

The **co-operative**
asset management

UK Corporate Governance and Voting Policy

October 2011



A Principles

A.1 The Co-operative Asset Management considers that corporate governance is of central importance in the companies in which it invests, to create and sustain long-term shareholder value. This is in line with our longstanding commitment to responsible investment (RI) and stewardship. The Co-operative Asset Management is committed to applying responsible investment principles across all of its portfolios. This is in line with principle 3 of the UN's Principles for Responsible Investment (PRI).

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 promote 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 In developing and applying its engagement and voting policy and guidelines, The Co-operative Asset Management will take account of the provisions of the UK Corporate Governance Code and of institutional guidelines, such as those of the Association of British Insurers. In applying this policy, 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 To ensure consistency, **all voting decisions are made by the Responsible Shareholding Committee**, which is chaired by the Chief Investment Officer and comprises senior fund managers, financial analysts, corporate governance specialists and responsible investment specialists.

B.4 In general The Co-operative Asset Management will vote as follows:

FOR

a resolution is consistent with these guidelines, accords with best practice and is in shareholders' long-term interests.

ABSTAIN

- a resolution falls short of best practice, but the issue is not sufficiently material to oppose management, or
- a 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

a resolution is inconsistent with these guidelines, does not accord with best practice and is not in shareholders' long-term interests.

B.5 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.

C.2 Company Boards

C.2.1 Composition

- In line with 'The UK Corporate Governance Code' (formerly the Combined Code), published in June 2010, The Co-operative Asset Management believes that at least half the board, excluding the chairman, should comprise non-executive directors except for smaller companies, which should have at least two independent non-executive directors.
- 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 UK Corporate Governance 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 the capacity to devote sufficient time to their duties as a non-executive.
- The Co-operative Asset Management would not normally support the resolution adopting the Report and Accounts if material concerns persisted in respect of board composition.

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 they chair, 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 UK Corporate Governance Code (June 2010).

"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 UK Corporate Governance 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.

C.2.6 Chairman and Chief Executive

In line with The UK Corporate Governance Code, The Co-operative Asset Management strongly believes that the positions of Chairman and Chief Executive should be separated. **The Co-operative Asset Management will usually vote against the election of a director holding both positions.**

In line with the UK Corporate Governance Code, the Chairman should, on appointment, meet the independence criteria.

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. In such a case, the former chief executive would expect to hold the position for only a short transitional period, and assurance would be sought 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 judged by ability** to perform their job, rather than by age.

C.2.8 Gender

Recommendation 1 of the Davies review of Women on Boards, states:

"All chairmen of FTSE 350 companies should set out the percentage of women they aim to have on their boards in 2013 and 2015. Chairmen should announce their aspiration goals within the next six months (by September 2011)."

Investee companies who hold their AGMs after this date will be assessed as to whether they have made a public statement of aspirational levels of women on their boards, as per Lord Davies' recommendations.

The Co-operative Asset Management (TCAM) will, in the first instance, abstain on the re-election of the Chairman of the Nomination Committee, should a company fail to disclose such an aspiration or fail to elect any women to an all male board.

Should a company not put forward all its directors for annual re-election, we will abstain on the re-election of the Chairman or members of the Nomination Committee – dependent upon who is put forward for re-election.

In applying this policy TCAM will remain mindful that this is a multi-faceted topic and consequently will adopt a pragmatic approach, analysing on a case-by-case basis several factors, such as the length of tenure of the Chair of the Nomination Committee and the merit of any explanation why aspirations or appointments have not been forthcoming. **We will also take into account membership of the 30% Club.**

In 2013, TCAM may escalate to a vote against where there is still no progress or indication of positive momentum.

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 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.

It is recognised that, in instances of strong performance which significantly add to long-term value, executive directors may legitimately receive high remuneration. However, The Co-operative Asset Management cannot support structures where high remuneration may be received for average or even poor performance.

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.

The Co-operative Asset Management will be especially supportive of remuneration structures that incorporate material environmental, social and sustainability-related performance measures linked to verifiable KPIs.

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

Bonuses awarded without reference to performance targets are generally considered unacceptable. In granting performance-based payments the remuneration committee should also have due regard to the long-term capital stewardship of the business; for instance, a minimum credit quality should be maintained as a pre-condition to any award.

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 adequately assess 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, golden hellos or retention bonuses.
- service contracts allow potential for reward for failure (see section 3).
- clawback provisions are absent.

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.

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 will be especially supportive of remuneration structures that incorporate material, environmental, social and sustainability-related performance measures linked to KPIs.

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. ABI Principles of Remuneration, September 2011).

The Co-operative Asset Management considers that schemes should be subject to performance conditions that provide a meaningful alignment with company strategy and objectives. In doing so, the chosen targets should take account of performance in a relative (peer comparison) and absolute (underlying growth) sense and be mindful of the need to retain a focus on long-term capital stewardship.

All performance periods should be for a minimum of three years and an appropriate vesting scale should govern the level of vesting at different performance points. This should be calibrated to the effect that marginal amounts (0-25%) vest for average or threshold performance and full vesting only occurs for outstanding performance.

