

# F&C

## Corporate Governance: Operational Guidelines

France

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**F&C**  
Investments

Expect excellence

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These guidelines set out F&C Management Ltd's (F&C) expectations of companies in terms of good corporate governance and explain how F&C exercises its votes on French companies.<sup>1</sup> They should be read in conjunction with F&C's "Responsible Ownership" policy, which describes F&C's overall philosophy and general approach to voting and engaging with companies.<sup>2</sup>

The guidelines are structured as follows:

- Preamble
- Overview of key principles and F&C's approach
- Role, structure and operation of boards
- Board committees
- Report and Accounts
- Remuneration
- Shareholder rights
- Voting matters
- Investment institutions.

### Preamble

The following outlines F&C's Corporate Governance policies and guides its voting on all stocks. It applies to all F&C retail portfolios, and the resultant voting record is published each month, along with detailed explanations, on F&C's website.<sup>3</sup>

F&C's 'House' voting policies are also applied to F&C's institutional client portfolios. However, each of F&C's institutional clients has ultimate control over the determination and execution of its voting policy. F&C will recommend a voting stance to its clients on the basis of these policies, but will defer to its clients in individual cases where they may choose to vote otherwise. In cases where an individual client's voting preference is at odds with the F&C recommended position, this will be applied solely to that client's funds, and shall under no circumstances apply to the voting instructions issued on behalf of other F&C client portfolios. F&C House policies are disapplied should a client demand it, though they always reflect our voting behaviour on all F&C retail funds. As regards institutional client funds, these policies apply at all times, except in cases where individual institutional clients may wish to amend voting decisions on particular stocks held within their own portfolios. At no time shall individual client voting decisions affect the decisions taken on behalf of other F&C clients. Institutional clients receive a full detailed report of their funds' voting record on a quarterly basis, and have the option of publishing it if they wish. F&C's voting and governance policies underpin its engagement with investee clients, and guide its voting at AGMs and EGMs.

**F&C will apply these guidelines when voting on behalf of clients, unless otherwise instructed.** F&C's voting and governance policies underpin its engagement with investee clients, and guide its voting at AGMs and EGMs.

Prior to 2008, investors who wished to cast their vote at a French company meeting were prevented from trading in the run up to a general meeting, causing their voting rights effectively to be 'blocked'. France's decision to implement a 'record date' in 2007 (which allowed investors to record a specific date at which they held their shares), removed shareblocking, and delivered increased voting access to non-resident investors. This increase has led F&C to develop this first set of guidelines specifically for companies listed in France. F&C expects to update this document annually, to reflect regulatory changes, evolving market practices and any other relevant developments.

These guidelines take into consideration the December 2008 recommendations released by the business trade groups Association Française des Entreprises Privées (AFEP) and the Mouvement des Entreprises de France (MEDEF), which resulted in the creation of the AFEP-MEDEF Corporate Governance Code of Listed Corporations (hereafter the 'AFEP-MEDEF Code'). The AFEP-MEDEF Code draws upon the Viénot reports of 1995 and 1999, on the Bouton report of 2002, and on the 2007 and 2008 recommendations by AFEP and MEDEF. These guidelines also consider the 2009 'Recommendations on Corporate Governance' issued by the Association Française de la Gestion Financière (AFG).

As well as codes initiated by the business community, F&C's guidelines also take into account regulatory developments. In France, this includes the new governance provisions of the law, 'Loi en faveur du Travail, de l'Emploi et du Pouvoir d'Achat' (TEPA), in 2007, which requires companies to put severance agreements, based on performance conditions, to a vote.

Many companies in France are still controlled by large majority or family shareholders. F&C is concerned that in some cases, the interests of controlling shareholders may diverge from those of minority shareholders. As a result, F&C's corporate guidelines for France take into consideration those aspects of board structure, shareholder rights and remuneration which serve to provide protection for minority shareholders relative to controlling shareholders.

1. General Operational Guidelines and Country specific guidelines for France, Germany, Japan, the Netherlands, the UK and the United States are available within the Governance and Sustainable Investment section on the F&C website: <http://fandc.com/governance>.

2. <http://fandc.com/governance>.

3. <http://fandc.com/governance>.

# 1. Overview of key principles and approach

F&C has established a global philosophy and approach to corporate governance and exercising its votes. Its approach is based on the overarching principles of:

- An empowered and effective board and management team;
- Appropriate checks and balances in company management structures
- Effective systems of internal control and risk management covering all significant issues, including corporate responsibility issues
- A commitment to promoting throughout the company a culture of transparency and accountability that is grounded in sound business ethics and
- A remuneration policy that rewards the creation of long-term shareholder value through the achievement of corporate objectives.

As a global investor, F&C recognises that such principles may be expressed differently in different markets. Therefore, its voting

policies take account of local practices and are applied in a pragmatic fashion that reflects an integrated understanding of local and international good practice. In all cases, F&C aims to achieve the same result: the preservation and enhancement of long-term shareholder value through management accountability and transparency in reporting.

Achieving best practice in corporate governance is a dynamic process between board, management and shareholders. F&C encourages companies to engage in the process of shaping and meeting evolving standards of best practice. While F&C's voting is strongly rooted in a clear set of corporate governance principles, it strives to approach each company's case on its merits and relies on staff expertise and discretion to tailor voting. F&C encourages companies to make contact to discuss any areas where they consider divergence from its guidance to be necessary and justified.<sup>4</sup> When F&C does not vote with directors' recommendations, it writes to the company and explains the reasons why.

## 2. Role, structure and operation of boards

### Introduction

F&C uses the term 'board' to cover the unitary board, the two tier board, and the unitary board supported by an executive body whose members may or may not be members of the public company board. In France, the majority of companies now have a unitary board, though the two-tier board structure can still be employed.

The board is ultimately responsible for the management of the company. This is mainly achieved through the delegation of powers to the executive management. The board should receive the report of the executive on the conduct of the business, and it should question the executive on these matters. However, certain matters should be reserved for the board. It is responsible for testing and setting strategy proposed by the executive, and for succession planning of both the executive and the board as a whole.

The structure, composition and operation of boards will vary from country to country and company to company. Certain elements of effective boards are universal, and these are detailed below under the following sub-headings:

- Size and structure;
- Roles and independence;
- Competence, objectivity and renewal;
- Effective functioning of boards; and
- Accountability to shareholders.

Other factors will vary depending on the nature of the company's

business, its country of domicile, its size and complexity, its stage of development, its ownership structure, the remit of the board and the skills of the individuals on the board. Wherever possible, F&C will strive to reflect in its voting the individual circumstances facing each company, based on its understanding of how they may affect its long-term profitability. F&C welcomes and encourages overtures from companies to draw its attention to specific areas where they believe such departures from its guidance are justified.

### Board size and structure

Both unitary and two-tier board structures exist in France. The recommendations of the AFEP-MEDEF Code refer specifically to companies with a unitary board, but invite companies with a two-tier board structure, or controlled companies, to make the appropriate adjustments to implement the Code's recommendations. F&C does not favour one structure over the other, but believes that achieving an appropriate balance of inside and external perspectives is paramount.

### Unitary board

Companies with unitary boards should ensure that the board reflects an appropriate mix of executive, and independent non-executive directors (see "Balanced composition" on page 4 and "Effective functioning of boards" on page 5).

