that maintain government censorship or monitoring of the Internet;
› The market-specific laws or regulations applicable to Internet censorship or monitoring that may be imposed on the company; and
› The level of controversy or litigation related to the company’s international human rights policies and procedures.

Disclosure on Plant Closings

Shareholders have asked that companies contemplating plant closures consider the impact of such closings on employees and the community, especially when such plan closures involve a community’s largest employers. Social Advisory Services usually recommends voting for greater disclosure of plant closing criteria. In cases where it can be
shown that companies have been proactive and responsible in adopting these criteria, Social Advisory Services recommends against the proposal.

**Social Advisory Services Recommendation:** Vote for shareholder proposals seeking greater disclosure on plant closing criteria if the company has not provided such information.

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**Environment**

Proposals addressing environmental and energy concerns are plentiful, and generally seek greater disclosure on a particular issue or seek to improve a company’s environmental practices in order to protect the world’s natural resources. In addition, some proponents cite the negative financial implications for companies with poor environmental practices, including liabilities associated with site clean-ups and lawsuits, as well as arguments that energy efficient products and clean environmental practices are sustainable business practices that will contribute to long-term shareholder value. Shareholders proponents point out that the majority of independent atmospheric scientists agree that global warming poses a serious problem to the health and welfare of our planet, citing the findings of the Intergovernmental Panel on Climate Change. Shareholder activists argue that companies can report on their greenhouse gas emissions within a few months at reasonable cost. The general trend indicates a movement towards encouraging companies to have proactive environmental policies, focusing on maximizing the efficient use of non-renewable resources and minimizing threats of harm to human health or the environment.

**Environmental/Sustainability Reports**

Shareholders may request general environmental disclosures or reports on a specific location/operation, often requesting that the company detail the environmental risks and potential liabilities of a specific project. Increasingly, companies have begun reporting on environmental and sustainability issues using the Global Reporting Initiative (GRI) standards. The GRI was established in 1997 with the mission of developing globally applicable guidelines for reporting on economic, environmental, and social performance. The GRI was developed by Ceres, (formerly known as the Coalition for Environmentally Responsible Economies, CERES) in partnership with the United Nations Environment Programme (UNEP).

Ceres was formed in the wake of the March 1989 Exxon Valdez oil spill, when a consortium of investors, environmental groups, and religious organizations drafted what were originally named the Valdez Principles, and later to be renamed the CERES Principles. Corporate signatories to the CERES Principles pledge to publicly report on environmental issues, including protection of the biosphere, sustainable use of natural resources, reduction and disposal of wastes, energy conservation, and employee and community risk reduction in a standardized form.

The Equator Principles are the financial industry’s benchmark for determining, assessing and managing social and environmental risk in project financing. The Principles were first launched in June 2003 and were ultimately adopted by over forty financial institutions during a three year implementation period. The principles were subsequently revised in July 2006 to take into account the new performance standards approved by the World Bank Group’s International Finance Corporation (IFC). The third iteration of the Principles was launched in June 2013 and it amplified the banks’ commitments to social responsibility, including human rights, climate change, and transparency. Financial institutions adopt these principles to ensure that the projects they venture in are developed in a socially responsible manner and reflect sound environmental management practices.

**Social Advisory Services Recommendation:**
Vote for shareholder proposals seeking greater disclosure on the company’s environmental and social practices, and/or associated risks and liabilities.

Vote for shareholder proposals asking companies to report in accordance with the Global Reporting Initiative (GRI).

Vote for shareholder proposals seeking the preparation of sustainability reports.

Vote for shareholder proposals to study or implement the CERES principles.

Vote for shareholder proposals to study or implement the Equator Principles.

Climate Change/Greenhouse Gas Emissions

Climate change has emerged as the most significant environmental threat to the planet to date. Scientists generally agree that gases released by chemical reactions including the burning of fossil fuels contribute to a “greenhouse effect” that traps the planet’s heat. Environmentalists claim that the Greenhouse Gases (GHG) produced by the industrial age have caused recent weather crises such as heat waves, rainstorms, melting glaciers, rising sea levels and receding coastlines. Climate change skeptics have described the rise and fall of global temperatures as naturally occurring phenomena and depicted human impact on climate change as minimal. Shareholder proposals requesting companies to issue a report to shareholders, “at reasonable cost and omitting proprietary information,” on greenhouse gas emissions ask that the report include descriptions of corporate efforts to reduce emissions, companies’ financial exposure and potential liability from operations that contribute to global warming, their direct or indirect efforts to promote the view that global warming is not a threat, and their goals in reducing these emissions from their operations. Shareholder proponents argue that there is scientific proof that the burning of fossil fuels causes global warming, that future legislation may make companies financially liable for their contributions to global warming, and that a report on the company’s role in global warming can be assembled at reasonable cost.

Social Advisory Services Recommendation:

› Vote for shareholder proposals seeking information on the financial, physical, or regulatory risks it faces related to climate change on its operations and investments, or on how the company identifies, measures, and manage such risks.

› Vote for shareholder proposals calling for the reduction of GHG or adoption of GHG goals in products and operations.

› Vote for shareholder proposals seeking reports on responses to regulatory and public pressures surrounding climate change, and for disclosure of research that aided in setting company policies around climate change.

› Vote for shareholder proposals requesting reports on greenhouse gas emissions from companies’ operations and/or products.

Invest in Clean/Renewable Energy

Filers of proposals on renewable energy ask companies to increase their investment in renewable energy sources and to work to develop products that rely more on renewable energy sources. Increased use of renewable energy will reduce the negative environmental impact of energy companies. In addition, as supplies of oil and coal exist in the earth in limited quantities, renewable energy sources represent a competitive, and some would argue essential, long-term business strategy.

Social Advisory Services Recommendation:

› Vote for shareholder proposals seeking the preparation of a report on a company’s activities related to the development of renewable energy sources.

› Vote for shareholder proposals seeking increased investment in renewable energy sources unless the terms of the resolution are overly restrictive.
Energy Efficiency

Reducing the negative impact to the environment can be done through the use of more energy efficient practices and products. Shareholders propose that corporations should have energy efficient manufacturing processes and should market more energy efficient products. This can be done by utilizing renewable energy sources that are cost-competitive and by implementing energy efficient operations.

Social Advisory Services Recommendation: Vote for shareholder proposals requesting a report on company energy efficiency policies and/or goals.

Operations in Environmentally Sensitive Areas

Canadian Oil Sands

Proposals asking for a report on oil sands operations in the Athabasca region of Alberta, Canada have appeared at a number of oil and gas companies. Alberta’s oil sands contain a reserve largely thought to be one of the world’s largest potential energy sources. Rising oil sands production in Alberta has been paralleled with concerns from a variety of stakeholders—including environmental groups, local residents, and shareholders—regarding the environmental impacts of the complicated extraction and upgrading processes required to convert oil sands into a synthetic crude oil. The high viscosity of bitumen makes its extraction a challenging and resource-intensive process; the most common extraction technique involves pumping steam into the oil sands to lower the viscosity of bitumen in order to pump it to the surface.

One of the most prominent issues concerning oil sands is the large volume of greenhouse gases (GHG) associated with production. Oil sands are by far one of the most energy-intensive forms of oil production, releasing three times more GHG emissions from production than conventional oil.

Shareholders have kept up pressure on the issue of potential long-term risks to companies posed by the environmental, social, and economic challenges associated with Canadian oil sands operations. Resolutions on the topic have focused on requesting greater transparency on the ramifications of oil sands development projects.

Arctic National Wildlife Refuge

The Arctic National Wildlife Refuge (ANWR) is a federally protected wilderness along Alaska’s North Slope. In the past, legislation proposed in both the House and Senate that, if passed, would allow a portion of this area to be leased to private companies for development and production of oil, has been witnessed. Oil companies have expressed an interest in bidding for these leases given the opportunity. In response, shareholder activists have filed resolutions asking these companies to cancel any plans to drill in the ANWR and cease their lobbying efforts to open the area for drilling. Proponents of shareholder proposals on this issue argue that the Coastal Plain section of the ANWR is the most environmentally sensitive area of the refuge, that the majority of Alaska’s North Slope that is not federally designated wilderness already provides the oil industry with sufficient resources for oil production, and that advocates of drilling in ANWR overstate the benefit to be derived from opening the wilderness to oil production. Those in favor of opening the area up to drilling note that only a small portion of ANWR would be considered for exploration, and if drilling were to take place, it would be on less than one percent of the entire area, that modern technology reduces the environmental impact of oil drilling on both the land and surrounding wildlife, and that oil production in ANWR would have considerable benefit to company shareholders, Alaskans, and the United States as a whole.
Social Advisory Services Recommendation:
› Vote for requests for reports on potential environmental damage as a result of company operations in protected regions.
› Vote for shareholder proposals asking companies to prepare reports or adopt policies on operations that include mining, drilling or logging in environmentally sensitive areas.
› Vote for shareholder proposals seeking to curb or reduce the sale of products manufactured from materials extracted from environmentally sensitive areas such as old growth forests.

Hydraulic Fracturing

Shareholder proponents have elevated concerns on the use of hydraulic fracturing, an increasingly controversial process in which water, sand, and a mix of chemicals are blasted horizontally into tight layers of shale rock to extract natural gas. As this practice has gained more widespread use, environmentalists have raised concerns that the chemicals mixed with sand and water to aid the fracturing process can contaminate ground water supplies. Proponents of resolutions at companies that employ hydraulic fracturing are also concerned that wastewater produced by the process could overload the waste treatment plants to which it is shipped. Shareholders have asked companies that utilize hydraulic fracturing to report on the environmental impact of the practice and to disclose policies aimed at reducing hazards from the process.

Social Advisory Services Recommendation: Vote for requests seeking greater transparency on the practice of hydraulic fracturing and its associated risks.

Phase Out Chlorine-Based Chemicals

The Environmental Protection Agency (EPA) identified chlorine bleaching of pulp and paper as a major source of dioxin, a known human carcinogen linked to have negative effects to humans and animals. A number of shareholder proposals have been filed in recent years asking companies to report on the possible phase-out of chlorine bleaching in the production of paper because of the practice’s negative environmental impact.

Social Advisory Services Recommendation:
› Vote for shareholder proposals to prepare a report on the phase-out of chlorine bleaching in paper production.
› Vote on a case-by-case basis on shareholder proposals asking companies to cease or phase-out the use of chlorine bleaching.

Land Procurement and Development

Certain real estate developers including big-box large retailers have received criticism over their processes for acquiring and developing land. Given a 2005 Supreme Court decision allowing for the usage of eminent domain laws in the U.S. to take land from property-owners for tax generating purposes, as well as certain controversies outside of the U.S. with land procurement, some shareholders would like assurances that companies are acting ethically and with local stakeholders in mind.

Social Advisory Services Recommendation: Vote for shareholder proposals requesting that companies report on or adopt policies for land procurement and utilize the policies in their decision-making.

Report on the Sustainability of Concentrated Area Feeding Operations (CAFO)
The potential environmental impact on water, aquatic ecosystems, and local areas from odor and chemical discharges from CAFOs has led to lawsuits and EPA regulations. Certain shareholders have asked companies to provide additional details on their CAFOs in addition to those with which the companies contract to raise their livestock.

**Social Advisory Services Recommendation:** Vote for requests that companies report on the sustainability and the environmental impacts of both company-owned and contract livestock operations.

**Adopt a Comprehensive Recycling Policy**

A number of companies have received proposals to step-up their recycling efforts, with the goal of reducing the company’s negative impact on the environment and reducing costs over the long-term.

**Social Advisory Services Recommendation:**
- Vote for shareholder proposals requesting the preparation of a report on the company’s recycling efforts.
- Vote for shareholder proposals that ask companies to increase their recycling efforts or to adopt a formal recycling policy.

**Nuclear Energy**

Nuclear power continues to be a controversial method of producing electricity. Opponents of nuclear energy are primarily concerned with serious accidents and the related negative human health consequences, and with the difficulties involved in nuclear waste storage.

**Social Advisory Services Recommendation:**
- Vote for shareholder proposals seeking the preparation of a report on a company’s nuclear energy procedures.
- Vote case-by-case on proposals that ask the company to cease the production of nuclear power.

**Water Use**

Shareholders may ask for a company to prepare a report evaluating the business risks linked to water use and impacts on the company’s supply chain, including subsidiaries and bottling partners. Such proposals also ask companies to disclose current policies and procedures for mitigating the impact of operations on local communities in areas of water scarcity.

