

The **co-operative**
asset management

UK Corporate Governance and Voting Policy

September 2009



A Principles

- A.1** The Co-operative Asset Management considers that sound corporate governance in the companies in which it invests is of central importance to create and sustain long-term shareholder value.
- A.2** The Co-operative Asset Management considers that it is the responsibility of institutional investors to act as owners of the companies in which they invest and will seek to maximise value from its investments by using its influence as a shareholder, through engagement and the use of its voting rights, to further good corporate governance in investee companies.
- A.3** The Co-operative Asset Management regards voting in a responsible, informed and consistent manner by institutional investors to be a fiduciary duty.
- A.4** Unless there are compelling reasons of confidentiality, institutions should apply principles of transparency in corporate governance and voting practices.
- A.5** It is not the duty of institutional investors to act as regulators, enforcing the provisions of particular codes. In developing and applying its engagement and voting policy and guidelines, The Co-operative Asset Management will have due regard for the provisions of the Combined Code, and of institutional guidelines, such as those of the Association of British Insurers. In applying this policy, however, The Co-operative Asset Management will apply discretion and have due regard for the particular circumstances of an investee company, whilst vigorously pursuing the interests of its customers. The Co-operative Asset Management recognises that best practice can develop ahead of code provisions.

B Governance Monitoring and Voting Procedures

- B.1** **The Co-operative Asset Management is always prepared to discuss company affairs with management and, as a responsible shareholder, will actively pursue any matters of concern.** The Co-operative Asset Management will seek urgent dialogue with a company's management in cases where concerns over strategy, performance or governance might threaten shareholder value.
- B.2** In cases where a board is not responsive, The Co-operative Asset Management will consider further active involvement, including, where appropriate:
- meeting directors, including non-executives
 - making joint representations with other institutions
 - using its voting power to oppose the board

- attending general meetings and making public statements
- submitting resolutions at general meetings
- with other investors, requisitioning an extraordinary general meeting.

- B.3** The voting process is illustrated in the chart at the end of this document.
- B.4** To ensure consistency, **all voting decisions are made by the Responsible Shareholding Committee**, which is chaired by the Executive Director, Asset Management, and comprises senior fund managers, corporate governance specialists and socially responsible investment specialists.
- B.5** In general The Co-operative Asset Management will vote as follows:
- FOR** the resolution is consistent with these guidelines, accords with best practice and is in shareholders' long-term interests
- ABSTAIN**
- i. the resolution falls short of best practice, but the issue is not sufficiently material to oppose management, or
 - ii. the matter is material, although not fundamental, and The Co-operative Asset Management has not previously raised the matter with the company (The Co-operative Asset Management would normally vote against a resolution on which it had previously abstained for the same reason; an abstention can be, therefore, a means of warning a company, where appropriate, before voting against an issue)
- AGAINST** the resolution is inconsistent with these guidelines, does not accord with best practice and is not in shareholders' long-term interests.
- B.6** As a matter of course, **The Co-operative Asset Management informs companies in advance** of all instances when it intends to vote against or abstain on any resolution proposed by the directors at a general meeting, and is prepared in all cases to explain its course of action.

C Governance and Voting Guidelines

C.1 Support of Company Management

The Co-operative Asset Management will seek actively to support the board of a company that acts in the long-term interests of shareholders.

The Co-operative Asset Management will normally seek to support the existing board in the case of a hostile takeover. Each case is reviewed individually and it is recognised that cases will occur where clear strategic advantages arise from a takeover.

The Co-operative Asset Management will not seek to support aboard whose record does not give grounds for confidence in its future performance.

C.2 Company Boards

C.2.1 Composition

- In line with 'The Combined Code of Corporate Governance' (July 2003) The Co-operative Asset Management believes that at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent, except for smaller companies, which should have at least two independent non-executive directors (Code Provision A.3.2).
- The Co-operative Asset Management considers that there should be at least three independent non-executive directors on a company's board (or at least two independent non-executive directors for smaller companies).
- The Co-operative Asset Management would not normally support the election of a non-executive director who was not independent of the company unless a majority of non-executives would still be independent.
- The Co-operative Asset Management would normally vote against the election of a non-executive who was not independent if the company had insufficient independent directors to discharge key functions under the Combined Code.
- The Co-operative Asset Management would not normally support the re-election of a non-executive director who, in The Co-operative Asset Management's opinion, has other commitments, such as a large number of other directorships in public companies, that might affect his capacity to devote sufficient time to his duties as a non-executive.

