
Bath & North East Somerset Council

Monitoring Review of Shareholder Voting 2014
Avon Pension Fund

Prepared by:

manifest

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1 Introduction

1.1 Aim of Shareholder Vote Monitoring

This is the fourth year (third full year of analysis) for which Manifest has undertaken a thematic review of the shareholder voting of the Avon Pension Fund (APF), putting Avon's fund manager voting behaviour into a comparative and wider context. The aim of the report is to provide further understanding of:

- voting activity taken on behalf of the Fund
- wider voting issues
- governance standards at companies
- how the Fund's investment managers use voting rights

As an on-going annual report, the report assesses progress in terms of company's governance standards versus best practice, as well as Avon's fund managers' use of votes in putting their investment governance preferences across to companies. Throughout the report, where there are comparisons to be made to the previous year's data, the previous year's data is shown in brackets (thus).

Importantly, this report looks at the full picture of how Avon's fund managers are making use of the Fund's voting rights and will therefore enable Avon to better understand and challenge fund managers about the role their voting activity plays in ownership strategy. The report enables Avon to fulfil the objectives of the Stewardship Code in constructively challenging external fund managers in their stewardship activities.

1.2 Voting in Context

Avon's voting policy gives discretion to managers to vote in line with their own voting policy and therefore does not require managers to follow Manifests' best practice template. It is important to note therefore, that the Manifest best practice template should not be viewed as a measure of 'success' or 'compliance' but more of an aspirational benchmark for best practice company behaviour.

The use of shareholder voting rights is not the only means by which shareholder concerns can be communicated to management; however, use of these rights is something that investors are being asked to consider in a more strategic, holistic manner. Managers implement their voting policy in conjunction with other shareholder tools, such as engagement, as a part of their investment management. It should therefore be noted that investment managers may be supportive of company management through a period where engagement has occurred and management are working towards making improvements from that engagement activity.

1.3 Scope of Analysis

The period covered by this report encompasses the period of the 1st January 2014 to the 31st December 2014. It represents a full years' voting.

Manifest analyses the issues at hand to provide a 'Template Guidance' for each voting resolution. This guidance is the result of assessing the company and the resolutions proposed for the meeting in light of a Voting Template framed upon corporate governance best practice policy developed by Manifest for Avon.

Members should consider the Voting Template as a best practice policy in terms of corporate governance standards for investee companies, rather than in terms of voting decisions by investors and therefore not a benchmark target for Avon's managers.

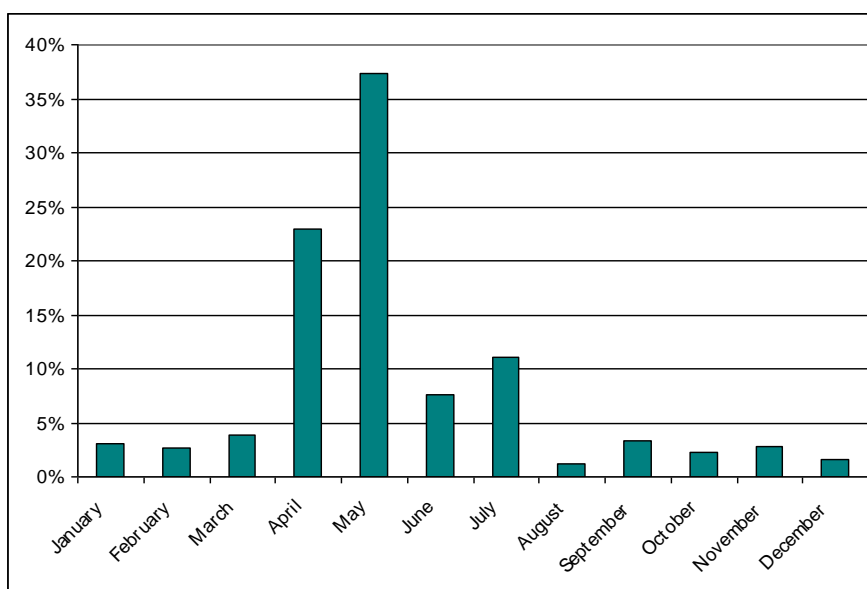
The precise tactical use of voting rights is in itself a strategic investment consideration taken by managers. Therefore, for the purposes of this report, Members should bear in mind that the fact the Voting Template identifies an issue of concern (i.e. suggests there may be a reason to not support management or requiring further fund manager review) in relation to a resolution, is more significant than whether the template suggests an ‘Abstain’, ‘Against’ or ‘Case by Case’ consideration. It is in this light that we have analysed and compared fund manager voting against issues of potential concern, with the emphasis on ‘potential’.

1.4 Peak workloads

Institutional investors are faced with a highly seasonal cycle of activity when it comes to voting shares. With the vast majority of companies reporting a financial year end of the 31st December, there is a resultant surge in the number of annual meetings relating to that year end during quarter 2 of the calendar year, especially in April and May. Figure 1: Percentage of Total Annual Resolutions Voted Per Month below shows the percentage of total annual resolutions voted by Avon’s fund managers per month, covered by the full monitoring survey. It shows graphically the severe concentration of voting decisions that occurs in April and May of the calendar year, with 60% of the voting occurring during those two months, and a further 19% during June and July.

Asset owners like the Avon Pension Fund should be aware that such a high concentration of work inevitably leads to the commoditisation of voting decisions and especially the likelihood of outsourcing voting decision-making responsibility to outside consultants. This dynamic is becoming the focus of regulatory scrutiny in the UK, France, Europe, the US, Canada and Australia, especially towards proxy research consultants, and the role that investors play in retaining control of voting decisions.

Figure 1: Percentage of Total Annual Resolutions Voted Per Month



1.5 Governance Hot Topics

There follows at the end of the report a selection of short pieces on issues of topical relevance to institutional investors in 2014.

2 Executive Summary

Section 3 (“Explanation of Voting Activity & Monitoring Approach”) explains what shareholder voting is and what types of issues shareholders are frequently asked to vote upon. It also sets out the number of meetings voted by Avon’s fund managers in 2014, and explains how Manifest approaches monitoring the fund manager voting at those events.

Manifest undertook full monitoring of meetings in companies in mainstream markets (primarily the UK, Europe and North America). The research brought a total of 1,166 meetings, comprising a total of 17,711 resolutions. Taking into account occurrences of more than one fund manager voting on the same resolution, a total of 21,880 resolution analyses have been undertaken. Of these:

- 10,550 were voted by BlackRock, again representing the largest proportion of the report data;
- 7,609 were resolutions where the Voting Template highlighted potential governance concerns and fund managers supported management; and
- 746 were voted against management.

Whilst the number of resolutions where concerns were identified but the funds managers supported management seems relatively high, this is ultimately evidence to support the significance of the word ‘potential’. Not all concerns merit a vote against management, especially where investors may prefer to use other communications to articulate their concerns before using their share voting rights. Conversely, the report also shows evidence where investors have opposed management even where no governance concerns were highlighted, which suggests an organic, active use of voting rights to enhance the wider ownership process.

Section 4 (“Common Policy Issues at Investee Companies”) examines the range of governance issues and considerations which lie behind the resolutions on which Avon’s fund managers were asked to vote, and detailing those which Manifest identified most frequently among the companies at whose meetings the fund managers voted.

Board balance and remuneration issues remain the most frequently identified concerns, partly because they are the substantial issues of the most frequently voted resolutions. The most common specific best practice governance criteria against which Manifest found Avon’s portfolio companies to fall short were:

- Committee independence;
- Lack of performance measures relating to ESG issues in incentive pay;
- Individual director independence concerns;
- Bonus as a percentage of salary;
- Board size;
- Lack of performance conditions for incentive pay; and
- Overall Board independence.

These are the substantial issues on which investors should focus, rather than whether specific resolutions were opposed or otherwise. Many of these are issues which have been consistently identified in this analysis every year. New company law regulations have come into force in the UK which have had an effect upon the way in which remuneration issues are taken into account and voted upon, with the introduction of a new separate binding vote on remuneration policy.

In the case of board considerations, this is explained by the fact that so many of the resolutions pertain to board structures (not least director elections, which are by far and away the most numerous resolution type). It should be noted that there may be multiple concerns highlighted in terms of board structure or director elections and that generally there are therefore much fewer actual resolutions to vote on than identified concerns.

By comparison with previous years, the concern of gender diversity on the board has diminished in prominence, which mirrors progress being made on the issue by companies (for example, there are now very few or no FTSE100 companies with no women on their board, a fact publicised in March 2015 by the Cranfield University School of Management's annual benchmarking report, which also identified 41 FTSE100 and 65 FTSE250 companies now had hit Lord Davies target of 25%).

The next step of the analysis is to study patterns of voting behaviour, both in terms of Avon's fund managers as well as shareholders in general (Section 5 "Aggregate Voting Behaviour"). We also examine which types of resolution have been the most contentious (Section 6 "Voting Behaviour by Resolution Category"). In terms of overall patterns of voting behaviour, with the marginal exception of TT International, none of Avon's fund managers voted with management noticeably more than shareholders in general, although BlackRock did support management marginally more than shareholders in general during 2014. Invesco and Genesis supported management noticeably less.

As has continued to be the case, remuneration related resolutions prove to be the most consistently contentious resolution category of those routinely and predominantly proposed by management as well as the lowest level of alignment with the governance best practice analysis. Common issues were absence of claw back and/or malus provisions in incentive pay, absence of ESG considerations in setting incentive pay, and over-generous caps on annual and long term incentive pay plans. The absence of claw-back provisions (one of the features of remuneration concerns two years ago) was again high up the list of concerns this year.

Overall, Avon's managers in 2014 were marginally less active in expressing concerns through their votes at corporate meetings than the average shareholder. Whereas general dissent in 2014 stood at 3.64% on average (compared to just short of 5% in 2013), Avon's fund managers opposed management on 3.56% of resolutions (down from 5.17% in 2012). This is the first year in which this has been the case, but is against a backdrop where shareholders in general have (on average) voted against management less, and where fewer issues of concern have been identified in the Manifest research. This suggests that the level of governance risk in the Avon portfolio is at its lowest point since this monitoring began.

In terms of specific themes, one prominent concern from 2012 related to absence of arrangements for claw-back of bonus, which last years research showed has receded in prominence, has now regained prominence. In this 2014 report, committee independence related concerns are comparatively greater in prominence, although there are also signs that companies in general are addressing board-wide independence concerns. With the recent focus on board diversity, we may be seeing board composition improvement at the same time.

In general terms this research has in the past suggested that we would expect to see overall trends improve over time, but that in the short term, the relative frequency of various governance themes may come and go in line with contemporary concerns and developments. This year's report very much supports this hypothesis, with comparatively lower levels of concerns and dissent both from Avon's fund managers and shareholders in general, but many of the identified themes still very familiar.

A summary of the major developments and debates in global (and especially domestic) corporate governance and voting follows in the Hot Governance Topics, featuring amendments to the UK Corporate Governance Code, impact of the new Directors' Remuneration Report Regulations in the UK one year on, changes to the UK Pre-Emption Group Guidelines, progress on the EU Shareholders Rights Directive Part II, a fund manager monitoring initiative and a new Japanese Stewardship Code.

3 Explanation of Voting Activity & Monitoring Approach

This section explains what shareholder voting is and what types of issues are frequently voted upon. It will also identify the number of meetings voted by Avon's fund managers in 2014, and explains how Manifest approaches monitoring the fund manager voting at those events.

