

September 2010

The UK Stewardship Code

Statement of Compliance by F&C Investments

F&C Investments (F&C) is a London-based global asset management firm with institutional and retail clients collectively representing over £149 billion of assets¹. F&C manages funds on behalf of insurance companies, institutional investors, pension funds and private individuals. Through its Responsible Engagement Overlay service (reo[®]), which has been in operation since 2000, F&C has also been mandated to engage and vote on behalf of a number of insurers, pension funds and banks whose money is managed by other parties.

F&C has long been an active voice in support of robust corporate governance standards for companies in all jurisdictions where F&C invests. In this context F&C in the past has endorsed and followed the Institutional Shareholders' Committee (ISC) statement on the Responsibilities of Institutional Shareholders and Agents, as well as the subsequent development of the ISC Code. F&C is supportive of the development of the Stewardship Code in the UK². As an active investor for many years, F&C believes that robust engagement and voting by institutional investors is critical to the health of financial markets and long-term value creation. This is particularly so in the UK's principles-based, "comply or explain" regulatory regime, whose effectiveness requires active involvement by investors to engage with companies and monitor their compliance to the UK Corporate Governance Code.

F&C notes that the Financial Reporting Council (FRC) has encouraged institutional investors to publish by the end of September 2010 a statement on their website of the extent to which they are in compliance with the Stewardship Code. This document serves as F&C's statement of compliance; F&C's responses to the Code and its guidance are noted below *in italics*. We welcome further dialogue with the FRC, as required, to provide further detail on F&C's compliance with the principles of the Code.

Principle 1

Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.

FRC Guidance on Principle 1:

The disclosure should include:

- how investee companies will be monitored. In order for monitoring to be effective an active dialogue may, where necessary, need to be entered into with the investee company's board;
- the strategy on intervention;
- internal arrangements, including how stewardship is integrated with the wider investment process;
- the policy on voting and the use made of, if any, proxy voting or other voting advisory service, including information on how they are used; and
- the policy on considering explanations made in relation to the UK Corporate Governance Code.

¹ As of 30 June 2010, F&C Management directly managed £95 billion (€116 billion, \$142 billion) in assets. In addition, F&C has been mandated to vote and/or engage in dialogue on behalf of a further 20 investment institutions whose assets, including equities and corporate bonds, total £54 billion (€66 billion, \$80 billion).

² F&C made a submission to the Financial Reporting Council's 2010 consultation on the UK Stewardship Code. Please see: http://www.fandc.com/FundNets_FileLibrary/file/FRC_Stewardship_Code_April_2010.pdf

F&C Position on Principle 1: *F&C has long published its Responsible Ownership Policy which outlines how it discharges its stewardship responsibilities:*

http://www.fundnets.net/fn_filelibrary//file/Corporate_Governance_Responsible%20Ownership_Policy_and_Principles_for_Corporate_Governance_January_2010.pdf

Additional aspects of disclosure requested by the FRC with regard to Principle 1 are as follows:

- *The process for monitoring companies and the strategy for intervention is described in greater detail in our commentary below on Principle 3.*
- *F&C's Governance and Sustainable Investment (GSI) team takes the lead in coordinating company engagement and outreach, working closely together with F&C fund managers. The integration into the wider investment process is bolstered by the GSI team's daily meetings with fund managers, attending company meetings together with fund managers, as well as regular consultation and dialogue between the GSI team and F&C fund managers on key voting questions, corporate actions or other relevant strategic, operational and financial developments at companies in F&C's investment holdings.*
- *As discussed in greater detail under Principle 6, F&C has published corporate governance and voting policies for a number of jurisdictions, including the UK. These are updated annually and reviewed by F&C's Corporate Governance Committee. F&C's corporate governance guidelines for the UK are publicly available on its website:*
http://www.fundnets.net/fn_filelibrary//file/Corporate_Governance_Operational_Guidelines_United_Kingdom_January_2010.pdf
- *All of F&C's voting decisions are guided by its own corporate governance guidelines. F&C votes using Broadridge's Proxy Edge electronic proxy voting platform. F&C also subscribes to various voting advisory services, including Glass Lewis, ABI IVIS and Manifest. These voting services are used as supporting information in the voting process. However, it should be noted that F&C makes its own voting decisions and does not use external voting services to make voting decisions on its behalf.*
- *F&C supports the UK Corporate Governance Code, and its UK voting policies are consistent with the Code. Accordingly, F&C encourages UK listed companies to conform to the UK Corporate Governance Code. When a company chooses not to comply with the Code, F&C will consider the merits of the company's explanation. In cases where F&C is unsatisfied with the explanation and regards the departure as material, F&C will follow up with the company through engagement and proxy voting as appropriate.*

Principle 2

Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.