C.2.2 Senior Independent Non-Executive Director

The Co-operative Asset Management acknowledges the importance of the role of the Senior Independent Non-Executive Director. He/she should be a member of all the sub-board committees, ideally as the Chairman of the Remuneration and Audit Committees.

The Co-operative Asset Management considers that, in normal circumstances, a chairman who is independent of management should be the normal channel of communication between shareholders and the board.

It acknowledges, however, that the Senior Independent Non-Executive Director can also be an important link between shareholders and the board, for example, relating to functions of the committees he chairs, or in circumstances where the chairman is unable to resolve a particular issue. It is necessary for the credibility of the role that the director nominated is demonstrably independent and The Co-operative Asset Management will not support the re-election of a person identified as the Senior Independent Non-Executive Director whom it considers is not independent by the definition set out in note 2.3.

C.2.3 Independence

In considering whether a director is independent, The Co-operative Asset Management will have regard to the following definition extracted from "The Combined Code of Corporate Governance" (July 2003) based on the definition set out in the "Review of the Role and Effectiveness of Non-Executive Directors" by Derek Higgs, published in January 2003, which has been incorporated into the guidelines of the Association of British Insurers.

"The board should identify in the annual report each non-executive director it considers to be independent. The board should determine whether the director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgement. The board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination, including if the director:

- has been an employee of the company or group within the last five years
- has, or has had within the last three years, a material business relationship with the company either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the company
- has received or receives additional remuneration from the company apart from a director's fee, participates in the company's share option scheme or a performance-related pay scheme, or is a member of the company's pension scheme
- has close family ties with any of the company's advisers, directors or senior employees
- holds cross-directorships or has significant links with other directors through involvement in other companies or bodies
- represents a significant shareholder, or
- has served on the board for more than nine years from the date of their first election".

C.2.4 Suitability for Election

Shareholders should be given sufficient biographical information on directors presented for election to enable them to make an informed choice. **The Co-operative Asset Management will not normally support the re-election of a director with a poor attendance record.**

C.2.5 Nomination Committee

In line with the Combined Code, The Co-operative Asset Management considers that appointments should be based upon the recommendations of a nominations committee, the majority of whom should be independent directors (Code Provision A.4.1). The chairman of the nomination committee should either be the Board Chairman, who is independent on appointment, or another independent director.

C.2.6 Chairman and Chief Executive

In line with the Combined Code, The Co-operative Asset Management believes that the positions of Chairman and Chief Executive should be separated (Code Provision A.2.1).

The Co-operative Asset Management will usually vote against the election of a director holding both positions.

In line with the Combined Code, the Chairman should on appointment meet the independence criteria (Code Provision A.2.2).

In the absence of evidence to the contrary, it will be assumed that a Chairman who holds an executive position will in fact be the Chief Executive. It is recognised that there may, in exceptional circumstances, be occasions when the combination of both positions can be justified, but **the onus must rest on the directors to demonstrate this** to shareholders.

The Co-operative Asset Management does not consider it appropriate for a former chief executive to become chairman of the same company (Code Provision A.2.2). In such a case, The Co-operative Asset Management would expect the former chief executive to hold the position for only a short transitional period, and The Co-operative Asset Management would seek assurance from the company that a replacement was being sought.

C.2.7 Age of Director

The Co-operative Asset Management believes that a director's suitability for election **should be gauged by ability** to perform his job rather than by age.

C.3 Directors' Remuneration

C.3.1 Remuneration Committee

The Co-operative Asset Management considers the remuneration committee to be fundamental to the fair consideration, determination and application of a company's remuneration policy.

The Co-operative Asset Management considers that remuneration committees should consist wholly of independent non-executive directors (Code Provision B2.1) with access to independent external advice.

C.3.2 Remuneration Policy/Report

Clearly all companies will seek to attract, retain and incentivise executives of sufficient calibre to create and sustain long-term shareholder value in the business. However, as with all other areas of expenditure, care should be taken that no more remuneration is paid than is necessary to reach corporate objectives.

The Co-operative Asset Management will be supportive of remuneration structures that incentivise directors by relating a significant proportion of remuneration to long-term value added to shareholders by the executive directors.

It is recognised that, in instances of strong performance which significantly add to long-term value, executive directors may legitimately receive very high remuneration.

However, The Co-operative Asset Management cannot support structures where high remuneration may be received for poor or even average performance.

It is important that base salaries be controlled and that higher rewards should be based on suitable personal and corporate performance targets.

Bonuses without performance targets are generally not acceptable.