3.1 Voting Opportunities

Voting Resolutions

The majority of meetings at which shareholders are asked to vote during the year are Annual General Meetings, at which there is legally defined, mandatory business which must be put to the shareholders. Few resolutions are actually non-binding in nature. The main non-binding resolutions at an AGM are the receipt of the report and accounts and the approval of the remuneration report.

Like investment decisions, the consideration of shareholder voting decisions often takes into account multiple questions, including company disclosures, company practices, shareholder preferences and wider engagement strategy undertaken by fund managers.

This is especially true on the report and accounts resolution. A vote against a particular resolution such as the report and accounts may be explained by any number of various potential factors.

Voting strategy should be seen as an important part of the wider investment process, by using voting rights both positively and negatively to mitigate risk in the equity portfolio. This may mean that, despite the presence of some potentially significant issues, investors may agree to support management in the short term with their votes in return for the company in question addressing concerns in the longer term.

This report will analyse voting resolutions and look at the Fund's investment managers' approach to voting in more detail in a subsequent section of the report.

Meeting Types

Manifest's experience is that companies have approximately 1.1 to 1.2 meetings per year on average. The majority of meetings at which investors vote during the year are Annual General Meetings (AGMs), at which there is legally defined, mandatory business (Meeting Business) which must be put to the shareholders. These items will vary from market to market and are a function of local company law.

Mandatory business typically includes:

- Receiving of the annual report and accounts;
- Director (re)elections;
- Director remuneration;
- Approval of annual dividend; and
- Reappointment and remuneration of auditors.

AGM business will often also contain resolutions to approve the issue of new share capital up to a certain maximum (for example in the UK this is usually one third of current Issued Share Capital (ISC)), along with an accompanying request for the dis-application of pre-emption rights which is usually used for the payment of share-based remuneration schemes for employees. This is why, as noted above, AGMs have a significantly larger number of resolutions on average than do other types of meetings.

This pattern continued to become more marked this year due to the introduction in the UK of two remuneration report votes – one on policy and the other on practice (refer to appendix for definition). Recently, UK and European companies in particular have begun to change the legal terminology for non-Annual General Meetings. As a consequence, some meetings during the period under review were reported as an EGM (Extra-ordinary General Meeting), whilst other meetings identical in nature were reported as simply General Meetings (GM). In future, GM will replace the term 'EGM'. A Special General Meeting (SGM) is what some companies might use to refer to an EGM, where a Special Resolution is the substance of a meeting (i.e. a resolution which requires a special (higher) level of support or turnout).

Other types of meetings include Court Meetings which are technically called by a Court of Law (most commonly in the UK when there is a need to approve a Scheme of Arrangement), rather than by management, and Class Meetings where only shareholders of a specified class of share may vote.

3.1.1 Meetings in the full monitoring sample by Fund Manager

During the period under review, of the 1,377 meetings in the full monitoring sample Avon Fund Managers voted at, 85.80% were AGMs (88.04% in 2013), with the majority of the rest constituting GMs 7.64% (6.29% in 2012) and EGMs 4.28% (3.2%). The remaining were nearly all Court Meetings 1.36% (0.31%) or Special General Meetings 0.79% (compared to 1.75%) and Class meetings 0.14% (0.31% during 2013), with no Ordinary General Meetings (2 in 2013).

This is broken down per manager as follows. The total number of meetings voted by managers (1,401) exceeds the total number voted at for the fund (1,011) because of instances where more than one fund manager voted at the same meeting:

Table 1: Meeting types by fund manager

| Fund Manager | Companies | AGM | GM | EGM | SGM | Class | Court | Grand Total |
|-------------------------|---------------|--------------|------------|-----------|-----------|----------|-----------|--------------|
| BlackRock | 618 | 609 | 86 | 33 | 2 | 1 | 12 | 743 |
| Invesco | 213 | 213 | | 6 | 4 | | | 223 |
| State Street | 192 | 190 | 1 | 17 | 3 | 1 | | 212 |
| Jupiter | 59 | 59 | 10 | 1 | | | 4 | 74 |
| TT International | 55 | 53 | 7 | 1 | | | 1 | 62 |
| Schroders | 45 | 42 | 2 | | 2 | | 1 | 47 |
| Pyrford | 22 | 22 | 1 | | | | 1 | 24 |
| Genesis | 14 | 14 | | 2 | | | | 16 |
| Total | 1,011* | 1,202 | 107 | 60 | 11 | 2 | 19 | 1,401 |

* Represents the total number of unique companies, not the sum total of companies or capital types voted by each manager.

Although we would expect there to be a 1:1 ratio between the number of companies voted and the number of AGMs voted (on the basis that all companies should have an AGM during the year), the small differences are likely to be explained by portfolio turnover. For example, if a fund manager sells a position in a company in June whose AGM is normally in September, replacing it with stock in a company whose AGM is in March, the fund manager will have owned two companies but had no AGMs to vote in either. However, where non-AGMs have taken place, these are still counted and therefore explain why the number of companies voted may exceed the number of AGMs voted. This is not as unlikely as it may seem – often when a company de-lists, a shareholder meeting is required, making it quite plausible that a company may have an EGM but no AGM during the year.

The very small number of meetings voted by Genesis in this sample of ‘full’ monitored meetings means that full detailed analysis is not meaningful. This is due to the investment universe of their mandate.

3.2 Monitoring Approach

The Manifest Voting Template (Voting Template) analyses and considers best practice governance expectations in the context of company meeting business (i.e. what can be voted at a shareholder meeting). Where there are local variations to best practice questions (for example, the length of time after which an independent director may no longer be deemed independent), Manifest applies the local market variation to the assessment, so that we only flag an issue as of concern if the company in question fails to meet their local standards. Where no issues of concern are identified in connection with a resolution, the Voting Template will naturally suggest supporting management.

Manifest monitors companies using this Voting Template in order to:

- Consistently identify company-specific governance policy issues, and
- Monitor and benchmark the actual voting behaviour of investment managers compared to
 - ⇒ the average shareholder (based on meeting outcomes) and
 - ⇒ the best practice governance standards (based on regulatory and public policy standard).

The Voting Template is not a prescriptive list of mandatory voting requirements. It is understood that investment managers actual voting behaviour will differ from the Voting Template. This is due to variances in views on governance and voting issues, investment strategy and the role of voting within on-going engagement and stewardship strategy. As such it offers the Fund a “sense check” of the stewardship approach managers are taking.

4 Common Policy Issues at Investee Companies

This section develops the themes identified in the previous chapter by examining the range of governance issues and considerations which lie behind the resolutions on which shareholders are asked to vote, and detailing those which Manifest identified most frequently among the companies Avon's fund managers have voted meetings for. This can be considered as a measure for governance standards at companies.

By comparison with previous years, fewer concerns have been identified at portfolio companies.

4.1 Introduction

Corporate governance is important to investors because it defines the system of checks and balances between the executive management of the company and its owners. Without appropriate levels of independence, accountability, remuneration, experience and oversight, corporate governance would offer shareholders little protection from the risk that their investee company is badly managed.

Analysis of the Voting Template settings allows for an in-depth study of the specific governance issues which have been identified by Manifest's research and analysis process. We have selected the most common issues which have been triggered by the Voting Template, to illustrate the most common 'issues' with resolutions voted by the Avon fund managers according to the preferences set out in the Voting Template used by Manifest for monitoring fund manager voting.

There were 8,138 resolution analyses where one or more concerns were identified by Manifest during 2014.

When considering the most common policy issues Manifest identified at the meetings researched in the Avon portfolios, comparison with last year's analysis shows that, in general, fewer issues of concern were identified at companies during 2014. This is explained in part by there being a slightly smaller number of resolutions in the data set. However, changes in the patterns of frequency also suggest some inferences.

We have compared the relative positions of each of the most common concerns identified within the list between this year and last year.

Of those which have moved up the list, or are new to it altogether, many relate to board and committee structures, with some cross-over with remuneration. Whilst the highest of them strictly speaking relates to governance, the fact that some remuneration issues continue to be prominent in relative frequency underlines the importance of governance as a management issue. In this case, as in last year's report the inference is that there is a relationship between the effectiveness of remuneration committee and the level of control over incentive pay.

The substance of the remuneration-related concerns which have moved up the list includes consideration of ESG issues in setting performance targets for incentive remuneration, the level of the upper bonus cap expressed as a percentage of salary for executive directors and a lack of disclosure of performance measures used for the exercise of options or vesting of awards.

Table 2: Most Common Policy Issues

| Table Position | 2014 | 2013 | Position Change | Description |
|----------------|-------|-------|-----------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | 1,713 | 3,320 | ↑ (2) | Less than 50-100% of the Nomination Committee are independent of management |
| 2 | 786 | 1,055 | ↑ (8) | Nominee is not considered to be independent by the Board |
| 3 | 737 | 3,229 | = | Less than 50-100% of the Audit Committee are independent of management |
| 4 | 725 | 1,049 | ↑ (9) | Nominee has served for more than 84-144 months on the board |
| 5 | 724 | 1,124 | ↑ (7) | There are no disclosures to indicate that the remuneration committee considers ESG issues when setting performance targets for incentive remuneration |
| 6 | 553 | 786 | ↑ (10) | The upper bonus cap for any of the executive directors as a percentage of salary exceeds 100-150% of salary |
| 7 | 553 | 626 | ↑ (12) | The (Supervisory) Board will exceed 15-21 members following the meeting |
| 8 | 478 | 642 | ↑ (11) | Nominee is a non-independent member of the remuneration committee and less than 50-100% of the remuneration committee are independent |
| 9 | 426 | 549 | ↑ (17) | Nominee represents a major shareholder |
| 10 | 375 | | NEW | The Board does not recommend a vote For the proposal |
| 11 | 361 | 550 | ↑ (16) | Nominee is a non-independent member of the Audit Committee and the percentage of the Audit Committee considered to be independent is less than 50-100% |
| 12 | 343 | 564 | ↑ (14) | The aggregate award of the director receiving the largest aggregate LTIP award during the year exceeded 100-250% of salary (on a market value basis, based on maximum possible vesting) |
| 13 | 337 | | NEW | There is no independent verification of the Company's ESG reporting |
| 14 | 315 | 2,940 | ↓ (4) | Less than 50-100% of the remuneration committee are independent directors |
| 15 | 279 | | NEW | A Nomination Committee does not exist (or its membership is not disclosed) |
| 16 | 249 | | NEW | The percentage of the Board comprised of independent directors is less than 25%-100% |
| 17 | 226 | | NEW | The roles of Chairman and CEO are Combined |

Overall, Manifest flagged 17,715 policy issues across the 21,880 resolution analyses undertaken for this report. This includes instances where the same resolution was analysed multiple times due to fund managers voting on the same resolution. Some resolutions were subject to multiple issues. Because of this, the following section includes an indication of the resolution category that each concern may be associated with.

4.1.1 Notes on the operation of best practice governance analysis

Readers should note that the Manifest voting guidance system allows for an individual governance issue to be applied to multiple resolutions. This is because, for the most part, there is not a one to one match between a policy issue and a specific resolution. This means that the list below is heavily weighted towards those considerations which are associated with the most frequent resolution type – board resolutions, and specifically, director elections.