FRC Guidance on Principle 2:

An institutional investor's duty is to act in the interests of all clients and/or beneficiaries when considering matters such as engagement and voting. Conflicts of interest will inevitably arise from time to time, which may include when voting on matters affecting a parent company or client. Institutional investors should put in place and maintain a policy for managing conflicts of interest.

F&C Position on Principle 2:

F&C has a detailed Conflict of Interest Policy, applicable to all staff, outlining how conflicts of interest are managed. The policy identifies areas where potential conflicts might exist, and details aspects of prevention, management,



disclosure and how employees might report potential conflicts internally. This policy is reviewed annually and is accessible by staff through the company intranet.

Aspects of F&C's conflicts of interest policy of relevance to investor stewardship are as follows:

F&C manages all portfolios in accordance with each client's investment agreement, mandate guidelines and restrictions. Any potential conflicts which arise are managed using firewalls, appropriate segregation of duties and management oversight.

- *F&C only undertakes stocklending with the prior approval from the client and in accordance with the client's investment management agreement, or appropriate supplementary legal documentation.*
- *F&C's Governance & Sustainable Investments (GSI) team sets the criteria on which F&C will vote on any matter in the absence of standing instructions from the client. Policies determined by the GSI team are regularly reviewed and ratified by F&C's Corporate Governance Committee.*
- *In terms of voting and engagement F&C also considers potential conflicts of interest where F&C is an interested party. This includes F&C plc, its strategic partners, as well as F&C's clients, where conflicts could arise as a result of an existing economic relationship. For example, in voting on its shareholdings in F&C plc, the GSI team applies Glass Lewis recommendations based on Glass Lewis' interpretation of F&C's voting policies-- and does not override the Glass Lewis recommendation. This can result in F&C's votes not supporting specific resolutions at F&C plc general meetings.*
- *Significant safeguards are in place to ensure that reo® clients have identical access to engagement data as do F&C fund managers, and that confidential external client data are kept strictly out of reach of F&C fund managers. These safeguards include:*
 - *The GSI team's engagement database is available only to members of the GSI team and select IT support staff. It is not accessible by F&C fund managers.*
 - *The GSI team folder on F&C IT systems is available only to members of the GSI team and other necessary departments such as the compliance and disclosures team.*
 - *reo® engagement reports are distributed simultaneously to all clients, including overlay clients and in-house managed funds.*

Principle 3

Institutional investors should monitor their investee companies.

FRC Guidance on Principle 3:

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.

As part of this monitoring, institutional investors should:

- seek to satisfy themselves, to the extent possible, that the investee company's board and committee structures are effective, and that independent directors provide adequate oversight, including by meeting the chairman and, where appropriate, other board members;
- maintain a clear audit trail, for example, records of private meetings held with companies, of votes cast, and of reasons for voting against the investee company's management, for abstaining, or for voting with management in a contentious situation; and

- attend the General Meetings of companies in which they have a major holding, where appropriate and practicable.

Institutional investors should consider carefully explanations given for departure from the UK Corporate Governance Code and make reasoned judgments 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.

Institutional investors should endeavour to identify problems at an early stage to minimise any loss of shareholder value. If they have concerns they should seek to ensure that the appropriate members of the investee company's board are made aware of them.

Institutional investors may not wish to be made insiders. They will expect investee companies and their advisers to ensure that information that could affect their ability to deal in the shares of the company concerned is not conveyed to them without their agreement.

