

Investment Management Association



**Adherence to the
FRC's Stewardship Code
At 30 September 2012**

June 2013



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June 2013

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Key findings

This third report on adherence to the FRC's Stewardship Code looks at the activities that support institutional investors' commitment in practice. It summarises the responses to a questionnaire sent to 241 signatories as at 30 September 2012, an increase from 172 as at 30 September 2011 and 75 as at 30 September 2010.

The total number of respondents increased to 103 in 2012 from 83 in 2011 and 50 in 2010. Asset Managers still make up the majority of respondents and managed £702 billion of UK equities (2011: £668 billion; and 2010: £590 billion) representing 36 per cent of the UK market. The Owner respondents owned £31 billion (2011: £31 billion; and 2010: £15 billion).

Against this, the overall response rate fell to 43 per cent in 2012 from 48 per cent in 2011 and from 67 per cent in 2010. This reflects the steady decrease in the average size of respondent in terms of assets managed/owned over the three years and those that only participated more recently tend to have less resource for such exercises. Moreover, the 2010 respondents participated before the FSA required UK asset managers to disclose their commitment to the Code or their alternative strategy. They are likely to have a higher response rate in that they would tend to be more dedicated to stewardship and want to demonstrate that dedication.

As Service Providers have a distinct role and do not hold equities for investment purposes, they are presented separately in this report. Thus, unless otherwise stated, references to "respondents" refer to Asset Manager and Asset Owner respondents only.

Policies (section 3)

All 2012 respondents have a public policy statement on how they discharge their stewardship responsibilities under the Code (Code statement), consistent with 2011. Also consistent with prior years, the majority include their conflicts of interest policy within their Code statement. Where respondents do not, their Code statement clarifies that the policy is available on request.

The FRC encourages signatories to review their Code statements annually. 77 per cent of respondents did so with 29 per cent updating them, for example, to

reflect the revised Corporate Governance and Stewardship Codes or the appointment of third parties to undertake stewardship. Many of the remaining 23 per cent are in the process of reviewing their Code statements or plan to in the near future.

The proportion of respondents that refer to their stewardship responsibilities in mandates continues to increase but the rate of progress has slowed. Thus whereas in 2010 only 13 per cent of all respondents' mandates referred to stewardship responsibilities, in 2011 and 2012 this increased to 33 and 35 per cent, respectively. Certain respondents highlighted that as stewardship is integral to the investment process, it is exercised for all mandates.

Structure and resources (section 4)

Stewardship can be conducted in-house or outsourced. Where it is outsourced respondents regularly monitor their external asset manager or overlay service provider.

The majority of 2012 respondents conduct stewardship in-house, consistent with 2011. For just over 70 per cent of these, dedicated specialists have a role which may be in addition to that of the portfolio managers/analysts. Whilst this is consistent with 2011, in 2010 it was nearly 80 per cent reflecting the more dedicated 2010 respondents which are likely to have more established processes and a specialist resource to work alongside the portfolio managers.

Commentators have questioned whether the involvement of specialists means that stewardship is not integrated into the investment process. It is clear that this is not the case and that where specialists are involved they are integrated into the investment process in some way. For example, for around 80 per cent of respondents in all three years, portfolio managers set or approve the stewardship policy. Moreover, for around 60 per cent of respondents in both 2012 and 2011, portfolio managers make the final decision on controversial votes - a decrease from 71 per cent in 2010. In addition, for nearly half of respondents both portfolio managers and stewardship specialists attend external meetings with companies; a decrease from 56 per cent in 2011.

Overall, headcount increased over the three years reflecting the increase in the number of respondents. However, the average headcount per respondent fell to 17 in 2012 from 21 in 2011 and 20 in 2010; reflecting the fact that those that only responded more recently tend to have less resource.

Dedicated specialists have a range of qualifications, for example, an MBA or the CFA Charter, together with experience as portfolio managers. A few provide in-house training on stewardship and a number seek to ensure that others in their organisation are made aware of stewardship.

Service providers supplement these resources and are used widely to facilitate the voting process and provide research. Eighty-six per cent of respondents use a provider to process instructions (2011: 77 per cent; and 2010: 81 per cent). Where a provider supplies research it nearly always also provides vote recommendations but no respondent follows a provider's recommendation without due consideration. Generally such recommendations highlight issues. In this context, respondents only gave details in relation to their UK holdings which may not reflect the position for overseas holdings.

Monitoring and engagement, together with practical examples (section 5)

The proportion of respondents that monitor all investee companies as part of the investment process increased to 76 per cent in 2012 from 70 per cent in 2011 and 67 per cent in 2010.

Respondents not only engage when they have an equity holding in that 36 per cent also engage when they have a fixed income holding and 24 per cent a private equity holding. Although this will be influenced by the terms of the mandate and the investment allocation. Nor is engagement limited to the UK in that over 80 per cent of respondents engage in the rest of Western Europe.

Engagement tends to be prioritised when there are issues and investor concern over the perceived disconnect between directors' pay and company performance saw what became known as the

shareholder spring" in 2012. Indeed most engagement in both 2012 and 2011 was in relation to board remuneration, followed by company strategy and objectives. In this context, remuneration is subject to an annual vote and it may be that companies initiate the engagement, as opposed to the respondents, in the interests of ensuring the board remuneration report is approved. The least engagement was in relation to pre-emption rights reflecting the fact that there were very few rights issues in 2012.

To see what happens in practice, respondents were asked for details of how they engaged in relation to five companies in the period to 30 September 2012:

- Barclays plc
- WPP plc
- G4S plc
- Xstrata plc
- SABMiller plc

Overall, 61 per cent of respondents with a holding engaged with these companies. There were different issues in relation to each company as reflected in the amount of engagement and the individuals involved.

Most engagement was with Barclays where the main focus was remuneration which had been an issue for some time. Matters unfolded rapidly during 2012 culminating in regulatory fines in relation to the bank's LIBOR submissions and the resignations of the Chairman, Chief Executive, Remuneration Committee Chair and the Chief Operating Officer. There was a lot of engagement with the Executive Directors and Management, an indication that the issues were more fundamental than those around governance and remuneration.

There were similar amounts of engagement with G4S on the proposed acquisition of ISS and with Xstrata on the proposed merger with Glencore. In both instances, this engagement tended to be by the portfolio managers or analysts with the Executive Directors reflecting the focus on a transaction where value was at stake.

The least engagement was in relation to WPP and SABMiller where the focus was on remuneration and the proposed combination of the roles of Chief Executive and Chairman, respectively.

There were varying levels of collective engagement but there were more joint meetings between respondents and representatives from Barclays and Xstrata than with the other companies. In general, all respondents considered collective engagement worthwhile as it gave a consistent message to the company concerned. In addition, in those instances where conflicts of interest arose, respondents gave details on how they were addressed.

At the relevant AGMs, respondents registered higher votes against particular resolutions than the meeting overall. (The slight exception being the re-appointment of Martin Sorrell as Chief Executive of WPP.) All registered significant votes against the respective Remuneration Report and the re-appointment of the Remuneration Committee Chair. This is indicative of the fact that a vote against the Remuneration Report sends a signal to a company without necessarily destabilising its board by voting against the individual directors.

In three of the five examples, respondents considered their engagement to be successful in that they achieved their objectives. This was particularly the case at G4S where the acquisition was cancelled and Xstrata where the terms of the merger were improved. However, at Barclays and WPP only half of the respondents were satisfied with the company's response in that they considered there was still room for improvement.

For many respondents engagement is part of the on-going investment process and they continue to engage with these companies. This engagement may not necessarily be limited to the issues raised in this report which relate to a specific period.

Voting (section 6)

Voting levels increased again in nearly all markets in 2012 potentially meaning that overseas markets are more accessible with fewer barriers to voting. A greater proportion of respondents vote all their UK shares – 88 per cent in 2012 as compared to 86 per cent in 2011 and 81 per cent in 2010.

The proportion of respondents that inform management in advance when voting against or abstaining on a resolution decreased slightly to 35 per cent in 2012 from 39 per cent in 2011. Nearly all of these respondents committed to the Code in 2010. Thirty-two per cent rarely or never notify management in advance.

Sixty-five per cent of the 2012 respondents make their voting records public. This has decreased from 73 per cent, mainly due to four 2011 respondents that disclose not responding in 2012. It tends to be the larger respondents that disclose – the 2012 respondents that disclose held 90 per cent of the assets managed/owned by all respondents. The majority update the information quarterly and disclose all vote decisions without rationale. A further 15 per cent explain in their Code statement why they do not make voting records public, the main reason being that they only disclose to clients.

Reporting (section 7)

Nearly all the 2012 respondents report to clients on stewardship and/or voting, with the proportion reporting both stewardship and voting increasing slightly since 2011. 53 per cent report at a minimum quarterly (2011: 66 per cent; and 2010: 56 per cent).

Encouragingly, the proportion of respondents that have obtained an independent opinion on their voting and stewardship processes increased to 14 per cent in 2012 from 10 per cent in 2011 and eight per cent in 2010. A number that committed to obtaining such an opinion in 2011 have now done so. Of those that have not, just over a quarter have had their voting and/or stewardship processes reviewed by internal audit.

1. Introduction

The Financial Reporting Council (FRC) first issued the Stewardship Code (the Code) in July 2010 and a revised version in September 2012¹. The Code operates on a 'comply or explain' basis and aims to enhance the quality of engagement between institutional investors and companies to help improve long-term returns to shareholders and the efficient exercise of governance responsibilities. It sets out good practice on engagement with investee companies, which includes monitoring companies, entering into a dialogue with boards and voting at general meetings.

The Code is directed in the first instance to institutional investors, asset owners and asset managers, with equity holdings in UK listed companies. In particular, the 2012 version of the Code further clarified asset owners' role in stewardship.

The Investment Management Association (IMA) has worked with the FRC in developing an exercise to monitor adherence to the Code. There have been three such exercises, covering the periods to 30 September 2010, 2011 and 2012, respectively.

A Steering Group, chaired by the FRC's Chief Executive, provides direction and independent oversight. The members of the Steering Group are set out in Appendix 1.

Institutional investors that had signed up to the Code were invited to complete a questionnaire. The questionnaire was agreed with the Steering Group and sent to the 241 institutional investors that had signed up as at 30 September 2012. In summary, the questionnaire requested details of:

- the public policy statement.
- the level of resources employed and the use, if any, of proxy voting agencies.
- the integration of stewardship into the investment process.
- how monitoring is prioritised, markets and issues engaged with, together with practical examples.
- voting and whether voting records are publicly disclosed.
- the frequency of reports to clients, the information reported, and whether an independent opinion on voting and stewardship processes is obtained.

This report is a summary of the results. The collation of the individual submissions that support the report has been reviewed by Ernst & Young. The IMA would like to thank all respondents for their contributions and the members of the Steering Group who gave their time.

¹ FRC Stewardship Code.

2. Profile of respondents

Types of respondent

241 institutional investors that had signed up to the Code as at 30 September 2012 - 177 Asset Managers, 52 Asset Owners and 12 Service Providers - were sent a questionnaire, which aimed to determine the activities that supported the signatories' commitment in practice. Of these, 69 were new signatories since 2011.

As shown in Table 1, the response rate in 2012 was 43 per cent, which is lower than 2011: 48 per cent; and 2010: 67 per cent. The higher response rate in 2010, particularly from Asset Managers, reflects a commitment to the Code prior to it becoming a regulatory requirement². Thus a higher initial response rate would be expected as these respondents would tend to be more dedicated to stewardship and want to demonstrate that dedication.

As at 30 September 2012, Asset Manager respondents held £702 billion in UK equities, representing 36 per cent of the UK equity market⁴, and Asset Owner respondents owned £31 billion⁵ (Table 2). Each of the Asset Manager respondents had an average of £9.6 billion of assets under management compared to an average of £11.5 billion per Manager in 2011 and £14.4 billion in 2010. Similarly each of the Asset Owner respondents owned an average of £1.3 billion, compared to an average of £1.5 billion per Owner in 2011 and £2.1 billion in 2010. Thus the average size of respondent in terms of assets managed/owned has decreased steadily since 2010. This may also account for the falling response rate and may impact other results in this report.

It should be noted that as the Asset Managers may be managing the Asset Owners' holdings, the details reported by the Owners and Managers may relate to the same holdings and be double-counted. Service Providers do not hold equities for investment purposes.

Table 1: Types of respondent and response rate

	No. of questionnaires sent			Percentage response rate		
	2012 ³	2011	2010	2012	2011	2010
Asset Managers	177	128	58	41	45	71
Asset Owners	52	34	12	44	59	58
Service Providers	12	10	5	58	50	40
Total/overall rate	241	172	75	43	48	67

Table 2: Types of respondent and assets managed/owned

	No. of respondents			Assets managed/owned (£billion)		
	2012 ⁶	2011	2010	2012	2011	2010
Asset Manager	73	58	41	702	668	590
Asset Owner	23	20	7	31	31	15
Service Provider	7	5	2	N/A	N/A	N/A
Total	103	83	50	733	699	605

² The Financial Services Authority Conduct of Business Rule 2.2.3 came into effect on 6 December 2010 and required UK asset managers to disclose their commitment to the Code or their alternative strategy.

³ Two respondents previously categorised themselves as Asset Owners but as Asset Managers for 2012.

⁴ Excludes eight Asset Managers that were unable to provide this figure.

⁵ Excludes one Asset Owner that was unable to provide this figure.

⁶ Two respondents previously categorised themselves as Asset Owners but as Asset Managers for 2012.

Stewardship can be impacted according to the type of respondent and its structure. For example, whether an Asset Manager manages its owner's assets or is independent and only manages those of a third party, whether an Asset Owner is a pension fund, charity or other, and the type of service a Service Provider offers. Thus Asset Managers were asked for information on their parent, Asset Owners were asked about the type of assets and Service Providers were asked about the type of service provided.

While these distinctions should be borne in mind when reading this report, they are not necessarily clear-cut. For example, one respondent classified as an Asset Owner manages its own and third party assets, and provides corporate governance services to others (a so-called overlay service).

Asset Managers

Consistent with 2011, nearly half of the Asset Managers are independent⁷, while 18 per cent are owned by insurers and 12 per cent are subsidiaries of an Asset Owner that may invest on behalf of their owner's pension fund (see Table 3).

Table 3: Asset Managers – parent

	No. of respondents		Percentage of respondents	
	2012	2011	2012	2011
Retail bank	3	3	4	5
Investment bank ⁸	7	3	10	5
Insurer ⁹	13	14	18	24
Independent ¹⁰	35	27	48	47
Asset owner ¹¹	9	5	12	9
Other	6	6	8	10
Sample size	73	58	73	58

⁷ Three are part of groups that are independent.

⁸ One is owned by an investment services company, another is part owned by an investment and retail bank.

⁹ For one owned by an insurer, the assets under management are unrelated to the insurance business, for another, the parent company provides long terms savings and investment.

¹⁰ Two are listed, one is owned by an investment trust and another by the founding partners.

¹¹ Two are Occupational Pension Schemes, one is owned by its not for profit clients and the other is a Foundation for sustainable development owned by Swiss pension funds.

¹² One is also a "service provider/consultant".

Asset Owners

Similar to 2011, over 80 per cent of the Asset Owners are pension schemes, with nearly half represented by Occupational Pension Schemes. Of the two "other"; one is a pension provider and the second is a "self-managed investment trust" (see Table 4).

Table 4: Asset Owners – type

	No. of respondents		Percentage of respondents	
	2012	2011	2012	2011
Occupational pension scheme ¹²	11	8	48	40
Public pension scheme	8	7	34	35
Private pension scheme	–	2	–	10
Charity/foundation	2	1	9	5
Other	2	2	9	10
Sample size	23	20	23	20

Service Providers

As shown in Table 5, the majority of Service Providers offer proxy voting services. These may vary, ranging from providing research through to issuing voting recommendations and vote execution services. One Service Provider advises asset owners on the management and stewardship of their assets. As stated in its policy: *“We encourage our clients to support the Code, and to carefully consider the implications and challenges it presents both for them and also for their delegated agents, the investment managers”*.

Table 5: Service Providers - service

	No. of respondents		Percentage of respondents	
	2012	2011	2012	2011
Proxy voting services ¹³	6	3	86	60
Consultant	1	2	14	40
Sample size	7	5	7	5

As the Service Providers do not manage or own equities, a number of questions did not apply to them, or they were approached from a different viewpoint. Thus the Service Providers' responses are presented separately in this report.

¹³ One is a “provider of research into corporate environmental, social and governance performance”.

3. Policies

Public policy statement

One of the requirements of committing to the Code is to have a public statement on how stewardship responsibilities are to be discharged. **Principle 1** states that: “institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities”. The Guidance sets out the matters that should be included.

As stated in the preface to the Code: “disclosures made by institutions under the Code should assist companies to understand the approach and expectations of their major shareholders. They should also assist those issuing mandates to institutional fund managers to make a better informed choice, thereby improving the functioning of the market and facilitating the exercise of responsibility to end-investors.

“As with the UK Corporate Governance Code, the Code should be applied on a “comply or explain” basis. In reporting terms this entails providing a statement on the institution’s website that contains:

- a description of how the principles of the Code have been applied, and
- disclosure of the specific information listed under Principles 1, 5, 6 and 7; or
- an explanation if these elements of the Code have not been complied with”.

Only those that committed to the Code were invited to complete the questionnaire, thus all respondents have a public policy statement on how they discharge their stewardship responsibilities (Code statement). However, two Asset Owners (one in 2011) did not maintain their own website and their Code statement is on the FRC’s website.

Each of the Service Providers has its Code statement on its website except for one where it is on the FRC’s website.

Conflicts of interest

An institutional investor’s duty is to act in the interests of its clients and/or beneficiaries when considering matters such as engagement and voting. However, conflicts of interest arise from time to time and **Principle 2** requires that: “institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship which is publicly disclosed”.

The FRC’s 2012 Report on Developments in Corporate Governance noted: “the updated Code also encourages more disclosure on how conflicts of interest are managed. In November the FSA published a review on this subject which concluded that “many [asset management] firms had failed to establish an adequate framework for identifying and managing conflicts of interest”. In the light of this finding the FRC believes it would be in asset managers’ own interest to be more transparent about how they deal with these matters¹⁴”.