For example, concerns relating to board or committee independence may be taken into consideration for the approval of the report and accounts (Audit & Reporting), director elections and possibly remuneration related resolutions (where the remuneration committee is insufficiently independent, concern with their proposals may be highlighted). Manifest reflects board accountability in its research by placing the analysis of the relevant board committee in the context of analysis of the governance matters for which they are responsible.

4.2 Conclusions on common policy issues

Taken as a whole, this analysis shows just how many different considerations there are that go into assessing the governance of a typical company.

Although the volume (in absolute terms) of the most common governance concerns Manifest identifies is heavily affected by the high number of director election resolutions compared to other types of resolution, readers should not dismiss the significance of board-related considerations (director election).

The election of directors, and the governance structures which they constitute on the board, is the lifeblood of accountability between boards and owners. It is the (non-executive) individuals on the board whose job it is to protect and look out for the interests of shareholders, so it follows that they are held accountable regularly and that a wide number of considerations are taken into account. Therefore, 6 of the top 8 concerns (indeed, 11 of the top 17) relate to director independence and the effect that has on the functioning of the board and its committees. Of the top 8, the only exceptions to this are the questions of integration of Environmental, Social and Governance (ESG) issues into incentive remuneration setting and the level of annual bonus available to executive directors.

The second most common group of issues identified relate to remuneration. This is again in part due to some of their association with director elections (executive director elections demand consideration of whether the proposed remuneration and incentive structure for the individual being proposed for (re)-election is appropriate. The remuneration related issues most commonly flagged continue to relate to the level at which the potential for excessive incentive pay might be capped (both short and long term incentive pay), the lack of linkage to ESG issues as well as the governance of remuneration policy itself.

These two general themes, taken together, raise questions about the significance with which many companies view the quality of board input, as well as their approach and attitude towards pay for performance. These questions are on-going general concerns which are as prevalent today as they were 5 years ago (although commentators would argue that they are higher profile now than then).

4.3 Audit & Reporting

Annual report resolutions are frequently those on which concerns about general board structures and practices may be concentrated, in addition to issues relating to the verification and reporting of information.

4.3.1 Audit committee independence

We assess the independence of the audit committee, in terms of whether there is a sufficient number and/or proportion of directors deemed independent (by reference to the local best practice standards).

It is a consideration for the approval of financial and non-financial reporting, because it relates to judging the independence of the audit process which underpins company reporting and therefore has been flagged on Report & Accounts resolutions.

4.3.2 No independent verification of ESG reporting

The growth in importance of ESG considerations in investment heightens the profile of ESG information provided by companies and hence increases the need for its veracity. As more investors use ESG information in their investment decisions, it follows that such information should be subject to levels of verification equivalent to those of more traditional disclosures such as financial updates and governance reports.

4.3.3 No evidence to suggest ESG performance targets are used for incentive pay

Similar to the point above, the growth in importance of ESG matters for investors leads to a desire to see ESG factors feature among the targets used for determining incentive pay – a part of making executives incentivised to promote better ESG standards through the businesses they manage.

4.3.4 The number of meetings held by the non-executives without the executives present.

We identify where there has been no meeting of Non-executives without Executives present disclosed by the company.

It is important for the Non-executives to meet without the Executives present in order to be able to have a free and open discussion about matters which may be more difficult to discuss with the presence of those who are running the business day to day.

4.3.5 The roles of Chairman and Chief Executive Officer are combined

We identify where the roles of Chair and Chief Executive Officer (CEO) and are performed by the same person.

The over-concentration of power in one single office or person is a key potential risk factor in any organisation. Despite the fact that some markets (notably France and the US) have much more relaxed standards on this question than most others, investors increasingly expect companies to separate the roles of CEO and Chair. It is associated with the Audit & Reporting category because it is applied to consideration of the report and accounts.

4.3.6 Audit tenure

We analyse how long the audit company has retained its mandate with the company without change.

Recent legislation – including in the UK - has tightened rules relating to the length of time a company may retain the same auditor without re-tendering. The notion is that the longer an audit company (and an auditor) serves the company, the more they may have aligned interests which could affect the objectivity of the audit work they are responsible for. These regulatory developments have had the effect of establishing greater expectation on this question by investors globally, irrespective of local market traditions.

4.3.7 Auditor pay for non-audit work

We analyse the relationship between non-audit fees and audit fees both on an annual basis and separately on an aggregate three year basis.

The value of non-audit related consultancy work is naturally a consideration for the approval of auditor elections and remuneration, given the potential for conflicts of interest and the importance of audit independence, and therefore has been flagged on Auditor resolutions.

4.4 Board

Many of the most common governance criteria that were triggered all pertain to board structures and independence, which are considerations in director elections. Readers will note that the most common type of resolution in the voting portfolio was director elections (they accounted for 49% of all resolutions), which largely explains the fact the below criteria are flagged most frequently.

4.4.1 Nomination Committee Independence

We identify where the Nomination Committee does not have a sufficient number of or proportion of independent directors by reference to the local standards within which the company operates.

Globally it is acknowledged that the Nomination Committee should consist of at least a majority of independent directors. Independence and objectivity of input are the best conditions for the nomination of suitably independent and diverse candidates for future board positions.

4.4.2 Individual is non-independent member of a committee which is not suitably independent

Where an individual is partly or solely the reason why a committee is not deemed sufficiently independent, the re-election of that individual to the board may be called into question.

The committee independence criterion may vary across markets and company size.

4.4.3 Board considers the nominee is not independent

Most frequently the board will acknowledge that the nominee fails one or more of the independence criteria that apply to non-executive directors, and that the individual's independence may be compromised. This code therefore is nearly always flagged alongside one of the other independence criteria.

4.4.4 Independence criterion: Tenure

This consideration is applied to the re-election of non-executive directors, and the 'trigger' varies between 7 and 12 years depending on the market. The UK (and most common) standard is 9 years.

Whilst tenure is frequently one of the independence criteria set out in the governance codes, it is perhaps the least critical of the criteria in terms of strict application. The Financial Reporting Council (FRC) is the guardian of the UK Corporate Governance Code and research they have commissioned Manifest to do has witnessed a visible relaxation of investors' attitudes towards holding companies responsible to the letter on this specific issue.

Because of this, companies are, in turn, less worried about putting forward for election directors who may have been at the company for a little (but not much) over nine years, on the basis that their character of independence is not suddenly compromised materially and that their expertise is of more value to the board. Investors should expect to see some degree of succession management, however.

4.4.5 Board size

Many jurisdictions have soft or hard law provisions which determine a maximum size for the board. We therefore highlight where company boards are too large in the context of director election resolutions.

A board which is too large may be unwieldy in its decision-making, and could suffer from a lack of focus in arriving at decisions about strategic direction and in performing its oversight function effectively.

4.4.6 Independence criterion: represents a major shareholder

An individual's ability to serve all shareholders as an independent non-executive may be compromised where they represent a major shareholder on the board. Some markets establish an explicit threshold for establishing a majority shareholder for the purposes of this consideration (10% in Belgium, for example), whereas most do not.

4.4.7 A nomination committee does not exist (or its membership is not disclosed).

Without a clear nomination committee and process, the provenance of director election proposals is unclear. This is therefore a consideration which has flagged on director elections.

4.4.8 Percentage of female directors on the board

A number of Manifest customers ask us to track the issue of female representation on the board as a part of the wider debate on board diversity.

Whilst the issue of female directors on the board may not be a critical risk consideration on its own, the fact that director independence in general is so frequently flagged might point to a wider problem with adequate application of diversity considerations when making board appointments, of which female presence on the board is perhaps the most obvious measure.

4.4.9 Nominee is non-executive, non-independent and the board is not sufficiently independent

We monitor whether boards' composition meets the independence criteria of the market where they operate. Where it doesn't, and the individuals who are contributing to this concern are up for (re)election, we highlight board composition as a concern in the context of their (re)election proposal.

4.4.10 Member of an audit committee allowing high non-audit fees

The relationship between the fees paid to the auditor for audit work and that paid for non-audit work is a core consideration regarding the independence of the auditor and, correspondingly, the potential reliability of company reporting.

Directors who are responsible (through their membership of the audit committee) for the auditor being paid for additional non-audit-related work to an extent which may compromise the independence of the audit work (usually where non-audit fees exceed audit fees), may be held individually accountable through this consideration.

4.5 Remuneration

Remuneration related resolutions are most frequently to do with the proposal and approval of the Remuneration Report or the approval of new or amended incentive plans, and sometimes the approval of specific payments made to directors.

4.5.1 The upper bonus cap, where set and disclosed, exceeds (100-150)% of salary

This consideration was triggered by remuneration report resolutions. The market standard limit for the bonus cap, expressed as a percentage of salary, varies from market to market.

4.5.2 Consideration of ESG issues when setting performance targets

This consideration was flagged mainly on Remuneration Report resolutions but also significantly on financial reporting resolutions.

The growth of the importance of ESG or Sustainability considerations not just from the point of view of responsible investment but also the strategic importance of sustainable business means that investors often now look for the inclusion of ESG related targets within the framework of performance related pay.

4.5.3 Lack of claw back or malus/forfeiture on incentive pay

It has become increasingly important for investors to be able to hold executives to account for adjustments to the performance figures which previously triggered the defrayal of bonuses. We therefore highlight where remuneration policies and bonus schemes do not feature such mechanisms.

This underlines the importance of having all measures which are used for the determination of bonus payments – including ESG performance measures - to be externally verified.

4.5.4 The aggregate award of the director receiving the largest aggregate LTIP award during the year exceeded (100-250)% of salary (on a market value basis, maximum possible vesting).

This consideration was also triggered uniquely by remuneration report resolutions. Clearly, this relates to the structural quantum of incentive pay, by picking up on the ‘worst case scenario’ of full vesting of an award. As with upper bonus caps, the standard limit applied varies from market to market.

4.5.5 Remuneration committee independence

Independence of the remuneration committee is a criterion which is taken into consideration in a number of contexts, including the approval of the remuneration report and other remuneration-specific resolutions (remuneration reports, bonuses and long term incentive plans) and election of directors who are currently on the committee.

The importance of independent input from the remuneration committee needs little introduction in the current climate. Remuneration committees may sometimes contain the chief executive, because of the link between remuneration and company strategic implementation. This may often trigger an independence concern.

4.5.6 Length of the performance period used to measure attainment of long term targets

There has been some debate about what constitutes ‘long term’ when considering long term incentives. Local best practice codes often stipulate a minimum of three years, though some institutional investors are holding companies to a higher standard of 5 years.

4.6 Capital

4.6.1 The Authority sought exceeds 5-50% of issued share capital

Although it does not feature in

Table 2 above, the most common capital-related concern highlighted is where a company board seeks permission for authority to issue new shares, or allocate share capital, sometimes for a specified purpose (for example, for the purpose of executive or employee incentive pay). Where the amount of share capital concerned exceeds a certain threshold, it may be of concern to shareholders (who may wish to have the right to choose to maintain ownership of a certain proportion of the company, so would want the ability to obtain their proportion of the new share issue in order to do so). The stipulated proportion may frequently be defined in local corporate governance codes under provisions designed to protect the rights of shareholders.

4.6.2 Dividends proposed to be paid to shareholders exceed profits

Also worthy of note in the context of capital related resolutions is the question of whether proposed dividends exceed profits. Companies may have a dividend policy which commits them to a certain level of dividend payment over the short to medium term. On occasion it is possible that where profits fall below the levels projected for that same time frame, the company is committed to paying a higher dividend than can be covered by profits attributable to the financial year in question. It is normal for the shortfall to be covered by reserves, but of course it is a question which deserves to be highlighted in the context of the long term financial sustainability of the company.