### Two-tier board

Two-tier board structures comprise a supervisory board and a management board. Where there is more than one body forming the board, companies should maintain an effective mechanism for the

<sup>4</sup> F&C expects to vote at all company meetings. These votes will usually be by proxy, except where specific circumstances make attendance by a representative of F&C desirable. When F&C does not vote with directors' recommendations, it writes to the company and explains the reasons why.



various elements of the board to work together, and should explain how this happens. This system should ensure that the most effective use is made of all the individuals involved, so that companies can capitalise on the unique skills and experiences of their directors.

Neither board should be too large; between five and ten members is typically suitable. The ratification of the acts of the management and supervisory board should be the subject of separate votes.

### **The role of the chairman and separation of principal roles**

The roles of Chairman and Chief Executive Officer (CEO) are substantively different and generally should be separated. F&C regards separation of the roles as important for securing a proper balance between executives and minority shareholders, and preserving accountability within the board. F&C recognises that it is common practice in France to combine these two roles. Moreover, the AFEP-MEDEF Code stipulates that it is at the discretion of the board to combine the roles. If for any reason the roles are combined, this should be explained and justified in the report and accounts. In all such cases, the board should designate a strong senior independent non-executive director.

### **Roles and independence**

The composition of the board is of the utmost importance. Boards should have meaningful representation of both executive and non-executive elements. Non-executives should normally be wholly independent of the company, although F&C recognises that, in certain cases, connected non-executives have a valuable role to play. In building an effective board, the company should seek candidates from the widest pool of relevant talent so as to ensure properly informed board discussions. F&C's more detailed expectations are set out below.

#### **Role of the chairman**

The chairman sets the agenda of the board in consultation with the company secretary, the executive and the directors. He is the person responsible for the appointment and removal of the chief executive (CEO).

In large companies, where the Chairman is by definition not considered independent, or if the Chairman is an ex-CEO, it is advised that he neither chair any of the board committees nor be a member of any committee, except the nomination committee. He should attend all committee meetings by invitation.

#### **Executive directors**

Including executives in board meetings is essential to enhance discussion and allow independent directors to gain the fullest understanding of company operations. When there is a unitary board, executives who attend most meetings should be members of the board, but their number should not outweigh the number of independent non-executives.

#### **Non-executive directors**

Non-executive directors have a valuable contribution to make to the development of the company. This is a demanding role. While F&C

does not have rigid rules about the number of directorships an individual can hold, he<sup>5</sup> must have sufficient time and energy to discharge the role properly, particularly during business situations requiring exceptional investments of time. Factors that determine the appropriate number of directorships are the size of the company, its complexity, its circumstances, other commitments that a director has and the results of board evaluation, among others. F&C considers that holding over four directorships in large companies is likely to be excessive for even a full-time non-executive director, especially if participating in board committees. A reasonable number is likely to be lower for a full-time executive. In addition, nominating committees should carefully consider the time required for other demanding leadership roles, such as the boards of private companies and large charitable organisations.

#### **Proportion of non-executive directors**

While F&C generally expects all widely-held companies to have a majority of independent directors, it believes that having an appropriate mix and balance of skills is more important than a fixed proportion of non-executive directors. However, it is essential to have enough independent non-executive directors for an adequate spread of views on the board and for membership of the board committees. For companies with controlling or majority shareholders, F&C also encourages companies to have boards that have a majority of independent directors. However, in cases where the controlling or majority shareholder opts to elect a majority of non-independent directors to the board, there should be a sufficient number of independent non-executives on the board to allow key committees (normally audit and remuneration) to operate with full independence. For this to be achieved, F&C would, in most cases, go beyond the requirements of the AFEP-MEDEF Code and expect there to be a minimum of one-third of board directors to be independent in companies with a controlling shareholder.

#### **Independence of non-executive directors**

Independence of individual directors is valued, but a well balanced board is valued above all. F&C will support non-independent directors when they bring skills, sector knowledge and other experience that justify their presence on the board.

For public companies, independent non-executive directors on the supervisory board should:

- Not be former executives of the company. F&C does not support the idea of a "cooling off" period for former executives, although in the case of individuals who have served in a junior capacity, a hiatus may be appropriate;
- Not have close family ties with the company's advisors, directors or senior employees;
- Not have served on the board for more than 12 years, as they may lose their independent perspective;
- Not hold cross-directorships or have significant links with other directors where there is a power imbalance between the directors (see 'Interlocking boards' on page 4);
- Not be major shareholders or representatives of any special

5. F&C encourages companies to nominate competent male and female board members. However, for simplicity, F&C uses the terms "chairman" and "he", "his" and "him" irrespective of the gender of the individual occupying that post.

interest group, including government representatives in cases of state ownership or representatives of affiliated companies;

- Have no significant commercial involvement with the company as professional advisers, auditors, major suppliers, customers, investment bankers or commercial bankers;
- Not be entitled to performance-related pay, stock options, or pensions; and
- Not normally hold other directorships in companies in a closely-related industry.

However, F&C's applies a principles-based approach, as it seeks to ensure that directors are able to act in the interests of the company and its shareholders. Companies should consider using the corporate governance report or annual proxy to explain the board evaluation process, and to justify the value that non-independent directors bring to the board.

### Interlocking boards

F&C seeks to ensure that directors are not only independent from the company, but also from their fellow directors. F&C strongly discourages the practice of interlocking board memberships. In cases where this does exist, F&C expects companies to disclose interlocking board relationships and to explain how the independence of individual directors is preserved when directors jointly serve on two or more of the same boards.<sup>6</sup> In cases where directors were board directors are also members of other company boards, these board members should not be members of the same board committees, particularly the audit and compensation committees.

### Role of Employee Works Councils & Employee Representatives

If employee shareholdings exceed 3% of a company's corporate capital, French legislation requires companies to appoint one or more employee directors to the board. These directors are nominated by the board and approved by shareholders. French law also provides for representatives from Employee Works Councils to be involved in the proceedings of the Board in an advisory capacity. F&C recognises employees as important stakeholders and therefore encourages management and supervisory boards to consult with employee works councils and/or employee directors regarding any significant business changes. Where companies put forward employee directors to serve on the board, F&C does not consider these directors to be fully independent, without further information provided by the companies; therefore, it would not expect them to sit on the audit or remuneration committees.

F&C recognises employees as important stakeholders and therefore encourages management and supervisory boards to consult with employee works councils and/or employee directors regarding any significant business changes. Where companies put forward directors nominated by the works council to serve on the board, F&C does not consider these directors to be fully independent, without further information provided by the companies; therefore, it would not expect them to sit on the audit or remuneration committees.

## Competence, objectivity and renewal

### Competencies and perspectives

A relevant and suitably diverse mix of skills and perspectives is critical to the quality of the board and the strategic direction of the company. Companies should therefore strive to widen the pool of potential candidates to ensure that they draw on the richest possible combination of competencies and outlooks. The use of specialist recruitment consultants and other appropriate sources, including public advertisement, should be considered.

Boards should recruit members with the best possible combination of skills and experience and should affirm the value of individual diversity, including diversity of gender, ethnic origin, nationality, professional background and many other factors so as to enhance the board's and the company's overall performance. While boards should not be transformed overnight, F&C looks for an equal opportunities policy or diversity statement, and seeks evidence that the basic principles of openness and effectiveness are achieved.