Consistent with previous years, the majority of respondents include their conflicts of interest policy in their Code statement, although for some this is a summary and the full document is available to clients or on request (see Table 6). A higher proportion of respondents have a standalone public policy on conflicts (12 per cent compared to 6 per cent in 2011). Those that do not make their policy public state in their Code statement that their conflicts of interest policy is available on request.

Table 6: Public conflicts of interest policy

	Percentage of respondents	
	2012	2011
Standalone	12	6
Within or referenced in Code statement	82 ¹⁵	90
Not public	6	4
Sample size	96	78

¹⁴ FRC, Developments in Corporate Governance 2012, Page 23.

¹⁵ 12 respondents that stated either “standalone” or “not public” are included in this category in that a summary of the policy is in their Code statement with the full document available to clients. In addition, two stated in their Code statement that conflicts should not arise.

Among the Service Providers, one respondent's conflicts of interest policy is in its Code statement while for four it is a standalone policy. One respondent commented: *"It is currently being written. In addition, we flag up any potential conflict of interest on the front page of our research reports when applicable"*.

Reviewing policy statements

The FRC's 2012 Report on Developments in Corporate Governance noted: *"it is important that signatories keep their statements up to date. The 2012 edition of the Code recommends that signatories review, and if necessary update, their statements at least annually"¹⁶*.

Respondents were asked for the first time if they reviewed their Code statements during the year. As shown in Table 7, 77 per cent of respondents did so. The changes made by 29 per cent as a result included:

- reflecting the appointment of third parties to conduct stewardship on their behalf (three).
- reflecting the revised Corporate Governance and Stewardship Codes (seven). As one clarified: *"The statement was extensively redrafted to bring it into line with the revised Stewardship Code. In particular the statement has been extended to include our fixed income activities and we have expanded our description of our Conflict of Interest policies and our approach to collective engagement. We have also referred to our stock lending activities for the first time". Another stated: "The change was minor in the year to 30 September 2012: we updated the reference to the external verification of our stewardship activities stating that in light of new guidance from the ICAEW, we are reviewing our position with regards to this aspect of the Code"*.
- updating specific voting guidelines (four), for example one: *"amended Policy on annual re-election of directors and voting disclosure"*.
- reflecting changes to their internal policies (nine) for example: *"strengthened statement on conflicts of*

interest, the role of proxy-voting agencies in our processes, securities lending processes and clarified that we contact all companies ahead of voting against or abstaining on an issue".

In contrast, 23 per cent of respondents did not complete a review of their Code statements, most of which were either in the process of reviewing them or are due to review them in the near future. A minority of respondents were waiting for the FRC to publish the revised Code in September 2012. Other instances include:

- one respondent waiting for changes to its company structure.
- another respondent intending to review its statement as part of a wider update: *"We are currently in the process of developing a more detailed corporate governance policy which we expect to issue in 2013; hence a review of our previous statements was not considered necessary"*.
- one respondent that did not consider there was any catalyst for review.

Table 7: Statement reviewed

	Percentage of respondents
	2012
Reviewed	
Changes made	29
No changes made	48
	77
Not reviewed	23
Sample size	96

Two of the Service Providers reviewed their statements during the year, albeit they did not make any changes. A further four did not review their statements; three waiting for the revised Code or updates from the European Commission whilst one felt it had already met the requirements of the new Code¹⁷.

¹⁶ Page 23.

¹⁷ The other Service Provider did not confirm.

Client mandates

The preface to the Code states: *“institutional shareholders are free to choose whether or not to engage but their choice should be a considered one based on their investment approach. Their managers or agents are then responsible for ensuring that they comply with the terms of the mandate as agreed”*.

The FRC 2012 report of developments in Corporate Governance noted that: *“The FRC considers that if asset owners want managers to pursue a stewardship approach on their behalf – and 70 per cent of the respondents to the NAPF survey considered that the most effective form of engagement was through their investment manager – then the best way of achieving this is to make the manager accountable by making explicit reference to stewardship in the mandate¹⁸”*.

As shown in Table 8, for 68 per cent of respondents “all” or “some” mandates refer to stewardship responsibilities. The most significant change is that whereas in 2010 only 13 per cent of “all” respondents’ mandates referred to stewardship responsibilities, in 2011 and 2012 this increased to 33 and 35 per cent, respectively.

Table 8: Mandates that refer to stewardship responsibilities

	Percentage of respondents		
	2012	2011	2010
All clients/managers	35	33	13
Some clients/managers			
Three quarters	10	5	
Half	6	8	
A quarter	17	19	
	33	32	54
None	26 ¹⁹	26	25
No response	1	9	8
Not applicable	5 ²⁰	–	–
Sample size	96	78	48

On the question of whether Asset Managers’ clients requested changes with regard to stewardship, comments included:

- while one Asset Manager does not manage specific “Socially Responsible Investment” (SRI) funds, stewardship is integral to its investment process and there has been an increase in the number of queries about stewardship over the last 12 to 18 months. This was echoed by another Asset Manager: *“Yes, the focus on stewardship and ESG integration appears to be increasing from clients globally. Majority of new mandates have requirements but there is still a large proportion of existing clients and funds which have not made changes to the old set ups and IMA’s”*.
- one Asset Manager saw more using its engagement service and another now provides an overlay service to a large new pension provider conscious of its duties regarding responsible investment.
- two Asset Managers noted that many clients formally stipulate stewardship in their mandates, but as stewardship is an integral part of their investment process it is exercised for all clients.

Certain Asset Owners changed their mandates: four to include an overlay service to provide voting and engagement services. One Asset Owner considered that its commitment to stewardship is understood rather than specified in its mandates.

¹⁸ Page 23.

¹⁹ This includes one Asset Manager that does not award external mandates.

²⁰ This question was not asked of five Asset Owners that conduct stewardship in-house as they do not have external mandates.

4. Structure and resources

Structure

In fulfilling obligations under the Code, stewardship can either be conducted in-house or outsourced, in full or in part, to a third party. This is not relevant for the Service Providers which are excluded from this section.

In 2012 a slightly higher proportion of respondents conduct stewardship in-house as compared to 2011 (see Table 9).

Table 9: How stewardship is conducted

	Percentage of respondents	
	2012	2011
Outsourced		
External investment manager	8 ²¹	12
Overlay service provider	9	6
	17	18
In-house	83	82
Sample size	96	78

Outsourced

Where stewardship is outsourced, respondents monitor providers. There are a range of approaches where the provider is an external investment manager:

- in the case of five respondents, the external investment managers report quarterly. Two clarified: *"The Fund monitors its voting and engagement agents throughout the year, requiring quarterly reporting of votes and engagement activities, and including their level of compliance with the UK Stewardship Code, and works with them to improve the quality and quantity of their stewardship activities"*. The other: *"Weactively manage our service providers and monitor their performance on our behalf on a quarterly basis.All our managers must show they have the potential to perform well, not just financially but also in implementing our Responsible Investment and Environmental Overlay Strategies. Quarterly reports will typically contain details of engagements, including outcomes, as well as global voting activity"*.

- for one respondent, stewardship is discussed in regular meetings.
- for another, monitoring is part of their due diligence: *"When investing with underlying managers we review and seek to confirm that they actively monitor their investee companies appropriately and consistent with their own investment strategies and objectives. As part of [Manager's] due diligence process, we review the strategies and methods applied by underlying managers in pursuing their investment strategies and objectives, including any strategy for escalating their investment activities to protect, preserve and enhance shareholder value"*.

Where stewardship is outsourced to a provider of an overlay service:

- five respondents receive quarterly reports, three of which have quarterly meetings with their provider. One noted: *"engagements are also discussed more frequently when the urgency of the situation dictates the need"*.
- one respondent receives a weekly statement on forthcoming general meetings.
- two respondents outsource voting to a provider that either follows the respondent's clients' voting guidelines or the respondent's policy.

There are 16 respondents that outsource out of the total of 96. These are excluded from the remainder of this report.

In-house

The majority, 83 per cent, of respondents undertake all or some stewardship in-house. For those that only do some in-house:

- seven Asset Owners appoint external managers to manage and exercise stewardship in respect of some of their assets but the Owner exercises stewardship for assets managed in-house.
- two Asset Managers run 'funds of funds' and expect the relevant managers to exercise stewardship.

²¹ Includes one respondent that did not answer and its response for 2011 is reflected in the table.

- four respondents outsource elements of stewardship to a service provider or other third party: “[The Manager] exercises votes and where necessary intervenes in an objective and informed way”.
- one Asset Manager works with its parent company.

Where stewardship is in-house, for just over 70 per cent of respondents, dedicated specialists and others have a role which may be in addition to that of the portfolio managers/analysts. Whilst this is consistent with 2011, in 2010 it was nearly 80 per cent reflecting the more dedicated 2010 respondents which are likely to have more established processes and a specialist resource to work alongside the portfolio managers. In addition, the fact that some respondents reduced their specialist resource in 2012 played a part.

Resources

Overall the total headcount increased year on year (by 43 in 2012 and by 499 in 2011) reflecting the increase in the number of respondents (see Table 10). In addition, the average headcount per respondent was 17 in 2012; 21 in 2011 and 20 in 2010. This decrease in average headcount reflects the decrease in the average assets managed/owned per respondent in that smaller respondents tend to have less resource. For example, 2012 respondents that managed/owned more than £1 billion assets each had an average headcount of 21 whereas those with under £1 billion assets have an average of nine.

The four Asset Owners where “others” are responsible for stewardship included:

- “An asset owner who outsources fund management to external managers, [where] the voting function and corporate engagement reside with the fund managers for now. Our in-house Responsible Investment team at [Owner] exercises oversight and has dialogue with our fund managers on the voting and engagement activity. We also get assistance on vote monitoring and decisions, engagement and RI [Responsible Investment] policy development from our Responsible Ownership partner.”
- “Investment Committee and Head of Finance.”
- “Dedicated in house ESG specialist - role overseen by CIO and CEO (three internal staff). RI activities in general are overseen by Investment Committee and ultimately the [Owner's] board. As a 100% externally managed asset owner, our Number 1 engagement target vis a vis stewardship is our fund managers and ensure that they are adhering to their Stewardship Code commitments. This evaluation and should and is incorporated into the overall evaluation of their service on an ongoing basis.”
- “The Governance Officer, Investment & Governance Manager, Deputy Secretary and Secretary (Chief Executive).”

Table 10: Primary resource responsible

		Headcount		
		<i>No. of respondents</i>		
		2012	2011	2010
Portfolio managers/analysts supported by by dedicated specialists looking at policy	Portfolio managers	221	81	57
	Specialists	22	16	3
	Others	7	4	–
<i>No. of respondents</i>		11	3	2
Portfolio managers/analysts working alongside dedicated specialists	Portfolio managers	547	640	469
	Specialists	170	166	94
	Others	35	24	–
<i>No. of respondents</i>		37	36	24
Dedicated specialists only	Specialists	40	29	38
	Others	8	6	–
<i>No. of respondents</i>		4	3	4
Others		10	2	–
<i>No. of respondents</i>		4	1	–
Total headcount where specialists and others have a role		1,060	968	661
<i>No. of respondents</i>		56	43	30
Portfolio managers/analysts only	Portfolio managers	224	284	108
	Others	27	16	–
<i>No. of respondents</i>		23	18	8
Total	Portfolio managers	992	1,005	634
	Specialists	232	211	135
	Others	87	52	–
Overall headcount		1,311	1,268	769
Overall no. of respondents		79²²	61	38
Average headcount		17	21	20

²² One respondent was unable to provide the head count and is not represented in the text or table.

Integration into the investment process

Engagement on strategy and performance may often be handled by the portfolio managers/analysts, with specialists handling particular aspects such as corporate governance and SRI. At times, this dual approach can give rise to questions as to whether those conducting stewardship represent the views of the portfolio managers responsible for the investment and how stewardship is integrated into the investment process.

The FRC's 2012 Report on Developments in Corporate Governance notes: *"If senior management within institutions consider stewardship important they should reflect this in how they prioritise their available resources, and consider whether they can use them more efficiently. In particular, the FRC believes portfolio managers could take on some work commonly left to corporate governance specialists, especially where this leads to a better integration of governance considerations and investment decision-making. Relevant subjects might include strategy, succession-planning, and the quality of management and the board, and risk oversight²³".*

The Guidance to **Principle 1** states that the stewardship policy should disclose: *"internal arrangements, including how stewardship is integrated with the wider investment process"*.

Where specialists are involved, respondents were asked how stewardship is integrated into the investment process. The results are illustrated in Table 11.

With the exception of one Asset Owner, all respondents integrate stewardship into the investment process in some way. Consistent with previous years, for around 80 per cent of respondents, portfolio managers or analysts set and/or approve the stewardship policy. Moreover, in 2012 and 2011, for around 60 per cent of respondents, portfolio managers or analysts make the final decision on controversial votes - a decrease from 71 per cent in 2010. For nearly half of respondents both portfolio managers and stewardship specialists "always" or "often" attend external meetings with companies; a decrease from 56 per cent in 2011.

Table 11: Integration into the investment process

	Percentage of respondents		
	2012	2011	2010
Portfolio managers/analysts set and/or approve stewardship policy	80	79	77
Portfolio managers/analysts make final decision on a controversial vote	61 ²⁴	61	71
Dedicated specialists attend external investee company meetings with portfolio managers/analysts			
<i>Always</i>	5	12	7
<i>Often</i>	43	44	19
<i>Sometimes</i>	37	30	58
<i>Never/N/A</i>	13	7	-
<i>No response</i>	2	7	16
Dedicated specialists meet internally with portfolio managers/analysts			
<i>Often</i>	57	68	-
<i>Sometimes</i>	30	23	-
<i>Never/N/A</i>	11	2	-
<i>No response</i>	2	7	-
Sample size	56	43	30

Some provided further clarification on how stewardship is integrated into the investment process. For example:

- *"We endeavour to identify the issues, financial and ESG, within companies that we believe could have a material impact on shareholder value. In addition to the integration of ESG being a fundamental part of our investment process, our investment teams will often take the lead on engaging with companies on significant corporate governance matters."*
- *"The individual with responsibility for stewardship policies attends and participates in the relevant weekly investment meetings with portfolio managers and the team responsible for stewardship have full access to all of the systems and data used by the investment team. The portfolio managers and analysts also have critical input into voting decisions."*

²³ Page 27.

²⁴ Includes one respondent that answered "no" but clarified: "In controversial situations, portfolio managers generally make a recommendation, but the final decision is the responsibility of the Proxy Voting Committee".

- *“There is a broad policy of integrated stewardship across equity and fixed income decisions which are made in collaboration with the dedicated specialists.”*
- *“Governance risk measures are part of the investment process in the UK and Europe and we have regular meetings with the global fund management team to discuss relevant governance issues.”*

One respondent explained that portfolio managers make all voting decisions, not just controversial ones, although they may be based on the specialists’ recommendations. For two others, the CIO or CEO makes the voting decision on controversial issues. Another respondent considers stewardship to be the responsibility of the portfolio managers: *“[Owner] requires its managers to monitor investee companies and engage with company management where Environmental, Social or Governance (ESG) practices fall short of best practice. All managers are required [to] report back quarterly on any activity undertaken. In addition, [Owner] will not appoint fund managers who are unable to demonstrate capabilities in this area”.*

Some described how their approach to integration has changed:

- three respondents noted that there had been changes to personnel and teams. One: *“recently appointed a senior investment person to take forward and further integrate [their] stewardship policy”.* Another moved away from a standalone team integrating ESG issues across all investment products. For the third, a portfolio manager with over 27 years’ experience had *“recently taken on the role within the investment team to lead on Stewardship, ESG integration and Investee Company Corporate Governance. This now provides a dedicated specialist within the investment team”.*
- two respondents reviewed their approach to stewardship; one developing a systematic approach for analysts to take account of stewardship issues in their company analysis, while for the other it is still under discussion.

Experience

The FRC’s 2012 Report on Developments in Corporate Governance notes: *“A number of company chairmen said they were having more regular contact with shareholders... However, the interest varied from institution to institution, and the consensus view was that, while those who had traditionally been involved in engagement had raised the standard of their engagement, there was little sign of greater numbers being involved²⁵”.*

and

“The FRC continues to believe that investors should have opportunities for developing their engagement skills. The FRC is encouraged by the initiative from the CFA Society of the UK to develop training materials on governance analysis and will be watching with interest the take-up of these materials in the market²⁶”.

The majority of respondents with dedicated specialists provided information on the training given to and experience of their teams. Of these, 30 mix a range of investment qualifications (e.g. an MBA or qualifications from the CFA Institute) with industry experience:

- *“Our Head of Sustainability Research has post-graduate qualifications in environmental technology as well as 18 years of experience in working with companies on sustainability issues including 5 years engaging with companies as an institutional investor.”*
- *“Portfolio managers and analysts will be qualified and experienced as FSA Approved Persons/CF30s and Training and Competence Category 14s (Managing Investments) with the attendant obligations of CPD to maintain their Approved Persons/T&C status. One dedicated specialist is a Fellow Chartered Accountant with extensive industry experience with CPD obligations. The other dedicated specialists and others have extensive industry experience and keep up to date through industry conferences.”*
- *“Our Head of Corporate Governance has 12 years investment experience and holds the CFA and IMC qualifications. Our Corporate Governance Manager has 18 years investment experience and holds the IMC.”*

²⁵ Page 24.

²⁶ Page 30.