**Social Advisory Services Recommendation:**
- Vote for shareholder proposals seeking the preparation of a report on a company’s risks linked to water use.
- Vote for resolutions requesting companies to promote the “human right to water” as articulated by the United Nations.
- Vote for shareholder proposals requesting that companies report on or adopt policies for water use that incorporate social and environmental factors.

**Kyoto Protocol Compliance**

With the Kyoto Protocol operational as of February 2005, ratifying countries have agreed to reduce their emissions of carbon dioxide and five other greenhouse gases. While some signatories have yet to release specific details of corporate regulations, the impact on multinationals operating in Kyoto-compliant countries is anticipated to be significant.
Social Advisory Services Recommendation: Vote for shareholder proposals asking companies to review and report on how companies will meet GHG reduction targets of the Kyoto-compliant countries in which they operate.

Health and Safety

Toxic Materials

Social Advisory Services Recommendation:
› Vote for shareholder proposals asking companies to report on policies and activities to ensure product safety.
› Vote for shareholder proposals asking companies to disclose annual expenditures relating to the promotion and/or environmental cleanup of toxins.
› Vote for shareholder proposals asking companies to report on the feasibility of removing, or substituting with safer alternatives, all “harmful” ingredients used in company products.

Product Safety

Social Advisory Services Recommendation:
› Generally vote for proposals requesting the company to report on or adopt consumer product safety policies and initiatives.
› Generally vote for proposals requesting the study, adoption and/or implementation of consumer product safety programs in the company’s supply chain.

Workplace/Facility Safety

Social Advisory Services Recommendation:
› Vote for shareholder proposals requesting workplace safety reports, including reports on accident risk reduction efforts.
› Vote shareholder proposals requesting companies report on or implement procedures associated with their operations and/or facilities on a case-by-case basis.

Report on Handgun Safety Initiatives

Shareholders may ask for a company to report on policies and procedures that are aimed at curtailing the incidence of gun violence. Such a report may include: implementation of the company’s contract instruction to distributors not to sell the company’s weapons at gun shows or through pawn shops; recalls or retro-fits of products with safety-related defects causing death or serious injury to consumers, as well as development of systems to identify and remedy these defects; names and descriptions of products that are developed or are being developed for a combination of higher caliber/maximum capacity and greater conceal-ability; and the company’s involvement in promotion campaigns that could be construed as aimed at children. The Sandy Hook Principles were established to commemorate the victims of gun violence and to encourage positive corporate behavior in response to the proliferation of gun violence in America.

Social Advisory Services Recommendation:
› Vote for shareholder proposals asking the company to report on its efforts to promote handgun safety.
› Vote for shareholder proposals asking the company to stop the sale of handguns and accessories.

Phase-out or Label Products Containing Genetically Engineered Ingredients
Shareholders have asked companies engaged in the development of genetically modified agricultural products to adopt a policy of not marketing or distributing such products until “long term safety testing” demonstrates that they are not harmful to humans, animals or the environment. Until further long term testing demonstrates that these products are not harmful, companies in the restaurant and prepared foods industries have been asked to remove genetically altered ingredients from products they manufacture or sell, and label such products in the interim. Shareholders have also asked supermarket companies to do the same for their own private label brands.

Social Advisory Services Recommendation:
› Vote for shareholder proposals to label products that contain genetically engineered products or products from cloned animals.
› Vote for shareholder proposals that ask the company to phase out the use of genetically engineered ingredients in their products.
› Vote for shareholder proposals that ask the company to report on the use of genetically engineered organisms in their products.
› Vote for shareholder proposals asking for reports on the financial, legal, and operational risks posed by the use of genetically engineered organisms.

Tobacco-related Proposals

Under the pressure of ongoing litigation and negative media attention, tobacco companies and even non-tobacco companies with ties to the industry have received an assortment of shareholder proposals seeking increased responsibility and social consciousness from tobacco companies and as well as firms affiliated with the tobacco industry.

While the specific resolutions for shareholder proponents vary from year to year, activist shareholders consistently make the tobacco industry a prominent target. Examples of shareholder proposals focused on tobacco include: warnings on the risks of tobacco smoke and smoking-related diseases, attempting to link executive compensation with reductions in teen smoking rates, the placement of company tobacco products in retail outlets, a review of advertising campaigns and their impact on children and minority groups, prohibiting non-tobacco companies from entering into contracts with tobacco companies, and requesting restaurant operators maintain smoke-free restaurants.

In June 2009, the Family Smoking Prevention and Tobacco Control Act was signed into law, giving the FDA authority to regulate the tobacco industry for the first time, including the power to block or approve new products as well as the nicotine and other content in existing tobacco products. This legislation empowers the imposition of a ban on tobacco advertising within 1,000 feet of schools and playgrounds, require FDA-approved graphic warning labels that occupy 50 percent of the space on each package of cigarettes.

In September 2009, the FDA issued a ban on the sale of flavored cigarettes, exercising its regulatory power in a major way over tobacco for the first time under the new law. The ban affected tobacco products with chocolate, vanilla, clove, and other similar flavors.

Social Advisory Services Recommendation:
› Vote for shareholder proposals seeking to limit the sale of tobacco products to children.
› Vote for shareholder proposals asking producers of tobacco product components (such as filters, adhesives, flavorings, and paper products) to halt sales to tobacco companies.
› Vote for shareholder proposals that ask restaurants to adopt smoke-free policies and that ask tobacco companies to support smoke-free legislation.
› Vote for shareholder proposals seeking a report on a tobacco company’s advertising approach.
› Vote for shareholder proposals at insurance companies to cease investment in tobacco companies.
› Vote for proposals at producers of cigarette components calling for a report outlining the risks and potential liabilities of the production of these components.
› Vote for proposals calling for tobacco companies to cease the production of tobacco products.
› Vote for shareholder proposals asking companies to stop all advertising, marketing and sale of cigarettes using the terms “light,” “ultra-light,” “mild,” and other similar words and/or colors.
› Vote for shareholder proposals asking companies to increase health warnings on cigarette smoking. (i.e.: information for pregnant women, “Canadian Style” warnings, filter safety).

**Adopt Policy/Report on Drug Pricing**

Pharmaceutical drug pricing, both within the United States and internationally, has raised many questions of the companies that are responsible for creating and marketing these treatments. Shareholder proponents, activists and even some legislators have called upon drug companies to restrain pricing of prescription drugs.

The high cost of prescription drugs is a vital issue for senior citizens across the country. Seniors have the greatest need for prescription drugs, accounting for a significant portion of all prescription drug sales, but they often live on fixed incomes and are underinsured.

Proponents note that efforts to reign-in pharmaceutical costs will not negatively impact research and development (R&D) costs and that retail drug prices are consistently higher in the U.S. than in other industrialized nations. Pharmaceutical companies often respond that adopting a formal drug pricing policy could put the company at a competitive disadvantage.

Against the backdrop of the AIDS crisis in Africa, many shareholders have called on companies to address the issue of affordable drugs for the treatment of AIDS, as well as tuberculosis and malaria throughout the developing world. When analyzing such resolutions, consideration should be made of the strategic implications of pricing policies in the market.

**Social Advisory Services Recommendation:**
› Vote for shareholder proposals to prepare a report on drug pricing.
› Vote for shareholder proposals to adopt a formal policy on drug pricing.
› Vote for shareholder proposals that call on companies to develop a policy to provide affordable HIV, AIDS, tuberculosis, and malaria drugs in third-world nations.
› Vote for proposals asking for reports on the economic effects and legal risks of limiting pharmaceutical products to Canada or certain wholesalers.
› Vote case-by-case proposals requesting that companies adopt policies not to constrain prescription drug re-importation by limiting supplies to foreign markets.

**Government and Military**

Weapons-related proposals may target handguns, landmines, defense contracting, or sale of weapons to foreign governments.

**Prepare Report to Renounce Future Landmine Production**

Although very few companies currently produce landmines, some companies continue to have links to landmine production or produce components that are used to make landmines. Shareholders have asked companies to renounce the future development of landmines or their components, or to prepare a report on the feasibility of such a renunciation.
Prepare Report on Foreign Military Sales

Shareholders have filed proxy resolutions asking companies to account for their policies surrounding the sale of military equipment to foreign governments. The proposals can take various forms. One resolution simply calls on companies to report on their foreign military sales, provide information on military product exports, disclose the company’s basis for determining whether those sales should be made, and any procedures used to market or negotiate those sales. Another resolution calls for companies to report on “offsets” e.g. guarantee of new jobs in the purchasing country and technology transfers. Offsets involve a commitment by military contractors and the U.S. government to direct benefits back to a foreign government as a condition of a military sale.

Social Advisory Services Recommendation:
› Vote for shareholder proposals to report on foreign military sales or offset agreements.
› Vote case-by-case on proposals that call for outright restrictions on foreign military sales.

Depleted Uranium/Nuclear Weapons

Depleted uranium is the less radioactive uranium that is left behind after enriched uranium is produced for nuclear reactor fuel and fissile material for nuclear weapons. The main difference is that depleted uranium contains at least three times less U-235 than natural uranium. However, it is still weakly radioactive. Shareholders want reports on companies’ policies, procedures and involvement in the said substance and nuclear weapons.

Social Advisory Services Recommendation:
Vote for shareholder proposals requesting a report on involvement, policies, and procedures related to depleted uranium and nuclear weapons.

Adopt Ethical Criteria for Weapons Contracts

Shareholders have requested that companies review their code of conduct and statements of ethical criteria for military production-related contract bids, awards, and execution to incorporate environmental factors and sustainability issues related to the contract bidding process. Sustainability is a business model that requires companies to balance the needs and interests of various stakeholders while concurrently sustaining their businesses, communities, and the environment for future generations.

Social Advisory Services Recommendation:
Vote for shareholder proposals asking companies to review and amend, if necessary, the company’s code of conduct and statements of ethical criteria for military production-related contract bids, awards and execution.

Animal Welfare

Animal Rights/Testing

Shareholders and animal rights groups, including People for the Ethical Treatment of Animals (PETA), may file resolutions calling for the end to painful and unnecessary animal testing on laboratory animals by companies developing products for the cosmetics and medical supply industry. Since advanced testing methods now produce many reliable results without the use of live animals, Social Advisory Services generally supports proposals on this issue. In cases where it can be determined that alternative testing methods are unreliable or are required by law, Social Advisory Services recommends voting against such proposals. Other resolutions call for the adoption of animal welfare
standards that would ensure humane treatment of animals on vendors’ farms and slaughter houses. Social Advisory Services will generally vote in favor of such resolutions.

**Social Advisory Services Recommendation:**

› Vote for shareholder proposals that seek to limit unnecessary animal testing where alternative testing methods are feasible or not barred by law.
› Vote for shareholder proposals that ask companies to adopt or report on company animal welfare standards or animal-related risks.
› Vote for shareholder proposals asking companies to report on the operational costs and liabilities associated with selling animals.
› Vote for shareholder proposals to eliminate cruel product testing methods.
› Vote for shareholder proposals that seek to monitor, limit, report, or eliminate the outsourcing of animal testing to overseas laboratories.
› Vote for shareholder proposals to adopt or adhere to a public animal welfare policy at both company and contracted laboratory levels.
› Vote for shareholder proposals to evaluate, adopt, or require suppliers to adopt Controlled Atmosphere Killing (CAK) slaughter methods.

**Political and Charitable Giving**

**Lobbying Efforts**

Shareholders have asked companies to report on their lobbying efforts on proposed legislation or to refute established scientific research regarding climate change, the health effects of smoking, fuel efficiency standards etc. Proponents have pointed to potential legislation on climate change, the lethargic pace of improvements in fuel efficiency standards in the U.S. automotive industry, and the highly litigious nature surrounding the tobacco industry as rationales for greater transparency on corporate lobbying practices that would shed light on whether companies are acting in the best long-term interests of their shareholders. Proponents of lobbying resolutions typically request enhanced disclosure of lobbying policies and expenditures, including a report on the policies and procedures related to lobbying, amounts used for various types of lobbying, and any membership or payments to a tax-exempt organization that writes and endorses model legislation.

**Social Advisory Services Recommendation:**

› Vote for shareholder proposals asking companies to review and report on their lobbying activities, including efforts to challenge scientific research and influence governmental legislation.
› Vote for proposals requesting information on a company’s lobbying (including direct, indirect, and grassroots lobbying) activities, policies, or procedures.