F&C Position on Principle 3:

- *F&C's GSI team and fund managers actively monitor investee companies. Among other things, this includes voting on F&C's holdings, and engaging with companies, when relevant, on financial, strategic, governance, social, ethical and environmental themes.³*
- *F&C also uses a range of research tools that help to prioritise and facilitate the monitoring and analysis of companies in F&C's portfolio from financial, governance and sustainability perspective. Service providers to F&C's GSI team in this regard include EIRIS, SIRIS, GMI, The Corporate Library, ABI IVIS and ISS.*
- *F&C makes use of these research tools, along with its own direct analysis of the companies in its investment holdings, to identify companies for further engagement and outreach. This is done in the context of the GSI team's portfolio monitoring process, which is used to flag issues of potential concern for company dialogue.*
- *F&C maintains a proprietary in-house database that provides detailed documentation and a clear audit trail of F&C's engagement with companies. F&C provides a confidential report on its company engagement to its reo® clients on a quarterly basis, highlighting the number of individual engagements, the specific issues engaged upon, as well a quarterly list of "milestones" – F&C's term for positive engagement outcomes.*
- *With regard to voting, F&C's voting database maintains a record of all votes and reasons for voting against management or for voting with management in contentious situations. As noted below, this voting record is in the public domain on F&C's website, and is updated on a monthly basis. F&C also communicates to the chairmen of investee companies with regard to specific resolutions that F&C has voted against in company general and extraordinary meetings to ensure that the company's board is aware of F&C's specific concerns.*
- *Attending company general meetings is not a normal part of F&C's engagement, as F&C conducts most of its engagement with companies on a 1:1 basis-- or collectively with other investors. However F&C will attend a company's general meeting in cases where F&C judges this to be the most effective means of communicating to the company.*

Principle 4

³ The policies on Corporate Governance are employed by the F&C Group with the following exceptions: F&C Portugal, F&C REIT, F&C Alternative Investments, F&C Partners, F&C Private Equity and Thames River Capital.

Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.

FRC Guidance on Principle 4:

Institutional investors should set out the circumstances when they will actively intervene and regularly assess the outcomes of doing so. Intervention should be considered regardless of whether an active or passive investment policy is followed. In addition, being underweight is not, of itself, a reason for not intervening. Instances when institutional investors may want to intervene include when they have concerns about the company's strategy and performance, its governance or its approach to the risks arising from social and environmental matters.

Initial discussions should take place on a confidential basis. However, if boards do not respond constructively when institutional investors intervene, then institutional investors will consider whether to escalate their action, for example, by:

- holding additional meetings with management specifically to discuss concerns;
- expressing concerns through the company's advisers;
- meeting with the chairman, senior independent director, or with all independent directors;
- intervening jointly with other institutions on particular issues;
- making a public statement in advance of the AGM or an EGM;
- submitting resolutions at shareholders' meetings; and
- requisitioning an EGM, in some cases proposing to change board membership.

F&C Position on Principle 4:

- *F&C makes use of the research tools outlined above in the discussion on Principle 3 to flag anomalies or breaches of good business or practices that might call for engagement or intervention. The GSI team also has regular dialogue with F&C fund managers to discuss with them problem situations that warrant escalation. This is a standard operating practice for F&C, and this resulted in focused engagement on 1644 companies globally in 2009. This activity included 314 face-to-face meetings with companies, 89 of which were at Board level.*
- *As a broader framework for internal governance F&C has established a Corporate Governance Committee (CGC) comprised of senior executives, including members of F&C's Executive Committee. The CGC is a formal body for reviewing F&C's governance policies. Its Terms of Reference include the following:*
 - *Defining best practice towards corporate governance including, where appropriate, social and environmental issues as well as financial and fiduciary.*
 - *Ensuring that F&C has clear, documented guidelines in place for determining how it votes its shares in investee companies.*
 - *Monitoring that shares in investee companies are voted in line with clients' own policy or F&C guidelines, if selected.*
 - *Reviewing specific investee company cases should they be particularly difficult or contentious.*

The last bullet point is of particular relevance to Principle 4, in that it provides a senior forum for escalation to review problematic cases with companies in F&C's investment holdings.

Principle 5

Institutional investors should be willing to act collectively with other investors where appropriate.

FRC Guidance on Principle 5:

At times collaboration with other investors may be the most effective manner in which to engage. Collaborative engagement may be most appropriate at times of significant corporate or wider economic stress, or when the risks posed threaten the ability of the company to continue. Institutional investors should disclose their policy on collective engagement. When participating in collective engagement, institutional investors should have due regard to their policies on conflicts of interest and insider information.