- *“30 years combined experience in corporate governance. Both are Fellows of the Institute of Chartered Secretaries and Administrators (ICSA) with one holding the ICSA’s project award in Corporate Governance as well as the Investment Management Certificate. The other is also a trained accountant. Both regularly attend and speak at conference on corporate governance and stewardship.”*
- *“Three have more than ten years’ investment / governance experience; the fourth has more than five years’ experience. All attend external industry events in the course of their work.”*
- *“Head of Corporate Governance team is a former portfolio manager and analyst, with over 25 years of industry experience and is a member of [the] CFA Institute. The other 4 members of the team have investment industry experience of between 6 and 25 years, with training in corporate governance, analysis and voting.”*
- *“Our Proxy Voting Specialist has many years of experience in the role and is guided by senior investment professionals and members of the Legal and Compliance Department.”*

Five respondents conduct training in-house:

- *“Dedicated specialists are members of the Institutional Client Management team. ICM team members receive training from senior ICM management. Also, ICM team members stay in frequent contact with the client service professionals of our proxy voting recommendation services. ICM team members attend conferences to stay abreast of important industry developments.”*
- *“A formal qualification is not a requirement of the role of dedicated specialist however, all members of team will receive formal in-house training on an on-going basis.”*

As to how other employees in the organisation are made aware or are involved in stewardship, a number of respondents provided details:

- some make others aware to the extent that the stewardship policies are distributed and/or available to all.
- others update employees through monthly or quarterly reports, or in one case a weekly email: *“All investment and distribution teams (300+ people) receive a weekly internal email updating them of engagement activity and proxy voting conducted, as well as updates on industry trends ... The GRI team also present formally to investment teams on the ESG performance of their funds and design a quarterly engagement strategy with teams”.*
- a few made specific reference to training. One stated: *“Portfolio managers/analysts are aware of our commitments as signatories to external codes/principles. Our senior portfolio manager for UK equities and one of the analysts recently completed the responsible investment training course offered by the Responsible Investment Association Australasia.”* This was echoed by another firm: *“[the Manager] is also running a series of internal education sessions to refresh awareness of obligations under the Stewardship Code”.*
- about a third indicated that other staff are fully aware of what is involved: *“All staff in the business are fully aware of what stewardship entails and are either directly involved in implementing the policy in our investment process or are involved in communicating our activity to our investors and potential investors”.*

Service providers

Resources are often supplemented by service providers that process voting instructions and provide research, recommendations and other customised services. The Guidance to **Principle 1** states that the stewardship policy should disclose: *“the use made of, if any, proxy voting or other voting advisory service, including information on how they are used”*.

The FRC’s 2012 Report on Developments in Corporate Governance notes: *“Companies continue to report concerns about the role of proxy advisors in the voting process. At the European level this has led to a consultation about possible regulation or other action by the European Securities and Markets Authority (ESMA), and the European Commission has stated that it will consider an initiative to improve the transparency of the activities of proxy advisors in 2013 as part of its Action Plan.”*

and

“The new edition of the Stewardship Code makes this clear when it says that “institutional investors may choose to outsource to external service providers some of the activities associated with stewardship. However, they cannot delegate their responsibility for stewardship. They remain responsible for ensuring those activities are carried out in a manner consistent with their own approach to stewardship”²⁷.

Processing voting instructions can be resource intensive and respondents tend to use agencies for this purpose. As shown in Table 12, 86 per cent of respondents use at least one agency, compared to only 13 per cent that do not use such a service.

Table 12: Service providers that process voting instructions

No. of providers	Percentage of respondents		
	2012	2011	2010
Three +	2	–	4
Two	10	13	10
One	74	64	67
None	13	17	15
No response	1	6	4
Sample size	80	64	48

Slightly fewer respondents (78 per cent) use a service provider to supply research, with 38 per cent using more than one (see Table 13).

Table 13: Service providers that provide research

No. of providers	Percentage of respondents	
	2012	2011
Three +	12	–
Two	26	–
One	40	–
None/No	21	–
No response	1	–
Sample size	80	–

Where respondents receive research from service providers, nearly all (94 per cent or 58) also receive recommendations. As shown in Table 14, an increasing proportion of respondents make voting decisions without “necessarily” regarding the service providers’ recommendations compared to 2011 (2012: 46 per cent; 2011: 40 per cent). Over one-half (2012: 54 per cent; 2011: 56 per cent) follow recommendations “sometimes” and no respondent “always” follows them (2011: 4 per cent; 2010: 3 per cent). In 2010 two respondents always followed a provider’s recommendations, one of which now does not “necessarily” follow and the other only “sometimes” follows.

²⁷ Pages 26 and 27.

Table 14: Are recommendations followed?²⁸

No. of providers	Percentage of respondents		
	2012	2011	2010
Not necessarily			
>Four	–	–	8
Four	7	7	–
Three	3	6	8
Two	15	11	13
One	21	16	18
	46	40	47
Sometimes			
>Four	2	9	–
Four	–	7	3
Three	–	–	–
Two	–	24	16
One	50	16	31
Not given	2	–	–
	54	56	50
Always			
One	–	4	3
Sample size	58	55	38

Three respondents commented that it can appear that they do follow providers' recommendations in that their decisions may coincide with the recommendation.

Among those respondents that "sometimes" follow, the recommendation is based on a tailored policy which:

- is followed when the holding is below a certain threshold (two).
- can be overridden by the portfolio managers (six).
- is generally followed but the portfolio managers have the final say (four).

- for one respondent: "Recommendations to vote against or to abstain, and resolutions not covered by the policy ('refers'), are reviewed by governance specialists (and by portfolio managers/analysts for holdings in active funds)... Our intended vote was different from the external provider for around 27% of against or abstain recommendations. Company engagement caused us to change our vote on a further 15% of recommendations. For refer recommendations, our initial view was to vote for on just over 50% of the resolutions concerned".

- another follows: "for specific client mandates which [the Manager] has been instructed to vote in line with their own policy".

A quarter of respondents receive standard recommendations which are used in a variety of ways:

- in the case of four respondents for routine matters or small/index holdings, with one clarifying that: "Large holdings, or contentious issues, or votes in relation to companies we have identified as 'governance outliers', and all M&A and business-related votes are referred to portfolio managers for a decision. [Manager] never issues automated standing instructions to vote in a certain way - every single vote is scrutinised on a case-by-case basis".

²⁸ In 2012 respondents were asked to be specific about their use of providers, which may skew the comparison to prior years.

- for three respondents to highlight items which may be against their own or a client's guidelines:
 - *“We generally use proxy research as a flag to investigate matters further, discuss issues with the fund managers or engage with the company. We do not use proxy research to automatically guide our voting actions and decisions are made on a case-by-case basis - with the exception of those clients who have mandated [the Manager] to follow ISS's recommendations unless authority to vote contrary is provided.”*
 - *“Our voting service provider, use Glass Lewis as their primary source of research, which does provide voting recommendations. [The Providers] then overlay their research/recommendations with their internal voting policy, which is broadly in line with ICGN principles. Over the past year (i.e., from September 2011 to September 2012), [the Provider] followed approximately 95% of Glass Lewis' recommendations (very rough estimate).”*
- for one respondent when it has a conflict of interest.

Three respondents may disregard recommendations if engagement justifies doing so or if they do not consider them to be in their clients' best interest: *“If we have engaged with a company and received assurances that issues will be addressed in future, we might well ignore a negative recommendation”.*

5. Monitoring and engagement, together with practical examples

Principle 3 states that: “institutional investors should monitor investee companies” and guidance that: “investee companies should be monitored to determine when it is necessary to enter into an active dialogue with their boards. This monitoring should be regular and the process clearly communicable and checked periodically for its effectiveness. Institutional investors should endeavour to identify problems at an early stage to minimise any loss of shareholder value”.

Principle 4 is that: “institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value”.

Monitoring

The majority of respondents, 76 per cent, monitor all companies as part of their investment process, an increase on 2011, with only 16 per cent basing it on the size of holding or when significant issues arise (see Table 15). For the one “other” respondent, it was a: “Combination of significant holdings and significant issues”.

Table 15: Prioritisation of monitoring

	Percentage of respondents		
	2012	2011	2010
All companies/part of the investment process	76	70	67
By size of holding	8	17	19
When there are significant issues ²⁹	8	2	–
Delegated to manager/overlay service ³⁰	5	2	6
Other	1	6	4
No response	2	3	4
Sample size	80	64	48

Five Service Providers monitor all companies as part of their service. Of the two that do not, one delegates monitoring to external parties. One Provider stated:

“On the one hand, [Service provider] does have ethical considerations in our own cash investments...As a service provider to investors, [the Service Provider] updates the risk profiles we have on companies for investors on an on-going basis. These risk profiles assist investors in complying with the Stewardship Code, amongst other purposes”.

Markets/Indices

Respondents were asked whether they engage and vote the shares of, or only vote the shares of, companies included in particular indices or listed on AIM (see Table 16). This question was not relevant for Service Providers.

There is a decrease in the percentage of respondents that both engage and vote in 2012 compared to 2011. For companies in the FTSE 100 index this went from 88 per cent to 78 per cent, while for the FTSE 250, it went from 83 to 75 per cent. However, there is an increase in the percentage of respondents that only vote shares: from 8 per cent to 14 per cent for the FTSE 100 and from 11 per cent to 13 per cent for the FTSE 250. These changes would be explained by the 2012 respondents representing a wider range of institutional investors and on average tending to be smaller and having less resource.

Table 16: Companies engaged with and shares voted or where shares only voted

	Percentage of respondents				
	Engage and vote		Vote only		Engage
	2012	2011	2012	2011	2010
FTSE 100	78	88	14	8	100
FTSE 250	75	83	13	11	98
FTSE Small Cap/fledgling	59	72	13	6	92
AIM	55	64	11	6	65
No response	4	2	4	2	–
Sample size	80	64	80	64	48

²⁹ In 2011 this was “When vote against/voting issues”.

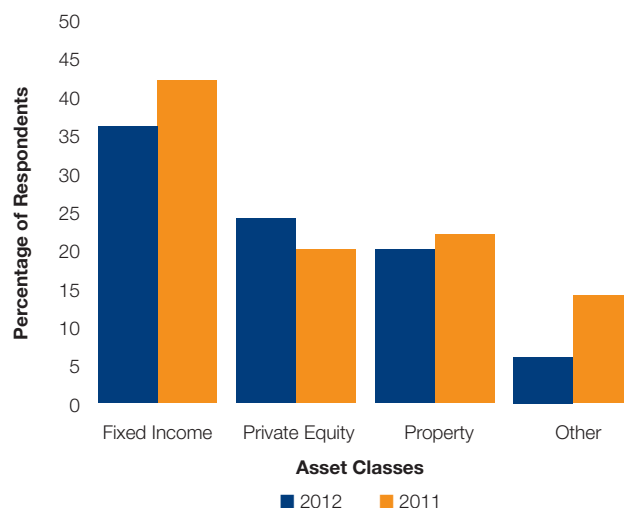
³⁰ Three Asset Owners outsource management but have in-house specialists. One Asset Manager is a fund of funds manager and outsources monitoring to the individual fund managers.

Whilst the Code is mainly directed at institutional investors with UK equity holdings, the FRC’s 2012 Report on Developments in Corporate Governance stated: “The 2012 edition of the Code now encourages signatories to explain which of their funds or products are covered by the approach described in their statements. Where institutions apply a stewardship approach to other asset classes, they are encouraged to disclose this as well ³¹”.

As shown in Chart 1, respondents engage with asset classes other than equities, with fixed income investments being the most common (36 per cent). However, whilst for fixed income investments the 2012 percentage decreased slightly from 2011, a higher percentage, just under a quarter of respondents, engage with private equity holdings. This may reflect the change in respondents’ profiles with smaller respondents tending to focus more on private equity and less on fixed income investments. Those that engaged with other asset classes stated:

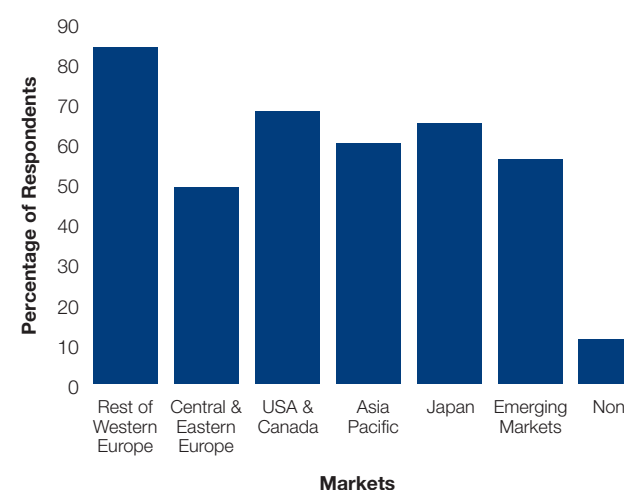
- “We routinely monitor existing and potential deposit fund (cash) counterparties management of environmental, social and governance (ESG) risk on a regular basis across each of our deposit funds; and take further action if necessary.”
- “Where there is an overlap with our equity holdings. We believe that the engagements we conduct with companies from an equity perspective have direct relevance to fixed income (and other) investors as the focus of our engagements is on risk management, enhanced disclosure and quality of management and leadership at issuers. There is, in our view, a commonality of interests on these matters between equity and debt investors.”
- “Non-listed UK banks.”
- “Infrastructure where listed.”

Chart 1: Engagement with asset classes other than equities



Respondents were asked for the first time whether they engage with companies in markets outside the UK. As shown in Chart 2, over 80 per cent engage with companies in the rest of Western Europe. Only 11 per cent do not engage outside the UK.

Chart 2: Engagement in markets outside the UK – 2012



³¹ Page 23.

Prioritisation

Engagement tends to be prioritised according to issues. The FRC's 2012 report on Developments in Corporate Governance notes that: *"A number of company chairmen said they were having more regular contact with shareholders and that the interest of the latter in discussing strategy had increased³²".*

and

"A large part of the engagement effort still seems to be directed towards remuneration, especially the detailed analysis of complex performance share and option schemes. Concerns have been raised that pressure on resources could become acute towards the end of 2013 as companies start consulting on their remuneration policies ahead of the introduction of the new binding vote. Companies and shareholders should plan for this³³".

Table 17 shows respondents' ranking of the most frequently addressed issues in 2012 and 2011. Most engagement in both years was in relation to board remuneration, followed by company strategy and objectives. In this context, remuneration is subject to an annual vote and it may be that companies initiate engagement, as opposed to the respondents, in the interests of ensuring the board remuneration report is approved. The least engagement was in relation to pre-emption rights reflecting the fact that there were very few rights issues in 2012.

Table 17: Most frequently addressed issues

	Ranking	
	2012	2011 in aggregate ³⁴
Board remuneration	1	1
Strategy and objectives	2	2
Board leadership – Chairman/CEO	3	8
Board diversity & committee membership	4	3
Corporate actions and restructuring	5	10
Environmental/social issues	6	4
Mergers and acquisitions	7	6
Board succession planning	8	9
Risk appetite	9	5
Pre-emption rights	10	7
Sample size	80	64

Remuneration was also the most common issue for Service Providers, followed by board diversity & committee membership³⁵. One Provider only engaged on environmental and social issues, adding: *"the issues [Service Provider] currently engages with certain companies are: climate change, bribery, human rights in the resource sector, water in the food and beverage sector, overall ESG risk management, supply chain management, plus specific engagement related to companies in alleged breach of international norms".*

³² Page 24.

³³ Page 27.

³⁴ Ranked according to the number of companies engaged with on the issue.

³⁵ Two did not respond to this question as it was not relevant.

Annual General Meetings

In 2012 28 per cent of respondents (2011: 30 per cent; 2010: 38 per cent) attended Annual General Meetings “whenever possible” or “where they have a major holding and/or where appropriate” (see Table 18). The decrease reflects the reduction in the average size of respondent in terms of assets managed/owned and that newer respondents tend to have less resource. Of the 31 per cent that selected “other”, a third attend where practical or necessary, for example, when it is at a convenient location or where the deadline to vote has been missed. For one respondent this would be: *“about ten a year where we have a major concern or are not being listened to”*.

Of the remainder that stated “other”:

- eight respondents rarely attend or do so on an exceptional basis, though for one respondent this would constitute less than five meetings a year.
- six respondents attend occasionally but would do so when required.
- two respondents have not attended any so far, though both would consider doing so.

Table 18: Attendance at Annual General Meetings

	Percentage of respondents		
	2012	2011	2010
Whenever possible	8 ³⁶	2	–
Where have a major holding, and/or where appropriate and practicable	20	28	38
Other	31	36	35
Never	37	33	25
No response	4	1	2
Sample size	80	64	48

Four of the Service Providers never attend AGMs, one attends “whenever possible” and two do so in certain instances.

Practical examples

To assess what actually happens in practice, respondents were asked how they escalated matters and engaged on certain issues with particular companies. For example:

- whether it had a holding, whether there were any conflicts of interest, whether it had any concerns and whether it engaged.
- what it did. For example, the number of engagements³⁷ it had, either on its own or at the company’s instigation, who the engagement was between (whether it was the portfolio manager, the dedicated stewardship specialist or a mixture of the two) and who they engaged with at the company. Whether there was collaboration and whether this was helpful.
- how it voted on specific resolutions.
- whether it achieved what it wanted and if engagement would be on-going.

The companies concerned were:

- Barclays plc
- WPP plc
- G4S plc
- Xstrata plc
- SABMiller plc

The analysis is set out in Appendix 3 and summarised below. The main focus of engagement with these companies was strategic and governance matters but a small number of respondents gave details in relation to certain ethical issues (CSR). The latter are not reflected in this report as they do not relate to the main issues under examination.

Generally engagement with companies is not within the remit of the Service Providers, but where they provided details, they are included in Appendix 3.

³⁶ Includes one respondent that answered “other” and clarified *“During the past year, we attended all shareholder meetings at UK investee companies”*.

³⁷ In this context, the term “engagements” is taken to mean contacts with the company at either the respondent’s or the company’s instigation.

Barclays plc

During 2012 events at Barclays unfolded rapidly, culminating in fines from regulators for misconduct related to its London Interbank Offered Rate (LIBOR) submissions and the subsequent resignations of key board members and senior management.

Sixty-five per cent of respondents with a holding engaged with Barclays. For just under three quarters of these, the main issue was remuneration with some also concerned about leadership and succession and others about the LIBOR issue. The concerns about remuneration were largely an indication that there were more fundamental issues around the culture at Barclays. To quote: *“Explanations regarding the LIBOR scandal and assurances that the Company will turn the corner on culture, values and behaviours to minimise the risk of issues such as this happening again. Regarding culture, there is an opportunity to become more ethical, less greedy and more aware of their role in society”*.

The issues meant there was more engagement with Barclays than with any of the other companies in the examples. Respondents had an average of 6.7 engagements each, though eight respondents had 10 or more each. This was mainly with the Chairman and Company Secretary (it is understood that the Company Secretary attended most meetings). There was also much engagement with the Executive Directors and Management reflecting the fact that the issues were more fundamental than simply those around governance.

Two thirds of those that engaged were involved in collaborative engagement, mainly via joint meetings with Barclays. This was considered helpful as it gave a consistent and shared message to Barclays.

At the 2012 AGM the Chairman, Marcus Agius, apologised for the bank's failure to communicate over remuneration. 77 per cent of respondents voted against the Remuneration Report which compared with an overall vote against of 27 per cent. There was a backdrop of a general debate about the allocation of profit and whether this went to investors by way of dividend or was paid out in bank bonuses. 58 per cent of respondents voted against the re-election of the

Remuneration Committee Chair, Alison Carnwath, all but one of which voted against the Remuneration Report. Respondents held her accountable for the remuneration issue. This compares with an overall vote of 21 per cent against. Prior to the AGM, the Chief Executive's and Finance Director's bonuses had been halved until certain targets were met.