**Political Contributions/Non-Partisanship**

As evidenced by the U.S. Supreme Court’s January 2010 decision in *Citizens United vs. Federal Election Commission* that lifted restrictions on corporate spending in federal elections, changes in legislation that governs corporate political giving have, rather than limiting such contributions, increased the potential for corporate contributions to the political process and the complexity of tracking such contributions.

Proponents of political spending resolutions generally call for enhanced disclosure of political contributions, including a report on the policies and procedures for corporate political campaign contributions and trade association expenditures, the respective amounts of such donations using company funds, or an assessment of the impacts of such contributions on the firm’s image, sales and profitability. Shareholder advocates of these proposals are concerned with
the lack of transparency on political giving and the increasing involvement and influence of corporations in the political process.

Social Advisory Services Recommendation:
› Vote for proposals calling for a company to disclose political and trade association contributions, unless the terms of the proposal are unduly restrictive.
› Vote for proposals calling for a company to maintain a policy of political non-partisanship.
› Vote against proposals asking a company to refrain from making any political contributions.

Charitable Contributions

Shareholder proponents of charitable-contributions related resolutions may seek greater disclosure on a company’s charitable donations including dollar amounts, sponsorships, and policies on corporate philanthropy. Social Advisory Services is generally supportive of increased transparency around corporate charitable giving. However, some resolutions extend beyond mere disclosure requests and attempt to influence or restrict companies’ contributions to specific types of beneficiaries in a manner that furthers particular objectives supported by the proposal sponsors. Social Advisory Services believes that management is better positioned to decide what criteria are appropriate for making corporate charitable contributions. Also, some of the proposals may require companies to poll their shareholders as part of the grant-making process. Since majority of companies generally have thousands of shareholders, contacting, confirming, and processing each individual opinion and/or consent would be a burdensome and expensive exercise.

Social Advisory Services Recommendation:
› Generally vote for shareholder resolutions seeking enhanced transparency on corporate philanthropy.
› Vote against shareholder proposals imposing charitable giving criteria or requiring shareholder ratification of grants.
› Vote against shareholder proposals requesting that companies prohibit charitable contributions.

Disclosure on Prior Government Service

Shareholders have asked companies to disclose the identity of any senior executive and/or other high-level employee, consultant, lobbyist, attorney, or investment banker who has served in government. Although the movement of individuals between government and the private sector may benefit both, the potential also exists for conflicts of interest, especially in industries that have extensive dealings with government agencies.

Social Advisory Services Recommendation: Vote for shareholder proposals calling for the disclosure of prior government service of the company’s key executives.

Consumer Lending and Economic Development

Adopt Policy/Report on Predatory Lending Practices

Predatory lending involves charging excessive fees to subprime borrowers without adequate disclosure. More specifically, predatory lending includes misleading subprime borrowers about the terms of a loan, charging excessive
fees that are folded into the body of a refinancing loan, including life insurance policies or other unnecessary additions to a mortgage, or lending to homeowners with insufficient income to cover loan payments.

**Social Advisory Services Recommendation:** Vote for shareholder proposals seeking the development of a policy or preparation of a report to guard against predatory lending practices.

### Disclosure on Credit in Developing Countries (LDCs) or Forgive LDC Debt

Shareholders have asked banks and other financial services firms to develop and disclose lending policies for less developed countries. Proponents are concerned that, without such policies, lending to developing countries may contribute to the outflow of capital, the inefficient use of capital, and corruption, all of which increase the risk of loan loss. In the interest of promoting improved LDC lending practices and responsible loan disclosure, Social Advisory Services generally supports voting for such proposals. In cases where it can be determined that companies have been proactive and responsible in developing policies, Social Advisory Services may recommend a vote against the proposal’s adoption. Social Advisory Services usually opposes proposals that call for outright loan forgiveness; such action represents an unacceptable loss to lending institutions and their shareholders. Social Advisory Services may support such proposals at banks that have failed to make reasonable provisions for non-performing loans as a means to encourage a change in policy.

**Social Advisory Services Recommendation:**
- Vote for shareholder proposals asking for disclosure on lending practices in developing countries, unless the company has demonstrated a clear proactive record on the issue.
- Vote against shareholder proposals asking banks to forgive loans outright.
- Vote case-by-case on shareholder proposals asking for loan forgiveness at banks that have failed to make reasonable provisions for non-performing loans.
- Vote for proposals to restructure and extend the terms of non-performing loans.

### Community Investing

Shareholders may ask for a company to prepare a report addressing the company’s community investing efforts. Such proposals also ask companies to review their policies regarding their investments in different communities.

**Social Advisory Services Recommendation:** Vote for proposals that seek a policy review or report addressing the company’s community investing efforts.

### Miscellaneous

#### Adult Entertainment

Traditionally, there have not been many proposals filed in the area of adult entertainment. However, with the consolidation of the communications industry, a number of large companies have ended up with ownership of cable companies. These cable companies may offer their customers access to pay-per-view programming or channels intended for adult audiences. Proponents of shareholder proposals on this issue ask cable companies and companies with interests in cable companies to assess the costs and benefits of continuing to distribute sexually-explicit content, including the potential negative impact on the company’s image.

**Social Advisory Services Recommendation:** Vote for shareholder proposals that seek a review of the company’s involvement with pornography.
Abortion/Right to Life Issues

Shareholder proposals pertaining to abortion and right to life issues are rare. However, in the past shareholders have asked companies to stop manufacturing abortifacient drugs; to separate abortifacient drug operations from other operations; or to discontinue acute-care or physician management practices that involve support for abortion services. As long as abortion is legal, Social Advisory Services’ position is that issues related to abortion should be a personal decision, not a corporate one. Therefore Social Advisory Services recommends abstaining on anti-abortion and right-to-life proposals.

Social Advisory Services Recommendation: Abstain on shareholder proposals that address right to life issues.

Anti-Social Proposals

A number of ‘anti-social’ shareholder proposals have been filed at companies requesting increased disclosure. While these proposals’ requests are very similar to those submitted by shareholder advocates within traditional socially responsible investor circles, the underlying motives for filing the proposals appear to be very different. In addition to charitable contribution proposals, anti-social proposals addressing climate change, sustainability, and conflicts of interest may be seen at shareholder meetings. Despite implicitly different motivations in some of these proposals, the underlying requests for increased disclosure, in some cases, may be worth shareholder support.

Social Advisory Services Recommendation:

› Vote against shareholder proposals that do not seek to ultimately advance the goals of the social investment community.
› Vote case-by-case on anti-social shareholder proposals seeking a review or report on the company’s charitable contributions.

Violence and Adult Themes in Video Games

Perceptions of increased sex and violence in video games have led certain shareholders to question the availability of adult-themed content to children and teens. The Entertainment Software Ratings Board, which provides ratings for video games, has classified approximately 34 percent of the total games it reviews as either Teen, Mature, or Adults Only.

Social Advisory Services Recommendation: Vote for shareholder proposals asking for reports on company policies related to the sale of mature-rated video games to children and teens.
9. MUTUAL FUND PROXIES

Election of Trustees and Directors

Social Advisory Services Recommendation: Vote case-by-case on the election of directors and trustees, following the same guidelines for uncontested directors for public company shareholder meetings. However, mutual fund boards do not usually have compensation committees, so do not withhold for the lack of this committee.

Investment Advisory Agreement

An investment advisory agreement is an agreement between a mutual fund and its financial advisor under which the financial advisor provides investment advice to the fund in return for a fee based on the fund’s net asset size.

Social Advisory Services Recommendation: Votes on investment advisory agreements should be evaluated on a case-by-case basis, considering the following factors:

› Proposed and current fee schedules;
› Fund category/investment objective;
› Performance benchmarks;
› Share price performance as compared with peers;
› Resulting fees relative to peers;
› Assignments (where the advisor undergoes a change of control).

Changing a Fundamental Restriction to a Non-fundamental Restriction

Fundamental investment restrictions are limitations within a fund’s articles of incorporation that limit the investment practices of the particular fund.

Social Advisory Services Recommendation: Vote case-by-case on proposals to change a fundamental restriction to a non-fundamental restriction, considering the following factors:

› The fund’s target investments;
› The reasons given by the fund for the change; and
› The projected impact of the change on the portfolio.

Change Fundamental Investment Objective to Non-fundamental

Social Advisory Services Recommendation: Vote against proposals to change a fund’s fundamental investment objective to non-fundamental.

Distribution Agreements

Distribution agreements are agreements between a fund and its distributor which provide that the distributor is paid a fee to promote the sale of the fund’s shares.

Social Advisory Services Recommendation: Vote case-by-case on distribution agreement proposals, considering the following factors:

› Fees charged to comparably sized funds with similar objectives;
› The proposed distributor’s reputation and past performance;
› The competitiveness of the fund in the industry; and
› The terms of the agreement.
Approving New Classes or Series of Shares

Social Advisory Services Recommendation: Vote for the establishment of new classes or series of shares.

Convert closed-end fund to open-end fund

Although approval of these proposals would eliminate the discount at which the fund’s shares trade. The costs associated with converting the fund, in addition to the potential risks to long-term shareholder value, outweigh the potential benefits of the conversion.

Social Advisory Services Recommendation: Vote case-by-case on conversion proposals, considering the following factors:

 › Past performance as a closed-end fund;
 › Market in which the fund invests;
 › Measures taken by the board to address the discount; and
 › Past shareholder activism, board activity, and votes on related proposals.

Proxy Contests

Social Advisory Services Recommendation: Vote case-by-case on proxy contests, considering the following factors:

 › Past performance relative to its peers;
 › Market in which fund invests;
 › Measures taken by the board to address the issues;
 › Past shareholder activism, board activity, and votes on related proposals;
 › Strategy of the incumbents versus the dissidents;
 › Independence of directors;
 › Experience and skills of director candidates;
 › Governance profile of the company;
 › Evidence of management entrenchment.

Preferred Stock Proposals

Social Advisory Services Recommendation: Vote case-by-case on the authorization for or increase in preferred shares, considering the following factors:

 › Stated specific financing purpose;
 › Possible dilution for common shares;
 › Whether the shares can be used for antitakeover purposes.

Mergers

Social Advisory Services Recommendation: Vote case-by-case on merger proposals, considering the following factors:

 › Resulting fee structure;
 › Performance of both funds;
 › Continuity of management personnel; and
 › Changes in corporate governance and their impact on shareholder rights.
Business Development Companies – Authorization to Sell Shares of Common Stock at a Price below Net Asset Value

Social Advisory Services Recommendation: Vote for proposals authorizing the board to issue shares below Net Asset Value (NAV) if:
› The proposal to allow share issuances below NAV has an expiration date that is less than one year from the date shareholders approve the underlying proposal, as required under the Investment Company Act of 1940;
› A majority of the independent directors who have no financial interest in the sale have made a determination as to whether such sale would be in the best interests of the company and its shareholders prior to selling shares below NAV; and
› The company has demonstrated responsible past use of share issuances by either:
   › Outperforming peers in its 8-digit GICS group as measured by one- and three-year median TSRs; or
   › Providing disclosure that its past share issuances were priced at levels that resulted in only small or moderate discounts to NAV and economic dilution to existing non-participating shareholders.

Change in Fund’s Subclassification

Social Advisory Services Recommendation: Vote case-by-case on changes in a fund’s sub-classification, considering the following factors: a) potential competitiveness; b) current and potential returns; c) risk of concentration; d) consolidation in target industry.

Changing the Domicile of a Fund

Social Advisory Services Recommendation: Vote case-by-case on re-incorporations, considering the following factors: a) regulations of both states; b) required fundamental policies of both states; c) the increased flexibility available.

Disposition of Assets/Termination/Liquidation

Social Advisory Services Recommendation: Vote case-by-case on proposals to dispose of assets, to terminate or liquidate, considering the following factors: a) strategies employed to salvage the company; b) the fund’s past performance; c) the terms of the liquidation.

Authorizing the Board to Hire and Terminate Subadvisers Without Shareholder Approval

Social Advisory Services Recommendation: Vote against proposals authorizing the board to hire or terminate subadvisers without shareholder approval if the investment adviser currently employs only one subadviser.

Name Change Proposals

Social Advisory Services Recommendation: Vote case-by-case on name change proposals, considering the following factors: a) political/economic changes in the target market; b) consolidation in the target market; and c) current asset composition.