The other main means of returning capital to shareholders is via share buyback mechanisms.

4.7 Corporate Actions

The Corporate Actions category covers a narrow and specific set of considerations. As a result, none of the governance concerns typically associated with this category featured in our analysis of the most common concerns identified by the policy, simply because the issues to which they relate don't come up on a typical corporate agenda very regularly.

However, of those times when they did come up, the two most common flags concerned were to identify that a proposal was about profit sharing agreements, acquisitions, related party transactions and schemes of arrangement. A scheme of arrangement (or a "scheme of reconstruction") is a court-approved agreement between a company and its shareholders or creditors (e.g. lenders or debenture holders). It may effect mergers and amalgamations and may alter shareholder or creditor rights.

4.8 Shareholder Rights

The shareholder rights category covers resolutions which relate specifically to resolutions which may affect the ability of shareholders to exercise some element of their rights (usually in a negative way by reducing ownership rights). It is therefore still a relatively rare resolution type to occur. They therefore encompass not only rules about shareholder voting, but also things such as the rules according to which a shareholder (or shareholders) may requisition a meeting, a resolution at a meeting, the way in which a shareholder meeting is conducted and shareholder rights in the event of a (hostile) takeover situation.

4.9 Sustainability

4.9.1 Political donations

Under European jurisdictions, companies are required to seek approval for so-called political donations. These resolutions are not specifically for party political donations as the EU include expenditure towards the realisation of political aims such as political lobbying, trade association memberships etc.

4.9.2 The amount of the proposed authority exceeds £25,000

Whilst it may seem arbitrary to set an absolute figure on such a resolution, this is actually in line with investor preferences in the sense that it would not seem appropriate for shareholders to approve a figure expressed relative to company size or turnover as that would imply that political donations are an acceptable routine aspect of corporate life. Secondly, given that laws relating to disclosures require absolute amounts to be disclosed, an absolute limit is also a more transparent means of applying a preference.

5 Aggregate Voting Behaviour

Having discussed above the general themes of the most frequent contentious issues in each resolution category, the next step is to consider how Avon’s fund managers voted. This section sets out and compares how Avon’s fund managers voted, as compared to general shareholder voting patterns (as shown by the meeting results data collected by Manifest as a part of the monitoring service), in the context of different categories of resolution.

With the exception of TT International, none of Avon’s fund managers voted with management noticeably more than shareholders in general (i.e. by more than a factor of 2%), it should also be noted that Jupiter and BlackRock voted with management more than shareholders in general but not to the same extent as TT. Invesco, Schroders and Genesis supported management noticeably less.

5.1 Fund Manager Voting Comparison

Table 3 below shows the total number of resolutions voted by each fund manager during the period under review. It shows the proportion of all resolutions which each fund manager voted with management, compared with the proportion of resolutions where the best practice Voting Template suggested supporting management. Lastly, it shows how shareholders were reported to have voted where meeting results were available from the companies in question. Manifest seeks to collect the meeting results data for all meetings analysed. In certain jurisdictions, provision of such information by companies is not guaranteed. However, of the 21,880 resolutions analysed in this report, Manifest obtained poll data for 19,318 resolutions, allowing for a meaningful analysis of the resolution data set.

Table 3: Overall Voting Patterns

| Fund | Resolutions Voted | Avon Managers Supported Management | General Shareholders Supported Management | Template For Management |
|------------------|--------------------------|-------------------------------------------|--------------------------------------------------|--------------------------------|
| BlackRock | 10,550 | 98.64% | 97.06% | 68.95% |
| State Street | 4,140 | 94.71% | 96.45% | 64.61% |
| Invesco | 3,314 | 91.70% | 94.72% | 42.58% |
| Jupiter | 1,234 | 98.22% | 96.93% | 69.21% |
| TT International | 1,194 | 99.58% | 96.40% | 65.41% |
| Schroder | 706 | 92.49% | 95.07% | 41.50% |
| Pyrford | 457 | 95.19% | 95.90% | 72.21% |
| Genesis | 285 | 86.32% | 95.98% | 49.82% |
| Total | 21,880 | 96.44% | 96.36% | 62.89% |

Table 3 shows that fund managers vote with management a high proportion of the time, and that the best practice Voting Template identifies potential governance issues on a far higher proportion of resolutions than the fund managers choose to oppose.

Using the “Template For Management” data as a proxy for compliance with corporate governance best practice expectations, the companies in the Pyrford, Jupiter, State Street, and TT portfolios display a comparatively higher level of compliance with governance best practice. These portfolios compare particularly favourably with those of Invesco, Genesis and Schroder’s portfolios, which show lower levels of convergence with the voting policy template.

This continues to reflect Jupiter’s practice of accommodating a company’s governance characteristics in their investment decision-making, whereas BlackRock, for example, as an index investor must hold all stocks in the index irrespective of governance (or other) characteristics. In addition, the Jupiter portfolio is limited to UK whereas the BlackRock, Schroder, Invesco and Genesis portfolios are global and therefore are exposed to a much higher potential variance of general governance standards, in particular this may be more marked for Genesis who invest solely in Emerging Markets. Pyrford’s active stock picking approach is perhaps also reflected by a similarly high level of compliance with governance best practice.

We can compare each fund manager’s overall voting pattern with how other shareholders voted on the same resolutions (using our own analysis of the voting results data (where made available by companies)). Table 3: Overall Voting Patterns shows that, as in previous years, Avon’s fund managers oppose management to almost exactly the same degree as all shareholders in general do, however by comparison with other shareholders in general, Avon’s fund managers’ level of voting with management has consistently crept up over time to a point where in 2014, management was opposed by Avon’s fund managers a little less than by shareholders in general. However, there are some variances between the respective fund managers.

As was the case in the 2012 and 2013 monitoring reports, TT have again supported management more than most shareholders, supporting management practically all the time. Conversely, Blackrock’s levels of support for management are slightly higher than those of shareholders in general compared to the previous year, for the second report running, in the context of generally higher levels of support by comparison to the previous year. Jupiter’s support of management is further in excess of other shareholders compared to the previous year, as was also the case in 2013, and remains notably higher than the general average. It is likely that Jupiter’s mandate has the effect of ensuring that the companies in which they are invested tend to have higher standards of governance to begin with. Additionally, the degree to which it is possible to positively engage with portfolio companies in the UK market lends Jupiter to being in a position to continue to support management even where technical concerns may appear to persist.

Despite the highest level of compliance with the corporate governance standards of the Voting Template, Pyrford does not support management at their respective investee companies more than the other fund managers. However, Pyrford’s level of support for management is almost exactly in line with shareholders in general.

State Street, Schrodgers, Genesis and Invesco’s support for management is all notably lower than general shareholder support, though in Genesis’ case especially, statistical insignificance is a concern. At an aggregate level it is difficult to make thematic observations about why State Street, and Invesco have supported management less than shareholders in general, other than to say that as overseas equity managers it could be an indicator that the use of voting rights is likely to play a more significant part of the engagement process with companies than for the other fund managers and the opportunities for engaging directly with companies are fewer. This could have to do as much with engagement strategy as it could be taken as a measure of shareholder advocacy per se.

State Street, although supporting management to a lesser degree than shareholders in general, do so to a less marked extent than Schroders and Invesco. However, taking the “Template For Management” measure as a proxy, the degree to which portfolio companies display potential issues of concern is broadly comparable to those in the BlackRock portfolios, whereas the cases of Schroders and Invesco voting is notably less supportive of management, mirroring the fact that those portfolios also attract far more “Template Against Management”.

In 2012 there was a discernible pattern from fund manager to fund manager in terms of general shareholder support for management and the degree to which the policy template identified potential concerns. However, during 2014 (as in 2013), this was again not the case, with average shareholder dissent within a very narrow band of between 94.7% and 97%.

Jupiter and TT International portfolio companies remained the highest both in terms of shareholder support and meeting the requirements of the policy template, this year joined by BlackRock. Invesco portfolio companies were notably at the other end of both spectrums. However, State Street companies were certainly comparable in their “compliance” with those in the TT portfolio, but received a notably lower level of support from shareholders and State Street themselves, compared to the average.

6 Voting Behaviour by Resolution Category

Table 4 and Table 5 below show headline figures as to how shareholders voted on each resolution category in general. The sections which follow them then show more detail into the sub-themes of each resolution category, showing in turn how the considerations relevant to each category and sub-category fit together to translate governance policy into possible voting action.

Using the vote outcome data collected in respect of the significant majority of meetings at which Avon fund managers have voted, we have combined the meeting results with our classification of meeting business, so as to identify which were the most contentious resolutions and the reasons for them being contentious.

6.1.1 Dissent by resolution category

Where Manifest uses the term ‘Dissent’, this is the result of having added up all votes not supporting the management recommendation, represented as a percentage of all votes cast (‘Against’ plus ‘Abstain’ votes where Management recommended a ‘For’ vote and ‘For’ plus ‘Abstain’ votes where Management recommended ‘Against’).

Where there was no clear recommendation from company management, we have not counted any votes cast on those resolutions as dissent.

In respect of shareholder proposed resolutions, dissent is measured by taking into account votes cast differently to the management recommendation (which may most commonly have been “Against”).

Table 4: General Dissent By Resolution Category

| Resolution Category | Number of Resolutions | Results Available | Average Dissent |
|---------------------|-----------------------|-------------------|-----------------|
| Board | 10,722 | 9,304 | 2.80% |
| Capital | 3,655 | 3,381 | 2.90% |
| Audit & Reporting | 2,828 | 2,552 | 1.69% |
| Remuneration | 2,607 | 2,397 | 7.62% |
| Shareholder Rights | 1,342 | 1,062 | 6.73% |
| Corporate Actions | 345 | 261 | 2.96% |
| Sustainability | 299 | 293 | 10.56% |
| Other | 82 | 68 | 12.80% |
| Grand Total | 21,880 | 19,318 | 3.64% |

* “Average Dissent” calculated from general shareholder voting results where available.

Table 4 above shows the most common categories of resolutions at meetings voted at by Avon’s fund managers. When looking at the general average dissent levels (i.e. the meeting results data), it is clear that shareholders in general support management to a considerable extent, even on the most contentious issues.

Average dissent across all resolutions in 2014 was noticeably lower than in previous years (at 3.64%), whereas in 2013 it had been again up compared to the previous year 4.97% (4.35% in 2012). This represents an approval rating of greater than 96% overall.

Avon’s fund managers in 2014 were, on average, slightly less active in expressing concerns through votes at shareholder meetings, voting against management on 779 occasions out of 21,880 resolutions, constituting an overall average opposition level of 3.56% (down from 5.17% in 2013, following 4.65% in 2012 and 4.22% in 2011). This shows that, in line with general shareholder dissent, Avon’s fund managers also voted against management to a lesser extent compared to the prior year, for the first time since this analysis has been undertaken for the fund. Some more patterns within this are demonstrated and explored more fully below.

As was the case in all previous years, remuneration related resolutions proved to be the most consistently contentious resolution categories, of those routinely and predominantly proposed by management. The following section analyses the above categories in more detail, by exploring patterns of opposition to the resolution sub-categories in each.