Although the re-election of the Chairman and Chief Executive were supported, both resigned in the summer of 2012, together with the Chief Operating Officer and Chair of the Remuneration Committee.

Just over half of those that engaged considered they achieved their objectives. Some on the basis Barclays made changes to the bonuses, though in certain cases other issues were still outstanding for example: *“Although the Company made concessions (i.e. agreeing to defer 50% of the bonus and making this subject to further performance conditions), our concern was not addressed in full in that bonuses should have been significantly reduced and they weren't. However, our concerns increased regarding the greed and culture of the company when the LIBOR scandal was announced and our underlying concerns [changes at board level] were largely dealt with without us having the opportunity to raise these”*.

However, 37 per cent did not achieve their objectives as the changes were too moderate or only partially addressed issues. The majority of respondents indicated that engagement would be on-going.

WPP plc

Against a backdrop of significant votes against the 2011 Remuneration Report, WPP sought to award a 30 per cent increase in its Chief Executive's, Martin Sorrell's, base salary for 2012.

Over half of the respondents with a holding engaged with WPP, the most significant issue being remuneration. Some wanted to understand the basis for the compensation, but the majority wanted changes and many provided suggestions to WPP. As one stated: *“We wanted to provide suggestions to WPP's management about a compensation plan that would better align Mr Sorrell's economic interests with shareholders”*.

One respondent with a conflict at senior executive levels engaged and: *“informed the company in advance of our engagement over the year of the relationship and pursued our engagement with the same rigour as we would have done without this relationship”*.

There was less engagement with WPP than with Barclays - an average of 3.1 engagements each. This was mainly with the Chairman and investor relations, reflecting the fact that engagement was principally on a corporate governance issue. Just under half of respondents collaborated with other investors and reinforced their disapproval.

At the June 2012 AGM in Dublin, 83 per cent of respondents voted against the Remuneration Report (compared to an overall vote against of nearly 60 per cent) mainly as they considered the Chief Executive's remuneration too high. This reflected dissent over a number of years and a perception that WPP had not taken sufficient notice of shareholders' signals at previous AGMs.

Forty-five per cent voted against the re-election of the Remuneration Committee Chair, Jeffrey Rosen, nearly all of which also voted against the Remuneration Report. (This compares to an overall vote of 22 per cent against his re-election as a Director).

However, all respondents supported the re-election of the Chief Executive, Martin Sorrell. As one summarised: *“We voted in favour of the re-election of Mr Sorrell as we considered him to be a highly effective CEO for WPP who we supported continuing in the role, however, our vote against the remuneration report demonstrated that we did not consider this to be at any cost”*.

This was the least successful of the practical examples in that the majority of respondents intended to continue to engage and just over a half did not achieve their objective. To quote: *“Remuneration levels further increased in 2012 despite a significant vote against in 2011. Hence, despite obvious investor discontent and discussions with the company to address these, the Company has not listened”*.

G4S plc

During 2011 G4S announced the proposed acquisition of ISS A/S, a Danish company. This was to be funded by a rights issue and both the rights issue and the acquisition were subject to shareholder approval.

Sixty-five per cent of respondents with a holding engaged with G4S. The majority focused on the acquisition of ISS; some wanted to understand more about it, whilst others wanted to put a stop to it. To quote: *“Having been unable to gain sufficient assurances around the strategic rationale as well as the potential risk exposure of the ISS acquisition we wanted the company to withdraw from the transaction. Subsequent to the failure of the acquisition we wanted to ensure both appropriate accountability as well as receive reassurances around the company's desire to return to its previously stated strategy”*.

Most of the engagement was with the Executive Directors and investor relations with respondents predominantly represented by portfolio managers/analysts. This reflects the engagement focusing on a transaction as opposed to a corporate governance issue. Respondents had an average of five engagements each, though one noted a total of 28, 20 of which were with investor relations. Half of those that engaged collaborated with other investors.

The proposed acquisition was cancelled in November 2011. In addition, Chief Executive, Nick Buckles, waived his £750,000 bonus in March 2012 voicing regret over “wasting £50m on the deal which did not happen”. G4S later announced that the Chairman, Alf Duch-Pedersen, would retire during 2012 once his successor had been identified.

This was the most successful practical example, with nearly all respondents achieving their objectives particularly as G4S did not proceed with the acquisition. This was reflected at the June 2012 AGM where the majority of respondents supported both the Remuneration Report and the re-election of the Chief Executive, Nick Buckles, with 75 per cent and 87 per cent supporting each resolution, respectively. (Overall 99 per cent of votes were in support of both Resolution 2, approval of the Remuneration Report, and Resolution 4, the re-election of Nick Buckles.) To quote: *“Resolution 2: We supported the freeze of base*

salaries for 2012 and were in agreement with the Remuneration Committee that, in light of a number of factors affecting the Group in 2011, it would not be appropriate to consider the payment of an annual bonus for the Directors for the year. We had no material issues with the bonus and LTIP performance targets”.

Xstrata plc

In 2011 Xstrata's board announced a proposed merger with Glencore. The merger required 75 per cent of shareholders, excluding the Glencore shareholding of 34 per cent, to approve the merger.

Shareholders voiced concerns over the terms of the merger as well as over executive remuneration. Over 70 per cent of respondents with a holding engaged with the main focus being the merger. Concerns related to the terms of the deal, the retention package and the resulting governance arrangements. To quote: *“The engagement objective was to convey our concerns that i) the deal did not provide sufficient value for Xstrata shareholders; ii) we needed to be convinced that management incentives were truly aligned with the interests of long-term institutional shareholders; and iii) we believe the widespread views of shareholders were not being listened to by management and the Board needed to act upon this”.*

There were many instances of collaboration with other investors.

This had the second highest number of engagements after Barclays with an average of 4.7 contacts each although one respondent had ten contacts with investor relations. In the main engagement was with Executive Directors and investor relations with respondents' portfolio managers and/or analysts taking the lead. As for G4S this reflects the fact that engagement focused on a transaction as opposed to a corporate governance issue.

At the May 2012 AGM, Xstrata faced criticism in relation to its Remuneration Report and 80 per cent of respondents voted against it (compared to an overall vote of 37 per cent against). To quote: *“Examination of the remuneration report highlighted a number of concerns: There were clauses allowing disproportionately high termination payments. There was a lack of clarity around the circumstances to justify*

the magnitude of LTIP awards and the low threshold for these awards”.

With the backdrop of the proposed merger and with concerns over independence and remuneration, 25 per cent and 22 per cent of respondents voted against the re-election of Non-Executive Director, Ivan Glasenberg, and Remuneration Committee Chair, David Rough, respectively. Whilst overall the re-election of the two directors was supported there were significant votes against of 14 per cent and 19 per cent, respectively. Only three respondents both supported the re-election of these directors and approved the Remuneration Report; one as it was focused on optimising the best terms for Xstrata and the retention payment had not yet been revealed.

Seventy per cent of respondents achieved their objectives in that their engagement delivered their message or they gained a better understanding of the business and the merger. For others the terms of the merger improved, for example: *“the offer for Xstrata shareholders has been improved and the remuneration arrangements are now subject to performance conditions and a separate vote; giving shareholders a real choice when casting their vote”.*

However, some still had reservations: *“Engagement was helpful to better understand the status of the deal and we welcome the company giving shareholders an opportunity to vote on remuneration arrangements. However, the voting on the deal and remuneration has been made overly complicated and we still don't believe in retention payments - they don't work and quantum still feel high”.*

Those that did not achieve their objectives included those that remained unconvinced about the deal, for example: *“Remained uncomfortable regarding the process prior to the recommendation, the decision to offer 'retention' packages, unconvinced on merits of the deal”.*

A number continue with their engagement: *“It's really too soon to determine whether our engagement with Xstrata has been successful [or] not. The company has decided to proceed with the merger with Glencore which is a positive from our perspective although this has yet to be approved by shareholders but the retention arrangements remain in place. As indicated*

above, we feel that further Board change may well be necessary in the event that the merger proceeds meaning that our engagement with Xstrata is still very much work in progress”.

SABMiller plc

SABMiller announced that from the 2012 until the 2013 AGM its Chief Executive, Graham Mackay, would be joint Chairman and Chief Executive. The Senior Independent Director, John Manser, wrote to shareholders explaining why this arrangement was appropriate.

Nearly half of respondents with a holding engaged with SABMiller with the majority focusing on board independence. They wanted more information or to voice concerns over the joint role and the lack of independent Non-Executive Directors. To quote: *“We hoped to achieve a better understanding of the succession management process at SABMiller to enable us to form a judgement as to whether exceptional circumstances prevailed that would justify [Manager] supporting the elevation of the CEO, Graham MacKay, to Executive Chairman. It was also an opportunity for us to explain our thinking on the matter”.*

Others wanted a better understanding of SABMiller’s strategy going forward, one specifically noted: *“We had concerns about the group’s strategy and its approach to mergers & acquisitions. The purchase of Fosters in particular was a fully priced acquisition of a mature business in a developed market. We were keen for the company to show more discipline in this area going forwards”.*

Although engagement mainly focused on board structure and the lack of independent directors, relatively few respondents engaged with the Senior Independent Director in that contact was mainly with the Executive Directors and investor relations. On average respondents had 2.9 engagements each.

Only two respondents collaborated with other investors; less than with the other examples.

At the July 2012 only 58 per cent of respondents voted for the re-election of the Chief Executive, Graham Mackay (compared to an overall vote of 94 per cent in support) highlighting concerns over the roles of Chairman and Chief Executive being combined. In addition, the majority, 63 per cent, voted against the Remuneration Report due to concerns over the performance criteria and disclosures (compared to an overall vote of 23 per cent against).

One respondent that voted for the re-election of Graham Mackay stated: *“... we were persuaded by the company’s arguments that there was sufficient commercial merit for the appointment of Graham Mackay as Chairman for us support this proposal”.*

65 per cent of respondents that engaged achieved their objectives as they gained a better understanding of the business or were satisfied with SABMiller’s direction. Others put forward their concerns and one specifically considered the company had acknowledged that its board structure needed to change. Where respondents did not achieve their objectives it was due to the lack of change in the board.

6. Voting

The Guidance to **Principle 6** states that: *“institutional investors should seek to vote all shares held. They should not automatically support the board. If they have been unable to reach a satisfactory outcome through active dialogue then they should register an abstention or vote against the resolution. In both instances, it is good practice to inform the company in advance of their intention and the reasons why”*.

In addition, the Guidance to **Principle 3** states: *“institutional investors should consider carefully explanations given for departure from the UK Corporate Governance Code and make reasoned judgements in each case. They should give a timely explanation to the company, in writing where appropriate, and be prepared to enter a dialogue if they do not accept the company's position”*.

Service Providers were not asked to complete this section.

Voting policy and processes

During 2012, 40 per cent of respondents made changes to their voting policy or processes. Of these 40 per cent revised their voting policy:

- *“Updated the policy to reflect changes the FRC made in the Code³⁸ on diversity provisions and changes to dividend expectations.”*
- *“Voting Policies are reviewed annually. The last review took place in Autumn 2011 and the revised policies were adopted in January 2012. A number of amendments to the UK, North American and International voting policies were made to reflect the knowledge and experience gained from the 2010/11 voting season and to provide clarification on how individual votes should be exercised. Amendments were also made to take account of changes to the UK Corporate Governance Code and changes in UK and global best practice.”*

- *“The [Manager's] Proxy Committee (the “Committee”) redefined the considerations to be evaluated regarding ‘say on pay’ agenda, and the Committee adopted an anti-gross up policy - to vote Against any gross ups paid to executives, i.e. the ‘reimbursement’ of employment taxes, etc.”*
- one respondent introduced a specific new conflict of interest voting guideline.

A further four are currently reviewing their policy or it is subject to regular review.

Nearly a half of these respondents also changed their processes, including:

- two respondents that now vote in more global markets, for one this was where there are no impediments to voting such as share blocking.
- seven respondents that changed their resources, with four of these increasing the number of dedicated specialists. Two of these moved responsibility for stewardship, with one creating a new role and the other restructuring engagement which has *“driven [it] more to ensure ESG considerations are more integrated within the investment processes”*.
- six respondents that changed their service providers.

Holdings voted in particular markets

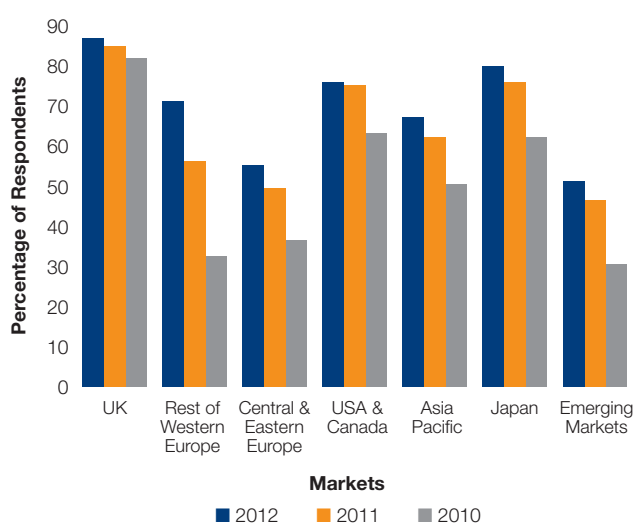
The FRC's 2012 report on Developments in Corporate Governance notes: *“Overall voting levels at annual general meetings continue to increase. In the first six months of 2012 the average turnout was 73.1 per cent, up from 70.9 per cent in the same period in 2011, and from 65.8 per cent in 2008. Average turnout in the UK is above the average of 65.9 per cent across seventeen European markets, although turnout also increased in the majority of those markets this year³⁹”*.

³⁸ A revised Corporate Governance Code was issued in September 2012.

³⁹ Page 25.

Respondents' voting levels remain high in all markets, with 55 per cent voting "all" shares held and 77 per cent voting "all" or "most". Across all markets, there has been an increase in the percentage of respondents that vote all shares held. This is shown in Chart 3, with detailed results set out in Appendix 4.

Chart 3: Markets where all shares voted



Advising management

Over a third of respondents (35 per cent) "always" or in the "majority of instances" provide management with advance notice of their reasons for abstaining or voting against a management resolution. A further 12 per cent do so in arrears (see Table 19).

In contrast, 43 per cent inform in advance "occasionally" or "very rarely", but of these, nine respondents "always" or in the "majority of instances" do so in arrears.

Table 19: Advising management

	Percentage of respondents				
	Voting against or abstaining on management resolution				2010
	2012		2011		
	Notify in advance	Notify in arrears	Notify in advance	Notify in arrears	Notify
Always	20	3	16	2	17
Majority of instances	15	9	23	9	29
Occasionally	29	19	30	20	17
Very rarely	14	15	16	14	10
Never	18	13	12	13	2
When not in advance	–	11	–	20	–
N/A as in advance	–	24	–	19	–
Other	–	–	–	–	19
No response	4	6	3	3	6
Sample size	80	80	64	64	48

Disclosure of voting records

The Guidance to **Principle 6** states that: “*institutional investors should disclose publicly voting records and if they do not, explain why*”.

As shown in Table 20, nearly two thirds of respondents (65 per cent) disclose their voting records. This has decreased from 2011 (73 per cent) mainly due to the fact that four 2011 respondents that disclose did not participate in 2012. It tends to be the larger respondents that disclose in that the 2012 respondents that disclose held 90 per cent of the assets managed/owned by all respondents.

Of the third (33 per cent) that do not disclose, 15 per cent explain the reason why. Reasons vary:

- nine respondents only disclose to clients, one clarifying: “*We do not publicly disclose detailed voting records, as we consider these to be proprietary to our clients. We disclose aggregated global statistics data only*”.
- for two respondents, publication is under review.
- one respondent provides the information on request.

This is not relevant for two Asset Owners where holdings are managed by external managers. For one, the external managers decide whether or not to report. The other publishes a summary of each manager’s policy under the Code and its Code statement states: “*The Trustee’s Responsible Investment policy commits it to disclosing a summary of voting activities annually on the Scheme website*”.

Table 20: Disclosure of voting records

	Percentage of respondents		
	2012	2011	2010
Disclose voting information ⁴⁰	65	73	65
Do not disclose			
Reason disclosed ⁴¹	15	14	–
Reason not disclosed	15	11	–
Commit to publish	3	2	–
	33	27	33
No response	2	–	2
Sample size	80	64	48

Of the 65 per cent that disclose voting information, over two thirds (68 per cent) publish all voting decisions (see Table 21). Of these, six per cent give the rationale for all decisions, eight per cent provide the rationale for votes against or abstained, with a further ten per cent also giving the rationale for exceptional votes. Nearly a third (32 per cent) publish a summary voting report that includes information on votes against management, however, only 14 per cent state the rationale.

⁴⁰ Includes one respondent that publishes a global voting report.

⁴¹ Four respondents did not give a reason for non-disclosure but are included in the table as they disclose the reason in their code statement.

Table 21: All votes publicly disclosed

	Percentage of respondents		
	2012	2011	2010
All votes			
Rationale for all	6	9	–
Rationale for against or abstained, and exceptional	10	6	–
Rational for against or abstained	8	4	–
No rationale	44	49	–
	68	68	68
Summary report	32	30	32
No response	–	2	–
Sample size	52	47	31

The majority of respondents (60 per cent) publish voting information quarterly in arrears, a further 25 per cent publish it annually in arrears and one respondent publishes it more than a year in arrears (see Table 22).

Table 22: Disclosure of voting information in arrears

	Percentage of respondents	
	2012	2011
Quarterly or less	60	57
Six months	13	13
One year	25	28
More than one year	2	2
Sample size	52	47

7. Reporting

Clients/beneficiaries

Principle 7 states that: “institutional investors should report periodically on their stewardship and voting activities”.

In accordance with the Guidance: “those that act as agents should regularly report to their clients details on how they have discharged their responsibilities. Such reports will be likely to comprise both qualitative as well as quantitative information. The particular information reported, including the format in which details of how votes have been cast are to be presented, should be a matter for agreement between agents and their principals”.

As shown in Table 23, nearly all respondents (96 per cent) report to clients or beneficiaries. One-half of these (2011: 61 per cent; 2010: 54 per cent) report quarterly and for a further 23 per cent the frequency varies by client⁴².