1940 Act Policies

Social Advisory Services Recommendation:
› Vote case-by-case on policies under the Investment Advisor Act of 1940, considering the following factors: a) potential competitiveness; b) regulatory developments; c) current and potential returns; and d) current and potential risk.
› Generally vote for these amendments as long as the proposed changes do not fundamentally alter the investment focus of the fund and do comply with the current SEC interpretation.
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1. OPERATIONAL ITEMS

Financial Results/Director and Auditor Reports

Social Advisory Services Recommendation: Vote for approval of financial statements and director and auditor reports, unless:

› There are concerns about the accounts presented or audit procedures used; or
› The company is not responsive to shareholder questions about specific items that should be publicly disclosed.

Appointment of Auditors and Auditor Fees

Social Advisory Services Recommendation: Generally, vote for the reelection of auditors and proposals authorizing the board to fix auditor fees, unless:

› The name of the proposed auditors has not been published;
› There are serious concerns about the effectiveness of the auditors;
› The lead audit partner(s) has been linked with a significant auditing controversy;
› There is a reason to believe that the auditor has rendered an opinion which is neither accurate nor indicative of the company’s financial position;
› The lead audit partner(s) has previously served the company in an executive capacity or can otherwise be considered affiliated with the company;
› The auditors are being changed without explanation; or
› For widely-held companies, fees for non-audit services exceed either 100 percent of standard audit-related fees or any stricter limit set in local best practice recommendations or law.

In circumstances where fees for non-audit services include fees related to significant one-time capital structure events: initial public offerings, bankruptcy emergence, and spinoffs; and the company makes public disclosure of the amount and nature of those fees which are an exception to the standard "non-audit fee" category, then such fees may be excluded from the non-audit fees considered in determining the ratio of non-audit to audit fees.

For concerns relating to the audit procedures, independence of auditors, and/or name of auditors, Social Advisory Services will focus on the auditor election and/or the audit committee members. For concerns relating to fees paid to the auditors, Social Advisory Services will focus on remuneration of auditors if this is a separate voting item, otherwise Social Advisory Services would focus on the auditor election.

Appointment of Internal Statutory Auditors

Social Advisory Services Recommendation: Vote for the appointment or reelection of statutory auditors, unless:

› There are serious concerns about the statutory reports presented or the audit procedures used;
› Questions exist concerning any of the statutory auditors being appointed; or
› The auditors have previously served the company in an executive capacity or can otherwise be considered affiliated with the company.

Allocation of Income

Social Advisory Services Recommendation: Vote for approval of the allocation of income, unless:

› The dividend payout ratio has been consistently below 30 percent without adequate explanation; or
› The payout is excessive given the company’s financial position.
Stock (Scrip) Dividend Alternative

Social Advisory Services Recommendation: Vote case-by-case on stock (scrip) dividend proposals, considering factors such as:

› Whether the proposal allows for a cash option; and
› If the proposal is in line with market standards.

Amendments to Articles of Association

Social Advisory Services Recommendation: Vote amendments to the articles of association on a case-by-case basis.

Virtual Meetings (UK/Ireland and Europe)

Social Advisory Services Recommendation: Generally vote for proposals allowing for the convening of hybrid* shareholder meetings if it is clear that it is not the intention to hold virtual-only AGMs.

Generally vote against proposals allowing for the convening of virtual-only* shareholder meetings.

* The phrase “virtual-only shareholder meeting” refers to a meeting of shareholders that is held exclusively through the use of online technology without a corresponding in-person meeting. The term “hybrid shareholder meeting” refers to an in-person, or physical, meeting in which shareholders are permitted to participate online.

Change in Company Fiscal Term

Social Advisory Services Recommendation: Vote for resolutions to change a company’s fiscal term unless a company’s motivation for the change is to postpone its AGM.

Lower Disclosure Threshold for Stock Ownership

Social Advisory Services Recommendation: Vote against resolutions to lower the stock ownership disclosure threshold below 5 percent unless specific reasons exist to implement a lower threshold.

Amend Quorum Requirements

Social Advisory Services Recommendation: Vote proposals to amend quorum requirements for shareholder meetings on a case-by-case basis.

Transact Other Business

Social Advisory Services Recommendation: Vote against other business when it appears as a voting item.
2. BOARD OF DIRECTORS

**Director Elections**

**Social Advisory Services Recommendation:** Vote for management nominees in the election of directors, unless:

- Adequate disclosure has not been provided in a timely manner;
- There are clear concerns over questionable finances or restatements;
- There have been questionable transactions with conflicts of interest;
- There are any records of abuses against minority shareholder interests; or
- The board fails to meet minimum corporate governance standards, including board independence standards.

**Diversity**

Social Advisory Services will evaluate gender diversity on boards in international markets when reviewing director elections, to the extent that disclosures and market practices permit.

- Generally vote against or withhold from incumbent members of the nominating committee if the board lacks at least one woman.
- **For Japan,** if the company has an audit-committee-board structure or a traditional two-tier board structure as opposed to three committees, vote against incumbent representative directors if the board lacks at least one woman.
- **For Canada, UK,** and **Australia,** vote against or withhold from incumbent members of the nominating committee if:
  - the board lacks at least one woman and one racially diverse director; and
  - the board is not at least 30 percent diverse.
  If the company does not have a formal nominating committee, vote against or withhold from the entire board of directors.

Vote for individual nominees unless there are specific concerns about the individual, such as criminal wrongdoing or breach of fiduciary responsibilities.

Vote against individual directors if absences at board meetings have not been explained (in countries where this information is disclosed).

Vote for employee and/or labor representatives if they sit on either the audit or compensation committee and are required by law to be on those committees. Vote against employee and/or labor representatives if they sit on either the audit or compensation committee, if they are not required to be on those committees.

**Material ESG Failures**

Vote against or withhold from directors individually, on a committee, or potentially the entire board due to:

- Material failures of governance, stewardship, risk oversight\(^1\), or fiduciary responsibilities at the company, including failure to adequately manage or mitigate environmental, social and governance (ESG) risks;
- A lack of sustainability reporting in the company's public documents and/or website in conjunction with a failure to adequately manage or mitigate environmental, social and governance (ESG) risks;

\(^1\) Examples of failure of risk oversight include, but are not limited to: bribery; large or serial fines or sanctions from regulatory bodies; significant environmental incidents including spills and pollution; large scale or repeat workplace fatalities or injuries; significant adverse legal judgments or settlements; or hedging of company stock.
Failure to replace management as appropriate;
Egregious actions related to the director(s)’ service on the boards that raise substantial doubt about his or her ability to effectively oversee management and serve the best interests of shareholders at any company.

For director elections, Social Advisory Services will also take into consideration market-specific provisions which are listed below:

**Canadian Guidelines**

**Board Structure and Independence (TSX)**

Vote withhold for any Executive Director or Non-Independent, Non-Executive Director where:
- The board is less than majority independent; or
- The board lacks a separate compensation or nominating committee.

**Non-Independent Directors on Key Committees (TSX)**

Vote withhold for members of the audit, compensation, or nominating committee who:
- Are Executive Directors;
- Are Controlling Shareholders; or
- Is a Non-employee officer of the company or its affiliates if he/she is among the five most highly compensated.

**Non-Independent Directors on Key Committees (TSX-V)**

Vote withhold for Executive Directors, Controlling Shareholders or a Non-employee officer of the company or its affiliates if he/she is among the five most highly compensated who:
- Are members of the audit committee;
- Are members of the compensation committee or the nominating committee and the committee is not majority independent; or
- Are board members and the entire board fulfills the role of a compensation committee or a nominating committee and the board is not majority independent.

**Overboarding-TSX**

Generally vote withhold for individual director nominees who:
- Are non-CEO directors and serve on more than five public company boards; or
- Are CEOs of public companies who serve on the boards of more than two public companies besides their own — withhold only at their outside boards.

**Externally-Managed Issuers (EMIs) –TSX and TSXV**

Vote case-by-case on say-on-pay resolutions where provided, or on individual directors, committee members, or the entire board as appropriate, when an issuer is externally-managed and has provided minimal or no disclosure about

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2 Although a CEO’s subsidiary boards will be counted as separate boards, Social Advisory Services will not recommend a withhold vote for the CEO of a parent company board or any of the controlled (>50 percent ownership) subsidiaries of that parent but may do so at subsidiaries that are less than 50 percent controlled and boards outside the parent/subsidiary relationship.
their management services agreements and how senior management is compensated. Factors taken into consideration may include but are not limited to:

- The size and scope of the management services agreement;
- Executive compensation in comparison to issuer peers and/or similarly structured issuers;
- Overall performance;
- Related party transactions;
- Board and committee independence;
- Conflicts of interest and process for managing conflicts effectively;
- Disclosure and independence of the decision-making process involved in the selection of the management services provider;
- Risk mitigating factors included within the management services agreement such as fee recoupment mechanisms;
- Historical compensation concerns;
- Executives’ responsibilities; and
- Other factors that may reasonably be deemed appropriate to assess an externally-managed issuer’s governance framework.

**Unilateral Adoption of an Advance Notice Provision**

Generally withhold from individual directors, committee members, or the entire board as appropriate in situations where an advance notice policy has been adopted by the board but has not been included on the voting agenda at the next shareholders’ meeting. Continued lack of shareholder approval of the advanced notice policy in subsequent years may result in further withhold recommendations.

**European Guidelines**

In *European markets*, Social Advisory Services looks at different factors to make determinations regarding director elections. The following factors are taken into account:

**Director Terms**

For **Belgium, France, Greece, the Netherlands, Spain, and Switzerland**, vote against the election or re-election of any director when his/her term is not disclosed or when it exceeds four years and adequate explanation for non-compliance has not been provided. In these markets, the maximum board terms are either recommended best practice or required by legislation. Under best practice recommendations, companies should shorten the terms for directors when the terms exceed the limits suggested by best practices. The policy will be applied to all companies in these markets, for bundled as well as unbundled items.

Vote against article amendment proposals to extend board terms. In cases where a company’s articles provide for a shorter limit and where the company wishes to extend director terms from three or fewer years to four years, for example, Social Advisory Services will recommend a vote against, based on the general principle that director accountability is maximized by elections with a short period of renewal.

**Bundling of Proposals to Elect Directors**

Bundling together proposals that could be presented as separate voting items is not considered good market practice, because bundled resolutions leave shareholders with an all-or-nothing choice, skewing power disproportionately towards the board and away from shareholders. As director elections are one of the most important voting decisions that shareholders make, directors should be elected individually.
For the markets of **Bulgaria, Croatia, Czech Republic, Estonia, France, Germany, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, and Slovenia** vote against the election or reelection of any directors if the company proposes a single slate of directors.

Bundled director elections in Poland may be supported for companies that go beyond market practice by disclosing the names of nominees on a timely basis

**Board Independence**

**Widely-held companies**

A. Non-controlled companies

› Generally vote against the election or reelection of any non-independent directors (excluding the CEO) if:
  › Fewer than 50 percent of the board members elected by shareholders, excluding, where relevant, employee shareholder representatives, would be independent, or
  › Fewer than one-third of all board members would be independent.

Greece and Portugal are excluded from Provision (1.) in the above-mentioned voting policy.

B. Controlled companies

› Generally vote against the election or reelection of any non-independent directors (excluding the CEO) if less than one-third of the board members are independent.

**Non-widely held companies**

Generally vote against the election or reelection of any non-independent directors (excluding the CEO) if less than one-third of the board members are independent.

**Definition of terms**

‘Widely-held companies’ are determined based on their membership in a major index and/or the number of Social Advisory Services clients holding the securities. For Sweden, Norway, Denmark, and Luxembourg, this is based on membership on a local blue-chip market index and/or MSCI EAFE companies. For Portugal, it is based on membership in the PSI-20 and/or MSCI EAFE index.

A company is considered to be controlled for the purposes of the above-mentioned voting policies if a shareholder, or multiple shareholders acting in concert, control a majority of the company’s equity capital (i.e. 50 percent + one share). If a company is majority-controlled by virtue of a shareholder structure in which shareholders’ voting rights do not accrue in accordance with their equity capital commitment (e.g. unequal or multi-class share structures), the company will not be classified as controlled unless the majority shareholder/majority shareholding group also holds a majority of the company’s equity capital.

**Disclosure of Nominee Names**

Vote against the election or reelection of any and all director nominees when the names of the nominees are not available at the time the proxy analysis is being written. This policy will be applied to all companies in these markets, for bundled and unbundled items.
Combined Chairman/CEO

Generally, vote against the (re)election of combined chair/CEOs at widely held European companies.