6.1.2 Dissent on shareholder proposed resolutions

Table 5: Shareholder Proposed Resolutions

| Resolution Category | Number Of Resolutions | Proportion Of All Such Resolutions | Average Dissent |
|---------------------|-----------------------|------------------------------------|-----------------|
| Shareholder Rights | 108 | 8.05% | 16.91% |
| Sustainability | 84 | 28.09% | 27.55% |
| Board | 81 | 0.76% | 21.55% |
| Remuneration | 55 | 2.11% | 13.48% |
| Other | 44 | 53.66% | 16.63% |
| Audit & Reporting | 15 | 0.53% | 11.32% |
| Capital | 7 | 0.19% | 1.40% |
| Grand Total | 394 | 1.83% | 19.13% |

* “Average Dissent” calculated from resolutions in respect of which shareholder voting results were available.

The largest single proportion of the resolutions relating to aspects of Shareholder Rights once again pertained to requests to amend company Bylaws so that shareholders may act by written consent (whereby shareholders could do so in lieu of a meeting, the necessary threshold typically being equivalent to the percentage of voting power that would be necessary to approve the action at a meeting). Many company articles actively preclude this. As was the case in 2013 these proposals proved relatively popular and management was defeated a number of times – evidence of shareholder action producing a positive outcome and the improvement of shareholder rights at portfolio companies.

Regarding Board-related resolutions, Board Composition (81 of the instances of shareholder proposed resolutions), Election Rules (24), Board Composition (19) and Director Elections (17) all feature prominently. The most common themes among the Board Election resolutions – all of which were in the USA - were the enhancement of shareholder rights through allowing shareholders to make board nominations, or proposals to provide for majority or cumulative vote standards for director elections. The most common themes among the Board Composition resolutions – again, all in the USA - were requests to adopt a policy of the Chairman being an independent director, which continues to be a significant area of debate in US corporate governance.

In terms of Sustainability-related resolutions, as was the case in the previous two years the largest proportion (over half again as in 2013) were requesting disclosure of political donations, all in the US,

where corporate political donations are a significant feature of the US system. Of the rest, nearly all were related to the improvement of sustainability reporting, or miscellaneous specific sustainability proposals, most of which were in the extractive industries sector, again as was the case in 2013 and 2012.

The largest proportion of the remuneration related shareholder proposals again came in the US, many requesting some sort of limit remuneration in some way, especially with regard to the use of stock options as a form of remuneration. This apparent focus on the quantum of remuneration as well as the format is to be noted.

Avon's managers voted with Management on just 54% of all shareholder proposed resolutions (compared with 95% in 2013), with especial support shown for shareholder proposals on sustainability reporting issues and political donations (where shareholder proposals were supported over 75% of the time).

6.2 Board

Board related resolutions constitute nearly half of all the resolutions voted during the year. This is almost completely down to the high number of director election resolutions on a typical AGM agenda, as can be seen from Table 6 below.

Table 6: Board Resolution Sub-Categories

| Resolution Sub-Category | Total Resolutions | Template With Mgt | Avon Voted With Mgt | Overall S/Holder Votes With Mgt |
|-------------------------|-------------------|-------------------|---------------------|---------------------------------|
| (Re-)Elect Directors | 9,447 | 59.42% | 96.86% | 97.34% |
| Directors Discharge | 969 | 88.54% | 99.79% | 97.94% |
| Board Committee | 142 | 91.55% | 95.77% | 97.56% |
| Other | 53 | 56.60% | 79.25% | 90.21% |
| Board Size & Structure | 48 | 87.50% | 100.00% | 74.43% |
| Election Rules | 30 | 16.67% | 53.33% | 76.43% |
| Board Composition | 26 | 23.08% | 61.54% | 95.88% |
| Remove Directors | 5 | 20.00% | 100.00% | 81.35% |
| Indemnification | 2 | 0.00% | 100.00% | 97.24% |
| Grand Total | 10,722 | 62.35% | 96.83% | 97.20% |

* "Overall Votes with Management" calculated from resolutions in respect of which shareholder voting results were available.

Consistent with the pattern of voting on resolutions overall, BlackRock, Jupiter and TT were the only Avon fund managers to support management more frequently than shareholders generally.

Nearly all of the top governance issues listed on page 15 are considerations relevant to the re-election of a director, and therefore to a very large extent explain the relatively low levels of alignment (62.35%) between the governance best practice template and company management recommendations on director elections in Table 6.

Of those resolutions where the fund managers opposed management on Director Elections (297) (581 in 2013) resolutions – of which 65 were instances where no governance issues were highlighted) the most frequent governance issues Manifest identified were:

Table 7: Board-related governance issues

| Issue | Instances |
|------------------------------------------------------------------|-----------|
| 1 (6) ↑ Nominee is not considered to be independent by the Board | 126 |
| 2 (8) ↑ Nominee represents a major shareholder | 76 |
| 3 (4) ↑ Nomination Committee independence levels | 59 |
| 4 (-) ↑ Overall board size | 53 |
| 5 (5) = Remuneration Committee independence level | 40 |
| 5 (7) ↑ Tenure | 40 |
| 7 (-) ↑ No disclosure of Nomination Committee | 28 |
| 8 (3) ↓ Audit Committee independence levels | 24 |

On many occasions, there were multiple concerns with each resolution, and it is likely that the quantum of governance concerns, rather than the substance of each individual concern *per se*, is what makes the fund managers more likely to register opposition to their re-election.

The proportion of resolutions where management was opposed without the identification of governance concerns (approximately 20% of all instances where management was opposed, compared to 10% last year) would suggest that fund managers are increasingly also not afraid to apply their own (investment) judgement on these issues.

6.3 Capital

Resolutions relating to the capital structure of a company frequently pertain to investment specific considerations. For that reason, governance best practice considerations are less frequently relevant, other than the extent to which proposals directly affect shareholders rights, where often the rules are well defined and relatively infrequently breached (such as the UK Pre-Emption Guidelines).

Therefore, many of the issues the policy template identifies are flagged as ‘Case-by-Case’ rather than as governance concerns *per se*, resulting in a much higher level of template support for management than Board related resolutions because ‘Case-by-Case’ is not counted as template being against management.

On the two largest resolution sub-categories, Avon’s fund managers voted against management marginally more often than shareholders in general, in particular in the case of share issues and pre-emption rights.

Perhaps unsurprisingly, dividend approvals are supported a very large percentage of the time by both fund managers and shareholders in general. One investment consideration on this issue is the balance between short and long-term investment return. Capital returned to shareholders in the short term through dividends cannot then be used by the company for potential revenue-enhancing investment in the future business.

Furthermore, especially in the case of “income” stocks, the reliability of the dividend is a factor in the stock valuation which could therefore fluctuate if the situation changed. Other means of returning capital to shareholders is through share buy-backs.

Table 8: Capital Resolutions Sub-Categories

| Resolution Sub-Category | Total Resolutions | Template With Mgt | Avon Voted With Mgt | Overall Votes With Mgt |
|--------------------------------------|-------------------|-------------------|---------------------|------------------------|
| Issue of Shares & Pre-emption Rights | 1,799 | 82.47% | 98.17% | 95.51% |
| Share Buybacks & Return of Capital | 890 | 81.89% | 98.99% | 98.49% |
| Dividends | 771 | 79.49% | 99.74% | 99.34% |
| Treasury Shares | 109 | 83.44% | 98.17% | 96.38% |
| Authorised Share Capital | 35 | 75.00% | 100.00% | 96.62% |
| Capital Structure | 27 | 71.43% | 100.00% | 98.96% |
| Equity Fundraising | 19 | 85.71% | 100.00% | 99.46% |
| Bonds & Debt | 5 | | 100.00% | 98.58% |
| Grand Total | 3,655 | 81.63% | 98.74% | 97.10% |

* "Overall Votes with Management" calculated from resolutions in respect of which shareholder voting results were available.

Nearly half of the resolutions in this category related to the issue of shares and pre-emption rights, which often form part of routine business at company AGMs, giving them the on-going permission to issue new shares up to a certain agreed level for the forthcoming year.

The three most frequent issues on capital related resolutions where there was a voting concern highlighted (as opposed to a 'Case by Case' flag) were the same as in 2013, but in all cases less numerous, as indicated by the arrows next to the figures for total instances observed in 2014:

- 1 New share issue authority exceeds 5-50% of existing share capital (220 ↓)
- 2 Ordinary dividends exceed profits (105 ↓)
- 3 Authority being sought is greater than 12-60 months (71 ↓)

6.4 Audit & Reporting

The results data we collected shows that resolutions related to audit and reporting were again the least contentious resolution category of all. However, because it includes resolutions which pertain to questions which are routine AGM meeting business in many countries, it nevertheless merits some analysis.

Table 9: Audit & Reporting Resolution Sub-Categories

| Resolution Sub-Category | Total Resolutions | Template With Mgt | Avon Voted With Mgt | Overall Votes With Mgt |
|--------------------------------|--------------------------|--------------------------|----------------------------|-------------------------------|
| Auditor Election | 1,104 | 55.07% | 99.73% | 97.83% |
| Report & Accounts | 1,024 | 21.88% | 99.51% | 99.11% |
| Auditor Remuneration | 596 | 63.26% | 99.83% | 98.23% |
| Appropriate Profits | 56 | 67.86% | 100.00% | 98.36% |
| Other A&R related | 37 | 37.84% | 94.59% | 93.69% |
| Auditor Independence | 10 | 90.00% | 70.00% | 89.86% |
| Auditor Discharge | 1 | 100.00% | 100.00% | 98.89% |
| Grand Total | 2,828 | 44.94% | 99.50% | 98.31% |

* "Overall Votes with Management" calculated from resolutions in respect of which shareholder voting results were available.

1,422 resolutions had at least one concern highlighted (not including 135 "Case-by-case" resolutions). Some of the most common concerns that Manifest identified are indicated in the table below. The very high degree to which Avon's fund managers have voted with management on resolutions of this type is a strong indicator that these are not governance concerns over which the fund managers wish to oppose management with their votes.

Table 10: Common Concerns Identified On Audit & Reporting Resolutions

| Issue | Instances (2013) |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------|
| 1 (-) - Less than 50-100% of the Audit Committee are independent of management | 595 (980) |
| 2 (2) - There is no independent verification of the Company's ESG reporting | 337 (370) |
| 3 (3) -There are no disclosures to indicate that the remuneration committee considers ESG issues when setting performance targets for incentive remuneration | 269 (310) |
| 4 (5) ↑ No meetings held by the non-executives without the executives present | 159 (215) |
| 5 (6) ↑ The aggregate non-audit fees exceed the aggregate audit fees paid on a three year average | 137 (210) |
| 6 (7) ↑ The roles of Chairman and CEO are combined | 187 (220) |
| 7 (4) ↑The auditors have provided statutory audit services to the Company for over 10 years | 111 (281) |
| 8 (8) - The aggregate non-audit fees exceed the aggregate audit fees | 107 (157) |
| 9 (5) ↓ Less than 25-66% of the Board is comprised of independent directors | 98 (146) |
| 10 (10) - Less than 50% of the Board, excluding the chairman, are considered to be independent according to local best practice | 97 (136) |

6.5 Remuneration

As noted above, Remuneration related resolutions continue to be the most contentious, attracting the highest average level of dissent of all of the resolution types routinely proposed by management as well as the lowest level of alignment with the governance best practice analysis.