F&C Position on Principle 5:

- *Collaboration with other investors is an important part of F&C's engagement outreach, and much of F&C's engagement is conducted on a regular basis with other investor groups.*
- *F&C has a long track record of collective engagement with other investors around the world. This includes our active involvement in investor bodies referenced elsewhere in this document, including:*
 - *Association of British Insurers (ABI) Investment Committee;*
 - *ABI Remuneration & Share Schemes Panel;*
 - *Quoted Companies Alliance (QCA) Corporate Governance Committee;*
 - *Investment Management Association (IMA);*
 - *National Association of Pension Funds (NAPF)*
 - *Global International Governance Network (GIGN);*
 - *International Corporate Governance Network (ICGN)—chairing the ICGN Business Ethics Committee;*
 - *Asian Corporate Governance Association (ACGA);*
 - *Council of Institutional Investors (CII);*
 - *UN Principles for Responsible Investment (PRI); and*
 - *Private Sector Advisory Group of the Global Corporate Governance Forum.*

Principle 6

Institutional investors should have a clear policy on voting and disclosure of voting activity.

FRC Guidance on Principle 6:

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. Institutional investors should disclose publicly voting records and if they do not explain why.

F&C Position on Principle 6:

- *F&C has developed 15 separate sets of voting and corporate governance guidelines that are customised to match the specific legal, regulatory, ownership and governance environments of individual jurisdictions around the world. In addition to F&C's general voting guidelines, the region/country-specific guidelines include the following jurisdictions: the UK; US; Japan; Germany; France; The Netherlands; South Korea & Taiwan; India; China; Russia, Ukraine & Kazakhstan; Latin America; Hong Kong, Malaysia & Singapore; Australia; Indonesia, The Philippines & Thailand.*

- *In 2009 F&C voted almost 58,000 resolutions at 5225 company meetings in 66 countries; in the UK F&C voted 8753 resolutions at 935 company meetings.*
- *It is F&C's policy to vote on its holdings and to disclose this voting activity publicly.*
- *It is also F&C's policy to write the chairmen or senior executives of companies a letter outlining each case in which F&C did not support management resolutions; F&C sent over 4000 such letters in 2009.*

Principle 7

Institutional investors should report periodically on their stewardship and voting activities.

FRC Guidance on Principle 7:

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

Transparency is an important feature of effective stewardship. Institutional investors should not, however, be expected to make disclosures that might be counterproductive. Confidentiality in specific situations may well be crucial to achieving a positive outcome.

Those that act as principals, or represent the interests of the end-investor, should report at least annually to those to whom they are accountable on their policy and its execution.

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 01/061 and SAS 702. The existence of such assurance certification should be publicly disclosed.

F&C Position on Principle 7:

- *F&C publicly reports its voting activities on a monthly basis. These reports contain details of votes on individual resolutions and an explanation of the reasons for any votes that do not support management. These voting reports are posted on F&C's website: http://www.fandc.com/FundNets_FileLibrary/file/co_gsi_voting_records_year_to_date.pdf F&C also reports publicly on its company engagement activities in its quarterly public reports. These reports provide detail on company engagement by number of companies, issue, geography, and reasons for engagement. F&C provides detailed quarterly confidential reports to clients outlining details of engagement on specific companies in client holdings. F&C also provides a public engagement report on an annual basis that is posted on its website: <http://www.fandc.com/new/Institutional/default.aspx?id=94094#75988>*
- *With regard to external assurance, F&C notes point 37 in the FRC's document "Implementation of the UK Stewardship Code", published in July 2010. This notes that a guidance of external assurance is currently being developed by a group led by the Institute of Chartered Accountants of England and Wales (ICAEW), and suggests that asset managers may wish to wait until this guidance is finalised before considering how best to comply with this part of the Stewardship Code. While F&C anticipates that it will seek external assurance regarding its Code compliance, F&C's current view is to wait for the publication of this ICAEW guidance before implementing this part of the Code.*



F&C Contact Person for matters relating to the Stewardship Code:

George Dallas
Director, Corporate Governance
Governance and Sustainable Investment
george.dallas@fandc.com
020 7011 4246