For total shareholder return (TSR) this would typically translate to 25% vesting at median, relative to the peer group on a sliding scale up to full vesting at upper decile. However, where high quantum grants are allocated, the lower vesting point should be adjusted so that high absolute levels of award do not vest for average performance. For instance, where potential award levels exceed 200% of salary, we would expect to see downward adjustment of the threshold vesting point, so that the incentive to outperform is not undermined.

When using earning per share (EPS) targets the remuneration committee should satisfy itself that they 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 5-10% 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 and strongly supports the principle of one share one vote.

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 (ARAs)

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.

The Co-operative Asset Management voting policy takes account of the Association of British Insurers' (ABI) assessments of disclosure as well as accepted best practice.

The Co-operative Asset Management voting policy further analyses the ARA for GHG emissions and climate change-related disclosure.

Analysing ARAs for climate change-related disclosure is in line with The Co-operative Asset Management's public response to the ARAs consultation, where we indicate our support for mandatory disclosure of Greenhouse Gas emissions. The Co-operative Asset Management believes that companies that make a significant contribution to climate change and/or are adversely or positively affected by it should disclose investment-relevant information on how they are managing these risks and opportunities.

The Co-operative Asset Management will:

- (i) **in the first instance, abstain on the Annual Reports and Accounts of companies for whom climate change is considered 'very relevant', where the company fails to disclose either through the Carbon Disclosure Project or its corporate literature the following:**
 1. narrative discussion of the relevance and materiality of climate change to the business
 2. gross CO₂ equivalent (CO_{2e}) emissions
 3. mitigation and adaptation strategies including targets (historical and future)
- (ii) as part of TCAM's longstanding commitment to engagement, we write to all companies where we are withholding support explaining the reasons and inviting dialogue
- (iii) where TCAM have previously abstained and the company demonstrates no visible improvement by the subsequent AGM, TCAM will escalate to a vote against
- (iv) reserve the right to move to an against vote in the first instance in cases of total non-disclosure from a high-impact company

- (v) TCAM will exercise its discretion to vary its voting pattern according to such factors including but not limited to the responsiveness of companies and other issues such as corporate governance.

In determining the quality of disclosure The Co-operative Asset Management will take into account the presence, or absence, of an assurance statement in sustainability data. In doing so, we will review the quality of such assurance and have due regard to the Carbon Smart report "Stuck on the starting blocks: the state of sustainability assurance in 2010".

Sustainability assurance should:

- clearly reflect the scope of matter material to both the company and its stakeholders
- transparently review the quality of reporting
- provide clear conclusions on data quality
- be conducted by a qualified, independent third party reviewer
- meet the requirements of a recognised standard
- be easily understood and jargon-free.

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.

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 independent non-executive directors, with at least three independent members, or at least two independent members for smaller companies.

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 UK Corporate Governance Code is of critical importance if a company is to manage its exposure to risk and implement appropriate internal management controls.

C.8 Other Matters

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. The fund manager's contract should provide no longer than one year's notice period and the Chairman must also be independent. In assessing the governance of Investment Trusts TCAM is supportive of the Association of Investment Trust Companies Code of Corporate Governance as best practice for the sector.

Finally we look for a statement of compliance with the FRC's Stewardship Code along with evidence of adherence.

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 global 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 at least quarterly. TCAM also provides detailed information on its responsible investment activities in the Responsible Investment Quarterly Review and Annual Review.

D.3 Disclosure of conflicts of interest

A conflict inventory will be maintained, and published periodically on our website, **co-operativeassetmanagement.co.uk**

D The Co-operative Asset Management's conflict of interest policy (Principle 2 of the Stewardship Code)

TCAM's Stewardship Code can be found at, **<http://co-operativeassetmanagement.co.uk/advisers/stewardship-code.php> TCAM was the first asset manager in the world to publish a comprehensive compliance statement in respect of the Stewardship Code.**

The Co-operative Asset Management recognise that during the course of our stewardship activities promoting environmental, social and governance good practice, conflicts of interest will inevitably arise from time to time, and we place a strong emphasis on ensuring these conflicts can be effectively identified, managed and disclosed.

D.1. Identification of conflicts of interest

Conflicts of interest are likely to arise from two sources:

- the activities of our parent The Co-operative Banking Group, and its ultimate parent The Co-operative Group
- the activities of our clients.

All proposed stewardship engagement is reviewed prior to its approval by our team of experienced environmental, social and governance analysts and the wider research team and fund manager are involved. The majority of potential conflicts of interests are identified during this review process.

D.2. Management of conflicts of interest

Potential stewardship conflicts of interest are investigated by environmental, social and governance analysts, prior to discussion by a committee of interested parties. The composition of the committee may vary depending on the nature of the potential conflict but will always include the Head of Responsible Investment and minutes are recorded of the meeting.

Conflicts will arise on an infrequent basis, which may prevent us on occasion from pursuing all aspects of stewardship activity. In each of these cases, we will seek to raise these issues directly with the other party to the conflict, rather than taking no further action.

For further information please contact

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