Table 11: Remuneration Resolution Sub-Categories

| Resolution Sub-Category | Total Resolutions | Template With Mgt | Avon Voted With Mgt | Overall Votes With Mgt |
|-------------------------------|-------------------|-------------------|---------------------|------------------------|
| Remuneration Report | 1,055 | 27.68% | 94.88% | 91.89% |
| Remuneration Policy | 640 | 90.78% | 95.16% | 93.04% |
| Long Term Incentives | 365 | 68.49% | 93.42% | 92.54% |
| Non-executive Remuneration | 136 | 63.24% | 98.53% | 95.66% |
| Remuneration - Other | 130 | 55.38% | 70.77% | 86.06% |
| Total Aggregate Remuneration | 115 | 94.78% | 86.96% | 91.73% |
| All Employee Share Plans | 49 | 100.00% | 100.00% | 98.58% |
| Policy – Other Components | 46 | 76.09% | 91.30% | 94.64% |
| Total Individual Remuneration | 46 | 97.83% | 91.30% | 93.43% |
| Item Individual Remuneration | 12 | 100.00% | 75.00% | 88.16% |
| Policy -Contracts | 6 | 33.33% | 50.00% | 97.78% |
| Short Term Incentives | 5 | 60.00% | 100.00% | 93.26% |
| Item Aggregate Remuneration | 2 | 100.00% | 100.00% | 92.38% |
| Grand Total | 2,607 | 59.00% | 93.17% | 91.89% |

* "Overall Votes with Management" calculated from resolutions in respect of which shareholder voting results were available.

However, readers will note the marked contrast between the proportion of all resolutions where the governance best practice template analysis raised concerns, and the proportion of all resolutions where

Avon’s managers (and shareholders in general) supported management. Although significantly lower than last year, the contrast is still marked.

The introduction of the vote on Remuneration Policy in the UK has certainly had an effect on this year’s statistics. With a lot of investors adopting a “wait and see” approach with regard to policy proposals (preferring to see how the Regulations bed in over 3-5 years), all but the most controversial policy proposals received respectable levels of support. By contrast, where opposition was expressed, it was often at a very high level, suggesting a more targeted approach on the part of investors.

Also, readers will note that “Remuneration – Other” (including termination payments and provisions) have attracted a much higher level of opposition from Avon’s managers, one of the most controversial aspects of remuneration considerations, along with resolutions dealing with individual remuneration.

Table 12: Common Concerns On Remuneration Resolutions

| Concern | Instances |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------|
| 1 (2) ↑ The upper bonus cap, where set and disclosed, exceeds 100-150% of salary | 486 (783) |
| 2 (1) ↓ No indication of consideration of ESG issues in performance targets for incentive pay | 455 (813) |
| 3 (3) - The largest aggregate LTIP award during the year exceeded 100-250% of salary of the director (on a market value basis, based on maximum possible vesting) | 343 (562) |
| 4 (8) ↑ No evidence of claw back measures in place in respect of the short-term incentives. | 194 (391) |
| 5 (7) ↑ No evidence of claw back measures in place in respect of the long-term incentives. | 188 (432) |
| 6 (6) - Less than 50-100% of the remuneration committee are independent directors | 161 (451) |
| 7 (5) ↓ The minimum performance measurement or options/share awards holding period is less than 2-3 years | 151 (511) |
| 8 (4) ↓ The exercise of options/ vesting of awards is not subject to performance conditions | 126 (552) |
| 9 (9) - The maximum potential severance payment exceeds 12 months' salary | 103 (320) |

Table 12 shows the most common governance best practice concerns associated with remuneration-related resolutions by Manifest over the year. Many of these issues have been prevalent on a consistent basis over time.

The quantum of bonus and long term incentive payments is possibly the most widely debated contentious issue in the corporate governance of public listed companies. Not far behind (indeed, as a part of the same debate) is the question of whether bonus and incentive pay should be clawed back, in the event that performance for which bonuses have previously been paid turns out not to have been actually realised.

Frequently, such considerations are all associated with the Remuneration Report resolutions, which showed the highest divergence between the governance best practice policy and fund manager voting.

The absence of performance conditions for the exercise of awards or options is also noteworthy, especially alongside accelerated vesting of awards in the event of a change of control in the company. Both of these concerns suggest an element of payment of incentive pay without setting down substantive performance targets in order to obtain it.

A separate, binding forward-looking policy vote was introduced for UK companies for 2014, which had a bearing on how investors voted. This came into force in respect of AGMs applying to financial years starting on or after the 1st October 2013, thereby affecting the 2014 AGM season. The main challenge for all concerned was having the sufficient resources to manage the workload of increased engagement between companies and investors.

6.6 Shareholder Rights

The shareholder rights category covers resolutions which relate specifically to the ability of shareholders to exercise some element of their rights. They therefore encompass not only rules about shareholder voting, but also things such as the rules according to which a shareholder (or shareholders) may requisition a meeting, a resolution at a meeting, the way in which a shareholder meeting is conducted and shareholder rights in the event of a (hostile) takeover situation.

They are important because they essentially relate to the extent to which investors are able to mitigate themselves against the risk of third parties making decisions which affect their investment in the company.

Table 13: Shareholder Rights Resolution Sub-Categories

| Resolution Sub-Category | Total Resolutions | Template With Mgt | Avon Voted With Mgt | Overall Votes With Mgt |
|-------------------------------|-------------------|-------------------|---------------------|------------------------|
| General Meeting Procedures | 523 | 95.41% | 98.09% | 92.60% |
| Other Articles of Association | 438 | 82.19% | 94.06% | 95.65% |
| Meeting Formalities | 288 | 86.81% | 99.31% | 92.97% |
| Shareholder Rights | 52 | 17.31% | 50.00% | 98.70% |
| Corporate Governance | 19 | 0.00% | 94.74% | 92.97% |
| Takeover Governance | 15 | 13.33% | 66.67% | 65.13% |
| Anti-takeover Provision | 7 | 14.29% | 71.43% | 74.08% |
| Grand Total | 1,342 | 83.53% | 94.63% | 93.27% |

* "Overall Votes with Management" calculated from resolutions in respect of which shareholder voting results were available.

Frequently, many of the issues in this category are relatively straight forward and many of the resolutions where there is complexity it is down to the proposal being made by shareholders, therefore inevitably likely to introduce some question that is comparatively out of the ordinary.

For example, a large number of the 'General Meeting Procedures' resolutions relate to the requirement in the UK for companies to request a routine permission to retain the right to call a non-AGM General Meeting at less than 21 days' notice. In the UK context, it is a simple consideration – to allow companies to retain the ability to do something they have had the right to do for many years, provided they do not take advantage of it. Avon's fund managers have voted "For" management to a much greater extent than shareholders in general simply because foreign shareholders are more frequently opposing 14 day notice period permissions, simply because their voting mechanisms are not efficient enough to be able to vote a meeting called with less than 21 days' notice.

The vast majority of the issues that Manifest research identified were to do with the nature of the resolution, rather than the substance - for example that the resolution is proposed by shareholders, or that the board does not make a recommendation on the resolution (common in US 'Say on Pay' frequency resolutions).

Some concerns related to the technicalities of shareholders rights were identified on a small number of resolutions, including instances where not all shareholders are given access to electronic voting, or where the company has made use of the right to call a meeting at 14 days' notice in the preceding year (a valid

consideration when deciding whether to approve permission to retain the right to call meetings at 14 days' notice in future).

Of the 72 (73) resolutions where fund managers opposed management on Shareholder Rights related considerations, 69 (32) were shareholder proposed resolutions. This suggests that, when it comes to shareholder rights protections, Avon's managers are very well motivated to protect their interests and those of their clients, and much better so by comparison with the previous year.

6.7 Corporate Actions

Whilst far less numerous, some statistical significance can be attributed to some of the Resolution Sub-Categories pertaining to Corporate Actions, which can be put to effect to explore why they number among the most contentious resolution sub-categories for Avon's fund managers.

Table 14: Corporate Actions Resolution Sub-Categories

| Resolution Sub-Category | Total Resolutions | Template With Mgt | Avon Voted With Mgt | Overall Votes With Mgt |
|----------------------------|-------------------|-------------------|---------------------|------------------------|
| Other Corporate Action | 156 | 30.13% | 99.36% | 99.14% |
| Significant Transactions | 85 | 2.35% | 97.65% | 96.79% |
| Related Party Transactions | 74 | 59.46% | 83.78% | 94.62% |
| Transactions - Other | 13 | 7.69% | 92.31% | 93.20% |
| Change of Name | 9 | 100.00% | 100.00% | 99.15% |
| Company Purpose & Strategy | 6 | 83.33% | 100.00% | 92.42% |
| Investment Trusts & Funds | 2 | 100.00% | 100.00% | 99.89% |
| Grand Total | 345 | 31.88% | 95.36% | 97.04% |

* "Overall Votes with Management" calculated from resolutions in respect of which shareholder voting results were available.

The majority of Corporate Actions resolutions trigger 'Case by Case' assessments, because of the nature of the issue at hand often being investment or company-specific, such as related party transactions, schemes of arrangement, disposals and acquisitions. Definitions of what might be 'good' or 'bad' decisions or perspectives in this context becomes decidedly subjective, as do comparisons of fund manager voting with management recommendations.

What can be observed is that Avon's fund managers are consistently much more likely to oppose approvals of related party transactions (commercial transactions between the company and related parties such as other companies for whom officers or directors of the company work). This is because related party and especially significant transactions may well entail significant potential conflicts of interest.

6.8 Sustainability

With the exception of political activity, charitable engagement and sustainability reports, once again virtually all resolutions in this category were proposed by shareholders, generally asking companies to either improve their reporting of, or performance on, specified sustainability issues. Because of this, meaningful routine categorisation of these issues is very challenging, because the specific content of proposal is defined by the proponent and could be about anything, from asking the company to close specific operations to requesting a one-off or regular report on employee conditions.

It is also not uncommon for most investors to vote with management on such issues unless the issue at hand is either one for which the investor (i.e.; fund manager) has a particular affinity or was involved with the tabling of the resolution itself.

Table 15: Sustainability Resolution Sub-Categories

| Resolution Sub-Category | Total Resolutions | Template With Mgt | Avon Voted With Mgt | Overall Votes With Mgt |
|----------------------------|-------------------|-------------------|---------------------|------------------------|
| Political Activity | 256 | 11.33% | 84.77% | 90.34% |
| Other ESG | 13 | 7.69% | 30.77% | 87.56% |
| Sustainability Report | 9 | 22.22% | 33.33% | 75.75% |
| Environmental Practices | 7 | 0.00% | 14.29% | 83.16% |
| Ethical business Practices | 6 | 0.00% | 66.67% | 78.99% |
| Charitable Engagement | 3 | 66.67% | 100.00% | 75.38% |
| Human Rights & Equality | 3 | 0.00% | 100.00% | 91.11% |
| Animal Welfare | 2 | 0.00% | 100.00% | 76.08% |
| Grand Total | 299 | 11.37% | 79.26% | 89.44% |

* “Overall Votes with Management” calculated from resolutions in respect of which shareholder voting results were available.

Under European jurisdictions, companies are required to seek approval for “political donations”, which encompass more than donations to specific political parties, and include expenditure towards the realisation of political aims such as political lobbying. It is notable that although there is a significant gap between the low proportion of political activity resolutions the policy template implies support for and the actual (higher) proportion of resolutions where the portfolio managers supported such proposals, Avon’s fund managers have opposed far more resolutions of this type than before this year. For the first time in this analysis, Avon’s fund managers have opposed management significantly more than shareholders in general on sustainability-related issues.