### Re-election of directors

To ensure that it retains an open and critical perspective, the board needs to be continually renewed. For this reason, all directors should be required to submit themselves for re-election at regular intervals. F&C encourages the chairman of the board, as well as the chairmen of the audit, remuneration and nomination committees to stand for annual re-election. This will serve to strengthen accountability on the core functions of the board. F&C also believes that a minimum of one-third of the board should stand for election annually.

### Nomination of directors

F&C strongly believes that a board nomination committee composed by a majority of independent non-executive directors, plus the company chairman, is best placed to identify and put forward suitable candidates for the board. Shareholders should only put forward candidates where there is clear evidence of ineffective board oversight and unwillingness to correct the problem. F&C expects companies to put forward only one candidate for each available position, as an indication that the company is clear about the value individual directors bring to the board.

### Balanced composition

F&C will consider voting against the chairman or members of nominating committees who have not constructed appropriately balanced, independent boards. Indicators include: an over-reliance on long-standing members where one-third of non-executive directors have served for more than 12 years; an over-reliance on affiliated directors; and a lack of any gender, racial, or national diversity. F&C considers that extended service on the board erodes non-executives' independence due to their involvement in previous business decisions. Therefore, after 12 years, directors should be subject to annual re-election, and should not serve on key board committees.

6. Such interlocking relationships can raise concerns when there is an imbalance of power between the two directors. The most common situation is when one of the individuals is an executive on the first board, and, therefore, is evaluated and remunerated by his fellow director. Therefore, on the second board where he is expected to serve as an independent non-executive, his independence may be compromised



### Retiring directors

F&C would not normally expect to see a retiring executive director retain a seat on the board as a non-executive director, except in highly unusual circumstances. Particular scrutiny would apply in the case of retiring CEOs if nominated for chairman. However, for two-tier boards, F&C recognises that there may be instances in which the contribution of former directors will be valuable in enhancing the supervisory board's understanding of the business. In such cases, F&C would expect that no more than one member of the supervisory board be a retiring executive, and would expect that all other members be fully independent. F&C would not expect a retiring CEO to assume the role of chairman. In such cases, F&C would look for reasoned justification from the company to explain this deviation from good practice.

### Effective functioning of boards

#### Drawing on expertise and knowledge of executives

In order to ensure the board has full understanding of the business, there needs to be an effective mechanism for the board to draw upon the expertise and knowledge of executives. This is particularly important in the case of supervisory boards, or other boards without significant executive representation, where it is important for executives to contribute to board discussions where appropriate. Where relevant, appropriate executives should be invited to attend board meetings.

#### Board evaluation

Evaluation is an important tool for improving board performance. All boards should implement an evaluation process, preferably conducted on an annual basis, that considers the effectiveness of the entire board, the contributions made by each member, its systems for interacting between the board and the management of the company in a meaningful fashion and any areas for improvement. The nominating committee may oversee the evaluation process and should report general findings and areas for improvement publicly to shareholders. F&C encourages companies to utilise external parties to assist in board evaluations and validate internal processes on a periodic basis.

#### Board meetings & attendance

The board should meet at regular intervals to ensure effective oversight of the company. F&C normally regards six meetings as a minimum, and, often, more frequent meetings are necessary. Director attendance at board meetings is crucial for making valuable contributions to the board and fulfilling fiduciary duties. F&C also expects directors to attend the annual meeting, and to facilitate communication with the shareholders whom they represent. The company should disclose the attendance record of individual directors in the annual report, as well as mechanisms for shareholders to communicate directly with the board. F&C may withhold support from directors with a poor attendance record or boards who fail to accommodate shareholder dialogue.

### NED-only meetings

Non-executive directors (NEDs) should meet without executive board members present, on a regular basis, e.g. prior to board meetings, and when circumstances demand. They should also have at least one meeting per year to hold an unconstrained discussion away from day-to-day business matters. Ideally, this should be chaired by a senior or lead independent director, although the chairman may be present provided he is a non-executive. Conversely, in the case of two-tiered boards, supervisory boards should meet with executives on a regular basis to minimise the risk that NEDs will become marginalised from the business.

Non-executive directors should also meet on a regular basis with the company's auditors, without management present.

### Training

All directors should receive appropriate training when appointed, and subsequently on regular occasions. Training needs should be identified during the board evaluation process. F&C encourages companies to develop director training plans that include educating directors on significant environmental, social and governance matters.

### Corporate secretary

The corporate secretary provides an important conduit for shareholders to address the board, and communicate with non-executive directors. The corporate secretary is accountable to the board rather than to management and should be appointed and employed specifically by the board, rather than by the company. The board is the only body that should have the authority to dismiss the corporate secretary.

### Accountability to shareholders

The board should proactively make itself available for consultation with shareholders on any substantive matter, whether or not it forms the subject of a vote, and may, to this end, appoint a senior or lead independent director to fulfil a formal liaison role. Directors should consult shareholders, particularly institutional shareholders, prior to seeking approval for resolutions at the annual general meeting (AGM) and other meetings where any resolution could be considered contentious or consultation is otherwise deemed appropriate.

The non-executive directors should also seek to establish lines of communication with the principal institutional shareholders, in separate meetings and by joining a few of the regular meetings that executive directors hold with institutional shareholders.

## Voting on board matters

- F&C will usually support directors' recommendations for board membership or ratification unless it has justified reservations. F&C will not support a director if it has strong concerns about the performance, integrity or independence of that individual (see "Voting on board committees" on page 8).
- F&C may signal its concern regarding the conduct of business by not supporting ratification of management board acts. F&C will not support ratification of supervisory board acts if it has serious concerns regarding elements of control, or board structure and composition.

- If no directors are standing for election, F&C may not support the approval of the company's report and accounts.
- F&C will vote against directors who fail to attend at least 75% of board meetings.
- Where there is more than one candidate proposed for a board position, F&C will vote in favour of the candidate F&C considers most suitable, and will take due note of any recommendation by directors.

## 3. Board Committees

**F&C considers it essential for the board to have independent audit and remuneration committees, as well as a nomination committee composed of a majority of independent directors.** While controlled companies may have a smaller proportion of independent directors, F&C nonetheless expects the audit and the remuneration committees to be fully independent. Corporate responsibility committees, focusing on ethics, health and safety, environmental issues and sustainability, are desirable, and in some cases essential. All board committees should report on their activities annually to shareholders (see section on "Reporting" on page 8).

### Nomination committee

A nomination committee should oversee all board and senior executive appointments. Normally it should be a committee of independent non-executive directors and the company chairman, drawing on executive advice as required. F&C prefers a fully independent committee. However, F&C recognises that in some instances, a representative of a large shareholder may be appropriate.

### Audit committee

The audit of a company provides an important safeguard for shareholders and for all those that have dealings with that company with regard to the control and financial status of the company.

### Composition and principal role

- Going beyond the recommendations of the AFEP-MEDEF Code, F&C believes that the audit committee should consist *exclusively* of non-executive directors, all of whom should be independent, and number at least three individuals. This is the case even for controlled companies. At least one should have recent and relevant financial experience, and all audit committee members

should be financially literate. The committee should be responsible for assessing the effectiveness, independence, qualifications, expertise and resources of the external auditors and oversee the process of review and issue of the accounts.