When the company provides assurance that the chair/CEO would only serve in the combined role on an interim basis (no more than two years), the vote recommendation would be made on a case-by-case basis.

In the above-mentioned situation, Social Advisory Services will consider the rationale provided by the company and whether it has set up adequate control mechanisms on the board (such as a lead independent director, a high overall level of board independence, and a high level of independence on the board’s key committees).

Election of Former CEO as Chairman of the Board

Generally vote against the election or reelection of a former CEO as chairman to the supervisory board or board of directors at widely held companies in Germany, Austria, and the Netherlands. In markets such as Germany, where the general meeting only elects the nominees and, subsequently, the new board’s chairman, Social Advisory Services will generally recommend a vote against the election or election of a former CEO, unless the company has publicly confirmed prior to the general meeting that he will not proceed to become chairman of the board.

Considerations should be given to any of the following exceptional circumstances on a case-by-case basis if:

› There are compelling reasons that justify the election or reelection of a former CEO as chairman; or
› The former CEO is proposed to become the board’s chairman only on an interim or temporary basis; or
› The former CEO is proposed to be elected as the board’s chairman for the first time after a reasonable cooling-off period; or
› The board chairman will not receive a level of compensation comparable to the company’s executives nor assume executive functions in markets where this is applicable.

Overboarded Directors

In Austria, Belgium, Denmark, Finland, France, Germany, Italy, Luxembourg, the Netherlands, Norway, Poland, Spain, Sweden, and Switzerland, at widely held companies, Social Advisory Services will generally recommend a vote against a candidate when he/she holds an excessive number of board appointments, as defined by the following guidelines:

› Any person who holds more than five mandates at listed companies will be classified as overboarded. For the purposes of calculating this limit, a non-executive directorship counts as one mandate, a non-executive chairmanship counts as two mandates, and a position as executive director (or a comparable role) is counted as three mandates.
› Also, any person who holds the position of executive director (or a comparable role) at one company and a non-executive chairman at a different company will be classified as overboarded.

An adverse vote recommendation will not be applied to a director within a company where he/she serves as CEO; instead, any adverse vote recommendations will be applied to his/her additional seats on other company boards. For chairmen, negative recommendations would first be applied towards non-executive positions held, but the chairmanship position itself would be targeted where they are being elected as chairman for the first time or, when in aggregate their chair positions are three or more in number, or if the chairman holds an outside executive position.

One Board Seat per Director
In cases where a director holds more than one board seat on a single board and the corresponding votes, manifested as one seat as a physical person plus an additional seat(s) as a representative of a legal entity, vote against the election/reelection of such legal entities and in favor of the physical person.

However, an exception is made if the representative of the legal entity holds the position of CEO. In such circumstances, Social Advisory Services will typically recommend a vote in favor of the legal entity and against the election/reelection of the physical person.

While such occurrences are rare, there have been cases where a board member may have multiple board seats and corresponding votes. Holding several board seats concurrently within one board increases this person’s direct influence on board decisions and creates an inequality among board members.

This situation has manifested in Belgium, Luxembourg, and France. This is not a good corporate governance practice, as it places disproportionate influence and control in one person.

**Composition of Committees**

**For widely-held companies,** generally vote against the (re)election of any non-independent members of the audit committee if:

- Fewer than 50 percent of the audit committee members, who are elected by shareholders in such capacity or another – excluding, where relevant, employee shareholder representatives – would be independent; or
- Fewer than one-third of all audit committee members would be independent.

For companies whose boards are legally required to have 50 percent of directors not elected by shareholders, the second criterion is not applicable.

Generally vote against the election or reelection of the non-independent member of the audit committee designated as chairman of that committee.

For widely-held companies in Belgium, the Netherlands, and Switzerland, vote against the (re)election of non-independent members of the remuneration committee if their (re)election would lead to a non-independent majority on that committee.

**For all companies:**

In Belgium, Denmark, Finland, France, Iceland, Luxembourg, the Netherlands, Norway, Spain, Sweden, and Switzerland, vote against the (re)election of executives who serve on the company’s audit or remuneration committee. Social Advisory Services may recommend against if the disclosure is too poor to determine whether an executive serves or will serve on a committee. If a company does not have an audit or a remuneration committee, Social Advisory Services may consider that the entire board fulfills the role of a committee. In such case, Social Advisory Services may recommend against the executives, including the CEO, up for election to the board.

**Voto di Lista (Italy)**

In Italy, director elections generally take place through the *voto di lista* mechanism (similar to slate elections). Since the Italian implementation of the European Shareholder Rights Directive (effective since Nov. 1, 2010), issuers must publish the various lists 21 days in advance of the meeting.
Since shareholders only have the option to support one such list, where lists are published in sufficient time, Social Advisory Services will recommend a vote on a case-by-case basis, determining which list of nominees it considers is best suited to add value for shareholders.

Those companies that are excluded from the provisions of the European Shareholder Rights Directive publish lists of nominees 10 days before the meeting. In the case where nominees are not published in sufficient time, Social Advisory Services will recommend a vote against the director elections before the lists of director nominees are disclosed. Once the various lists of nominees are disclosed, Social Advisory Services will issue an alert to its clients and, if appropriate, change its vote recommendation to support one particular list.

**The Florange Act (France) - Double Voting Rights**

For French companies that:

- Did not have a bylaw allowing for double voting rights before the enactment of the Law of 29 March 2014 (Florange Act); and
- Do not currently have a bylaw prohibiting double-voting rights; and either
  - Do not have on their ballot for shareholder approval a bylaw amendment to prohibit double-voting, submitted by either management or shareholders; or
  - Have not made a public commitment to submit such a bylaw amendment to shareholder vote before April 3, 2016;

Then, on a case-by-case basis, Social Advisory Services may recommend against the following types of proposals:

- The reelection of directors or supervisory board members; or
- The approval of the discharge of directors; or
- If neither reelection of directors/supervisory board members nor approval of discharge is considered appropriate, then the approval of the annual report and accounts.

**Composition of the Nominating Committee**

Vote for proposals in **Finland, Iceland, Norway,** and **Sweden** to elect or appoint a nominating committee consisting mainly of non-board members.

Vote for shareholder proposals calling for disclosure of the names of the proposed candidates at the meeting, as well as the inclusion of a representative of minority shareholders in the committee.

Vote against proposals where the names of the candidates (in the case of an election) or the principles for the establishment of the committee have not been disclosed in a timely manner.

Vote against proposals in **Sweden** to elect or appoint such a committee if the company is on the MSCI-EAFE or local main index and the following conditions exist:

- A member of the executive management would be a member of the committee;
- More than one board member who is dependent on a major shareholder would be on the committee; or
- The chair of the board would also be the chair of the committee.

In cases where the principles for the establishment of the nominating committee, rather than the election of the committee itself, are being voted on, vote against the adoption of the principles if any of the above conditions are met for the current committee, and there is no publicly available information indicating that this would no longer be the case for the new nominating committee.
Election of Censors (France)

For widely held companies, Social Advisory Services will generally recommend a vote against proposals seeking shareholder approval to elect a censor, to amend bylaws to authorize the appointment of censors, or to extend the maximum number of censors to the board.

However, Social Advisory Services will recommend a vote on a case-by-case basis when the company provides assurance that the censor would serve on a short-term basis (maximum one year) with the intent to retain the nominee before his/her election as director. In this case, consideration shall also be given to the nominee’s situation (notably overboarding or other factors of concern).

In consideration of the principle that censors should be appointed on a short-term basis, vote against any proposal to renew the term of a censor or to extend the statutory term of censors.

Cumulative Voting – Middle East and Africa (MEA)

For MEA markets, in cases where:

› Directors are proposed for (re)election through a cumulative voting system, or
› Director elections do not take place through a cumulative voting system, but the number of nominees up for (re)election exceeds the number of board vacancies,

Social Advisory Services will recommend a vote on a case-by-case basis, considering additional factors, for the purpose of identifying the best suited nominees to add value for shareholders. Positive vote recommendations will be issued preferentially in favor of the following categories of candidates:

› Candidates who can be identified as representatives of minority shareholders of the company, or independent candidates, namely:
   › Candidates who can be classified as independent according to SRI policy, or, failing that,
   › Candidates explicitly classified as independent per the company’s director classification.

› Candidates whose professional background may have the following benefits:
   › Increasing the diversity of incumbent directors’ professional profiles and skills (thanks to their financial expertise, international experience, executive positions/directorships at other listed companies, or other relevant factors.
   › Bringing to the current board of directors relevant experience in areas linked to the company’s business, evidenced by current or past board memberships or management functions at other companies.

› Incumbent board members and candidates explicitly supported by the company’s management.

Please see the International Classification of Directors on the following page.
Classification of Directors – International Policy 2019

Executive Director
› Employee or executive of the company or a wholly-owned subsidiary of the company;
› Any director who is classified as a non-executive, but receives salary, fees, bonus, and/or other benefits that are in line with the highest-paid executives of the company.

Non-Independent Non-Executive Director (NED)
› Any director who is attested by the board to be a non-independent NED;
› Any director specifically designated as a representative of a shareholder of the company;
› Any director who is also an employee or executive of a significant shareholder of the company;
› Any director who is also an employee or executive of a subsidiary, associate, joint venture, or company that is affiliated with a significant shareholder of the company;
› Any director who is nominated by a dissenting significant shareholder unless there is a clear lack of material connection with the dissident, either currently or historically;
› Beneficial owner (direct or indirect) of at least 10 percent of the company’s stock, either in economic terms or in voting rights (this may be aggregated if voting power is distributed among more than one member of a defined group, e.g., members of a family that beneficially own less than 10 percent individually, but collectively own more than 10 percent), unless market best practice dictates a lower ownership and/or disclosure threshold (and in other special market-specific circumstances);
› Government representative;
› Currently provides or has provided (or a relative provides) professional services to the company, to an affiliate of the company, or to an individual officer of the company or of one of its affiliates in the last fiscal year in excess of USD 10,000 per year;
› Represents customer, supplier, creditor, banker, or other entity with which the company maintains a transactional/commercial relationship (unless the company discloses information to apply a materiality test);
› Any director who has a conflicting relationship with the company, including but not limited to cross-directorships with executive directors or the chairman of the company;
› Relative of a current or former executive of the company or its affiliates;
› A new appointee elected other than by a formal process through the general meeting (such as a contractual appointment by a substantial shareholder);
› Founder/co-founder/member of founding family but not currently an employee or executive;
› Former executive or employee (five-year cooling off period);
› Years of service is generally not a determining factor unless it is recommended best practice in a market and/or in extreme circumstances, in which case it may be considered.
› Any additional relationship or principle considered to compromise independence under local corporate governance best practice guidance.

Independent NED
› No material connection, either direct or indirect, to the company (other than a board seat) or to a significant shareholder.

Employee Representative
› Represents employees or employee shareholders of the company (classified as "employee representative" and considered a non-independent NED).

Footnotes

[1] At least 10 percent of the company’s stock, unless market best practice dictates a lower ownership and/or disclosure threshold.
[2] For purposes of Social Advisory Services' director independence classification, “material” will be defined as a standard of relationship financial, personal, or otherwise that a reasonable person might conclude could potentially influence one's...
objectivity in the boardroom in a manner that would have a meaningful impact on an individual’s ability to satisfy requisite fiduciary standards on behalf of shareholders.

[3] “Relative” follows the definition of “immediate family members” which covers spouses, parents, children, stepparents, step-children, siblings, in-laws, and any person (other than a tenant or employee) sharing the household of any director, nominee for director, executive officer, or significant shareholder of the company.

[4] Professional services can be characterized as advisory in nature and generally include the following: investment banking/financial advisory services; commercial banking (beyond deposit services); investment services; insurance services; accounting/audit services; consulting services; marketing services; and legal services. The case of participation in a banking syndicate by a non-lead bank should be considered a transaction (and hence subject to the associated materiality test) rather than a professional relationship.

[5] A business relationship may be material if the transaction value (of all outstanding transactions) entered into between the company and the company or organization with which the director is associated is equivalent to either 1 percent of the company’s turnover or 1 percent of the turnover of the company or organization with which the director is associated. OR, a business relationship may be material if the transaction value (of all outstanding financing operations) entered into between the company and the company or organization with which the director is associated is more than 10 percent of the company’s shareholder equity or the transaction value, (of all outstanding financing operations), compared to the company’s total assets, is more than 5 percent.