7 Aggregate Analyses

Manifest has also assessed the aggregate voting patterns undertaken by the fund managers mainly in respect of voting in emerging or developing markets (including Far Eastern and African markets). Aggregate analysis does not drill down to identifying governance concerns on individual resolutions, but does look at the aggregate patterns of voting decisions taken by the fund managers. This is largely due to the fact the disclosure practices in these markets is traditionally not as high as we are used to in Europe and the US in particular, thereby hindering the statistical reliability of detailed analysis.

7.1 Genesis

Table 16 below shows the number of votable resolutions in each category type voted by Genesis, as well as their average support of management on each.

It shows overall a notably lower level of support for management than the fund managers in the detailed analysis above, which might not be a surprise given the relatively lower levels of disclosure and governance standards in many of the markets in which Genesis was voting.

This shows that Genesis has taken a progressively more active approach as often required in these markets, and continues to do so.

Table 16: Genesis Voting By Category

| Category | Total Resolutions | Voted with Management 2014 | Voted with Management 2013 | Voted with Management 2012 |
|--------------------|-------------------|----------------------------|----------------------------|----------------------------|
| Board | 535 | 77.99% | 77.24% | 96.19% |
| Audit & Reporting | 285 | 96.28% | 98.01% | 95.42% |
| Capital | 206 | 84.08% | 81.36% | 87.40% |
| Remuneration | 139 | 82.74% | 95.97% | 94.70% |
| Corporate Actions | 90 | 91.84% | 92.71% | 71.67% |
| Shareholder Rights | 55 | 79.71% | 89.04% | 87.94% |
| Other | 5 | 55.56% | N/A | N/A |
| Sustainability | 3 | 75.00% | 50.00% | 60.00% |
| Grand Total | 1,318 | 83.68% | 85.02% | 91.06% |

What is interesting is the breakdown of the average support of management by resolution category. Whilst Audit & Reporting resolutions are roughly in line with the patterns shown in section 6 above for all three years, the level of support on remuneration issues is much lower in 2014 than in previous years.

The emergence of better disclosure of remuneration issues in some of the markets in which Genesis votes may now demand a more discerning approach than was possible before.

Board related resolutions (including director elections) continue to show a significant drop compared to 2012. This is still largely explained by a high number of instances of “cumulative voting” resolutions (103). Cumulative voting is where a list of directors is presented to shareholders to vote, from which shareholders vote for their preferred candidate(s). As there is no management recommendation, any vote on these resolutions counts as “against” management recommendation. However, even allowing for these resolution types, Genesis supported management only 91.77% of the time on the remaining Board-related resolutions, which may reflect the specific issues arising (directors in particular for Emerging Market companies) notably regarding independence.

Genesis' vote reporting data didn't identify the country of each meeting this year.

7.2 Unigestion

Table 17: Unigestion Aggregate Resolutions Voting By Market

| Country | Total Resolutions | Voted With Management 2014 |
|--------------------|-------------------|----------------------------|
| Hong Kong | 256 | 83.98% |
| South Korea | 120 | 95.00% |
| Poland | 92 | 98.85% |
| Taiwan | 87 | 92.39% |
| Brazil | 62 | 88.71% |
| Thailand | 47 | 100.00% |
| Mexico | 41 | 97.50% |
| Turkey | 40 | 78.72% |
| China | 35 | 97.14% |
| South Africa | 34 | 88.24% |
| Malaysia | 32 | 90.63% |
| Philippines | 28 | 96.43% |
| Russia | 21 | 95.24% |
| Indonesia | 16 | 87.50% |
| Czech Republic | 11 | 90.91% |
| Grand Total | 922 | 90.67% |

Not dissimilar to Genesis, caution should be used regarding the statistical significance of this data when making inferences at the market level. By comparison with the data in the BlackRock section of the report, the dissent levels towards Hong Kong and South Korean companies are broadly similar.

Unigestion's overall support level stands at around 90%, which is lower than the average discussed in Section 6 above, but again, like Genesis, it is best explained by the fact that generally governance standards are lower in many of the markets where Unigestion are voting.

Table 18: Unigestion Voting By Category

| Category | Total Resolutions | Voted with Management 2014 |
|--------------------|--------------------------|-----------------------------------|
| Board | 391 | 90.54% |
| Audit & Reporting | 173 | 97.11% |
| Capital | 157 | 84.08% |
| Corporate Actions | 101 | 96.04% |
| Remuneration | 57 | 82.46% |
| Shareholder Rights | 40 | 87.50% |
| Sustainability | 3 | 100.00% |
| Grand Total | 922 | 90.67% |

Table 18: Unigestion Voting By Category above shows the number of votable resolutions in each category type voted by Unigestion, as well as their average support of management on each. Consistent with the analysis in Section 6.1.1 above, Unigestion opposes management more frequently on remuneration issues than any other, with Capital and Shareholder Rights issues being notable in their dissent levels too. This is explained largely because many of the resolutions in those two issues touch on the question of control (either dilution of ownership in the case of Capital and in the case of Shareholder Rights the voting rights associated with capital types or resolutions of a certain type).

Unigestion’s voting was in line with the voting policy in use in all instances.

7.3 BlackRock

The aggregate analysis for the other fund managers includes those markets where no detailed meeting analysis was carried out. In the case of BlackRock, the total number of resolutions voted by market is shown in Table 19 below.

The majority of the resolutions in question related to Japanese meetings. What is particularly noteworthy is the much lower average level of voting with management in all of these markets (Panama, Curacao and Liberia constituted a very small number of resolutions, so should be discounted as a statistical pattern), especially in Hong Kong and South Korea, in comparison to BlackRock’s average of 97% support for management in the detailed analysis. However, over the past three years, the general pattern of overall support for management by BlackRock has increased both in the detailed and aggregate analyses.

Table 19: BlackRock Aggregate Resolutions Voting By Market

| Country | Total Resolutions | Voted With Management 2014 | Voted With Management 2013 | Voted With Management 2012 |
|--------------------|-------------------|----------------------------|----------------------------|----------------------------|
| Japan | 5,601 | 91.72% | 90.55% | 88.51% |
| Hong Kong | 788 | 76.40% | 77.99% | 76.59% |
| South Korea | 779 | 87.16% | 73.47% | 78.78% |
| Singapore | 480 | 94.58% | 91.48% | 93.49% |
| Panama | 19 | 84.21% | 100.00% | N/A |
| Curacao | 14 | 100.00% | 100.00% | N/A |
| Liberia | 8 | 87.50% | 83.33% | 100.00% |
| Grand Total | 7,689 | 89.86% | 87.79% | 86.25% |

Table 20 shows the overall patterns of support for management shown by BlackRock broken down by resolution category across all of the resolutions in the aggregate analysis.

Noteworthy in the data set is the change in the level of support for management on Audit & Reporting resolutions. Lack of sufficient disclosure in order to be able to ascertain whether the financial statements could be approved was a significant problem in Singapore in 2013, though all such resolutions were supported in 2014.

Also noteworthy is the comparatively low level of support for resolutions pertaining to Shareholder Rights. This is again explained almost entirely by opposition to resolutions seeking approval of takeover defence plans (poison pills). Takeover defence mechanisms serve to artificially prevent hostile takeovers which may ultimately be in the interests of higher shareholder returns.

It is again notable that, as a proportion of the total number of resolutions in this aggregate analysis, remuneration resolutions form a much smaller percentage than the detailed analysis. This is strong evidence that a shareholder say on pay is much less well established in these markets, although readers will note an encouraging upward trend in these figures.

Also consistent with the detailed analysis is the high proportion of resolutions which are board related. This is again due to the very high proportion of resolutions which are director elections.

Table 20: BlackRock Aggregate Voting Patterns By Resolution Category

| Category | Total Resolutions | Voted with Management 2014 | Voted with Management 2013 | Voted with Management 2012 |
|--------------------|-------------------|----------------------------|----------------------------|----------------------------|
| Board | 5,747 | 91.23% | 90.44% | 88.58% |
| Capital | 747 | 83.13% | 82.02% | 83.67% |
| Remuneration | 516 | 83.53% | 83.33% | 71.10% |
| Audit & Reporting | 343 | 99.13% | 69.32% | 77.88% |
| Shareholder Rights | 192 | 69.79% | 12.24% | 80.27% |
| Corporate Actions | 90 | 95.56% | 92.88% | 93.80% |
| Sustainability | 54 | 100.00% | 100.00% | 97.78% |
| Other | 0 | N/A | 0.00% | 10.00% |
| Grand Total | 7,689 | 89.86% | 87.79% | 86.25% |

Conversely, there is a high level of support for management on sustainability issues. Readers may recall that many resolutions on sustainability issues are largely proposed by shareholders and are therefore often characterised by a comparatively higher level of dissent normally.

However, as was the case the previous years, a large proportion of the sustainability themed resolutions in 2014 were in Japan, which was subject to some very specific circumstances. With Japan relying so comparatively heavily on nuclear power for electricity generation, and the devastating effect of the earthquake and Tsunami of April 2011 on the Japanese nuclear power industry, Japanese shareholders in the many Japanese power companies tabled resolutions which generally had as their goal the reduction or eradication of the use of nuclear reactors to generate electricity, a proposal which was impractical in terms of the viability of the company. These resolutions recurred again in 2014, as they had done in previous years since 2011.

This explains the comparatively higher level of support for management from BlackRock on sustainability issues in this section.

7.4 State Street

State Street’s voting in the aggregate analysis markets is also relatively statistically significant, especially in Japan. Table 21 shows a higher level of support for management than BlackRock, but still slightly lower than the average level for Schroder voted events in the detailed analysis.

Table 21: State Street Aggregate Resolutions Voting By Market

| Country | Total Resolutions | Voted With Management 2014 | Voted With Management 2013 | Voted With Management 2012 |
|--------------------|-------------------|----------------------------|----------------------------|----------------------------|
| Japan | 2,746 | 95.74% | 94.32% | 95.18% |
| Hong Kong | 469 | 76.97% | 74.50% | 82.10% |
| South Korea | 383 | 95.04% | 91.35% | 90.51% |
| Singapore | 273 | 94.14% | 89.33% | 94.67% |
| Grand Total | 3,871 | 93.28% | 91.27% | 92.56% |

Similar to BlackRock, and identically to previous reports, State Street’s support for management at meetings of Hong Kong companies is noticeably lower than for Japan, Singapore or even South Korea.

Table 22: State Street Aggregate Voting Patterns By Resolution Category

| Category | Total Resolutions | Voted with Management 2014 | Voted with Management 2013 | Voted with Management 2012 |
|--------------------|-------------------|----------------------------|----------------------------|----------------------------|
| Board | 2,843 | 95.71% | 92.96% | 95.47% |
| Capital | 408 | 80.88% | 81.40% | 76.73% |
| Remuneration | 240 | 89.58% | 87.31% | 94.58% |
| Audit & Reporting | 174 | 98.85% | 98.20% | 97.76% |
| Corporate Actions | 133 | 78.95% | 81.25% | 93.44% |
| Sustainability | 35 | 94.29% | 97.37% | 93.62% |
| Shareholder Rights | 32 | 90.63% | 81.25% | 78.26% |
| Other | 6 | 100.00% | 57.14% | 50.00% |
| Grand Total | 3,871 | 93.28% | 91.22% | 92.56% |

As is the case throughout this and previous reports, the breakdown of the resolutions voted by State Street in the aggregate analysis by category in Table 22 shows that the majority of resolutions were board-related, due to the large number of director elections especially prevalent in Far East markets.