- F&C recommends that the independent members of the audit committee meet on a regular basis with the company's auditors and without company management. This may enable a better flow of information between auditors and the board.
- If there is no formal risk management committee in place, the audit committee normally should be accountable for the proper identification, management and monitoring of internal controls. This includes reviewing all significant financial and extra-financial risks. The audit committee is also normally responsible for reviewing internal business ethics systems, and ensuring that there is an effective mechanism for the confidential internal reporting of wrongdoing, whether within the company itself, or involving other parties, such as suppliers, customers, contractors or business partners. Business ethics control systems should include employee hotlines and other appropriate "whistleblowing" mechanisms related to financial fraud and any other breach of company policies and ethical codes. The audit committee typically may serve as the body to receive whistleblowing reports where no other acceptable body exists.
- The audit committee should also be accountable for the proper identification, management and monitoring of internal controls. This includes reviewing all significant financial and extra-financial risks. The audit committee is also responsible for reviewing internal business ethics systems, and ensuring that there is an effective mechanism for the internal reporting of wrongdoing, such as employee hotlines, related to financial fraud and any other breach of company policies and ethical codes. It may serve as the body to receive hotline reports where no other acceptable body exists.



- The audit committee is also responsible for monitoring and approving related-party transactions, and should ensure that any material related-party transactions do not disadvantage minority shareholders.
- The audit committee is responsible for publishing the annual audit report, which is essential for investors to the evaluation of the overall health of the business (see section on “Reporting” on page 8). In the event of a significant restatement of accounts or material weakness in internal controls, the chairman of the audit committee, possibly in conjunction with the senior auditor, should make himself available to shareholders upon request.

### Appointment of auditors

The auditors’ performance and appointment should be reviewed periodically, and an evaluation included within the audit report. Where the same firm remains as auditor for a period of time, there should be a policy of regular rotation of the lead auditor. F&C does not regard systematic rotation of audit firms as intrinsically desirable or in the best interest of shareholders. However, F&C does consider it to be desirable over the medium term to broaden the choice of auditors available to companies, and hence would encourage companies actively to consider using the broadest pool of audit firms wherever these can demonstrably meet the required standard of competence and global coverage. F&C expects that shareholders should be given the opportunity to vote on the appointment and payment of auditors.

### Auditor liability

F&C recognises the disproportionate risk that joint & several liability may place upon audit firms. However, F&C will only consider supporting auditor limitation liability agreements in exceptional circumstances, i.e. where the risk of a catastrophic and disproportionate claim can be demonstrated. In such circumstances, F&C expects companies to follow best practice, which includes the following:

1. Directors must assure themselves that audit quality will be preserved and enhanced
2. Auditor liability should be based on the principle of proportionality rather than a fixed monetary cap
3. Shareholder approval should be sought on a forward-looking rather than retrospective basis
4. Audit committees should ensure that a full explanation of the reasons for putting such a resolution to shareholders is disclosed
5. Directors should ensure that the effect of agreements throughout the group subsidiaries provide for proportionality.

### Fees paid to a company’s auditors in addition to audit fees

Where auditors carry out consultancy work in addition to auditing the company, this should be disclosed and the audit committee should consider whether there is a risk that the auditors’ impartiality may be jeopardised. The range, nature and tendering process for any such non-audit work, should be supervised by the audit committee, whose responsibilities in this area should be fully

disclosed. F&C recognises that there are certain areas of non-audit work where the company’s auditors may provide valuable expertise, without compromising independence. However, very large non-audit fees, or non-audit fees in excess of audit fees, may be an indicator of compromised independence.

### Risk management

The board as a whole is responsible for framing a company’s risk tolerance relative to its strategy and operations, and is also responsible for monitoring the company’s performance relative to defined risks. Financial, operational and reputational risks that are relevant to the company’s business should be included in this oversight, including material environmental, social and ethical risks.

Depending on the size and complexity of the company, a standalone risk management committee might be warranted. F&C does not have a specific expectation that a company establish a risk management committee, but does expect that in the absence of such a committee the board can demonstrate that it is alert to, and regularly monitors, company risks on an enterprise-wide basis. A risk management committee is a common feature of large bank boards, for example, but it need not be limited to financial institutions. In some companies risk management is overseen by the audit committee. However, a standalone risk committee may enhance board effectiveness in situations where the audit committee is already very stretched. It is a healthy practice for the board as a whole to review the company’s risk management as a standing item of regular board meetings.

### Remuneration committee

The remuneration committee is responsible for setting the remuneration of executive directors and senior executives, and should co-ordinate with the Group Human Resources function to develop a coherent and effective remuneration strategy throughout the company. F&C’s guidelines exceed the recommendations of the AFEP-MEDEF code in recommending the committee should consist *exclusively* of independent non-executive directors, at least three in number. F&C encourages remuneration committees to engage in direct dialogue with their largest institutional shareholders, so as to seek their input in developing remuneration policies. F&C does not expect to see employee representatives as members of the remuneration committee.

**The remuneration committee must consult with other board functions to ensure that pay mechanisms are well aligned with strategic goals and the corporation’s appetite for risk. Finally, the committee should be attentive to compensation across the corporation to assure itself that management is driving risk and strategy properly and addressing other important issues linked to pay such as discrimination and glass ceilings.**

### “Clawback” policies

The remuneration committee should maintain authority to withhold or reclaim (i.e. ‘claw back’) all or part of performance-based pay

from executives in cases where it deems it appropriate. This might occur following a significant restatement of accounts, where previously granted awards were paid on the basis of inaccurate figures or where the long-term outcomes of a specific strategy result in significant value destruction for shareholders.

### Corporate Governance Committee

F&C recognises that companies may choose to have the nominating committee or a specific corporate governance committee responsible for corporate governance practices and procedures. Regardless of the structure, the committee should monitor emerging regulatory and industry standards, strive to achieve global good practice, and should consult with institutional shareholders to understand investor expectations.

### Corporate responsibility, ethics or sustainability committees

F&C believes that a corporate responsibility, ethics or sustainability committee is highly desirable. In some cases, such as those of large companies exposed to significant social and environmental risks, they are essential. Such committees should both serve as a source of external perspectives on emerging business and societal concerns, and ensure that the company has proper internal control systems to identify and manage any risks that such issues may pose to the business.

## Voting on board committees

- F&C will not normally support non-independent and affiliated directors who serve on the three key committees. This includes directors who have served on the board for more than 12 years and continue to sit on key committees, as they can no longer be considered fully independent. However, if the company can clearly explain why their presence is necessary, then F&C may vote in favour.
- In general, F&C may vote against the reappointment of auditors where it is concerned that the ratio of non-audit to audit fees puts the auditors' independence into question.
- F&C will vote against audit committee members who are standing for re-election where it has reason to believe that a company's internal controls are inadequate or has other concerns related to the financial reports or the board's ethical conduct. This may include concerns over the independence of the auditor.
- F&C may vote against board directors who sit on committees that oversee anticorruption if company officials are charged with violations of anticorruption legislation, or if there are strong indicators that the company's internal controls relating to anticorruption have broken down.

## 4. Reporting

The report and accounts (a.k.a. annual report) is an important link in the chain of accountability. It should provide a full review of the achievements of the company and of standards followed during the accounting period. It should also outline the strategy for the development of the business.

The annual report and any proxy voting materials should be made available to shareholders in good time for consideration and discussion prior to the general meeting. F&C looks for a minimum of 20 working days. Such materials should be available in English and easily accessible, preferably on the company website.