[6] For example, in continental Europe and Latin America, directors with a tenure exceeding 12 years will be considered non-independent. In Hong Kong, Singapore and Taiwan, directors with a tenure exceeding nine years will be considered non-independent, unless the company provides sufficient and clear justification that the director is independent despite his long tenure. For purposes of independence classification of directors incorporated in the Middle East and Africa region, this criterion will be taken into account in accordance with market best practice and disclosure standards and availability.

[7] For MEA markets, directors’ past services as statutory auditor/partner of the statutory audit firm will be taken into account, with cooling-off periods in accordance with local market best practice.

Contested Director Elections

Social Advisory Services Recommendation: For contested elections of directors, e.g. the election of shareholder nominees or the dismissal of incumbent directors, Social Advisory Services will make its recommendation on a case-by-case basis, determining which directors are considered best suited to add value for shareholders.

The analysis will generally be based on, but not limited to, the following major decision factors:

› Company performance relative to its peers;
› Strategy of the incumbents versus the dissidents;
› Independence of directors/nominees;
› Experience and skills of board candidates;
› Governance profile of the company;
› Evidence of management entrenchment;
› Responsiveness to shareholders;
› Whether a takeover offer has been rebuffed; and
› Whether minority or majority representation is being sought.

When analyzing a contested election of directors, Social Advisory Services will generally focus on two central questions: (1) Have the proponents proved that board change is warranted? And if so, (2) Are the proponent board nominees likely to effect positive change (i.e., maximize long-term shareholder value).
Discharge of Board and Management

**Social Advisory Services Recommendation:** Generally vote for discharge of directors, including members of the management board and/or supervisory board, unless there is reliable information about significant and compelling controversies that the board is not fulfilling its fiduciary duties such as:

› A lack of oversight or actions by board members which invoke shareholder distrust related to malfeasance or poor supervision, such as operating in private or company interest rather than in shareholder interest;
› Any legal issues (e.g. civil/criminal) aiming to hold the board responsible for breach of trust in the past or related to currently alleged actions yet to be confirmed (and not only the fiscal year in question), such as price fixing, insider trading, bribery, fraud, and other illegal actions;
› Other material failures of governance, or fiduciary responsibilities at the company, including failure to adequately manage or mitigate environmental, social and governance (ESG) risks; or
› A lack of sustainability reporting in the company’s public documents and/or website in conjunction with a failure to adequately manage or mitigate environmental, social and governance (ESG) risks.

For markets which do not routinely request discharge resolutions (e.g. common law countries or markets where discharge is not mandatory), analysts may voice concern in other appropriate agenda items, such as approval of the annual accounts or other relevant resolutions, to enable shareholders to express discontent with the board.

Vote against proposals to remove approval of discharge of board and management from the agenda.

Director, Officer, and Auditor Indemnification and Liability Provisions

**Social Advisory Services Recommendation:**

› Vote proposals seeking indemnification and liability protection for directors and officers on a case-by-case basis.
› Vote against proposals to indemnify auditors.

Board Structure

**Social Advisory Services Recommendation:**

› Vote for proposals to fix board size.
› Vote against the introduction of classified boards and mandatory retirement ages for directors.
› Vote against proposals to alter board structure or size in the context of a fight for control of the company or the board.
3. CAPITAL STRUCTURE

Share Issuance Requests

General Issuances:

**Social Advisory Services Recommendation:** Evaluate share issuance requests on a case-by-case basis taking into consideration market-specific guidelines as applicable.

For *European markets*, vote for issuance authorities with pre-emptive rights to a maximum of 50 percent over currently issued capital and as long as the share issuance authorities’ periods are clearly disclosed (or implied by the application of a legal maximum duration) and in line with market-specific practices and/or recommended guidelines (e.g. issuance periods limited to 18 months for the Netherlands).

Vote for issuance authorities without pre-emptive rights to a maximum of 10 percent (or a lower limit if local market best practice recommendations provide) of currently issued capital as long as the share issuance authorities’ periods are clearly disclosed (or implied by the application of a legal maximum duration) and in line with market-specific practices and/or recommended guidelines (e.g. issuance periods limited to 18 months for the Netherlands).

For *UK and Irish* companies, generally vote for a resolution to authorize the issuance of equity, unless:

- The general issuance authority exceeds one-third (33 percent) of the issued share capital. Assuming it is no more than one-third, a further one-third of the issued share capital may also be applied to a fully pre-emptive rights issue taking the acceptable aggregate authority to two-thirds (66 percent);
- The routine authority to disapply preemption rights exceeds 10 percent of the issued share capital, provided that any amount above 5 percent is to be used for the purposes of an acquisition or a specified capital investment.

For *French* companies:

- Vote for general issuance requests with preemptive rights, or without preemptive rights but with a binding “priority right,” for a maximum of 50 percent over currently issued capital.
- Generally vote for general authorities to issue shares without preemptive rights up to a maximum of 10 percent of share capital. When companies are listed on a regulated market, the maximum discount on share issuance price proposed in the resolution must, in addition, comply with the legal discount (i.e., a maximum of 5 percent discount to the share listing price) for a vote for to be warranted.

For *Hong Kong* companies, generally vote for the general issuance mandate for companies that:

- Limit the issuance request to 10 percent or less of the relevant class of issued share capital;
- Limit the discount to 10 percent of the market price of shares; and
- Have no history of renewing the General Issuance Mandate several times within a period of one year which may result in the share issuance limit exceeding 10 percent of the relevant class of issued share capital within the 12-month period.

Generally vote for a general issuance of equity or equity-linked securities without preemptive rights when the share issuance limit is not more than 10 percent of the company’s issued share capital and 50 percent with preemptive rights for all *Singapore* companies, with the exception of Catalist-listed companies and Real Estate Investment Trusts.
For **Singapore** companies listed on the Catalist market of the SGX, generally vote for a general issuance of equity or equity-linked securities without preemptive rights when the share issuance limit is not more than 20 percent of the company's issued share capital and 100 percent with preemptive rights. For Real Estate Investment Trusts, generally vote for a general issuance of equity or equity-linked securities without preemptive rights when the unit issuance limit is not more than 20 percent of its issued unit capital and 50 percent with preemptive rights.

- For companies listed on the Main Market and ACE Market of the Bursa Malaysia Securities Bhd (Exchange), vote for issuance requests without preemptive rights to a maximum of 10 percent of currently issued capital. For real estate investment trusts (REITs), vote for issuance requests without preemptive rights to a maximum of 20 percent of currently issued capital.

For **Latin American** companies, generally vote for issuance requests with preemptive rights to a maximum of 100 percent over currently issued capital. Vote for issuance requests without preemptive rights to a maximum of 20 percent of currently issued capital. Specific Issuances requested will be evaluated on a case-by-case basis.

For shelf registration programs at Latin American companies (**Argentina, Colombia, Chile, Mexico and Peru**) Vote on a case-by-case basis on all requests, with or without preemptive rights. Approval of a multi-year authority for the issuance of securities under Shelf Registration Programs will be considered on a case-by-case basis, taking into consideration, but not limited to, the following:

- Whether the company has provided adequate and timely disclosure including detailed information regarding the rationale for the proposed program;
- Whether the proposed amount to be approved under such authority, the use of the resources, the length of the authorization, the nature of the securities to be issued under such authority, including any potential risk of dilution to shareholders is disclosed; and
- Whether there are concerns regarding questionable finances, the use of the proceeds, or other governance concerns.

### Increases in Authorized Capital

**Social Advisory Services Recommendation**: Vote for non-specific proposals to increase authorized capital up to 100 percent over the current authorization unless the increase would leave the company with less than 30 percent of its new authorization outstanding.

Vote for specific proposals to increase authorized capital to any amount, unless:

- The specific purpose of the increase (such as a share-based acquisition or merger) does not meet Social Advisory Services guidelines for the purpose being proposed; or
- The increase would leave the company with less than 30 percent of its new authorization outstanding after adjusting for all proposed issuances.

Vote against proposals to adopt unlimited capital authorizations.

### Reduction of Capital

**Social Advisory Services Recommendation**: Vote for proposals to reduce capital for routine accounting purposes unless the terms are unfavorable to shareholders.

Vote proposals to reduce capital in connection with corporate restructuring on a case-by-case basis.

### Capital Structures

**Social Advisory Services Recommendation**: Vote for resolutions that seek to maintain or convert to a one-share, one-vote capital structure.
Vote against requests for the creation or continuation of dual-class capital structures or the creation of new or additional supervoting shares.

**Preferred Stock**

**Social Advisory Services Recommendation:**
› Vote for the creation of a new class of preferred stock or for issuances of preferred stock up to 50 percent of issued capital unless the terms of the preferred stock would adversely affect the rights of existing shareholders.

› Vote for the creation/issuance of convertible preferred stock as long as the maximum number of common shares that could be issued upon conversion meets Social Advisory Services' guidelines on equity issuance requests.

› Vote against the creation of a new class of preference shares that would carry superior voting rights to the common shares.

› Vote against the creation of blank check preferred stock unless the board clearly states that the authorization will not be used to thwart a takeover bid.

› Vote proposals to increase blank check preferred authorizations on a case-by-case basis.

**Debt Issuance Requests**

**Social Advisory Services Recommendation:** Vote non-convertible debt issuance requests on a case-by-case basis, with or without pre-emptive rights.

Vote for the creation/issuance of convertible debt instruments as long as the maximum number of common shares that could be issued upon conversion meets Social Advisory Services' guidelines on equity issuance requests.

Vote for proposals to restructure existing debt arrangements unless the terms of the restructuring would adversely affect the rights of shareholders.

**Pledging of Assets for Debt**

**Social Advisory Services Recommendation:** Vote proposals to approve the pledging of assets for debt on a case-by-case basis.

**Increase in Borrowing Powers**

**Social Advisory Services Recommendation:** Vote proposals to approve increases in a company’s borrowing powers on a case-by-case basis.

**Share Repurchase Plans**

**Social Advisory Services Recommendation:** Generally vote for market repurchase authorities (share repurchase programs) if the terms comply with the following criteria:

› A repurchase limit of up to 10 percent of outstanding issued share capital;
› A holding limit of up to 10 percent of a company’s issued share capital in treasury (“on the shelf”); and
› Duration of no more than 5 years, or such lower threshold as may be set by applicable law, regulation, or code of governance best practice.
Authorities to repurchase shares in excess of the 10 percent repurchase limit will be assessed on a case-by-case basis. Social Advisory Services may support such share repurchase authorities under special circumstances, which are required to be publicly disclosed by the company, provided that, on balance, the proposal is in shareholders’ interests. In such cases, the authority must comply with the following criteria:

- A holding limit of up to 10 percent of a company’s issued share capital in treasury (“on the shelf”); and
- Duration of no more than 18 months.

In markets where it is normal practice not to provide a repurchase limit, Social Advisory Services will evaluate the proposal based on the company’s historical practice. However, Social Advisory Services expects companies to disclose such limits and, in the future, may recommend a vote against companies that fail to do so. In such cases, the authority must comply with the following criteria:

- A holding limit of up to 10 percent of a company’s issued share capital in treasury (“on the shelf”); and
- Duration of no more than 18 months.

In addition, Social Advisory Services will recommend against any proposal where:

- The repurchase can be used for takeover defenses;
- There is clear evidence of abuse;
- There is no safeguard against selective buybacks;
- Pricing provisions and safeguards are deemed to be unreasonable in light of market practice.

**Market-Specific Exceptions**

For **Italy** and **Germany**, vote for share-repurchase plans and share reissuance plans that would use call and put options if the following criteria are met:

- The duration of the options is limited in time to no more than 18 months;
- The total number of shares covered by the authorization is disclosed;
- The number of shares that would be purchased with call options and/or sold with put options is limited to a maximum of 5 percent of currently outstanding capital (or half of the total amounts allowed by law in Italy and Germany);
- A financial institution, with experience conducting sophisticated transactions, is indicated as the party responsible for the trading; and
- The company has a clean track record regarding repurchases.

For **Singapore**, generally vote for resolutions authorizing the company to repurchase its own shares, unless the premium over the average trading price of the shares as implied by the maximum price paid exceeds 5 percent for on-market and/or off-market repurchases.

**Reissuance of Shares Repurchased**

**Social Advisory Services Recommendation:** Vote for requests to reissue any repurchased shares unless there is clear evidence of abuse of this authority in the past.