In voting on the report/policy, The Co-operative Asset Management will consider whether the report demonstrates effective implementation of sound policy over the reporting period.

The Co-operative Asset Management will not normally support a remuneration policy/report where:

- the independence of the remuneration committee is compromised
- there is evidence of excessive remuneration having regard to the performance of the company
- it is not possible to determine the potential for excessive remuneration owing to poor disclosure by the company
- the company pays transactional bonuses
- there are serious inadequacies in share-based incentive schemes (see section 4)
- the company has bundled approval of remuneration schemes with the approval of a merger or other corporate action
- the company makes ex-gratia payments, such as non-contractual retirement bonuses
- service contracts allow potential for reward for failure (see section 3).

C3.3 Service Contracts

The Co-operative Asset Management considers that executives' service contracts should not normally provide for notice periods of longer than one year and will not normally support the election or re-election of a director whose notice period exceeds one year.

Provision for one year's pay on severance should relate to basic salary and include only bonuses already earned.

There should be no early vesting of awards under share-based incentive schemes on severance. Wherever possible, a company should seek to mitigate liabilities on severance and should publish its policy on mitigation in its remuneration report.

The Co-operative Asset Management will vote against the election of an executive director whose notice period exceeds two years or where severance entitlements exceed two years' salary.

It is recognised that there may be exceptional occasions when a longer than normal notice period is appropriate, but the onus must rest on the directors to demonstrate this.

Where a longer initial notice period is granted on appointment, the notice period should reduce to one year or less within one year.

C3.4 Share-based Incentive Schemes

The Co-operative Asset Management recognises the value of performance-related remuneration such as share-based incentive schemes. It considers, however, that such incentives should be designed to reward high performance that adds significantly to shareholder value.

The Co-operative Asset Management will not support schemes in which performance targets are not sufficiently challenging and where there is potential for excessively generous rewards. A meaningful prior financial commitment from executives who participate in schemes would normally be expected.

The Co-operative Asset Management would not support schemes which do not comply with the ABI guidelines on dilution and participation limits. In assessing the suitability of a scheme, The Co-operative Asset Management will have regard to relevant statements issued by the ABI (e.g. "Share Incentive Schemes – A Statement Of Principles" published in June 1999 and "Principles and Guidelines on Remuneration", updated in November 2005).

The Co-operative Asset Management considers that schemes should be subject to more than one performance target. There should be a measure of returns relative to a peer group (for example, using total shareholder return (TSR)) and a secondary measure which should relate to underlying value added (for example, real growth in earnings per share (EPS)).

All performance periods should be for a minimum of three years and there should be no opportunities to retest performance criteria. The Co-operative Asset Management prefers that a vesting scale should apply to awards, with a maximum vesting for median performance relative to the peer group of 25% of the total award. Full vesting should be for upper decile performance, with vesting on a sliding scale between those points. The remuneration committee should satisfy itself that targets based on EPS are not distorted by balance sheet adjustments (such as for share repurchases and other capital adjustments) and genuinely reflect underlying performance.

The Co-operative Asset Management would not normally support the adoption of a scheme that incorporated or permitted any of the following features:

- issuing of discounted share options
- repricing share options
- breaching of institutional guidelines on dilution
- automatic vesting on change of control or other trigger
- early vesting on severance
- waiving or lowering of performance targets
- retesting of performance targets
- insufficiently challenging performance targets (taking account of the size of awards and any vesting scale)
- amending material aspects of the scheme without reference to shareholders
- absence of individual participation limits
- excessive individual participation when considered in conjunction with awards under other schemes
- performance period of less than three years
- participation of non-executive directors in the scheme.

C.4 Share Capital

C.4.1 Authority To Issue Shares

The Co-operative Asset Management will normally vote for an authority to issue shares with pre-emption rights where the proposed issue is the lesser of the unissued ordinary share capital or a sum equal to one third of the issued ordinary share capital. The authority given should not last longer than five years.

C.4.2 Disapplication Of Pre-emption Rights

The Co-operative Asset Management will normally vote in favour of authorities to issue shares for cash other than from existing shareholders where the proposed issue is limited to 5% of the current issued share capital. Such authorities should be renewed annually. Other than in exceptional circumstances, The Co-operative Asset Management would vote against the waiver of pre-emption rights beyond the 5% limit.