Companies should have meaningful and transparent disclosure, so that investors can obtain a clear understanding of all important and relevant issues. The annual report should provide a full review of the achievements of the company and of standards followed during the accounting period. It should also outline the strategy for the development of the business and any significant factors affecting the company's future performance, including any significant social, environmental or ethical issues.

F&C favours reports that are:

- **Comprehensive**, covering the strategic direction of the business and all material issues, including any significant changes in the regulatory context and key ESG issues
- **Balanced**, with even-handed treatment of both favourable and unfavourable aspects
- **Transparent**, with narrative text that utilises plain language, and accounting notes that provide investors with a full understanding of the circumstances underlying the reported figures
- **Underpinned by KPIs** that drive business performance, are comparable over time, and are supported by detailed information on how they are calculated
- **Consistent and joined-up** with other company reporting, including the remuneration policy and corporate responsibility or sustainability reporting.

### Directors

Adequate biographical information on the directors should be provided for shareholders to be able to assess them. This should



include their information about their qualifications and experience, age, term of office, date of first appointment, level of independence, board committee membership and other personal and professional commitments that may influence the quality of their contribution and independence, e.g. other directorships, family and social ties, and affiliations with related companies or organisations.

## Board committees

### Nomination committee report

The committee should report annually on its activity, in particular, providing a detailed discussion of its process for identifying and appointing executive and non-executive directors and senior executives, including long term succession planning. It should also discuss the processes it employs to ensure that members reflect an appropriate diversity of perspectives, experiences and cultural backgrounds. Where necessary, the report should include a thorough discussion of the board's view of the independence of members where this might be questioned. The report should also include high-level results of the board evaluation process.

### Audit committee report

The audit committee should report on its conduct during the year and, in particular, on any specific matters of judgement relating to the application of accounting principles. It should also comment on the process for ensuring independence of the auditors and processes for supervising non-audit work, and how it considers the interests of minority shareholders with regard to material related-party transactions. F&C welcomes the opportunity to vote on the audit report.

### Qualified audit statement

Any qualification of the audit statement needs to be fully explained.

### System of internal controls and risk management

F&C expects companies to have in place robust systems for evaluating internal controls, including strong internal reporting and employee hotline or whistleblower systems. The audit or risk committee is responsible for receiving the results of these systems wherever necessary. If the audit committee's purview includes risk management, the audit committee report should also address the board's oversight of enterprise-wide risks. The directors should state, in the annual report, that they have reviewed the system of internal controls, including a proper evaluation of all risk factors and their management.

Either as part of the audit committee report or a standalone report, the company should explain the results of the company's review of internal controls, including any identified or potential weaknesses in internal controls and how the board plans to respond to these.

In line with the recommendations proposed by the Monitoring Committee's review, F&C expects companies to strengthen reporting of internal risk management and control. Internal risk reports should contain, to the extent necessary, a summary of the key trends and factors that may affect the company's future performance, including regulatory as well as significant social and

environmental impacts. F&C also expects a comprehensive description of the systems in place to provide internal risk management and control.

### Remuneration committee report

All French companies are required to publish an annual remuneration report. Good remuneration reporting outlines a company's overall philosophy and its policies and formulas for determining annual, short and long-term pay. F&C looks for remuneration reports to break down fixed versus variable pay and clearly to align total pay packages with long-term shareholder value. The remuneration committee should clearly disclose specific long-term performance targets and total potential pay-outs. If short-term performance targets cannot be disclosed due to commercial sensitivity, F&C encourages retrospective disclosure of short-term targets.

### Corporate responsibility or sustainability committee report

F&C encourages companies to report on any significant social, environmental or ethical risks and opportunities in their annual reports as well as the systems in place to manage these issues. This may be supported by more detailed disclosure, as appropriate, in a separate corporate responsibility or sustainability report (see Appendix).

### System of internal controls

The directors should state, in the annual report, that they have reviewed the system of internal controls, including a proper evaluation of all risk factors and their management.

### Code of corporate governance

There should be a full and clear statement of all matters relating to the application of the principles, sub-principles and provisions of the AFEP-MEDEF recommendations. The way the provisions are put into effect should be clearly discussed. F&C recommends that, in line with the AFEP-MEDEF Code, any deviations from the Code should be explained and put to a vote at the general meeting. Companies that have a listing on a US exchange must detail how they comply with the provisions of the Sarbanes-Oxley Act.

### Shareholder resolutions and access to the proxy statement

F&C encourages companies to engage in constructive dialogue with shareholders and other external stakeholders, to obviate the need for extraneous shareholder proposals. Where engagement is unsuccessful, F&C supports shareholders' right to submit a shareholder proposal for consideration by all investors. In these instances, companies should behave respectfully, by communicating promptly and fully with shareholders and refraining from obstructing the process. The board should provide a full and reasoned response to any shareholder proposal on the ballot. F&C considers all shareholder resolutions put forward and votes in accordance with its understanding of the long-term benefit to shareholders. F&C supports shareholder resolutions relating to the right to nominate or remove directors and relating to an advisory shareholder vote on pay.

## Voting on reporting and accounts

- F&C believes that companies' report and accounts should be put to shareholders for a vote. F&C will generally approve the report and accounts, unless it has significant concerns as to their completeness and accuracy.
- F&C expects companies to disclose significant ESG issues in the report and accounts. Where these are not disclosed, and additional information is not forthcoming through dialogue with the company, F&C may not support the report and accounts or ratify management or supervisory board acts.
- F&C may vote against the company's report and accounts or against the company's auditors in cases where auditor's fees are not reported or in cases where there have been material misstatements.

- F&C will withhold support from directors where there is insufficient biographical information to assess their qualifications and independence.

- F&C may not support the re-election of audit committee members where it has reason to believe that a company's internal controls are inadequate or where it has other concerns related to financial accounting or the integrity of the auditors.

## 5. Remuneration

French law requires companies to disclose levels of remuneration given to individual executive directors, as well as the policy applied by the company to determine the remuneration that is paid. With regard to the actual remuneration schemes, the AFEP-MEDEF Code stipulates that executive remuneration should be comprehensive, balanced, appropriately benchmarked, consistent, clear and reasonable. It recommends that clear information is provided regarding the fixed and variable components ('variable' components usually referring to cash bonuses). In addition, the code gives requirements for performance conditions of share options and performance shares to executive directors, stating that compensation should be fair while still allowing companies to attract, retain and motivate executive officers.

Levels of remuneration and other incentives should be adequate to recruit, incentivise and retain appropriate staff, reflecting the work carried out and the executives' contribution to the company. No director should be involved in setting his own remuneration. Given the worldwide upward trend in total remuneration, F&C expects greater disclosure and justification of benchmarks and performance targets, and that a significant proportion of total remuneration should be variable and subject to performance conditions. Any shift away from short-term incentives should not lead to an increase in overall remuneration. F&C does not set guidelines for levels of remuneration beyond the principles mentioned below.

### A 'Say on Pay'?

Neither French regulation nor the AFEP-MEDEF Code requires companies to submit their remuneration policy to a shareholder vote. However, with increasing levels of participation at general meetings, F&C encourages companies go beyond current market practice and put their remuneration report to an annual advisory shareholder vote. This recommendation is also supported by the Association de la Gestion Financière. F&C recognises that there is presently no legal structure in place requiring French companies to put remuneration to a vote, and therefore encourages the French regulatory authorities to make a 'say on pay' possible.

