

## **CORPORATE GOVERNANCE PROXY VOTING ACTIVITY**

### **March – May 2006**

During the period the Fund voted at a total of 759 company meetings - 139 European, 349 US and 271 UK. In respect of these meetings (a mixture of EGMs and AGMs) the Fund abstained or opposed 1,504 resolutions out of a total of 8,228, representing approximately 18% of all resolutions. During this period there were only 88 meetings where the Fund supported all the resolutions put forward by companies.

The Fund has a bespoke template for voting at UK meetings, however, the Fund currently follows Pirc's voting advice for European and US company meetings. The Fund will also use this guidance when it extends its voting coverage to Japan from June 2006.

PIRC is supporting the Government's challenge to amendments to the Company Law Reform Bill that threaten the ability of the Government to force public disclosure of fund managers' votes at company meetings. The TUC, which has about 1,000 member trustees on pension funds governing approximately £300bn managed by investment companies, argued that disclosure would enable all trustees to see how managers exercised trustees' ownership rights on their behalf. Several of the larger asset management firms already disclose voting data and more are planning to go down this route, but fund managers have lobbied against compulsory disclosure in terms of the expense of the burden.

PIRC has given a generally positive response to the FRC's (Financial Reporting Council) consultation on the Combined Code. It took the view that, whilst further movement could have been made, most of the proposals are in the interests of shareholders – for example, to provide shareholders voting by proxy with the option of withholding their vote and to require the publication of details of proxies lodged at the AGM where votes are taken on a show of hands. PIRC was less comfortable with the proposal to allow a chairman, independent at the time of appointment, to sit on the remuneration committee. PIRC considered that as matter of best practice this undermines the broader principle of the Code that no individual should dominate the board's decision making. The current code does not prevent any chairman being a member of the committee – the company just has to explain why it is appropriate in their situation. In PIRC's view, "comply or explain" is the appropriate maxim where companies regard the Chairman's membership of the remuneration committee to be justified.

<b>MEETING</b>	<b>RESOLUTIONS CAUSING SHAREHOLDER CONCERN</b>	<b>SHAREHOLDERS OPPOSING %</b>
Royal Dutch Shell Plc, AGM	Shareholder Resolution	93.17
Skyepharma Plc, EGM	Shareholder Resolution	52.97
Croda International Plc, AGM	Remuneration Report	51.51
Amvescap Plc, AGM	Remuneration Report	48.41
Abbot Group Plc, AGM	Remuneration Report	46.10
Next Plc, AGM	Elect Derek Netherton	42.86
Morgan Sindall Plc, AGM	Remuneration Report	41.19
Psion Plc, AGM	Long-Term Share Plan	39.84
Burren Energy Plc, AGM	Elect Michael Calvey	33.74
Evolution Group Plc, AGM	Approve the 2006 Performance SP	32.26

Although the Fund opposed most of the resolutions referred to above it will vote for a resolution if it believes the company has followed best practice, despite significant opposition sometimes from other shareholders. Background details on some of these resolutions where opposition was significant are as follows:

### **VOTING REVIEW**

### **Royal Dutch Shell Plc (AGM)**

The Ecumenical Council for Corporate Responsibility (ECCR) proposed a shareholder resolution. The group called for Royal Dutch Shell to draw up regional Memorandums of Understanding (MOU) with key stakeholder groups based on independently conducted social & environmental (S&E) impact assessments. The Fund did not accept that local communities should be able to have a veto over proposed developments. There were also doubts about the practical application of the proposal in terms of deciding who the appropriate stakeholders were in any given situation, how to carry out appropriate independent assessments and the legal status of the MOUs. A second requirement sought to make Shell's acquisition of companies, and their methods of extraction and refinement, also dependent on qualified independent assessment. The Fund considered the most appropriate response was to abstain as a signal to the company that it must continue to demonstrate improvements with respect to its approach to stakeholder engagement. The resolution was defeated with 93% opposition.

### **Skyepharma Plc (EGM)**

This meeting heard a shareholder proposal from a group of shareholders led by North Atlantic Value LLP (NAV), and including Morley Fund Management and Insight Investment Management. The resolution sought to appoint Robert Thian to replace Ian Gowrie-Smith, who had retired from the board, as a director. The Fund had no specific issues over the ability of Mr. Thian to act as a director of the company, and strongly supports shareholder resolutions as part of the governance framework in the UK market. However, the Fund did not consider that the shareholder's resolution made a sufficient case for the appointment of Mr. Thian on governance grounds and as a result voted against the proposal. The resolution was defeated narrowly with just over 52% voting in opposition.

### **Croda International Plc (AGM)**

The company's AGM witnessed the highest level of rejection of a company proposal (51%) this reporting quarter. The vesting targets attached to the newly approved long-term incentive schemes were considered insufficiently challenging and the Fund had further concerns over the chief executive's contract that provided for termination provisions in excess of one year's salary and benefits. The failure of the resolution to meet the voting guidelines resulted in the Fund participating in the oppose vote.