Of the two respondents that do not report, one’s policy statement states: “On request, we will disclose fully to our clients how we have voted any all other Environmental, Social, and Governance issues”. The other: “undertakes to review and report on voting records at least annually”.

	Percentage of respondents		
	2012	2011	2010
Monthly or more frequently	3	5	2
Varies according to client	23	20	31
Quarterly	50	61	54
Annually	20	11	11
Do not report	2	3	–
No response	2	–	2
Sample size	80	64	48

⁴² One noted that it reports twice a year.

⁴³ Two that selected “other” are included as they clarified that they report on both voting and stewardship.

Over one-half of respondents (56 per cent) provide details of both voting and stewardship activities when reporting to clients or beneficiaries. A further 21 per cent only provide details of voting (see Table 24). Of those that stated “other”:

- three report as requested by clients.
- nine respondents report on voting to all clients regularly, reporting on engagement may be less frequent, be less detailed or only to selected clients. For example: “[the Manager] provides quarterly voting reports for institutional clients and also bespoke quarterly engagement reports where mandated. In addition, institutional clients receive bespoke biannual voting and engagement reports which detail dialogue with companies covering ESG issues over the period under review. [The Manager] also publishes biannual Voting and Engagement Reports which provide high level voting statistics and highlights issues [the Manager] has engaged on during the six month period”.

Table 24: Content of reports

	Percentage of respondents		
	2012	2011	2010
Both voting and stewardship ⁴³	56	53	69
Stewardship only	2	2	2
Voting only	21	23	17
Other	15	19	10
No response/do not report	6	3	2
Sample size	80	64	48

Independent opinion

The Guidance to Principle 7 states that: *“those that sign up to this Code should consider obtaining an independent audit opinion on their engagement and voting processes having regard to the standards in AAF 01/06⁴⁴ and SAS 70⁴⁵”*.

The FRC’s 2012 Report on Developments in Corporate Governance states: *“One of the changes made in the 2012 edition of the Code was to strengthen the references to independent assurance of how asset managers carry out their stewardship activities. The Code now states that managers should obtain such assurance – although they can, of course, choose to explain rather than comply – and make the reports available to clients on request. In November 2012 the Institute of Chartered Accountants in England and Wales published an updated version of its AAF 01/06 Stewardship Supplement, one of the frameworks available for asset managers to use, to reflect changes in the Code⁴⁶”*.

Consistent with 2011, 20 per cent of respondents obtained an independent opinion on their voting process in the last 12 months. A further 14 per cent covered both voting and stewardship (2011: 10 per cent). However, around one-half of respondents (51 per cent) did not obtain an independent opinion and have no plans to do so (see Table 25).

Reasons for not obtaining an independent opinion varied:

- seven respondents did not consider it necessary; it had not been requested by clients, there were no requirements to do so, or it was not relevant to the particular fund structure.
- another seven respondents may revisit this issue at a later stage, one stating: *“We plan to revisit this once we have had feed-back from our investors on the usefulness and value of our approach”*.
- for four respondents processes are looked at by internal audit and for two by a third party audit that may not be considered independent.
- for three respondents, the cost of such verification would outweigh any benefit, with one respondent stating: *“As we are primarily retail fund managers, in our opinion the cost of such verification outweighs any benefit to our mainly retail investors. There is also no material demand from clients to provide such an independent assurance”*.
- another respondent considered: *“We are [a] small investment management company and feel that our stewardship and/or voting processes which we take very seriously complies with the standards in AAF 01/06 and SAS 70. These have been discussed and agreed between the Directors, senior management and compliance officer”*.
- one respondent’s back office function is outsourced and the proxy advisor has: *“independent quality management system certification ISO 9001:2008 with respect to the provision of stewardship support services to global institutional investors and other parties”*.

⁴⁴ The Audit and Assurance Faculty of the Institute of Chartered Accountants in England and Wales periodically issues guidance to its members. One such guidance note is AAF 01/06: Assurance reports on internal controls of service organisations made available to third parties, which provides guidance to reporting accountants.

⁴⁵ SAS 70: Service Organizations, is an auditing standard developed by the American Institute of Certified Public Accountants. It gives guidance to auditors in issuing an opinion on a service organisation’s description of its controls.

⁴⁶ Page 24.

Of the 51 per cent of respondents that do not plan to obtain an independent opinion, slightly more than a quarter included stewardship and/or voting processes within their own internal audit review, the majority of which was undertaken within the last 12 months. However, slightly less than three quarters do not intend to include these processes within their internal audit, reasons included:

- in five cases, there is no internal audit function.
- among three respondents, processes are either reviewed by the board or the compliance function.
- two respondents did not deem it necessary or requested.
- for one Asset Owner, its stewardship functions are mainly outsourced.

Five respondents may revisit this decision in the future.

Table 25: Independent opinion on processes⁴⁷

	Percentage of respondents		
	2012	2011	2010
Both voting and stewardship			
Over 12 months	–	–	–
Within last 12 months	14	10	6
Ad hoc	–	–	2
Voting only			
Over 12 months	–	–	2
Within last 12 months	20	20	36
Ad hoc	–	–	2
Intend to in respect of 2012	11	17	10
No, and no plans to do so	51	48	29
No response	4	5	13
Sample size	80	64	48

⁴⁷ The terms “current year” and “annually” in 2011 changed to “within last 12 months”; and “period not given” changed to “ad hoc” in 2012.

Appendix 1

Steering Group members

Stephen Haddrill (Chair)	Financial Reporting Council
Jocelyn Brown	Financial Reporting Council
Frank Curtiss	RPMI Railpen
Richard Davies	Investor Relations Society
David Jackson	BP
Huw Jones	M&G Investment Management
Yvonne Lenoir	EFAMA
Liz Murrall	IMA
Jarkko Syyrila	EFAMA
Frances Wells	IMA

Appendix 2

Respondents to the questionnaire

Asset Managers

Aberdeen Asset Management	Highclere International Investors
Aerion Fund Management	HSBC Global Asset Management
Alliance Bernstein	Impax Asset Management
Artemis Investment Management	Invesco Perpetual
Aviva Investors	Investec Asset Management
AXA Investment Managers	J O Hambro Capital Management
BAE Systems Pension Funds Investment Management	JPMorgan Asset Management
Baillie Gifford & Co	Jupiter Asset Management
BlackRock Asset Management	Kames Capital
BP Investment Management	Kempen Capital Management
Capital International	Kleinwort Benson Investors
Cavendish Asset Management	Lazard Asset Management
Cazenove Capital Management	Legal & General Investment Management
CCLA Investment Management	Lofoten Asset Management
CFB Methodist Church & Epworth	Longview Partners
CPH Capital	M&G Investment Management
Daiwa SB Investments	Martin Currie Investment Management
Ecclesiastical Investment Management	MFS International
Ethos Foundation Switzerland	Montanaro Asset Management
F&C Investments	Morgan Stanley Investment Management
Fidelity Investments International	Nettle Capital Management
Gottex Fund Management	Newton Investment Management
Governance for Owners	Oldfield Partners
Hansa Capital Partners	
Harding Loevner	
Henderson Global Investors	

Pyrford International
RC Brown Investment Management
Royal London Asset Management
Russell Investments
Schroder Investment Management
Scottish Widows Investment Partnership
Standard Life Investments
SVG Investment Managers
T. Bailey Asset Management
T. Rowe Price International
The Co-operative Asset Management
Thomas Miller Investment
Threadneedle Investments
TOBAM
TT International
UBS Global Asset Management
UK Financial Investments
Unigestion
Universities Superannuation Scheme
Vanguard Asset Management
Walter Scott & Partners
Wellington Management
WHEB Asset Management
William Blair

Asset Owners

Alliance Trust
BBC Pension Trust
British Airways Pensions
British Coal Staff Superannuation Scheme
Environment Agency
Greater Manchester Pension Fund
Hermes Equity Ownership Services
Joseph Rowntree Charitable Trust
Lincolnshire CC
London Pensions Fund Authority
Marks & Spencer Pension Scheme
National Employment Savings Trust
NI Local Government Officers' Superannuation Committee
North East Scotland Pension Fund
PACE
Pension Protection Fund
RBS Pension Trustee
Royal Mail Pensions Trustees
RPMI Railpen
Scottish Life
Strathclyde Pension Fund
The Mineworkers' Pension Scheme
The Wellcome Trust

Service Providers

Aon Hewitt
ECGS
EIRIS
Glass Lewis
Institutional Voting Information Service
ISS
Manifest

Appendix 3

Detailed practical examples

Barclays plc

Background

At the Annual General Meeting on 27 April 2012, Resolution 2 on the Directors' Remuneration Report received 27 per cent votes against. Resolution 5 on the re-election of the Chair of Remuneration Committee, Alison Carnwath, received 21 per cent votes against. At the AGM, the Chairman, Marcus Agius, apologised for the bank's failure to communicate over remuneration issues. Prior to the AGM, the Chief Executive, Bob Diamond, and Finance Director, Chris Lucas, had agreed to receive half of their bonuses for 2011 until certain targets were met. The Chairman, Marcus Agius, and Chief Executive, Bob Diamond, were re-elected as directors of the company with 96 per cent (Resolution 3) and 99 per cent (Resolution 7) of votes in support, respectively.

On 27 June 2012 Barclays admitted to misconduct related to submissions for the London Interbank Offered Rate (LIBOR) resulting in the FSA imposing a £59.5 million fine and further penalties by the US Department of Justice.¹

On 2 July 2012 Marcus Agius announced his intention to resign as Chairman; however, he remained as acting Chief Executive following the subsequent resignation of Bob Diamond on 3 July 2012 as Chief Executive. The Chief Operating Officer, Jerry del Missier, resigned on 3 July 2012, and Alison Carnwath resigned on 25 July 2012. On 12 August, it was announced that Sir David Walker would be appointed Chairman. He undertook to recruit a new Chief Executive and to reform pay structures². On 30 August Antony Jenkins was appointed Chief Executive.

Objectives

Of the 54 respondents with a holding, 35 engaged with Barclays. Remuneration was the main concern for 25 respondents, seven of which also had concerns about leadership/succession planning (Chart I). To quote one's objective: "1. To convey views regarding remuneration, in particular the tax equalisation payment made to the CEO and the scale of bonus payments. 2. To convey views regarding the performance of the Chairman of the Remuneration Committee and to press

for a change of Chairman of this Committee. 3. To convey views regarding the need for board Chairman succession to be addressed".

A further four of these also raised the LIBOR investigation. To quote: "Explanations regarding the LIBOR scandal and assurances that the Company will turn the corner on culture, values and behaviours to minimise the risk of issues such as this happening again. Regarding culture, there is an opportunity to become more ethical, less greedy and more aware of their role in society".

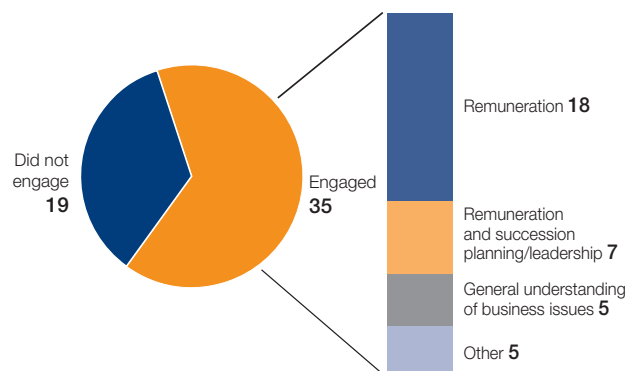
Five respondents wanted to understand the business better. Five "others" had varied objectives including to understand issues better, to rebuild trust and to gain an insight, and put across material concerns.

Four changed their holdings because of these issues, three making a small reduction, with one divesting completely.

Nineteen did not engage, reasons including:

- seven with an insignificant holding, two of which divested/reduced their holding.
- two that prioritised other matters.
- one that discussed the matter with the NAPF and took its lead.
- one that had a conflict of interest in that Barclays is a client and the holding was not significant.

Chart I: Engagement with Barclays – No. of respondents



¹ Justice.gov 12 June 2012

² BBC.co.uk 12 August 2012

Of the Service Providers, one engaged to confirm the facts and corroborate information. Four did not as this would be outside the remit of their service³.

Outcome

Eighteen of the 35 respondents that engaged achieved their objectives; seven on the basis Barclays changed its remuneration policy, though for some there were still outstanding issues. To quote:

- *“Yes and no; yes because the chair and CEO have left the company and there are now commitments to reduce the scale of the investment bank and reform remuneration, but no because significant progress is still required until we are fully satisfied.”*
- *“Although the Company made concessions (i.e. agreeing to defer 50% of the bonus and making this subject to further performance conditions), our concern was not addressed in full in that bonuses should have been significantly reduced and they weren’t. However, our concerns increased regarding the greed and culture of the company when the LIBOR scandal was announced and our underlying concerns [changes at board level] were largely dealt with without us having the opportunity to raise these.”*

Thirteen did not meet their objectives in that the changes were too moderate or only partially addressed their concerns.

One partially achieved its objectives in that the Chair of the Remuneration Committee changed in 2011, but was still not able to support the Remuneration Report⁴.

For 27 respondents engagement is on-going but for seven it is not⁵.

The Service Provider achieved its objective as it sought to confirm facts behind its research. It plans to continue to engage.

Details of engagement

Contact with Barclays

Respondents engaged extensively with Barclays; 31 respondents had a total of 209 contacts, an average of 6.7 each. Eight respondents each had ten or more contacts which frequently were with the Chairman and Company Secretary, although 18 also had contact with the Chair of the Remuneration Committee and Executive Directors (Table I). To quote: *“We had more than 10 contacts. Between 5-10 were with the Chairman, more than 10 with Executives, more than 10 with the Company Secretary and more than 10 with Investor Relations. More than 10 contacts were with Portfolio Managers/Analysts only and more than 10 were with Dedicated Specialists only”*.

Table I: Number of contacts and who with

	No. of contacts	No. of respondents
Chairman	58	21
Senior Independent Director	23	16
Remuneration Committee Chair	33	18
Non-Executive Directors	22	8
Executive Directors	41	18
Management	21	7
Company Secretary	72	19
Investor relations	34	9

Contact was mainly by portfolio managers/analysts and dedicated specialists separately although some did so jointly (Table II). One respondent’s portfolio managers/analysts had 28 contacts and noted that: *“senior management also became involved in this engagement”*.

Table II: Number of contacts and who by

	No. of contacts	No. of respondents
Portfolio managers/analysts only	71	14
Dedicated specialists only	110	21
Portfolio managers/analysts and dedicated specialists	52	16

³ These four are not represented in the practical examples.

⁴ Three did not state.

⁵ One did not state.

Four respondents did not provide details. Two do not record such details, one engaged through the NAPF and another noted that the: “[Manager] held a number of meetings and conference calls with the company over the course of the year ending October 2012. These included discussions with the Chair of the Remuneration Committee, the senior non-executive director, the company secretary, meetings with senior management including the CEO and various e-mail exchanges. The meetings covered a range of issues including remuneration, incorporation of risk in board decision-making, relationships with the regulators, the LIBOR scandal, performance of the company in particular in relation to returns, PPI payments and impact”.

The one Service Provider that engaged had five contacts with the Company Secretary, one of which included the Chairman.

Contact with other investors

Twenty five respondents collaborated with other investors. 19 had joint meetings with the company (Table III). Of the “other”, two: “Attended meetings hosted by the ABI as well as on-going discussions with other institutional investors”. Another: “... convened a well attended investor only group to discuss what the next steps should be on Barclays”.

All those that collaborated considered it helpful⁶, with 14 noting it gave a consistent and shared message to Barclays. As one stated: “the collaboration demonstrated to the company that there was broad agreement within the shareholder community and the collective influence brought to bear on the company probably accelerated the pace of change”.

Others commented that:

- efforts were coordinated allowing better access to information and better use of resources (three).
- combined holdings allowed higher level discussions than otherwise (three).
- collaboration provided a good “sounding board” to establish whether there were any other issues which should be addressed (two).

Table III: Collaboration

	No. of respondents
Joint meetings with the company	19
Collective agreement on how to vote	4
Other	10

The Service Provider did not collaborate.

2012 AGM

Two respondents attended the AGM.

Resolution 2, approval of the Remuneration Report

A number had extensive engagement and expressed concerns over the level of remuneration. Only six respondents voted in support of Resolution 2, the Remuneration Report (Table IV). Of these, one respondent voted in support, but voted against the re-election of the Chair of the Remuneration Committee, Resolution 5, due to poor communication and abstained on the re-election of the Chairman, Resolution 3, as he was also a member of the Remuneration Committee.

One respondent abstained as, “the Company confirmed that it would operate a normal limit of 5x salary and exceptional awards above this level would be subject to prior shareholder consultation”.

By far the majority, 24 respondents, voted against. To quote:

- “We had concerns about the Remuneration Report in regards to the level of disclosure; the excessiveness of the combined rewards paid and the lack of a link between pay and company performance.”
- “We do not believe the Remuneration Committee exercised sufficient discretion by granting substantial bonus awards to executive management for a year in which pre-tax profits and returns of risk weighted assets fell and the company continued not to cover the cost of its equity.”
- “We determined that performance targets were not stringent enough and did not align management and shareholder interests.”

⁶ Three did not explain why.

- *“After lengthy dialogue with members of the board (including the Chairman and Remuneration Committee Chairman) on remuneration and despite recent concessions made, [Manager] remained dissatisfied with the progress made on changing the bank’s remuneration practices - particularly in respect to the misalignment of distribution between shareholders and staff and considered an against vote was warranted.”*
- *“We have considered executive remuneration outcomes in respect of 2011 in the context of poor returns to shareholders and a disappointing share price performance. Following internal discussion we are of the view that the outcomes do not represent an appropriate link between pay and performance.”*
- *“The performance of the company for the year under review had been, in Mr Diamond’s own words, unimpressive and we were unable to reconcile the aggregate quantum awarded with the performance of the company.”*
- *“Our initial concern remained in that 200% out of a maximum bonus of 250% is too high when viewed in the context of shareholder returns. Therefore, deferring half the bonus, albeit with performance conditions, did not address our view that 200% is too much. The other point we made is that whilst deferral and further performance requirements are a good thing, executives are already well incentivised to reach the targets imposed on the deferral and all this will mean is that when and if the targets are met in 3 years time, not only will Bob be well paid under the incentive schemes but in addition, will receive a greater amount from a bonus that we did not believe should have been paid in the first place. This is why the gesture, though welcome, does not address our concerns.”*
- *“We voted against this resolution as result of not understanding how the bonus payments made to the top leadership of the bank could be justified, notwithstanding the late concession from the bank to underpin half the vesting of the award with the cost of capital. We were also concerned about the lack of reform of investment bank pay.”*

Nineteen of these also voted against or abstained on the re-election of the Chair of the Remuneration Committee and eight voted against or abstained on the re-election of the Chairman.