F&C's experience of voting on remuneration reports has shown that this is a valuable mechanism that improves dialogue and understanding between the board and international shareholders, and recommends that companies actively consult with their major shareholders regarding remuneration issues prior to the general meeting.

### Relationship to strategy and risk

F&C expects companies to demonstrate the alignment of their remuneration policy with their overall business strategy and planning. Performance metrics should relate to the company's articulated strategy and risk tolerance. Targets should be constructed to align executive incentives to the interests of long-term shareholders, and should not create incentives for executives to undertake short-term risks that might imperil longer-term performance.



## Disclosure

F&C seeks appropriately detailed disclosure of board and management remuneration packages (see “Remuneration committee report” on page 7). The purpose of the remuneration report should be to enlighten and enhance understanding; it should not be used simply as a compliance document. In line with the recommendations of the AFEP-MEDEF Code and the 2009 AFG guidelines, F&C recommends that the annual remuneration report should reflect total remuneration including cash, options, stock and benefits that executives may receive under different performance scenarios. Pension arrangements for executives and employees should be disclosed in detail, including expected funding and pay-out scenarios.

The company should enable shareholders to understand its remuneration strategy, and assure themselves that it is properly aligned with their long-term interests. As such, in line with the AFEP-MEDEF Code, F&C expects the remuneration of all directors, including all non-executive and executive directors, to be disclosed individually. F&C looks for banded disclosure of those individuals at sub-board level who make a significant contribution to the group.

Companies should also include details on how, and in which cases, the remuneration committee might exercise its authority to withhold or reclaim all or part of non-base pay from executives. Reports should be in plain language and include an explanation of the relevant tax implications for the company or the individual director.

## Pension arrangements

Pension arrangements for executives and employees should be disclosed in detail, including expected funding and pay-out scenarios. Additional pension schemes should comply with the recommendations of the AFEP-MEDEF Code, including requirements of seniority, the benchmark period used to calculate the benefits, inclusion of employees below executive director level, and should take into account the overall compensation plan. F&C may abstain or vote against pension arrangements that do not demonstrate consideration to these recommendations. In France, F&C may consider voting against a pension arrangement if it has concerns over a director's (executive or non-executive) overall remuneration package.

## Executive contracts

Executive contracts should not be for more than 12 months, except in unusual cases, for example where an initial 24-month period is required for recruitment. In such cases, the notice period should reduce month by month until the agreed period of no more than 12 months is attained.

## Severance pay

F&C welcomes the new requirements of the TEPA law introduced in France in 2007, which requires companies to put severance payments to shareholder vote. Severance payments relating to each director must be presented in individual votes. Unless adequate justification is provided, F&C will vote against severance agreements

including payments that are in excess of two years' compensation (fixed and variable), rewards granted in the event of inadequate performance or if a director elects to leave the company, and/or an absence of meaningful performance conditions attached to the rewards. F&C also recommends that if the executive director has served for less than two years, the amount of severance pay must be proportional to his or her length of service.

## Share schemes

F&C believes that strict guidelines should be observed with regard to the issue, or potential issue, of shares for incentive schemes, both as to the proportion of shares issued and to the rate at which these are issued each year. By way of guidance, F&C would expect no more than a total of 10% of a company's equity to be used for all share schemes within a 10-year period, with no more than 5% being available for discretionary schemes during this period. Treasury shares should be included within these limits. Good practice is to include all shares used, whether market purchase or newly issued, within these limits. F&C will deviate from these limits where it is convinced that the commercial drivers for it outweigh the dilution impacts. If the company is insufficiently transparent regarding the details of such schemes, F&C may abstain or even vote against them.

## Pay for performance

F&C supports the principle of motivating and rewarding executives through the granting of equity incentives.

In line with the AFEP-MEDEF Code, F&C recommends that performance targets should be clearly disclosed and stretching. F&C believes that the remuneration committee is in the best position to determine the most appropriate performance metrics for driving the long-term business strategy.

F&C believes that overall remuneration packages should reflect a range of performance targets and should not rely too heavily on the achievement of a single performance metric. In France, the most common form of longer-term incentive is the awarding of stock options or performance shares. F&C recommends, in line with the AFEP-MEDEF Code, that stock options and performance shares should not represent a disproportionate percentage of overall compensation, that awards are not limited to executive directors, and that awards should be made at the same calendar period in each year, in order to limit any windfall effects. Stock options awarded to executive directors should not be discounted and should be subject to demanding performance conditions that are met over a period of several consecutive years.

F&C opposes fixed caps on pay, and strongly believes that exceptional performance over a significant period merits an exceptional level of remuneration. F&C opposes retesting, and may withhold support of remuneration plans where the remuneration committee has used its discretion to reduce performance targets previously approved by shareholders.

F&C will consider one-off equity awards on a case-by-case basis in light of justification provided by the company. However, frequent use

of exceptional awards raises questions over the adequacy of the overall remuneration strategy and effectiveness of succession planning. F&C will take particular care when reviewing equity awards granted for the purposes of retention when such awards are not linked to stretching performance targets. Barring exceptional circumstances, F&C will not support the award of free shares to executives that were overlooked for the position of chief executive.

F&C encourages the inclusion of social, environmental and other non-traditional financial goals for performance bonus payments where these factors have a significant impact on the company's performance. F&C also expects a discussion of the process undertaken by the company to identify such factors and an explanation as to why it considers these factors to be relevant. If the company chooses not to include any such factors in an industry where they are significant contributors to business success, the company should explain the reasons for this.

#### **Holding periods, vesting and "Clawback" policies**

Bonus payment and long-term incentive schemes should be structured to reward long-term growth in shareholder value, and be subject to performance-vesting conditions. F&C encourages a portion of the short-term bonus to be satisfied in deferred shares. Longer-term incentive plans should be share-based, and F&C's recommendations exceed the AFEP-MEDEF Code requirements by calling for vesting periods to extend from three to five years.

The remuneration committee should maintain authority to withhold or reclaim (i.e. 'claw back') all or part of performance-based pay from executives in cases where it deems it appropriate. This might occur following a significant restatement of accounts, where previously granted awards were paid on the basis of inaccurate figures or where the long-term outcomes of a specific strategy result in significant value destruction for shareholders.

In particular, where representations that executives made to the audit committee about the integrity of controls have been revealed to be inaccurate, or where executives have failed to exercise due caution in the discharge of their duties, the company should consider seeking the reclamation of performance awards.

Clawback policies may also be supplemented with extended deferral periods for share and bonus plans. The potential liability in a clawback arrangement may be scaled back over time to reflect evidence of sustained performance. The applications of a clawback policy should also not be abused; for example, for public companies that have gone private, clawbacks should not be manipulated by private equity firms solely as a means to transfer wealth from former executives back to the private company.

#### **Employee ownership**

Widespread employee ownership can positively contribute to shareholder value as it further aligns employees' interests with those of shareholders. Such devices should not, however, be instituted as anti-takeover devices, and should be included within company-wide dilution limits. While F&C generally supports broad-based stock option plans, employee discounts should not exceed 20% on a

fixed date, the company should not extend loans to purchase options, and options should not be re-priced without shareholder approval. Non-executive directors should not be entitled to options and therefore should not be included in any such schemes.