### **Amvescap Plc (AGM)**

The company sought shareholder approval for its remuneration report. The Fund was concerned that the maximum awards available under the option schemes were not disclosed. The Fund had further doubts over the appropriateness of the targets attached to the share option scheme, as the earnings per share (EPS) requirements fell below brokers' forecasts, as well as the fact that compensation payments made during the year were not fully explained. In addition to remuneration policy concerns, bonus payments made to the chairman and chief executive were seen as excessive and not sufficiently based on performance. These concerns produced an oppose vote of over 48% including that of the Fund.

### **Abbot Group Plc (AGM)**

The company sought shareholder approval for its remuneration report. Much of the disclosed policy met the Fund's guidelines, however, the EPS growth targets attached to the Long Term Incentive Plan (LTIP) were insufficiently challenging. The Fund also noted that there is no evidence of share schemes that enable employees to participate in

business success. These concerns prompted the Fund to join 46% of votes cast in opposing the resolution.

### **Next Plc (AGM)**

The company requested shareholder approval for the election of Derek Netherton. The Non-executive director is not considered independent by the Fund as he has been on the board for more than nine years. The company's board structure compares well to many other quoted companies and there were sufficient independent directors to meet the Fund's guidelines and support the resolution. There was significant opposition to Mr Netherton's appointment (43%), however, the company stated they knew of no other reason for this other than his length of tenure on the board.

### **Morgan Sindall Plc (AGM)**

The Fund was comfortable with much of remuneration report including satisfactory disclosure of figures and scheme operations. The vesting targets under both aspects of the Morgan Sindall Executive Remuneration Plan were considered sufficiently challenging and within the Fund's voting guidelines, and combined remuneration was not excessive. The Fund did have concerns over the award of a discretionary bonus of 20,000 performance shares to the Chief Executive Paul Smith, as the Fund believes this type of award runs counter to the principles of transparent remuneration. These concerns together with further doubts over future bonus awards which are included in termination payments for directors led the Fund to oppose the resolution, along with 41% of other shareholders.

### **Psion Plc (AGM)**

Shareholders were asked to approve the Long-Term Share Plan (LTSP) proposed by the company. The Fund noted that given brokers' forecasts the targets attached to the scheme were sufficiently challenging. The most significant contravention of the Fund's guidelines was the company not adhering to the 5% and 10% dilution limits. The company did provide some justification for this, however, on balance the Fund viewed it most appropriate to join 40% of votes cast and oppose the resolution.

### **Burren Energy Plc, AGM**

Shareholder support was sought for Michael Calvey's election as a non-executive director. Mr Calvey was not considered independent according to the Fund's guidelines as he has a contractual right to participate in the profits of First NIS Regional Fund, SCIAF and the BVPE Fund, which together holds 8.41% of Burren Energy's issued share capital. The Fund had additional concerns regarding insufficient independent representation on the board and consequently opposed the resolution, along with 33% of other shareholders.

### **Evolution Group Plc, AGM**

The company requested shareholder approval for the 2006 Performance Share Plan. The Fund noted that plan failed to provide a vesting scale and also lacks stated maximum amounts. Further assessment indicated that the dilution limits were unacceptable as there is no individual 5% limit for this scheme, while the lack of the required financial commitment failed to adequately align the interests of participants with

shareholders. These concerns prompted the Fund to oppose the resolution together with 32% of votes cast.

## **OVERSEAS ISSUES**

### **Enron**

In May a jury at a federal district court in Houston found Kenneth Lay and Jeffrey Skilling, respectively the Chairman and CEO of Enron prior to the company's collapse, guilty on several counts, including securities and wire fraud and false statements to investors. With sentencing pending later this year, Skilling faces a prison sentence of up to 185 years, and up to 45 years for Mr Lay. There are mixed opinions as to whether regulations like the Sarbanes-Oxley Act will offer investors genuine protection from possible future US corporate scandals. Some have argued that the guilty verdicts at Enron prove the value of the legislation and will deter future corporate fraud. The Wall Street Journal, however, has reported that a number of major US corporations granted options to purchase stock at "remarkably low prices" – often at the company's lowest share price for the fiscal year, which, if it were an accident, would be statistically improbable. In spite of these concerns the overall impact of the legislation does appear to be beneficial, with a continuation of the drive towards strengthening the independence and accountability of US corporate boards.

### **Parmalat (Europe)**

In December 2005 the Italian Parliament approved the so-called "Parmalat bill". As far as the corporate governance of Italian companies is concerned, some important changes have been introduced. For example, in terms of directors' responsibilities, two thirds of the BoSA (Board of Statutory Auditors) or shareholders representing 2.5% of issued share capital can now take liability action against directors. A further effort to reinforce minorities' rights will see shareholders representing 2.5% of the share capital able to submit items to the AGM agenda. Another important move means the disclosure of stock option plans for both directors and top managers will have to meet stringent requirements. It has been noted that these reforms present a great opportunity for Italian companies to improve their corporate governance systems. The difficulty appears to be that the law requires that companies amend their by-laws in order to adapt to the new system, but still leaves room for discretion on how practically to do that.

This information is provided by PIRC in accordance with the Fund's voting template.

## **OVERSEAS VISITS**

The Fund was represented at the Rights & Responsibilities of Institutional Investors Conference in Amsterdam in March. The seminar provided a forum for discussion on developments in class actions and sustainability. The Chief Investment Officer attended the bi-annual meeting of the Council of Institutional Investors In Washington.