C.4.3 Share Repurchases

The Co-operative Asset Management will normally vote in favour of an authority for share repurchases provided that it complies with Listing Rule guidelines (e.g. limit of 15% of issued capital) and that directors demonstrate that this is the most appropriate use of a company's cash resources. To avoid the possibility of directors' being placed in a position of conflict of interest, The Co-operative Asset Management advocates the adjustment of relevant targets in executive bonus or share incentive schemes to take account of the increase in earnings per share caused by share repurchases.

C.4.4 Split Equity Capital Structure

The Co-operative Asset Management is opposed to the issue of equity shares with reduced or no voting rights.

C.5 General Meetings And Accounts

C.5.1 Agenda Structure

The Co-operative Asset Management considers that each substantive item of business at a general meeting should be the subject of a separate resolution. Sufficient explanation in respect of each resolution should be provided to enable shareholders to vote on an informed basis.

C.5.2 Resolutions To Receive The Report And Accounts

The Co-operative Asset Management does not necessarily regard voting against the receiving of the report and accounts as a vote of no confidence in the Board. However, in the case of serious breaches of corporate governance at a company, it might be appropriate to abstain from or vote against receiving the report and accounts.

Attention will be paid in respect of reporting Social, Ethical and Environmental (SEE) issues, bearing in mind the potential impact of a company's activities. If a company with material environmental impacts does not report on SEE matters and associated risks, The Co-operative Asset Management will not normally support the vote on receiving the report and accounts. In assessing the reporting, The Co-operative Asset Management will have regard to ABI's "Disclosure guidelines on Social Responsibility", published October 2001.

C.5.3 Dividends

A resolution in respect of dividends should be put separately from the resolution to receive the report and accounts. The Co-operative Asset Management will vote for the approval of dividends provided that the dividend is covered by earnings or, if it is not, that there is sufficient free cash flow and adequate explanation and justification is provided by the directors. The Co-operative Asset Management is generally in favour of allowing a scrip alternative to cash dividends.

C.6 Audit Function

C.6.1 Audit Committee

The Co-operative Asset Management strongly supports the establishment of an audit committee composed entirely of non-executive directors, with at least three independent members, or at least two independent members for smaller companies (Code Provision C.3.1).

Non-executive directors should have independent access to the auditors and a close working relationship with them. As a matter of routine, a part of each meeting should be held with the executive directors.

C.6.2 Auditor Independence

The Co-operative Asset Management will normally vote in favour of the appointment of an auditor recommended by a properly constituted audit committee provided that there are no issues that may compromise the independence of the auditor.

The Co-operative Asset Management considers that companies should fully disclose the nature of non-audit fees and explain why they do not compromise the auditor's independence. Audit committees should periodically review the independent status of their auditors.

C.7 Internal control

The Co-operative Asset Management considers that compliance with the internal control requirements of the Combined Code is of critical importance if a company is to manage its exposure to risk and implement appropriate internal management controls.

C.8 Sundry

C.8.1 Political Donations

The Co-operative Asset Management will normally vote against any authority that would allow directors to make donations to political parties. The Co-operative Asset Management would not oppose such an authority only in exceptional circumstances where there was a pressing business case in favour of the authority and where the authority would not have an unduly negative impact upon the company's reputation. It would be the responsibility of the board to demonstrate to shareholders' satisfaction the existence of such exceptional circumstances.

C.8.2 Memorandum And Articles Of Association

The Co-operative Asset Management considers that proposals to change a company’s memorandum and articles of association should be presented to shareholders with a separate resolution for each substantive change. The reasons for each change should be provided. The Co-operative Asset Management will normally support management if the changes are regulatory. However, in the absence of a full and clear explanation, The Co-operative Asset Management will abstain or vote against proposed amendments.

C.8.3 Investment Trusts

The Co-operative Asset Management considers it appropriate that the board of an investment trust should have no more than one representative from its investment managers. Furthermore, all other directors should be independent non-executive directors and

The Co-operative Asset Management will not support the re-election of a non-independent non-executive director if there is not a majority of independent directors amongst the non-executives.

C.8.4 Reporting on Performance

The Co-operative Asset Management considers that transparency is a necessary feature of Responsible Shareholding and, accordingly, **discloses details of all its UK votes on its website** and gives brief explanations for instances where it has not supported the management. The Co-operative Asset Management updates its record frequently, and records for meetings are normally posted on the meeting date. The Co-operative Asset Management also provides aggregate information on how it exercises its voting rights and the effectiveness of its engagement with investee companies on its website and through the Social Accountability Report.

Illustrative chart referred to in paragraph B.3

The Co-operative Asset Management Voting Process



*Responsible Shareholding Committee

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