### **Voting on remuneration**

- F&C will consider all votes relating to remuneration on their merits, and vote against a policy or individual schemes where it believes that these are in the best interests of the company and its shareholders.
- F&C will vote against schemes that could lead to excessive dilution unless there are extenuating circumstances.
- Where substantial awards can be made under a scheme, and it is not backed up by appropriate disclosure, F&C will usually vote against.
- If F&C considers the overall award package, severance payments or pension agreements to be excessive, and not aligned with performance, it will vote against. This includes remuneration for any director, including the chairman. Where companies do not put the overall award package to shareholder vote, F&C may vote against resolutions seeking approval of elements of remuneration, such as Related Party Transactions.
- F&C will vote against all employee share plans that include excessive discounts, loans to exercise options, or allow for re-pricing or re-testing.
- In rare cases, where F&C cannot vote on a remuneration-related matter that is of concern, it may withhold support from any or all members of the remuneration committee or the report & accounts.
- F&C may oppose the re-election of the chairman or members of the remuneration committee if the company lacks a far-reaching clawback policy despite recent material restatements.



## 6. Shareholder rights

The AFEP-MEDEF Code does not address shareholder rights as defined in the section below. F&C issues its own recommendations and draws upon the 2009 guidelines from the Association de la Gestion Financière (AFG).

### Liaison with shareholders

Companies should be ready, where practicable, to enter into dialogue with institutional shareholders based on an understanding of shared objectives. They should be proactive in making sure important news is imparted, subject to appropriate inside information procedures, and should react helpfully to investor questions. In investment meetings with companies, companies should be prepared to address relevant corporate governance, environmental and social issues.

### Issuance of Shares

F&C respects a company's right to issue shares to raise capital. However, share issuance should be strictly limited to that which is necessary to maintain business operations and drive forward company strategy. F&C recognises that the AFG guidelines allow for increases in share capital for up to 50% of a company's total share capital without holding a shareholders meeting. However, F&C normally will not support requests to increase authorised share capital that exceed one-third of existing capital, unless specific justification has been provided (e.g. to complete an acquisition or undertake a stock split).

### Pre-emption rights

F&C believes that pre-emption rights for existing shareholders are absolutely essential. Shares may be issued for cash without pre-emption or for remuneration purposes, subject to shareholder approval and to strict limits. While practice varies globally and the AFG guidelines allow for increases without pre-emptive rights for up to 15% of a company's share capital, F&C normally considers appropriate limits to be 5% in one year but no more than 7.5% in three years for general purposes, and no more than 10% in 10 years for remuneration. F&C normally will vote against requests to issue shares without pre-emption rights above these limits, unless companies have provided satisfactory justification.

### Share repurchase

F&C expects companies to repurchase shares in the market when it is advantageous for the company and its shareholders. Authority to repurchase shares should be subject to shareholder approval, limited to one year, and not exceed 15% of the issued equity. Any share repurchase must benefit all holders on equal terms taking account of options adjustment.

### Related-party transactions

Many companies are involved in material related-party transactions that represent a significant risk for minority shareholders—particularly in cases where there is a controlling shareholder. This risk is

mitigated in companies with fully independent audit committees whose responsibility it is to ensure that such transactions are conducted on the basis of arms-length valuations. F&C strongly encourages companies to establish such committees (see “Board committees” on page 6) and to secure prior shareholder approval for material related-party transactions. In light of continued concerns, F&C recommends that each company disclose any shareholdings that its controlling shareholders may have in other companies or investment vehicles that have a material interest in the company. In France, F&C supports the AFG recommendations that related-party transactions should be presented in separate resolutions, particularly those involving executive directors or family or controlled companies.

### Voting rights

F&C favours a share structure that gives all shares equal voting rights. F&C does not support the issue of shares with impaired or enhanced voting rights. This is common practice in France, where the law provides for the possibility of double voting rights. Some French companies continue to employ voting right ceilings (a cap on the number of votes a large shareholder can execute in the event of a low quorum at a general meeting). F&C welcomes the removal of voting caps in some French companies, and, given the steadily rising quorum levels since the elimination of shareblocking in 2007, encourages companies to completely eliminate these caps. F&C is likely to withhold support for capital-raising by companies with a capital structure that involves unequal voting rights. In the case of controlled companies, F&C will review any request to issue shares with preferential voting rights to determine why these are necessary and how minority shareholders will be protected.

### Mergers and acquisitions, spin-offs and other corporate restructuring

Bids and corporate restructuring are important as a means to maintain an efficient and competitive environment. However, some bids do not add to shareholder value, so in contested takeover bids, F&C will seek to discuss matters with management and the bidder. F&C expects boards to conduct thorough due diligence prior to pursuing any merger or acquisition and to seek to maximise shareholder value in any deal. F&C will normally support incumbent management, provided the financial terms, synergistic benefits, and management quality are sound.

F&C considers social and environmental risk implications of any corporate activity as part of its assessment, particularly in high-impact industries. It likewise expects the board to evaluate any potential social, environmental or ethical risks or liabilities of any business combination.

### Takeovers

In most cases, F&C regards poison pills as inappropriate and inefficient, unless they are of a strictly controlled and very limited duration. Where poison pills are deployed, companies should seek prior shareholder approval. In 2006, French regulators introduced

Bons de Souscription des Actions (or 'BSA rules'), which allow companies to request shareholder authority to issue warrants to existing shareholders, which would be convertible into shares in the event of a hostile takeover bid. F&C will oppose issuance of these warrants, as they function as *de facto* poison pills.

### Pension and other similar significant corporate liabilities

Companies should be aware of, and report to shareholders on, significant liabilities such as those arising from unfunded or underfunded pension commitments, or liabilities for medical cover. The extent of the liability should be reported and the plans, if any, that have been put in place to cover the deficit should be reported, including a reasonable time scale for action. The principal assumptions used in calculating amounts should form part of this disclosure. Other significant liabilities could include specific operational, environmental or social risks that the company faces. The company should provide some indication of how these risks can result in contingent liabilities.

### Shareholder resolutions

F&C considers all shareholder resolutions that appear on the ballot and votes in accordance with its understanding of the long-term benefit to shareholders. Companies should always provide a comprehensive discussion of management's position on all shareholder resolutions, and be available to respond to reasonable

enquiries from shareholders (see "Liaison with shareholders" on page 13). In circumstances where F&C has serious concerns about a company's governance, including social, environmental and ethical matters, and has been unsuccessful in establishing a fruitful dialogue, it may itself put forward resolutions to invite other shareholders to support calls for the adoption of better practices.

### Voting on shareholder rights

- F&C votes against any structure that may be used as a poison pill unless companies define strict mandatory limits as to their use.
- F&C will vote against the issuance of shares with unequal voting rights unless it is in the long-term interests of all shareholders.
- Where a company seeks authority to issue shares beyond defined limits, and does not provide a satisfactory justification, F&C will vote against such authority.
- F&C votes on shareholder resolutions in accordance with its understanding of the long-term benefit to shareholders.
- F&C will support resolutions seeking approval for the elimination of unequal voting rights, and may co-file such resolutions if direct dialogue with companies proves unsuccessful.

## 7. Voting matters

### Annual general meetings

There should be an annual physical meeting of the shareholders, and all the directors of the company should attend. F&C encourages the web-based transmission of meetings.

### Vote disclosure

F&C expects companies to disclose the voting results of their general meetings both at the meetings and on their websites, with a detailed breakdown of votes for and against as well as abstentions.