**Capitalization of Reserves for Bonus Issues/Increase in Par Value**

**Social Advisory Services Recommendation:** Vote for requests to capitalize reserves for bonus issues of shares or to increase par value.
Private Placement

Social Advisory Services Recommendation: For Canadian companies, vote case-by-case on private placement issuances taking into account:

- Whether other resolutions are bundled with the issuance;
- Whether the rationale for the private placement issuance is disclosed;
- Dilution to existing shareholders’ position:
  - issuance that represents no more than 30 percent of the company’s outstanding shares on a non-diluted basis is considered generally acceptable;
- Discount/premium in issuance price to the unaffected share price before the announcement of the private placement;
- Market reaction: The market’s response to the proposed private placement since announcement; and
- Other applicable factors, including conflict of interest, change in control/management, evaluation of other alternatives.

Generally vote for the private placement issuance if it is expected that the company will file for bankruptcy if the transaction is not approved or the company’s auditor/management has indicated that the company has going concern issues.
4. COMPENSATION

Preamble

The assessment of compensation follows the Social Advisory Services Global Principles on Executive and Director Compensation which are detailed below. These principles take into account global corporate governance best practice.

The Global Principles on Compensation underlie market-specific policies in all markets:

› Provide shareholders with clear, comprehensive compensation disclosures;
› Maintain appropriate pay structure with emphasis on long-term shareholder value;
› Avoid arrangements that risk “pay for failure;”
› Maintain an independent and effective compensation committee;
› Avoid inappropriate pay to non-executive directors.

European Guidelines

In line with European Commission Recommendation 2004/913/EC, Social Advisory Services believes that seeking annual shareholder approval for a company's compensation policy is a positive corporate governance provision.

In applying the Five Global Principles, Social Advisory Services has formulated European Compensation Guidelines which take into account local codes of governance, market best practice, and the Recommendations published by the European Commission. Social Advisory Services analyzes compensation-related proposals based on the role of the beneficiaries and has therefore divided its executive and director compensation policy into two domains:

› Executive compensation-related proposals; and
› Non-executive director compensation-related proposals

Executive Compensation-Related Proposals

Social Advisory Services Recommendation: Social Advisory Services will evaluate management proposals seeking ratification of a company's executive compensation-related items on a case-by-case basis, and, where relevant, will take into account the European Pay for Performance (EP4P) model outcomes within a qualitative review of a company's remuneration practices. Social Advisory Services will generally recommend a vote against a company's compensation-related proposal if such proposal fails to comply with one or a combination of several of the global principles and their corresponding rules:

› Provide shareholders with clear and comprehensive compensation disclosures:

3 Definition of Pay-for-Performance Evaluation:

Social Advisory Services annually conducts a pay-for-performance analysis to measure the alignment between pay and performance over a sustained period. With respect to companies in the European Main Indices, this analysis considers the following:

- Peer Group Alignment:
  - The degree of alignment between the company's annualized TSR rank and the CEO's annualized total pay rank within a peer group, each measured over a three-year period.
  - The multiple of the CEO's total pay relative to the peer group median.
- Absolute Alignment – the absolute alignment between the trend in CEO pay and company TSR over the prior five fiscal years – i.e., the difference between the trend in annual pay changes and the trend in annualized TSR during the period.
› Information on compensation-related proposals shall be made available to shareholders in a timely manner;
› The level of disclosure of the proposed compensation policy shall be sufficient for shareholders to make an informed decision and shall be in line with what local market best practice standards dictate;
› Companies shall adequately disclose all elements of the compensation, including:
   › Any short- or long-term compensation component must include a maximum award limit.
   › Long-term incentive plans must provide sufficient disclosure of (i) the exercise price/strike price (options);
     (ii) discount on grant; (iii) grant date/period; (iv) exercise/vesting period; and, if applicable, (v)
     performance criteria.
› Discretionary payments, if applicable.
› Maintain appropriate pay structure with emphasis on long-term shareholder value:
   › The structure of the company’s short-term incentive plan shall be appropriate.
   › The compensation policy must notably avoid guaranteed or discretionary compensation.
   › The structure of the company’s long-term incentives shall be appropriate, including, but not limited to,
     dilution, vesting period, and, if applicable, performance conditions.
   › Equity-based plans or awards that are linked to long-term company performance will be evaluated using
     Social Advisory Services’ general policy for equity-based plans; and
   › For awards granted to executives, Social Advisory Services will generally require a clear link between
     shareholder value and awards, and stringent performance-based elements.
   › The balance between short- and long-term variable compensation shall be appropriate
   › The company’s executive compensation policy must notably avoid disproportionate focus on short-term
     variable element(s)
› Avoid arrangements that risk “pay for failure”:
   › The board shall demonstrate good stewardship of investor’s interests regarding executive compensation
     practices (principle being supported by Pay for Performance Evaluation).
   › There shall be a clear link between the company’s performance and variable awards.
   › There shall not be significant discrepancies between the company’s performance and real executive
     payouts.
   › The level of pay for the CEO and members of executive management should not be excessive relative to
     peers, company performance, and market practices.
   › Significant pay increases shall be explained by a detailed and compelling disclosure.
   › Severance pay agreements must not be in excess of (i) 24 months’ pay or of (ii) any more restrictive provision
     pursuant to local legal requirements and/or market best practices.
   › Arrangements with a company executive regarding pensions and post-mandate exercise of equity-based
     awards must not result in an adverse impact on shareholders’ interests or be misaligned with good market
     practices.
› Maintain an independent and effective compensation committee:
   › No executives may serve on the compensation committee.
   › In certain markets the compensation committee shall be composed of a majority of independent members, as
     per Social Advisory Services policies on director election and board or committee composition.

In addition to the above, Social Advisory Services will generally recommend a vote against a compensation-related proposal if such proposal is in breach of any other supplemental market-specific voting policies.

**Non-Executive Director Compensation**

› Avoid inappropriate pay to non-executive directors.

**Social Advisory Services Recommendation**: Generally vote for proposals to award cash fees to non-executive directors.

Vote against where:
Documents (including general meeting documents, annual report) provided prior to the general meeting do not mention fees paid to non-executive directors.

Proposed amounts are excessive relative to other companies in the country or industry.

The company intends to increase the fees excessively in comparison with market/sector practices, without stating compelling reasons that justify the increase.

Proposals provide for the granting of stock options, performance-based equity compensation (including stock appreciation rights and performance-vesting restricted stock), and performance-based cash to non-executive directors.

Proposals introduce retirement benefits for non-executive directors.

Vote on a case-by-case basis where:

- Proposals include both cash and share-based components to non-executive directors.
- Proposals bundle compensation for both non-executive and executive directors into a single resolution.

**Equity-Based Compensation Guidelines**

**Social Advisory Services Recommendation:** Generally vote for equity based compensation proposals for employees if the plan(s) are in line with long-term shareholder interests and align the award with shareholder value. This assessment includes, but is not limited to, the following factors:

The volume of awards transferred to participants must not be excessive: the potential volume of fully diluted issued share capital from equity-based compensation plans must not exceed the following Social Advisory Services guidelines:

- The shares reserved for all share plans may not exceed 5 percent of a company's issued share capital, except in the case of high-growth companies or particularly well-designed plans, in which case we allow dilution of between 5 and 10 percent: in this case, we will need to have performance conditions attached to the plans which should be acceptable under Social Advisory Services criteria (challenging criteria). In addition, for companies in Hong Kong and Singapore, Social Advisory Services will support a plan’s dilution limit that exceeds these thresholds if the annual grant limit under the plan is 0.5 percent or less for a mature company (1 percent or less for a mature company with clearly disclosed performance criteria) and 1 percent or less for a growth company;
- The plan(s) must be sufficiently long-term in nature/structure: the minimum vesting period must be no less than three years from date of grant;
- The awards must be granted at market price. Discounts, if any, must be mitigated by performance criteria or other features that justify such discount.
- If applicable, performance standards must be fully disclosed, quantified, and long-term, with relative performance measures preferred.

**Market-specific provisions for France:**

- The potential volume from equity-based compensation plans must not exceed 10 percent of fully diluted issued share capital.
- In addition, for companies that refer to the AFEP-MEDEF Code, all awards (including stock options and warrants) to executives shall be conditional upon challenging performance criteria or premium pricing. For companies referring to the Middlenext Code (or not referring to any code) at least part of the awards to executives shall be conditional upon performance criteria or premium pricing. In both cases, free shares shall remain subject to performance criteria for all beneficiaries.
Finally, for large- and mid-cap companies, the company’s average three year unadjusted burn rate (or, if lower, on the maximum volume per year implied by the proposal made at the general meeting) must not exceed the mean plus one standard deviation of its sector but no more than one percentage point from the prior year sector cap.

**Compensation-Related Voting Sanctions**

Should a company be deemed to have egregious remuneration practices (as a result of one or a combination of several factors highlighted above) and has not followed market practice by submitting a resolution on executive compensation, vote against other "appropriate" resolutions as a mark of discontent against such practices.

An adverse vote recommendation could be applied to any of the following on a case-by case basis:

› The (re)election of members of the remuneration committee;
› The discharge of directors; or
› The annual report and accounts.

Failure to propose a resolution on executive compensation to shareholders in a market where this is routine practice may, by itself, lead to one of the above adverse vote recommendations regardless of the companies' remuneration practices.

**Stock Option Plans – Adjustment for Dividend (Nordic Region)**

**Social Advisory Services Recommendation:**

Vote against stock option plans in Denmark, Finland, Norway, and Sweden if evidence is found that they contain provisions that may result in a disconnect between shareholder value and employee/executive reward.

This includes one or a combination of the following:

› Adjusting the strike price for future ordinary dividends AND including expected dividend yield above 0 percent when determining the number of options awarded under the plan;
› Having significantly higher expected dividends than actual historical dividends;
› Favorably adjusting the terms of existing options plans without valid reason; and/or
› Any other provisions or performance measures that result in undue award.

This policy applies to both new plans and amendments to introduce the provisions into already existing stock option plans. Social Advisory Services will make an exception if a company proposes to reduce the strike price by the amount of future special (extraordinary) dividends only.

Generally vote against if the potential increase of share capital amounts to more than 5 percent for mature companies or 10 percent for growth companies or if options may be exercised below the market price of the share at the date of grant, or that employee options do not lapse if employment is terminated.

**Share Matching Plans (Sweden and Norway)**

**Social Advisory Services Recommendation:**

Social Advisory Services considers the following factors when evaluating share matching plans:

› For every share matching plan, Social Advisory Services requires a holding period.
› For plans without performance criteria, the shares must be purchased at market price.
For broad-based share matching plans directed at all employees, Social Advisory Services accepts an arrangement up to a 1:1 ratio, i.e. no more than one free share is awarded for every share purchased at market value.

In addition, for plans directed at executives, we require that sufficiently challenging performance criteria be attached to the plan. Higher discounts demand proportionally higher performance criteria.

The dilution of the plan when combined with the dilution from any other proposed or outstanding employee stock purchase/stock matching plans, must comply with Social Advisory Services’ guidelines.

Canadian Guidelines

Social Advisory Services Recommendation: Evaluate executive pay and practices, as well as certain aspects of outside director compensation on a case-by-case basis.

Vote against management say on pay (MSOP) proposals, withhold from compensation committee members (or in rare cases where the full board is deemed responsible, all directors including the CEO), and/or against an equity-based incentive plan proposal if:

- There is a misalignment between CEO pay and company performance (pay for performance)
- The company maintains problematic pay practices; or
- The board exhibits poor communication and responsiveness to shareholders.

Pay for Performance:

- Rationale for determining compensation (e.g., why certain elements and pay targets are used, how they are used in relation to the company’s business strategy, and specific incentive plan goals, especially retrospective goals) and linkage of compensation to long-term performance;
- Evaluation of peer group benchmarking used to set target pay or award opportunities;
- Analysis of company performance and executive pay trends over time, taking into account our Pay-for-Performance policy;
- Mix of fixed versus variable and performance versus non-performance-based pay.

Pay Practices:

- Assessment of compensation components included in the Problematic Pay Practices policy such as: perks, severance packages, employee loans, supplemental executive pension plans, internal pay disparity and equity plan practices (including option backdating, repricing, option exchanges, or cancellations/surrenders and re-grants, etc.);
- Existence of measures that discourage excessive risk taking which include but are not limited to: clawbacks, holdbacks, stock ownership requirements, deferred compensation practices etc.