Resolution 3, to re-elect the Chairman, Marcus Agius

Twenty one respondents voted in support of the re-election of the Chairman, Marcus Agius. To quote: *“We felt able to support the Board as we believed they had given us sufficient justification for their decisions”.*

Ten respondents voted against or abstained on the re-election of the Chairman. Seven on the basis the board should be held accountable for remuneration issues and two as they had concerns over leadership. To quote:

- *“We considered a vote against the re-election of all Remuneration Committee members was appropriate in view of the concerns over the bank’s remuneration practices. We considered an abstain vote for the remainder of the board appropriate as they are also accountable for the operation of the bank.”*
- *“We voted against this resolution as we did not believe that the chair provided sufficiently strong leadership of the board. We had been voting against his re-election for several years.”*
- *“[Manager] had a number of persistent concerns regarding the ability of the remuneration committee, and the board as a whole, to ensure remuneration was aligned to the performance of Barclays. Through our discussions with Barclays, we discovered the whole board had the responsibility of approving the remuneration policy and payments to the executive. We believe directors need to be held accountable for their actions. Therefore, we took the unprecedented decision to: - Vote against the approval of the remuneration report (advisory vote). – Vote against all members of the remuneration committee. – Abstain on all other non-executive directors in recognition of their oversight of remuneration.”*

Resolution 5, to re-elect the Chair of Remuneration Committee, Alison Carnwath

Eleven respondents voted for the re-election of the Remuneration Committee Chair. One respondent voted against the Remuneration Report but supported the re-election of the Remuneration Committee Chair, stating: *"We regarded the company's approach to remuneration as unsatisfactory but we did not vote against the re-election of the Chairman of the Remuneration Committee because this was the first time we had voted against Barclays' remuneration report and as a generality we only oppose the re-election of Remco Chairs in the event of a second successive objection to the remuneration policies. At the time of the AGM we were supportive of the positions of both the Chairman and the CEO"*.

Twenty respondents voted against or abstained on the re-election of the Remuneration Committee Chair holding her accountable for the unsatisfactory resolution of remuneration issues; all but one of which voted against the Remuneration Report. To quote: *"We voted against this director because of our concerns about the company's remuneration practices and how the remuneration policy was implemented. We believe the Remuneration Committee did not exercise appropriate discretion and could have demonstrated more leadership in helping the company to achieve a more restrained executive remuneration that is better balanced with shareholder returns"*.

Resolution 7, to re-elect the Chief Executive, Bob Diamond

The re-election of the Chief Executive, Bob Diamond, was supported by nearly all respondents in that only one abstained. To quote:

- *"Resolutions 3 and 7. At the time of the AGM and prior to our knowledge of LIBOR rate fixing within Barclays we were of the opinion that Mr Agius and Mr [Diamond] were suitability qualified and effective in their respective roles of Chairman and CEO."*
- *"For Bob Diamond as we hold Marcus Agius to account."*

⁷ Four did not state if they voted on resolutions 2, 3 and 5.

⁸ Five did not state if they voted on resolution 7.

⁹ This relates to all other examples in this section of the report.

Table IV: Resolutions 2, 3, 5 and 7

	Resolutions			
	2 ⁷	3	5	7 ⁸
	No. of respondents			
For	6	21	11	29
Against	24	8	18	–
Abstain	1	2	2	1

The Service Provider does not vote on its own behalf.

Conflicts

Six of the 35 respondents that engaged noted a conflict of interest. Five had a business relationship with Barclays, such as fund distribution or Barclays was a client. These conflicts were addressed by:

- the corporate governance team being independent of the investment team or other relevant team such as funds network (two).
- reporting to compliance and considering when deciding how to vote (one).
- one through: *"the application of our published Corporate Governance and Corporate Responsibility Voting Policy, transparency of reporting to clients, direct disclosure of significant conflicts of interest to clients and seeking explicit instructions from clients when necessary. We may also use "Chinese walls" to control the exchange of information between relevant personnel and use stop lists to prevent dealing in certain securities"*.
- requiring any voting decision to be independent of the conflict (one).

For the sixth, the conflict arose as a board member of the sponsoring pension scheme was a director of Barclays. It engaged but the shares of the sponsoring scheme were not voted.

One Service Provider had a potential conflict and operates a firewall that separates the proxy research function, such that the research team prepares analysis and vote recommendations independently⁹.

WPP plc

Background

At WPP's 2 June 2011 AGM, Resolution 2, approval of the Remuneration Report, received 42 per cent votes against. Subsequently WPP sought to award a 30 per cent increase in its Chief Executive's, Martin Sorrell's, base salary for 2012¹.

At the AGM in Dublin on 13 June 2012 Martin Sorrell faced criticism for "excessive" remuneration from a number of voting agencies and the Association of British Insurers. Resolution 2, approval of the Remuneration Report, received 60 per cent votes against. Resolution 14 the re-election of Jeffrey Rosen, Chair of the Remuneration Committee, received 22 per cent votes against. Resolution 16, the re-election of Martin Sorrell, received 98 per cent votes in support. In response, WPP announced on its website that the Board: "take the Remuneration Report vote seriously, will consult with many share owners, and will then move forward in the best interests of our share owners and our business".

Objectives

Twenty four of the 46 respondents with a holding engaged. For 18 respondents the main issue was remuneration (Chart II). Three wanted to understand the company's compensation practices, one considered levels were too high and 14 wanted changes, many of which provided suggestions to WPP. To quote:

- "We wanted to provide suggestions to WPP's management about a compensation plan that would better align Mr. Sorrell's economic interests with shareholders."
- "We do not believe that such an incentive structure is appropriate for WPP given the nature of the business and has long outlived its purpose of

encouraging significant executive shareholding in the company. We also questioned the need for a significant increase in quantum of fixed and variable pay available to the CEO and wished to establish the rationale behind the remuneration committee's decision as well as the remuneration committee's ability to exercise control over executive pay at WPP."

One also wanted to understand succession planning ahead of the AGM noting: "*It coincided with an increase in our share position. We wished to discuss some planned remuneration changes including some significant salary increases, and sought assurance that succession planning matters were in hand*".

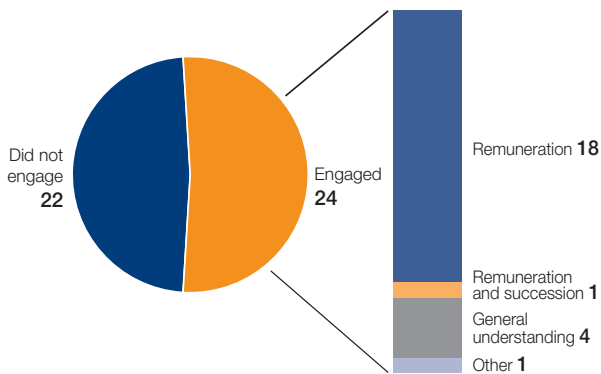
Three wanted to understand the business and its long term strategy and another to inform of its vote against.

Two changed their holding as a result of the issues, one increasing and the other reducing.

Twenty two did not engage, the reasons including:

- eleven with an insignificant holding, one of which divested during the period.
- four that did not consider there were any issues, with one stating: "*We believe that Martin Sorrell is woefully underpaid and we voted in favour of the remuneration report*" and another: "*We did not have a problem with the increase in Sir Martin Sorrell's pay package, given his involvement in forming the company and in its on-going management*".
- one that had advised the company of its views in the past and another that did not expect the company to change its views.
- three held the shares in funds where they do not engage.

¹ Guardian.co.uk 13 June 2012

Chart II: Engagement with WPP – No. of respondents

Only one Service Provider had an interest and engaged to confirm facts and corroborate information. Another did not have an interest but noted: *“Our clients directly engaged with the company based on our recommendations. We had expressed our concerns over the remuneration both in our public report on European remuneration and in our research report prepared for our clients only”.*

Outcome

Eleven out of the 24 respondents that engaged achieved their objectives; five gaining a better understanding of their issues, for example:

- *“After several discussions, we achieved the aim of gaining a better understanding of the board’s rationale for making changes to executive remuneration practices.”*
- *“It gave us a better understanding of their business model, drivers of growth and their strategic objectives.”*

Whatever the true nature of the Board’s relationship with the Chief Executive, one respondent alleged that its own strong opinion about that relationship was widely held: *“It confirmed my view that they are completely at the beck and call of the CEO. They [Directors on the Remuneration Committee] even stated that he doesn’t behave as if he only owns 2% of the company - he behaves as if [he] were the sole owner, to which everyone in the room stated - that is the problem!”*

Other comments included:

- able to offer an alternative remuneration plan or the company had adopted its suggestions (two).
- secured arrangements to engage the Chairman later in the year to address succession planning (one).
- the increase in pay was reduced (one).
- received an explanation for the salary increase which was acceptable. However, the explanation, that directors’ other commitments and residences meant that it was hard for them to attend [board] meetings, was not acceptable (one).

However, 13 did not achieve their objectives; six still had concerns that there were insufficient changes. For example:

- *“The engagement process was unsatisfactory and the outcome was unacceptable to us as shareholders. The widespread media coverage was damaging to the company’s reputation and to that of individual board members. We voted against the Remuneration Report.”*
- *“Remuneration levels further increased in 2012 despite a significant vote against in 2011. Hence, despite obvious investor discontent and discussions with the company to address these, the Company has not listened.”*
- *“While the company rowed back on the level of increase to the CEO’s salary from 50% to 30% over the year this still failed to allay our concerns around both the quantum and the timing of the awards, and indeed sent some further uncomfortable messages about broader governance issues at the company as well.”*

For two it was too soon to conclude in that they are continuing their dialogue, and another that it was *“... stone walled by the company and made our concerns clear via the media”.*

For seventeen respondents engagement is on-going.

The Service Provider achieved its objective as it sought to confirm facts behind its research.

Details of engagement

Contact with WPP

Twenty two respondents had a total of 69 contacts, an average of 3.1 each, with one having ten contacts mainly with the Chairman and management. Contact tended to be with the Chairman and investor relations, although the Chair of the Remuneration Committee and management were also points of contact (Table V). To quote:

- *“The Head of Reward was involved in all six meetings/calls, either on its own, with the Chairman, with the Remuneration Committee Chairman, or both.”*
- *“[Manager] held another meeting with WPP’s CEO to discuss executive remuneration on October 22nd and will meet with the Chairman and the Chair of the Remuneration Committee in November 2012.”*

Table V: Number of contacts and who with

	No. of contacts	No. of respondents
Chairman	17	8
Senior Independent Director	–	–
Remuneration Committee Chair	14	8
Non-Executive Directors	–	–
Executive Directors	9	6
Management	13	4
Company Secretary	9	8
Investor relations	13	8

Contact was mainly by the portfolio managers/analysts and dedicated specialists separately (Table VI). One, where dedicated specialists had contact with investor relations, noted: *“We hold WPP in index funds only, so not a stock that our fund managers would actively engage on”*.

Table VI: Number of contacts and who by

	No. of contacts	No. of respondents
Portfolio managers/analysts only	22	9
Dedicated specialists only	22	10
Portfolio managers/analysts and dedicated specialists	12	6

Two did not provide details, one stating: *“We had several meetings with the company and we collaborated with other investors”*.

The Service Provider had eight contacts, mainly with management, although it also had contact with the Chairman, the Chair of the Remuneration Committee and the Company Secretary.

Contact with other investors

Nine respondents collaborated with other investors, with six attending joint meetings with the company (Table VII). Of the others, one shared analysis and two participated in calls where a number of investors made their views clear.

All considered collaboration helpful, mainly as it provided a consistent message to the board and reinforced the level of disapproval. In particular, one did not consider it had a large enough holding to be heard on its own and another considered it helpful to understand different perspectives.

Table VII: Collaboration

	No. of respondents
Joint meetings with the company	6
Collective agreement on how to vote	1
Other	3

The Service Provider did not collaborate.

2012 AGM

None of the respondents attended the AGM in June 2012 in Dublin.

Resolution 2, approval of the Remuneration Report

Only four respondents voted in support of the Remuneration Report, Resolution 2 (Table VIII). To quote:

- *"If we have confidence in management, usually shown by having an investment in the first place, we vote in line with management's recommendations, usually in favour."*
- *"Relative to the UK marketplace, the chief executive's pay opportunity appears high, but relative to the company's global competitive set, it's toward the lower end, especially compared to US peers. In our view, the company's unique share-matching program offers incentives that are in sync with shareholder interests."*
- *"We supported the company, as we felt that executive remuneration (main discussion point) was designed in [a] way that links pay and performance, while minimizing the potential for rewarding failure. Furthermore, its design facilitates the achievement of strategic objectives, with the ultimate goal of creating shareholder value. Furthermore, a significant percentage of the remuneration is skewed towards long-term share-based pay."*
- *"We intended to vote ABSTAIN on the Remuneration Report as salary of Chief Executive Officer increased by 30% and his annual bonus opportunity increased from 3x to 5x salary without adequate justification. His salary was significantly above upper quartile for both the FTSE 100 index and the FTSE 100 Media sector. Abstain as all other elements of Remuneration acceptable. The company explained that he had received only 2 salary increases in the last 10 years and due to the international nature of the company, FTSE companies were not appropriate comparators. We therefore decided to vote FOR."*

The majority, 19 respondents, voted against the Remuneration Report. To quote:

- *"Resolution 2 on 2 June 2011 AGM: Against (A vote AGAINST the remuneration report is warranted. Significant basic salary increases have been provided to two Executive Directors and the bonus opportunities have been increased for two Executive Directors without sufficient justification in the remuneration report.) Resolution 2 on 13 June 2012 AGM: Against (A vote AGAINST approval of the remuneration report is warranted. The substantial enhancement of the CEO's remuneration package arises from a 30 per cent increase in salary and a more than doubling of the value of his annual bonus opportunity.)"*
- *"We were concerned about the increase in bonus opportunity and pension allowance for the CEO which was not consistent with our guidelines or with the spirit of the ABI's Principles of Remuneration."*
- *"In summary, arrangements were already too generous (we have voted against the remuneration report for a number of years) and we simply do not agree with the company's view that the increases are required so the company remains competitive with its global peers. We have some sympathy to the company's view that when considering benchmarks, WPP must be recognised as a highly successful, global company with the vast majority of its business and more than 90% of its employees being outside the UK, and all of WPP's natural comparators are based in the U.S., Europe and Asia. There simply are no relevant local UK comparators (i.e. two of WPP's closest comparators, Omnicom and Interpublic, are US-based and US-listed). However, the Company chooses to list in the UK so it has to be mindful of UK practice and UK shareholder views, particularly as there was a significant vote against the remuneration report last year. Our view is that US pay in particular is excessive and it is not in shareholders' interests to approach pay this way."*

Resolution 14, to re-elect Jeffrey Rosen, Chair of the Remuneration Committee

Ten respondents voted in support of the re-election of the Chair of Remuneration Committee, Jeffrey Rosen. Six of these voted against the Remuneration Report, but as one noted: *“The company’s approach to remuneration was not consistent with our guidelines. We supported the re-election of Jeffrey Rosen because we had supported the company’s remuneration vote in 2011 and we have a general policy of supporting the re-election of the Chairman of the Remuneration Committee unless we are voting against the report of the Remuneration Committee for a second time”*.

Another stated: *“For (In the absence of evidence to the contrary, the board of directors is in the best position to recruit individuals who will best contribute to the job of electing and monitoring a strong management team)”*.

All those that voted against Rosen’s re-election also voted against the Remuneration Report. Some clarified:

- *“Perception that the Board and the Remuneration Committee were not paying due attention to shareholder concerns expressed in a large “against” vote at 2011 AGM and the follow-up engagement.”*
- *“We do not consider that the Committee has represented well the interests of shareholders and we would observe that the vote on resolution 2, to approve the Remuneration Report, is an advisory vote.”*
- *“We were unable to support the re-election of the non-executive director, having lost confidence in his understanding of the role.”*

The two that abstained also voted against the Remuneration Report; one had material concerns about the Remuneration Committee’s strategy and the other stated: *“Compensation Committee members - we abstained to emphasise our concern over the handling of compensation policies and practices and to encourage the committee members to take a more robust approach in the future”*.

Resolution 16, to re-elect the Chief Executive, Martin Sorrell

All respondents voted in support of the re-election of Martin Sorrell, although many criticised his pay package. For example: *“We voted in favour of the re-election of Mr Sorrell as we considered him to be a highly effective CEO for WPP who we supported continuing in the role, however, our vote against the remuneration report demonstrated that we did not consider this to be at any cost”*.

Table VIII: Resolutions 2, 14 and 16

	Resolutions		
	2	14	16
	No. of respondents ²		
For	4	10	22
Against	19	10	–
Abstain	–	2	–

One respondent also noted how it voted on other resolutions: *“5) FOR. Re-elect Esther Dyson as a Director - FOR the re-election of a Non-Independent Non-Executive Director due to tenure since 1999, (overlapping with CEO), who was a member of the Remuneration Committee which should be wholly independent. The company has confirmed that she’ll be stepping down from this Committee before the next AGM. We could therefore vote FOR and review next year. 8) ABSTAIN. Re-elect Ruigang Li as a Director. ABSTAIN on the re-election of a Non-Executive Director who attended 3 out of 7 board meetings last year without adequate explanation. Attendance was well short of our 75% threshold. 10). AGAINST. Re-elect Koichiro Naganuma as a Director. AGAINST the re-election of a Non-Executive Director who attended 1 out of 7 board meetings last year without adequate explanation. Attendance was well short of our 75% threshold”*.

The Service Provider does not vote on its own behalf.

Conflicts

One respondent noted a conflict of interest at senior executive levels. It: *“informed the company in advance of our engagement over the year of the relationship and pursued our engagement with the same rigour as we would have done without this relationship”*.

² One did not state if it voted for Resolution 2, and two did not state for Resolutions 14 and 16.