F&C believes that companies have a right to know how their shareholders have voted, and therefore writes to all companies to explain any cases of votes against management, abstentions, or votes in favour that nevertheless were the subject of concerns.

In the spirit of transparency, F&C also makes available to both its institutional and retail fund customers a comprehensive record of its voting by publishing its aggregated voting record on its website on a monthly basis. Companies held in all F&C retail or institutional funds may also check their results on this web page. A summary of F&C's

voting record can be found in its quarterly Responsible Engagement Overlay (**reo**)<sup>7</sup> report, its annual corporate governance report and its annual Corporate Responsibility report.<sup>7</sup>

### Shareblocking

F&C believes that shareblocking, i.e. the practice of preventing shares from being transferred for a fixed period prior to the vote at a company meeting, acts to discourage shareholder participation and should be replaced with a record date. The recent adoption of the EU Shareholder's Rights Directive in June 2007 requires all EU member states to abolish shareblocking by 2009. F&C welcomes the removal of shareblocking in France. Where shareblocking still exists, F&C will follow client policy and may be prevented from voting because of concerns about failed trade settlement and extraordinary cost to clients.

### Stocklending

Stocklending is a widespread market practice involving the sale and contractually pre-agreed repurchase of a stock, collateralized by a basket of securities. Insofar as title to the stock passes from the

7. Available on <http://www.fandc.com/governance>.



“lender” to the “borrower”, this transaction is not, in fact, a loan, and therefore means that the voting right that attaches to the underlying stock cannot be readily detached and retained by the lender. Stocklending is an important factor in preserving the liquidity of markets and in facilitating hedging strategies; it also provides investors with a significant additional return on their investments because the sale-repurchase transaction includes a profit margin. Importantly, however, if the term of the “loan” coincides with an annual or extraordinary general meeting, the transfer of the voting right impairs the ability of the underlying shareowner to exercise his voting rights. In rare instances, this has led to abuse, where borrowers have deliberately entered into transactions to sway the outcome of a shareholder vote without any intention of owning the stock long-term.

F&C considers that the balance to be struck between stocklending and voting is a matter for individual decision by clients. For those clients wishing to be involved in stocklending, F&C’s policy is to accommodate this while retaining a minimum shareholding at all times, thereby ensuring that a vote is cast and any concerns are expressed directly through a letter to the company. Where significant voting issues arise, F&C will stop any further lending of stock, and, if necessary, will seek, on a reasonable-efforts basis, to recall all lent stock over the voting period. F&C also accommodates clients who do not wish to engage in stocklending at all, should they prefer to vote all stocks at all times.<sup>8</sup>

### Record dates

F&C recommends that a record date be set five working days prior to company general meetings for custodians and registrars to establish clearly those shareholders eligible to vote. This will give time for all relevant formalities to be completed and serves the same purpose as shareblocking without the disruptions noted above.

### Voting systems

F&C believes that shareholders have the right to appoint any reasonable person as proxy to vote their shares, either in person or electronically. F&C encourages the introduction of electronic voting systems that are accurate and provide an effective audit trail of votes cast.

Some companies have their shares held by a trust office that, in turn, issues depository receipts representing the economic ownership of the company. In these cases, the trust must solicit proxies from the holders of depository receipts without any limitations to voting rights. Where the holders of the receipts do not provide proxies, the trust office should abstain from voting. Where trusts direct votes based on various different authorities such as direct instruction or discretion, then the proportion of votes so exercised must be published. F&C believes that the authority to delegate discretion to the trust to execute voting rights should only follow an active instruction from the underlying security holder to do so, rather than be held as a default position established by the company.

### Bundled resolutions

Resolutions put to company meetings should cover single issues, or issues that are clearly interdependent. Any other practice potentially reduces the value of votes, and can lead to opposition to otherwise acceptable proposals. F&C will normally oppose resolutions that contain such inappropriately bundled provisions.

### Any other business

F&C expects to vote on resolutions the contents of which have been made clear to shareholders and are in the interests of the company and its shareholders. Where a resolution invites shareholders to vote on an “any other business” resolution, F&C will systematically vote against it.

### Political and charitable donations

F&C welcomes the opportunity to vote on company donations, if material. F&C supports charitable acts at an appropriate level, especially where an active donations policy supports the company’s engagement with its local or wider community. With respect to donations to political parties or to organisations closely associated with political parties, F&C considers that these are inappropriate and should be strictly avoided. However, in countries where the practice is widespread and deeply rooted, companies should at the very least submit their political donations policy and the past year’s donations record to a shareholder vote.<sup>9</sup>

8. This applies to funds directly managed by F&C. For clients of F&C’s responsible engagement overlay service (**reo**) service in cases where F&C does not manage the fund - clients will need to coordinate with their fund managers with regard to stocklending policies and practices.

9. For further details on F&C’s policy with regard to political lobbying and donations, click on Public Policy at <http://www.fandc.com/governance>.

## Appendix: Sustainability Reporting and Disclosure

F&C expects high standards of transparency from the companies in which it invests. This should include a narrative account within the annual report about the trends and factors affecting the performance and future development of the business. So-called “narrative reporting” is an important mechanism for improving the quality of dialogue between companies and their owners, covering the full range of factors underpinning long-term profitability. This includes areas that have not been traditionally covered in annual reports such as material environmental, social and governance

(ESG) issues. In high-impact sectors, we also expect companies to publish a comprehensive sustainability or corporate social responsibility report that provides more detailed information for a wider group of stakeholders such as employees, local communities, non-profit organisations, and government representatives. While F&C recognises that ESG reporting will vary across geography and sector, F&C has identified some overarching best practice guidelines, set out below.

### F&C’s 12 Steps to Best Practice ESG Reporting

#### Basic

- Identify significant ESG risks and opportunities for the business
- Establish and explain board accountability for ESG issues
- Set out policies for significant ESG issues and explain how they are implemented and monitored
- Establish and disclose targets and Key Performance Indicators for significant ESG issues covering global operations
- Describe systems for training board members and staff on ESG issues
- Report on performance against policies
- Identify and disclose any significant challenges in ESG management or areas of underperformance or non-compliance

#### Best practice

- Explain how ESG policies link to key operational and financial drivers
- Describe procedures for consulting key stakeholders and provide feedback on the range of views
- Describe procedures for verifying data including external verification
- Take account of widely-accepted reporting standards such as the Global Reporting Initiative
- Describe how ESG objectives are embedded into the corporate culture, including how they are reflected in remuneration policies and other performance management tools

## Winning gold with F&C

Delivering highly effective investment strategies is just one part of the service we provide. As principled asset managers, we are determined to lead our industry in all aspects of our business.

In 2009 F&C were voted winners of the 'Gold Standard' in the Fund Management category for the fourth year in succession. Only a few companies have been privileged enough to win a Gold Standard award, and as such, this is an exceptional achievement. The Gold Standard Awards aim to identify financial services companies that excel not just in service but in five key areas important to consumers of financial products and services:

### Financial strength

Ability to meet and exceed customer expectations

### Capability

Outstanding expertise and aptitude as a fund manager

### Service

Ability to maintain and grow an effective post-sales relationship

### Fair value

Assessing whether customers receive great value for money

### Trust

Ability to instil confidence in consumers

As a result, the Gold Standards are one of the hardest, most sought after awards in the financial market place.



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