Board Communications and Responsiveness:

- Clarity of disclosure (e.g. whether the company’s Form 51-102F6 disclosure provides timely, accurate, clear information about compensation practices in both tabular format and narrative discussion);
- Assessment of board’s responsiveness to investor concerns on compensation issues (e.g., whether the company engaged with shareholders and / or responded to majority-supported shareholder proposals relating to executive pay).
Advisory Vote on Executive Compensation (Say-on-Pay) Management Proposals

Social Advisory Services Recommendation: Vote case-by-case on management proposals for an advisory shareholder vote on executive compensation. Vote against these resolutions in cases where boards have failed to demonstrate good stewardship of investors’ interests regarding executive compensation practices.

In general, the management say on pay (MSOP) ballot item is the primary focus of voting on executive pay practices—dissatisfaction with compensation practices can be expressed by voting against MSOP rather than withholding or voting against the compensation committee. However, if there is no MSOP on the ballot, then the negative vote will apply to members of the compensation committee. In addition, in egregious cases, or if the board fails to respond to concerns raised by a prior MSOP proposal, then vote against or withhold from compensation committee members (or, if the full board is deemed accountable, all directors). If the negative factors involve equity-based compensation, then vote against an equity-based plan proposal presented for shareholder approval.

Equity Compensation Plans

Social Advisory Services Recommendation: Vote case-by-case on equity-based compensation plans using an "equity plan scorecard" (EPSC) approach. Under this approach, certain features and practices related to the plan are assessed in combination, with positively-assessed factors potentially counterbalancing negatively-assessed factors and vice-versa. Factors are grouped into three pillars:

Plan Cost: The total estimated cost of the company’s equity plans relative to industry/market cap peers, measured by the company's estimated Shareholder Value Transfer (SVT) in relation to peers and considering both:

SVT based on new shares requested plus shares remaining for future grants, plus outstanding unvested/unexercised grants; and

SVT based only on new shares requested plus shares remaining for future grants.

Plan Features:

Absence of problematic change-in-control (CIC) provisions, including:

Single-trigger acceleration of award vesting in connection with a CIC; and

Settlement of performance-based equity at target or above in the event of a CIC-related acceleration of vesting regardless of performance.

No financial assistance to plan participants for the exercise or settlement of awards;

Public disclosure of the full text of the plan document; and

Reasonable share dilution from equity plans relative to market best practices.

Grant Practices:

Reasonable three-year average burn rate relative to market best practices;

Meaningful time vesting requirements for the CEO’s most recent equity grants (three-year lookback);

The issuance of performance-based equity to the CEO;

A clawback provision applicable to equity awards; and

Post-exercise or post-settlement share-holding requirements (S&P/TSX Composite Index only).

Generally vote against the plan proposal if the combination of above factors, as determined by an overall score, indicates that the plan is not in shareholders’ interests. In addition, vote against the plan if any of the following unacceptable factors have been identified:

Discretionary or insufficiently limited non-employee director participation;

An amendment provision which fails to adequately restrict the company’s ability to amend the plan without shareholder approval;

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4 In cases where certain historic grant data are unavailable (e.g. following an IPO or emergence from bankruptcy), Special Cases models will be applied which omit factors requiring these data.
A history of repricing stock options without shareholder approval (three-year look-back);
The plan is a vehicle for problematic pay practices or a significant pay-for-performance disconnect under certain circumstances; or
Any other plan features that are determined to have a significant negative impact on shareholder interests.

**Director Compensation - TSX**

**Social Advisory Services Recommendation:** On a case-by-case basis, generally withhold from members of the committee responsible for director compensation (or, where no such committee has been identified, the board chair or full board) where director compensation practices which pose a risk of compromising a non-employee director’s independence or which otherwise appear problematic from the perspective of shareholders have been identified, including:

- Excessive (relative to standard market practice) inducement grants issued upon the appointment or election of a new director to the board (consideration will be given to the form in which the compensation has been issued and the board’s rationale for the inducement grant);
- Performance-based equity grants to non-employee directors which could pose a risk of aligning directors’ interests away from those of shareholders and toward those of management; and
- Other significant problematic practices relating to director compensation.

**Other Compensation Plans**

**Employee Stock Purchase Plans (ESPPs, ESOPs)**

**Social Advisory Services Recommendation:** Generally vote for broadly based (preferably all employees of the company with the exclusion of individuals with 5 percent or more beneficial ownership of the company) employee stock purchase plans where the following apply:

- Reasonable limit on employee contribution (may be expressed as a fixed dollar amount or as a percentage of base salary excluding bonus, commissions and special compensation);
- Employer contribution of up to 25 percent of employee contribution and no purchase price discount or employer contribution of more than 25 percent of employee contribution and SVT cost of the company’s equity plans is within the allowable cap for the company;
- Purchase price is at least 80 percent of fair market value with no employer contribution;
- Potential dilution together with all other equity-based plans is 10 percent of outstanding common shares or less; and
- The Plan Amendment Provision requires shareholder approval for amendments to:
  - The number of shares reserved for the plan;
  - The allowable purchase price discount;
  - The employer matching contribution amount.

Treasury funded ESPPs, as well as market purchase funded ESPPs requesting shareholder approval, will be considered to be incentive based compensation if the employer match is greater than 25 percent of the employee contribution. In this case, the plan will be run through the Social Advisory Services compensation model to assess the Shareholder Value Transfer (SVT) cost of the plan together with the company’s other equity-based compensation plans.

Eligibility and administration are also key factors in determining the acceptability of an ESPP/ESOP plan.

Social Advisory Services will also take into account other compensation and benefit programs, in particular pensions.
Deferred Share Unit Plans

**Social Advisory Services Recommendation:** Generally vote for Deferred Compensation Plans if:

- Potential dilution together with all other equity-based compensation is ten percent of the outstanding common shares or less.

Other elements of director compensation to evaluate in conjunction with deferred share units include:

- Director stock ownership guidelines of a minimum of three times annual cash retainer;
- Vesting schedule or mandatory deferral period which requires that shares in payment of deferred units may not be paid out until the end of three years;
- The mix of remuneration between cash and equity;
- Other forms of equity-based compensation, i.e. stock options, restricted stock.

International Guidelines

**Social Advisory Services Recommendation:** Evaluate executive and director compensation proposals on a case-by-case basis taking into consideration the Global Principles as applicable.
5. OTHER ITEMS

Reorganizations/Restructurings

**Social Advisory Services Recommendation**: Vote reorganizations and restructurings on a case-by-case basis.

Mergers and Acquisitions

**Social Advisory Services Recommendation**: Vote case-by-case on mergers and acquisitions taking into account the following:

For every M&A analysis, Social Advisory Services reviews publicly available information as of the date of the report and evaluates the merits and drawbacks of the proposed transaction, balancing various and sometimes countervailing factors including:

- **Valuation** - Is the value to be received by the target shareholders (or paid by the acquirer) reasonable? While the fairness opinion may provide an initial starting point for assessing valuation reasonableness, Social Advisory Services places emphasis on the offer premium, market reaction, and strategic rationale;
- **Market reaction** - How has the market responded to the proposed deal? A negative market reaction will cause Social Advisory Services to scrutinize a deal more closely;
- **Strategic rationale** - Does the deal make sense strategically? From where is the value derived? Cost and revenue synergies should not be overly aggressive or optimistic, but reasonably achievable. Management should also have a favorable track record of successful integration of historical acquisitions;
- **Conflicts of interest** - Are insiders benefiting from the transaction disproportionately and inappropriately as compared to non-insider shareholders? Social Advisory Services will consider whether any special interests may have influenced these directors and officers to support or recommend the merger;
- **Governance** - Will the combined company have a better or worse governance profile than the current governance profiles of the respective parties to the transaction? If the governance profile is to change for the worse, the burden is on the company to prove that other issues (such as valuation) outweigh any deterioration in governance.
- **Stakeholder impact** - Impact on community stakeholders including impact on workforce, environment, etc.

Vote against if the companies do not provide sufficient information upon request to make an informed voting decision.

Mandatory Takeover Bid Waivers

**Social Advisory Services Recommendation**: Vote proposals to waive mandatory takeover bid requirements on a case-by-case basis.

Reincorporation Proposals

**Social Advisory Services Recommendation**: Vote reincorporation proposals on a case-by-case basis.

Expansion of Business Activities

**Social Advisory Services Recommendation**: Vote for resolutions to expand business activities unless the new business takes the company into risky areas.
Related-Party Transactions

**Social Advisory Services Recommendation:** Vote related-party transactions on a case-by-case basis considering factors including, but not limited to, the following:

- The parties on either side of the transaction;
- The nature of the asset to be transferred/service to be provided;
- The pricing of the transaction (and any associated professional valuation);
- The views of independent directors (where provided);
- The views of an independent financial adviser (where appointed);
- Whether any entities party to the transaction (including advisers) is conflicted; and
- The stated rationale for the transaction, including discussions of timing.

If there is a transaction that is deemed problematic and that was not put to a shareholder vote, Social Advisory Services may recommend against the election of the director(s) involved in the related-party transaction or against the full board.

Antitakeover Mechanisms

**Social Advisory Services Recommendation:** Vote against all antitakeover proposals unless they are structured in such a way that they give shareholders the ultimate decision on any proposal or offer.

As of Feb. 1, 2016, for French companies listed on a regulated market, generally vote against any general authorities impacting the share capital (i.e. authorities for share repurchase plans and any general share issuances with or without preemptive rights, including by capitalization of reserves) if they can be used for antitakeover purposes without shareholders’ prior explicit approval.

Social and Environmental Proposals

**Social Advisory Services Recommendation:** Generally vote in favor of social and environmental proposals that seek to promote good corporate citizenship while enhancing long-term shareholder and stakeholder value. In determining votes on shareholder social and environmental proposals, the following factors are considered:

- Whether the proposal itself is well framed and reasonable;
- Whether adoption of the proposal would have either a positive or negative impact on the company’s short-term or long-term share value;
- Whether the company’s analysis and voting recommendation to shareholders is persuasive;
- The degree to which the company’s stated position on the issues could affect its reputation or sales, or leave it vulnerable to boycott or selective purchasing;
- Whether the subject of the proposal is best left to the discretion of the board;
- Whether the issues presented in the proposal are best dealt with through legislation, government regulation, or company-specific action;
- The company’s approach compared with its peers or any industry standard practices for addressing the issue(s) raised by the proposal;
- Whether the company has already responded in an appropriate or sufficient manner to the issue(s) raised in the proposal;
- Whether there are significant controversies, fines, penalties, or litigation associated with the company’s environmental or social practices;
- If the proposal requests increased disclosure or greater transparency, whether or not sufficient information is publicly available to shareholders and whether it would be unduly burdensome for the company to compile and avail the requested information to shareholders in a more comprehensive or amalgamated fashion; and
- Whether implementation of the proposal would achieve the objectives sought in the proposal.
Generally vote for social and environmental shareholder proposals that seek greater disclosure on topics such as human/labor rights, workplace safety, environmental practices and climate change risk, sustainable business practices etc.

Vote all other social and environmental proposals on a case-by-case basis, taking into account the considerations outlined above.
6. FOREIGN PRIVATE ISSUERS

Foreign private issuers ("FPIs") are defined as companies whose business is administered principally outside the U.S., with more than 50 percent of assets located outside the U.S.; a majority of whose directors/officers are not U.S. citizens or residents; and a majority of whose outstanding voting shares are held by non-residents of the U.S. Companies that are incorporated outside of the U.S. and listed solely on U.S. exchanges, where they qualify as FPIs, will be subject to the following policy:

Vote against or withhold from non-independent director nominees at companies which fail to meet the following criteria: a majority-independent board, and the presence of an audit, compensation, and a nomination committee, each of which is entirely composed of independent directors. Where the design and disclosure levels of equity compensation plans are comparable to those seen at U.S. companies, U.S. compensation policy will be used to evaluate the compensation plan proposals. All other voting items will be evaluated using the relevant regional or market proxy voting guidelines.

While a firm’s country of incorporation will remain the primary basis for evaluating companies, Social Advisory Services will generally apply its U.S. policies to the extent possible with respect to issuers that file DEF 14As, 10-K annual reports, and 10-Q quarterly reports, and are thus considered domestic issuers by the U.S. Securities and Exchange Commission (SEC). U.S. policies will also apply to companies listed on U.S. exchanges as Foreign Private Issuers (FPIs) and that may be exempt from the disclosure and corporate governance requirements that apply to most companies traded on U.S. exchanges, including a number of SEC rules and stock market listing requirements. Corporations that have reincorporated outside the U.S. have found themselves subject to a combination of governance regulations and best practice standards that may not be entirely compatible with an evaluation framework based solely on the country of incorporation.