G4S plc

Background

On 17 October 2011 G4S announced the proposed acquisition of ISS A/S, a Danish company, for approximately £5.2 billion. It also announced a 7 for 6 rights issue at 122p to raise approximately £2 billion to pay for the acquisition. The acquisition and rights issue were subject to shareholder approval at a General Meeting scheduled for 2 November 2011.

A number of shareholders had concerns over the price of the deal and registered votes against¹. As a consequence on 1 November 2011 G4S announced that it would cancel the deal².

On 13 January 2012 G4S announced that the Chairman, Alf Duch-Pedersen, would retire during 2012 once his successor had been identified³.

At the 7 June 2012 AGM, Resolution 2, approval of the Directors' Remuneration Report, received 99 per cent of votes in support. This followed Chief Executive, Nick Buckles, waiving his £750,000 bonus in March voicing regret over "wasting £50m on the deal which did not happen⁴". Resolution 4, the re-appointment of Nick Buckles, received 99 per cent votes in support. In May 2013, Nick Buckles announced he would be standing down.

Objectives

Nineteen of the 32 respondents with a holding engaged with G4S, together with two that did not have a holding. The majority, 16 respondents, wanted to discuss the proposed acquisition of ISS (Chart III). Nine of these wanted to understand the rationale for the deal, in one case seek an improved offer for shareholders and seven to oppose the deal. To quote:

- *"Expressed opposition to the deal to the company and it was subsequently dropped. The shares recovered from the fall that happened when the deal was announced."*

- *"Having been unable to gain sufficient assurances around the strategic rationale as well as the potential risk exposure of the ISS acquisition we wanted the company to withdraw from the transaction. Subsequent to the failure of the acquisition we wanted to ensure both appropriate accountability as well as receive reassurances around the company's desire to return to its previously stated strategy. We also engaged with the company on its CSR activities, particularly focussing on the integration of its CSR risks within its mainstream reporting, and pressed the company to integrate the two better given the size of the relevant risks it faces. We also want to see improvements in the company internal reporting systems to give it a better understanding of these risks."*

Others wanted to:

- address remuneration and that one director sits on too many boards.
- inform the company of their voting intention.
- gain comfort that the high profile concerns were being addressed.
- understand the business model and driver behind growth⁵.

Thirteen did not engage, reasons including:

- four with an insignificant holding.
- two that did not consider there were any issues.
- three held the shares in funds where they do not engage.

One respondent increased its holding as a result of these issues.

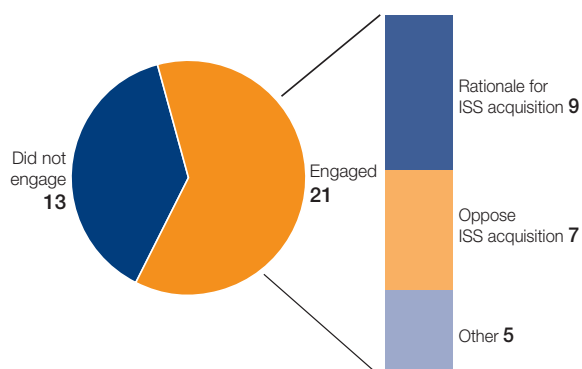
¹ Telegraph.co.uk 31 October 2011

² G4S.us announcements 1 November 2011

³ G4S.us announcements 13 January 2012

⁴ Guardian.co.uk 13 March 2012

⁵ One covered ESG themes.

Chart III: Engagement with G4S – No. of respondents

Only one Service Provider had an interest and engaged to confirm facts and corroborate information.

Outcome

Seventeen of the 21 respondents achieved their objectives⁶. Seven gained a better understanding of the proposed acquisition or communicated their view⁷. Seven wanted to stop the deal, to quote:

“We stopped the deal. We communicated concerns to the company’s advisers and the company’s executives. Following the deal failing, we met with the chairman and SID. They apologised. Compared with some other companies, that was impressive. They were also constructive when we suggested new board members. We anticipate an orderly consideration of the role of the CEO and transition, if necessary.”

“The company withdrew from the ISS acquisition, although our engagement on accountability and strategy subsequent to this is on-going.”

Three respondents did not achieve their objectives. For one this was because at the time the deal was still going ahead; and another had not been reassured by the company and had voted against the share issue⁸.

For eleven respondents engagement is ongoing.

The Service Provider achieved its objective as it sought to confirm facts behind its research.

⁶ One did not state.

⁷ Two did not state.

⁸ One did not state.

Details of engagement

Contact with G4S

Nineteen respondents had a total of 96 separate contacts, an average of five each. One respondent noted a total of 28 contacts, 20 of which were with investor relations. Investor relations was contacted the most times overall, although more respondents had contact with Executive Directors (Table IX).

Table IX: Number of contacts and who with

	No. of contacts	No. of respondents
Chairman	21	9
Senior Independent Director	5	5
Remuneration Committee Chair	–	–
Non-Executive Directors	4	2
Executive Directors	35	14
Management	5	2
Company Secretary	2	2
Investor relations	45	11

Contact was predominantly by portfolio managers/analysts, as it centred on the proposed acquisition as opposed to a governance issue (Table X). One respondent also noted that its portfolio managers spoke to G4S’s advisers about the deal.

Table X: Number of contacts and who by

	No. of contacts	No. of respondents
Portfolio managers/analysts only	47	14
Dedicated specialists only	14	4
Portfolio managers/analysts and dedicated specialists	20	5

Two respondents did not provide details, one as it does not record them; the other: *“wrote to the Company Secretary prior to the vote to explain to them the rationale for not supporting a number of the resolutions at the AGM”*.

The Service Provider had three contacts between its dedicated specialist and the Company Secretary.

Contact with other investors

Eleven respondents collaborated, four having joint meetings with the company with one noting: *“Along with other institutional investors we met the chair of the CSR committee as well as a number of other company representatives”* (Table XI). Of the others, one ran an engagement program on behalf of a group of asset owners, although it was not a holder, three liaised with other shareholders to confirm views, and another wrote a joint letter to G4S. All considered collaboration helpful in that it reinforced their concerns.

Table XI: Collaboration

	No. of respondents
Joint meetings with the company	4
Collective agreement on how to vote	2
Other	5

The Service Provider did not collaborate.

2012 AGM

None of the respondents attended the AGM.

Resolution 2, approval of the Remuneration Report

Twelve respondents voted in support of Resolution 2, the Remuneration Report (Table XII). Seven commented that this was as the CEO had waived his bonus in recognition of the failed ISS transaction. To quote:

- *“We supported the freeze of base salaries for 2012 and were in agreement with the Remuneration Committee that, in light of a number of factors affecting the Group in 2011, it would not be appropriate to consider the payment of an annual bonus for the Directors for the year. We had no material issues with the bonus and LTIP performance targets.”*

- *“Regarding remuneration, we had concerns over executive arrangements for 2011 which were flagged in our voting stance for the 2011 AGM. However, this year we note a number of positive practices and developments which has led us to support. No bonus was paid for 2011 (the RemCo and Directors agreed that this was not appropriate in light of a number of factors affecting the Group in 2011), the freezing of salaries for 2012 (the CEO’s salary remains at £830k), the reversion of the annual bonus pay-out scale to the pre-2011 levels, and in respect of the LTIP awards made from 2012 onwards, half of the awards will vest subject to EPS performance and half will now be based on TSR performance. The Committee believes that this will help to address the concerns expressed by some shareholders about over reliance on EPS as a measure of underlying performance. We welcome this move. Furthermore, this year the fund managers actually think the EPS numbers (real average annual growth of 4% to 11%) are reasonably challenging (particularly at the higher end).”*

Only three respondents voted against, one stating: *“We abstained on the company’s remuneration report for 2011. We note that no bonuses were awarded for 2011, which we believe was the correct course of action. However, our abstention reflects our concern that the EPS performance conditions in the LTIP are not sufficiently challenging. We would therefore encourage the company to revisit the conditions in the current executive remuneration strategy”.*

Four did not vote, of which two did not have a holding in G4S and could not vote, and a further one had divested before the AGM.

Resolution 4, to re-elect the Chief Executive, Nick Buckles

Fourteen respondents voted in support of the re-election of the Chief Executive, Nick Buckles. To quote:

- *“We noted that the CEO had waived his bonus for the year and all things considered felt that he was still the best person to be running the company.”*
- *“Resolution 4 At the time of the AGM we were unaware of the failures of Mr Buckles as CEO and G4S in delivering on its contracts and considered a vote in favour to be appropriate.”*

Table XII: Resolutions 2 and 4

	Resolutions	
	2	4
	No. of respondents ⁹	
For	12	14
Against	3	2
Abstain	1	–
Did not vote	4	4

The Service Provider does not vote on its own behalf.

Conflicts

Two respondents noted a conflict of interest. One *“Agreed to underwrite the share issue but subsequently became concerned about the scale of the issue and the associated debt facility. We voted against the deal at the EGM. Had the share issue proceeded we would have been remunerated for the underwriting”*. This was resolved as the issue was cancelled. The other: *“As significant investors, we were made ‘inside’ one week ahead of the deal”* and as such restricted trading to deal with the conflict.

⁹ One did not state if it voted.

Xstrata plc

Background

Xstrata's 2011 Annual Report noted that "the most significant issue before the Board in 2011 was a proposal received from Glencore, Xstrata's largest shareholder, for an all-share merger of the two companies. Following careful consideration, the independent directors of the board have unanimously recommended the proposal to shareholders"¹.

Glencore owned 34 per cent of Xstrata. The merger required 75 per cent of Xstrata shareholders, excluding Glencore, to vote in favour. Shareholders had concerns over the terms of the merger, as well as executive remuneration², and a shareholder meeting planned for 12 July was delayed to allow the terms to be renegotiated.

At the AGM on 1 May 2012, Resolution 3, to approve the Directors' Remuneration Report, received 37 per cent votes against. This reflected concerns that long-term incentive plans would vest once the proposed merger with Glencore had gone ahead³. There were also significant votes against the reappointment of two directors. Resolution 7, to re-elect Ivan Glasenberg, and Resolution 14, to re-elect the Chairman of the Remuneration Committee, David Rough, received 14 per cent and 19 per cent votes against, respectively. This was on the basis that they were not considered independent. In particular, Ivan Glasenberg was also Chief Executive of Glencore.

Delays to the deal were caused by one major shareholding building its stake in Xstrata and demanding an increase to the offer. Investors defeated a plan to increase incentives for Xstrata executives, with 32 per cent failing to back a proposal that needed 75 per cent of votes in support. A second resolution asking investors to back a takeover without the pay scheme received 79 per cent of votes in support, over the 75 per cent threshold for the deal to be approved. After the terms of the deal were approved, Sir John Bond, Chairman of Xstrata, announced his resignation⁴.

Objectives

Thirty-two of the 45 respondents with a holding engaged with Xstrata, together with one that did not have a holding (Chart IV). For 27 the main focus was the proposed merger, with some concerns related to the terms of the deal, the retention packages and resulting governance. To quote:

- *"We initially engaged with the company to hear their view on how they found the initial Glencore merger terms satisfactory and to share with them our disagreement."*
- *"To understand the rationale for the proposed transaction; highlight our concerns about execution risks, to ensure the proposed transaction was in the interests of Xstrata shareholders; and the removal of remuneration arrangements not in the interests of shareholders."*
- *"Discuss the economic rationale behind the Glencore/Xstrata merger, gain a better understanding of the proposed governance arrangements for the combined entity, and discuss the proposed incentive arrangements for members of Xstrata's management and Xstrata senior employees. In addition, we engaged Xstrata on its approach to managing the human rights and security risks it faces when operating in high-risk and conflict-affected countries, e.g. Philippines, Colombia."*
- *"The engagement objective was to convey our concerns that i) the deal did not provide sufficient value for Xstrata shareholders; ii) we needed to be convinced that management incentives were truly aligned with the interests of long-term institutional shareholders; and iii) we believe the widespread views of shareholders were not being listened to by management and the Board needed to act upon this."*
- *"We held three meetings with Xstrata management and two meetings with Glencore's management during the course of this year. We sought to improve our understanding of the merger and address some of our concerns."*

¹ Xstrata annual report 2011.

² Telegraph.co.uk 27 June 2012.

³ Guardian.co.uk 1 May 2012.

⁴ Guardian.co.uk 20 November 2012.

- *“Pre-announcement of the proposed merger with Glencore, we met with the company to give our views on remuneration arrangements. We only have small active holdings in Xstrata but have kept a very close eye on developments and engaged with the company on 1 Nov 2012. This meeting was to receive an update on the deal and the proposed pay arrangements.”*

Two focused on board composition and three others wanted to:

- improve understanding of the business.
- improve shareholder value.
- inform of their voting intention.

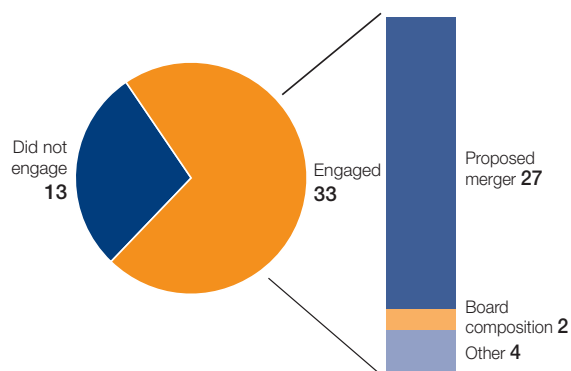
Four reduced their holdings and a further two divested completely as a result of these issues. To quote:

- *“Our interest was reduced after the initial engagement with the company and largely sold out of after the second engagement.*
- *“A decision was taken by the equity, commodity and responsible investment teams to sell out of our holding of Xstrata as our concerns were not alleviated through engagement and we felt this would be the most prudent course of action.”*
- *“Our shareholding in Xstrata fell materially during the course of the offer period although this was due to a combination of factors in addition to the matters which were under discussion with the company.”*
- *“We were shareholders of Xstrata leading up to the original offer made by Glencore in mid-February. However, based on the how the transaction was delivered and our outlook for commodity prices, we reduced our positions in Xstrata significantly over the course of February. In several funds, this position was reduced to zero.”*

Thirteen respondents did not engage, reasons including:

- eight with an insignificant holding, one of which divested during the period and one which engaged with Glencore.
- one held the shares in funds where it does not engage.
- one wanted to take an independent view.
- one was waiting to see the outcome of the proposed Glencore merger.

Chart IV: Engagement with Xstrata – No. of respondents



Two Service Providers engaged, one to confirm facts and the other to gain information on strategy and potential consequences of the merger with Glencore.

Outcome

Twenty three respondents achieved their objectives. For ten as the terms of the deal improved, for example: *“the offer for Xstrata shareholders has been improved and the remuneration arrangements are now subject to performance conditions and a separate vote; giving shareholders a real choice when casting their vote.”*

Nine expressed their concerns through their engagement or gained a better understanding of the business and/or the company's perspective on the merger, for example: *"better understanding of the merits of the proposal - articulated our concerns regarding the management incentives associated with the deal - articulated longstanding concerns regarding executive remuneration"*.

Seven respondents, however, still had reservations:

- *"Yes - to a certain extent. On the merger, main concern with merger were management incentive arrangements - after several rounds of discussions with shareholders, including [Manager], incentive arrangements got changed from cash to shares, and were made subject to the fulfilment of certain performance conditions. Moreover, the vote on these arrangements was de-coupled from the vote on the merger. Positive outcome on security and human rights - company has overall good policies and procedures but still facing significant challenges in implementation. Will continue to ask to improve practices and performance."*
- *"Partly. We gained a better understanding of the transaction. The company's response on remuneration did not alleviate our concerns."*
- *"We believe that the revised offer that Glencore provided was more reflective of our value of Xstrata. However, we continue to have concerns with the retention package, which although adjusted, continues to be excessive."*
- *"Only limited improvements achieved. With changes to management structure, an improved terms for Xstrata shareholders, and further votes on remuneration."*
- *"We encouraged amendment to the incentive proposals which were proving to be contentious and the board responded. The voting structure was also later amended but the complexity of the revised structure was not ideal."*

- *"We did achieve what we wanted to with regard to the terms of the merger. However we did not with regard to remuneration. The remuneration consultation initiated in 2011 did not proceed following the announcement of the possible merger."*
- *"Yes and no. Engagement was helpful to better understand the status of the deal and we welcome the company giving shareholders an opportunity to vote on remuneration arrangements. However, the voting on the deal and remuneration has been made overly complicated and we still don't believe in retention payments - they don't work and quantum still feel high."*

Nine respondents did not achieve their objective, reasons including:

- Xstrata did not respond to the engagement (one).
- still had concerns about and remained unconvinced on the merits of the deal (three). To quote: *"Remained uncomfortable regarding the process prior to the recommendation, the decision to offer 'retention' packages, unconvinced on merits of the deal,"* and *"The board and management failed to assuage our concerns, to address the issues which we consider critical, and persisted in persevering with the planned merger which we were unsupportive of."*
- on-going concerns and as such continuing engagement (two). To quote: *"Whilst we were successful with others defeating the original merger plan, even if the merger proceeds we will engage with the merged entity on appropriate management of the assets",* and *"It's really too soon to determine whether our engagement with Xstrata has been successful or not. The company has decided to proceed with the merger with Glencore which is a positive from our perspective although this has yet to be approved by shareholders but the retention arrangements remain in place. As indicated above, we feel that further Board change may well be necessary in the event that the merger proceeds meaning that our engagement with Xstrata is still very much work in progress."*

A further one stated: “Given the size of our holding it is a difficult challenge to fully achieve our objectives as a minority shareholders. However, there are positive elements in raising the concerns over the merger ratio and the management incentives as this ultimately contributed to the wider push from shareholders regarding the merger ratio and the appropriateness of the management incentives”.

For twenty one respondents engagement is on-going.

The Service Providers achieved their objectives, one as it sought to confirm facts behind its research.

Details of engagement

Contact with Xstrata

Of the 33 respondents that engaged, 29 had a total of 136 contacts with the company, an average of 4.7 each. The Executive Directors and investor relations were contacted the most. Over a third also had contact with the Chairman and Senior Independent Directors (Table XIII). In addition, others met or approached:

- Xstrata’s public relations agency (one).
- Xstrata’s advisers (two): “*These engagement statistics do not include our extensive contacts with company’s advisors during this period. Direct contact with the company was complicated by the fact that it was in an extended offer period and so all company contact with investors was heavily circumscribed by the Takeover Panel*”.
- the CEO of Glencore (one).

Table XIII: Number of contacts and who with

	No. of contacts	No. of respondents
Chairman	28	13
Senior Independent Director	21	12
Remuneration Committee Chair	8	6
Non-Executive Directors	4	1
Executive Directors	43	19
Management	14	9
Company Secretary	10	8
Investor relations	33	12

Contact was predominantly by portfolio managers/analysts as it centred on the proposed merger as opposed to a governance issue (Table XIV).

Table XIV: Number of contacts and who by

	No. of contacts	No. of respondents
Portfolio managers/analysts only	50	18
Dedicated specialists only	41	11
Portfolio managers/analysts and dedicated specialists	44	14

Three respondents did not provide details, but explained:

- engagement carried out through the NAPF.
- “*We have made our views known. There is, for now, little to be said. Engagement has been offered by the company but we have done all we can.*”
- “*Meetings were held with various board members, members of management, advisory firms and other shareholders to discuss the terms of the merger and proposed remuneration arrangements.*”

The two Service Providers had a total of 13 contacts, five being with the Senior Independent Directors and investor relations.

Contact with other investors

Twenty two respondents collaborated. 12 having joint meetings with the company (Table XV). Others collaborated:

- through the NAPF (one).
- by phone or email (three).
- with Xstrata's second largest shareholder and expressed concerns to other investors that the governance issues were not limited to remuneration but centred on who was the best steward of the company's assets (one).

All but one respondent considered collaboration helpful, reasons including:

- made progress or learnt useful lessons.
- achieved a common understanding between investors of the issues (two), although another noted: *"that there was a range of views about the benefits of the merger. There was not a totally common approach on all issues of the deal"*.
- gave a consistent message to the Board (seven), although one noted: *"The complexity and variety of issues to be considered meant that on individual issues there was not always agreement amongst the major investors participating but collective discussion with the Chairman ensured all issues were raised in one forum and were conveyed to the board via the Chairman for consideration"*. Another stated: *"In one sense the collaboration with other shareholders was helpful in that it maximised pressure on the Xstrata Board to respond to the governance concerns surrounding the retention payments in particular, but on the other hand it must be recognised that there was a wide spectrum of shareholder views on the merger itself so collaboration with other shareholders on this matter was not very productive"*.
- the size of holding did not justify a one-on-one meeting.

The one that did not find collaboration helpful did not want the deal to go ahead.

Table XV: Collaboration

	No. of respondents
Joint meetings with the company	12
Collective agreement on how to vote	1
Other	9

The Service Providers did not collaborate.

2012 AGM

None of the respondents attended the AGM in May of 2012.

One voted against all three resolutions as it wanted: *"To prevent the share issue from proceeding until the terms were improved"*.

Resolution 3, approval of the Remuneration Report

Only three respondents voted in support of Resolution 3, the Remuneration Report (Table XVI). One considered the AGM was only a minor part of engagement given the merger.

The majority, 24 respondents, voted against the report. To quote:

- *"Longstanding concerns over exceptional payments made under existing schemes; egregious termination payments for the CEO; concerns over alignment; concerns that all outstanding awards would vest in the event of the merger with Glencore"*.
- *"Concern over remuneration structures. The company's LTIP allows for 50% vesting for the attainment of threshold performance and shares vest in full on a change of control without reference to performance"*.

- *“Contractual termination provisions have the potential to lead to payments well in excess of one year’s basic salary, given that pension payments (190 per cent of basic salary for the CEO for 2011) and bonus (maximum 300 per cent of basic salary) are included within the calculation. In addition, this year’s remuneration report confirms that the CEO of Xstrata Zinc would receive a termination payment higher than what was previously disclosed. LTIP awards made to all three Executive Directors during 2011 and 2012 again exceeded the normal maximum limit under the plan. The exceptional circumstances justifying awards at this level have not been outlined in the remuneration report. The 2012 grant was made shortly after the announcement of the merger with Glencore. Completion of the deal will lead to full vesting of all outstanding awards regardless of whether or not the performance conditions have been satisfied.”*
- *“We have concerns over the high quantum of pay and potential pay (particularly given that significant award multiples are driven off high positioned based pay). In addition, provisions for termination under directors’ service contracts exceed one year’s remuneration which we do not support. Furthermore, termination payments (paid in lieu of notice and not if contracts are terminated for cause) include 100% of basic salary, pension and other benefits as well as the previous year’s bonus. For these purposes, annual bonus is capped at 300% of basic salary.”*
- *“Examination of the remuneration report highlighted a number of concerns: There were clauses allowing disproportionately high termination payments. There was a lack of clarity around the circumstances to justify the magnitude of LTIP awards and the low threshold for these awards.”*

Three abstained on the report:

- one still had reservations about several aspects, but anticipated a review of the policy.
- another had voted against on a number of occasions, but abstained as certain awards had been deferred.
- the last had concerns about several aspects though welcomed the company’s effort to conduct shareholder consultation.

Resolution 7, to re-elect Non-Executive Director, Ivan Glasenberg

Twenty one respondents voted in support of Resolution 7, the re-election of Ivan Glasenberg.

Six respondents voted against, five of which had concerns over the independence of board members. For example: *“The decision to vote against the two directors was due to the fact that they were not considered independent and there were concerns regarding board composition”*, and another *“Not enough independent directors on the board which raised grave concerns re the Glencore potential take-over”*.

One respondent abstained and commented: *“We abstained on the re-election of these three Directors again this year on the basis that, given the proximity of a corporate deal with the major shareholder, we were concerned that they may be disposed to act in the best interests of their sponsors”*.

Resolution 14, to re-elect Chair of the Remuneration Committee, David Rough

Twenty two respondents voted in support of Resolution 14, the re-election of David Rough, similar to Resolution 7. To quote: *“FOR the re-election of a Non-Independent Non-Executive Director due to tenure since 2002, overlapping with 3 Executive Directors, who chaired the Remuneration Committee and was a member of the Audit Committee, both of which should be wholly independent. There were sufficient Independent Non-Executive Directors to constitute these Committees if he stepped off. FOR, as this may cease to be relevant later this year due to the merger with Glencore. We will review the situation post-merger”.*

Of the six respondents that voted against, five also voted against Resolutions 3 and 7. To quote:

- *“We were unable to support the re-election of a non-executive not considered independent. Under the terms of the Relationship Agreement between the Company and its major shareholder, Glencore has the right to nominate three directors for appointment to the Board. The agreement stipulates that there will be at all times a majority of independent NEDs on the Board. However, we do not consider this to be the case. There appears to be only four independent non-executives on the board of thirteen. Consequently we are unable to support the re-election of non-independent non-executives.”*
- *“Res 7 (Ivan Glasenberg) and 14 (David Rough): Non-independent (directors and independent directors represent less than a majority of the board. Our vote on David Rough also reflected our concerns over remuneration arrangements, something he is ultimately responsible for (as Chairman of the Remuneration committee).”*

Table XVI: Resolutions 3, 7, 14

	Resolutions		
	3	7	14
	No. of respondents ⁵		
For	3	21	22
Against	24	6	6
Abstain	3	1	–
Did not vote	1	1	1

The Service Providers do not vote on their own behalf.

Conflicts

One respondent noted a conflict of interest as an adviser to the deal. They addressed the issue by outsourcing the voting decision to an independent fiduciary.

⁵ Two did not state if they voted for Resolution 3, and four for Resolutions 7 and 14.

SABMiller plc

Background

In April 2012, SABMiller announced that as from the AGM on 26 July 2012, its Chief Executive, Graham Mackay, would become joint Chairman and Chief Executive. Alan Clark, who at the time was in charge of European operations, would become Chief Operating Officer and succeed Graham Mackay as Chief Executive at the 2013 AGM¹.

It is a provision of the UK Corporate Governance Code that the roles of chairman and chief executive should not be exercised by the same individual. Senior Independent Director, John Manser, wrote to shareholders ahead of the 2012 AGM explaining that the arrangements were appropriate for SABMiller². At the AGM, Resolution 8 to re-elect Graham Mackay received 94 per cent of votes in support. Resolution 2 to approve the Directors' Remuneration Report received 23 per cent of votes against.

Objectives

Twenty of the 42 respondents with a holding engaged with SABMiller (Chart V). Twelve focused on board independence, with concerns over the Chairman's appointment and the lack of independent Non-Executive Directors. For example:

- *"We wanted to ensure that the company has sufficient independent leadership at board level through the appointment of a strong, senior independent director successor and further suitable director appointments made to the board."*
- *"We accept that the CEO has key relationships that are in shareholder's interests to keep. So we supported his move to the position of Chairman on this basis. However such a move requires the safeguard of an independent Senior Independent Director with a fresh perspective on the company, as we do not feel that we have this with the existing Senior Independent Director who has served on the board for 11 years."*

- *"We hoped to achieve a better understanding of the succession management process at SABMiller to enable us to form a judgement as to whether exceptional circumstances prevailed that would justify [Manager] supporting the elevation of the CEO, Graham Mackay, to Executive Chairman. It was also an opportunity for us to explain our thinking on the matter."*

Four of these also focused on remuneration: *"Raised concerns on remuneration with letter to company secretary. The reason why we have opposed the remuneration report is because we have concerns with the value share awards part of the ESAP which allows for retesting"*.

Three respondents wanted a better understanding of the business and its strategy going forward. To quote: *"We had concerns about the group's strategy and its approach to mergers & acquisitions. The purchase of Fosters in particular was a fully priced acquisition of a mature business in a developed market. We were keen for the company to show more discipline in this area going forwards"*.

Others wanted to:

- inform the company of their voting decision.
- gain a better understanding of the issues facing the company³.

Only two respondents changed their interest as a result of the issues, with one increasing its interest following meetings with management⁴.

Of those that did not engage, ten considered their holding was too insignificant, one clarifying: *"Our shareholding was relatively small, and we accepted the company's justification for departing from the recommendations of the Code"*.

A further five respondents did not identify any issues or were: *"...satisfied with the progress that the company is making in cutting costs and its overall strategy"*. Another stated: *"The transitional nature of the arrangement [chair and chief executive] had already*

¹ This was accelerated due to Graham Mackay's health issues, John Manser became acting Chairman.

² Guardian.co.uk 23 April 2012.

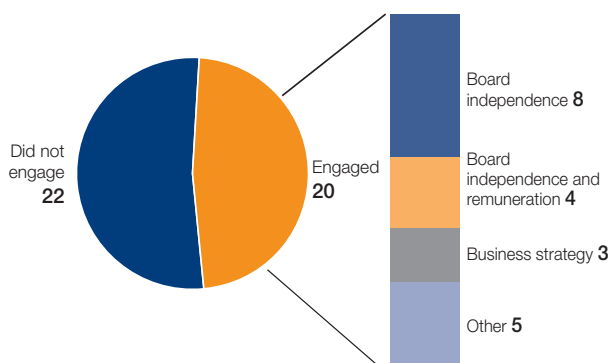
³ One did not state.

⁴ One did not state how.

been explained to us at a scheduled 1-2-1 meeting, and we were broadly comfortable with the issue”.

Two did not engage but voted against the combined chairman and chief executive role; three others held the shares in funds where they do not engage⁵.

Chart V: Engagement with SABMiller – No. of respondents



Only one Service Provider had an interest in the company during the period; it engaged to confirm facts and corroborate information.

Outcomes

Thirteen of the 20 respondents that engaged achieved their objectives.

Seven respondents achieved a better understanding of the business or were satisfied with the direction SABMiller was taking. This included one that felt SABMiller would take a more cautious approach to mergers and acquisitions, and for two others it was a commitment to board renewal. Four had been able to make their concerns known⁶.

One only partially achieved its objective as, whilst it had had the opportunity to provide input, SABMiller had not changed its remuneration arrangements.

Five respondents did not achieve their objectives, including:

- one that considered the company was not forthcoming in discussing the issues.
- two that were concerned about the lack of board independence of which one was also concerned about remuneration.
- one that still required reassurance that the Senior Independent Director could safeguard shareholder interests under the arrangements.
- another that wanted an appropriate Senior Independent Director appointed⁷.

Fourteen intended to continue to engage.

The Service Provider achieved its objective as it sought to confirm facts behind its research. It will continue to engage.

Details of engagement

Contact with SABMiller

Eighteen respondents noted a total of 52 contacts, an average of 2.9 each, with two that had nine contacts each. The highest number of contacts were with the Executive Directors and investor relations (Table XVII).

Table XVII: Number of contacts and who with

	No. of contacts	No. of respondents
Chairman	3	2
Senior Independent Director	5	4
Remuneration Committee Chair	–	–
Non-Executive Directors	–	–
Executive Directors	20	6
Management	6	2
Company Secretary	12	10
Investor relations	21	9

⁵ Two did not state.

⁶ Two did not state why.

⁷ Two did not state.

For nine respondents, the portfolio managers/analysts had multiple contacts, 42 in total. For another nine, the dedicated specialists had 13 contacts with the company (Table XVIII).

Table XVIII: Number of contacts and who by

	No. of contacts	No. of respondents
Portfolio managers/analysts only	42	9
Dedicated specialists only	13	9
Portfolio managers/analysts and dedicated specialists	8	4

Two respondents did not provide details of contacts, with one noting that it: *“wrote to the Company Secretary prior to the vote to explain to them the rationale for not supporting a number of resolutions at the AGM”*.

The Service Provider had three contacts with the Chairman and Company Secretary; it also noted contact with remuneration advisers.

Contact with other investors

Only three respondents collaborated, with two attending joint meetings with the company. Another sent a joint letter with another shareholder (Table XIX).

All that collaborated on the main issues considered it to be helpful.

Table XIX: Collaboration

	No. of respondents
Joint meetings with the company	2
Collective agreement on how to vote	–
Other	2

The Service Provider did not collaborate.

2012 AGM

Only one respondent attended the 2012 AGM.

Resolution 2, approval of the Remuneration Report

Seven respondents voted in support of Resolution 2, the Remuneration Report (Table XX). Two considered the report acceptable; another that the awards were justified and that disclosure was improving; and one supported the report following its engagement⁸.

Twelve voted against the Remuneration Report due to concerns with the performance criteria and with the disclosures. To quote:

- *“We were concerned about the structure of the rewards, the excessiveness of the combined rewards (in line with the concerns of our clients) and the link between company strategy and pay levels.”*
- *“We opposed the remuneration report, as we do not believe the performance targets attached to the Long-Term Incentive Plans are sufficiently challenging.”*
- *“Although the retrospective disclosure on the financial element of the annual bonus was improved in 2011/12, the annual report continues to lack disclosure on the personal element which accounts for 40 per cent of the annual bonus awards. We are also concerned about the ESOP awards being subject to a single performance condition and an overlap with the annual bonus scheme and ESAP, which all use EPS targets, thus leading to triple-dipping.”*
- *“The company is basing 40% of its annual bonus awards on non-quantitative personal performance objectives. There is no disclosure on these objectives and we therefore believe that the percentage of the personal element in the incentive plan is too high and/or the company needs to disclose more details on the performance objectives.”*

⁸ Three did not state.

- *“We had concerns with the value share awards part of the ESAP which allows for retesting. In addition, there is limited disclosure under the annual bonus plan.”*
- *“Our concerns regarding the performance criteria attached to the Share Option plan remain. They are based on EPS growth of between RPI+3-5 while consensus is in the region of 12% growth. The rewards are high, which we would not necessarily disagree with. However, if the performance dips for any reason, there is no safety net for investors as the targets are not challenging. This is the second year we have asked the company to revise the targets.”*

Seven of these also voted against or abstained on the re-election of Graham Mackay. In each case, respondents were not satisfied with the Remuneration Report and felt that the appointment of a combined chairman and chief executive was not best practice.

Resolution 8, to re-elect the Chief Executive, Graham Mackay

Eleven respondents voted to re-elect Graham Mackay, one noting that it was content with the board structure, and to quote others:

- *“... we were persuaded by the company's arguments that there was sufficient commercial merit for the appointment of Graham Mackay as Chairman for us supports this proposal.”*
- *“appointment is for a pre-determined and limited period of one year.”*

Three voted against in that as a matter of policy, they vote against a combined chairman and chief executive.

Five abstained, two on the basis it was an interim appointment, which might be justified in this instance, another would have preferred Mackay to have stepped down altogether after one year. Another stated: *“At the time of the AGM the Board comprised an Executive Chairman, two Executive Directors and 13 Non-Executive Directors of which 5 are considered independent meaning there is not a majority of independent non-executives on the board. We noted the proactive approach by the company in respect of explaining the move towards executive chairman. Given this, and the strong push on diversity of board make up, a mitigated abstention is recommended on the re-election of the executive chairman and the non-independent non-executives”.*

Table XX: Resolutions 2 and 8

	Resolutions	
	2	8
	No. of respondents ⁹	
For	7	11
Against	12	3
Abstain	-	5

The Service Provider does not vote on its own behalf.

Conflicts

None of the respondents that engaged reported any conflicts.

⁹ One did not state if it voted.

Appendix 4

Markets and proportion of shares voted

	UK			Rest of Western Europe			Central & Eastern Europe		
	2012	2011	2010	2012	2011	2010	2012	2011	2010
All	68	55	38	54	35	15	36	25	16
Most (>75%)	5	6	6	13	18	18	13	13	12
Majority (51-75%)	–	1	1	–	1	6	3	1	3
Some (25-50%)	2	–	–	1	2	2	3	3	1
Few (<25%)	2	1	1	4	3	2	5	3	5
None	–	1	–	3	2	2	4	5	6
No response	2	–	2	2	1	3	6	6	5
No equities held	1 ¹	–	–	3	2	–	10	8	–
Total	80	64	48	80	64	48	80	64	48

¹ One Asset Manager invests in funds and does not hold individual equities.

No. of respondents											
USA & Canada			Asia Pacific			Japan			Rest of the World		
2012	2011	2010	2012	2011	2010	2012	2011	2010	2012	2011	2010
51	41	28	45	33	22	52	41	27	33	24	13
7	5	8	12	10	10	5	5	7	12	10	13
2	2	–	1	4	1	–	–	1	7	5	4
1	1	2	2	1	2	1	–	1	4	3	2
3	2	2	3	2	4	4	5	3	3	5	4
2	3	4	3	2	4	2	2	4	4	4	6
5	3	4	5	4	5	6	3	5	7	5	6
9	7	–	9	8	–	10	8	–	10	8	–
80	64	48	80	64	48	80	64	48	80	64	48