Of those with a sufficient number of examples to draw patterns from, resolutions pertaining to share Capital (issue or re-issue of equity in particular) is the resolution type where the fund manager is most likely to oppose management. Given the subject matter (questions related to the issue of new capital are likely to catch the eye of financial analysts), it is unsurprising that this area is characterised by higher dissent levels from the fund manager.

It is again noteworthy that the proportion of the resolutions where State Street have opposed management is higher by comparison to the two previous years, and comfortably above 90%, even when voting in markets which are characterised by higher levels of governance related risk (such as control for example) than many others.

7.5 Invesco, Jupiter, TT International & Schroder

Invesco, Jupiter and TT international did not have any events to vote in the markets for which the aggregate analysis is undertaken. Given the very small number of meetings in the Schroder voting portfolio, there was not much meaningful analysis that could be added to the detailed analysis section.

8 Conclusions

This is the 4th annual report Manifest has produced for the Avon Pension Fund (the third with full year analysis). Consistent with the report on 2013 voting, there are patterns in common with the previous year's report. This is because, by and large, corporate governance risk-related issues change over the long term, rather than due to short term pressures. As is evidenced with the example of shareholder proposed resolutions in the US, specific themes can be and are raised with companies on a campaign / strategic basis on specific questions which, over time, contribute to positive progress (for example, proxy access and double voting rights).

We expect to see overall trends of gradual improvement in corporate governance standards continuing, but this is mitigated by the fact that some companies may 'lapse' and new companies may enter the market carrying with them the legacy of private ownership governance practices which also may fall short of the standards expected of publicly listed companies. Additionally, developments in the governance risk profile across equity asset allocation caused by changes to investment mandates from year to year may also have an effect upon the overall picture. Consequently, although we expect trends to improve over the long term, positively identifying them year on year is much harder to do.

For this reason, readers should not expect to see a marked change in companies' governance standards from year to year. What is more important is to understand how the fund's managers respond and react to identified concerns, and fund manager vote monitoring plays a central role in understanding this question. However, the three year trend both in identification of concerns and support for management proposals by fund managers suggests that gradual improvement is underway.

We anticipate that incentive performance measures, proxy access and the theme of "one-share, one-vote" may prove to be prominent themes in commentary about 2015, which will be characterised by regulatory developments in the role and rights of shareholders.

In the context of the new Remuneration Policy votes in the UK, we correctly anticipated in last year's report that claw back may once again be a prominent theme for 2014, now that remuneration policy has an explicit vote of its own. Given the direction of thinking at the FRC regarding issuer-investor engagement, we also anticipate companies may start to set out how they intend to engage with investors in the event of significant dissent on remuneration issues.

There are some key regulatory developments which come into play during 2014 that may have a bearing on next year's report. These include votes on remuneration policy, gender diversity, and shareholder voting rights where there is a majority owner. Further details on these developments may be found in the appendix, which covers:

- Impact of the new directors remuneration report regulations in the UK;
- Revisions to the UK Corporate Governance Code
- Progress on the EU Shareholder Rights Directive (part II)
- Red Lines Voting Initiative: Association of Member Nominated Trustees (AMNT)
- Pre-Emption Group revised guidance
- Japanese Stewardship Code
- UK's Investor Association Updates to Executive Pay Guidelines

In summary, this report shows evidence that governance concerns at portfolio companies during 2014 were at a lower level than in previous years, although in the emerging and Far East markets there is still clearly more cause for concern on certain issues, especially relating to control. Whilst governance change is a long term investment issue, signs of positive change in the short term are reason for cautious optimism that fund managers are having a constructive impact with their engagement strategy alongside use of ownership rights on behalf of the fund.

The results of the analysis show that fund managers are voting with management marginally more than shareholders in general, for the first time since this annual analysis has been undertaken.

Whilst there may be other governance themes where immediate positive progress is harder to determine, we are confident that continued monitoring should enable identification of further progress over the medium to long term. Additionally, with ever increasing pressure upon institutional investors and their asset managers for transparency about ownership processes, on-going monitoring of governance risk and voting activity remains a vital part of the activity of any responsible investment-minded investor.

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9 Hot Governance Topics

The following is largely a UK-focussed summary of governance developments. For a more detailed précis of governance developments globally, please refer to Manifest's report "Global Corporate Governance and Regulatory Developments 2013" which is available upon request.

9.1 Impact of the new Directors' Remuneration Report Regulations in the UK.

In July 2013, the UK government introduced revisions to the Companies Act 2006 relating to director's remuneration policy votes and reporting. In short, the previous arrangements for a single vote on a remuneration report which included review of pay in the financial year under review as well as proposals for future pay policy are being replaced by two votes, one advisory vote in respect of a pay report on the financial year under review, and a second binding vote on proposed pay policy.

Quoted companies with year ends on or after the 30th September 2013 are required to put their proposed remuneration policy to a simple majority binding vote at the AGM. Thereafter, companies can only provide remuneration or loss of office payments that are consistent with the approved policy unless they obtain shareholder approval at a general meeting to a revised policy or to the specific payments. Once approved by shareholders, a company can retain the policy for up to three years before being required to hold another binding policy vote, unless the separate vote on the remuneration report (implementation) is lost in the intervening period in which case a fresh policy vote is required the following year.

In addition to the future looking policy vote, the main changes to the reporting of pay include:

- Requirement to show an illustration of the level of awards that could pay out for various levels of performance;
- Requirement for reporting pay in a single, cumulative figure, including methodology for calculation to ensure consistency in approach; and
- Improved disclosure on the performance conditions used to assess variable pay of directors.

The aim of the regulations is to encourage better shareholder engagement with companies regarding remuneration, It is intended to do this by giving shareholders more powers to hold companies to account at AGM's for their pay practices and policies, in particular with the introduction of the binding policy vote and the reporting of a "single figure" for the purposes of evaluating total remuneration paid.

Ex-Post analysis carried out for the Department for Business, Innovation and Skills by Manifest identified that, by and large, companies had responded well both to the letter and, in most cases, the spirit, of the Regulations. Some areas for further attention were identified, including the possibility of losing an element of meaningfulness in disclosures through the use of boiler plate text. Attention was also drawn to the quality of disclosure of issuer engagement with investors, in particular in cases where a small subsection of shareholders was referred to, or even simply "shareholder representatives" as the basis for canvassing opinion. A number of companies silently posted "clarifications" of policy after publication of their meeting documentation but before the meeting itself, as a way of heading off a potential "Against" vote. These clarifications were not formally circulated to all shareholders and thus ran the risk of creating information imbalances between those who were party to the need for the clarification, and those to whom it was not announced. We also identified that it may be helpful for companies to consider positive confirmation of not having made termination payments or payments to past directors, rather than assuming a silence on the issue confirms no such payments have been made.

9.2 UK Revises Governance Code

The Financial Reporting Council (FRC) published its revised UK Corporate Governance Code which takes effect to UK listed companies for reporting years beginning on or after 1 October 2014. We summarise the main changes in the table below. As with most regulatory changes which seek to serve a broad constituency, the changes are a mix of positive and not so positive amendments.

A minimum threshold for **EGM notice periods** is welcome; many companies have sought to take advantage of a 14 calendar day minimum notice period despite the absence of any authority related to capital raising (the original premise for allowing an abbreviated period).

The changes on **going concern** follow the conclusions of the Sharman Review. The 2012 Code required boards to state if a company “is” a going concern. Investors’ second line of defence then came from the auditors opinion. Under the relevant accounting standards Auditors needed to make a decision about whether a board’s going concern assumption was “appropriate”. This was in fact the position leading up to the 2008 financial crisis - neither proved to be a defence in the context of the failure of financial institutions in 2008 and it is not surprising that changes have been made. The use of the term “appropriate” to define the boards responsibility in coming to a decision on applying accounting standards may lead to confusion given the pre-existing auditor responsibilities.

UK Governance Code – Changes at a Glance

| Issue | 2012 Code | 2014 Revised Code |
|-------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Going Concern Principle C.1.3 | Directors had to state if the company was a going concern. | Directors no longer need state if the company is a going concern. Companies should state whether they consider it appropriate to adopt going concern and identify any material uncertainties. The decision on whether the assumption of going concern accounts is <i>appropriate</i> was solely the auditors’ responsibility. |
| Risk and Internal Control reporting Principles C.2 and C.2.1 | Board was previously required to report on its review of effectiveness of risk management systems. | Reporting now specific to annual report (discretion allowed as to which section) No longer solely focussed on process. Companies should robustly assess their principal risks and explain how they are being managed or mitigated. Companies should monitor risk management and internal control systems and, at least annually, carry out a review of and report on their effectiveness. |
| Remuneration policy Principle D1 | Sufficient to attract retain and motivate directors and a significant proportion was required to be performance linked. | Attract, retain and motivate has gone. There is no steer now towards a preferred performance pay ratio. Greater emphasis be placed on ensuring that remuneration policies are designed with the long-term success of the company in mind, and that the lead responsibility for doing so rests with the remuneration committee. |
| Clawback and Malus Principle D1.1 | Companies only required to “give consideration” to the use of clawback provisions. | Companies “should” include clawback and malus provisions in performance pay arrangements. Companies should put in place arrangements that will enable them to recover or withhold variable pay when appropriate to do so, and should consider appropriate vesting and holding periods for deferred remuneration. |

| Issue | 2012 Code | 2014 Revised Code |
|----------------------------------------------------------|----------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Post dissent engagement Principle E.2.2 | Company had to publish results but the Code did not explicitly require further action. | No definition of “significant” however boards can no longer fail to take action if there is a significant level of voting dissent. Companies should explain how they intend to engage with shareholders when a significant percentage of them have voted against any resolution. |
| Notice of Meeting Principle E.2.4 | Code previously failed to state a threshold for producing EGM NoM . | Now companies required to provide an EGM notice 14 working days ahead of the meeting. |

The loss of “**attract, retain and motivate**” as a pay policy will not be mourned. The routine practice of buying unvested awards from a prior employer on recruitment undermined any retentive effect promised by such statements.

Finally, the FRC’s consultation feedback statements reveal some near misses which would have been potentially negative for shareholders. It appears that companies and audit firms lobbied for moving corporate governance disclosures online. The consequential loss of assurance that corporate governance disclosures are relevant to the latest published full year accounts has for the time being at least been avoided.

9.3 The EU Shareholders Rights Directive Part II

During 2014 the European Commission commenced the process of revising and updating the Shareholders Rights Directive, which came into force in 2007. The proposed Directive is approaching the final stage of negotiation – between the Parliament and the Council of Ministers.

Most significant in the context of this report is the fact that the Commission proposed measures designed to encourage better engagement with companies by institutional investors, because of a perception that the problem of short-term investment decisions is facilitating excessive risk-taking by companies. This implies disclosure of aspects of investment mandates which encourage:

- strategic alignment with the liabilities and duration of the investor;
- how the asset manager takes decisions based on the long term performance of a company;
- how the asset manager’s performance is evaluated; and
- information on portfolio turnover.

During the negotiations, the question of enhanced voting or dividend rights for long term shareholders has been proposed as a solution to the problem of short-termism. However, this brings more pressure to bear on the need for better ability to identify shareholders, in order to facilitate more efficient transmission of information, the exercise of shareholders rights, and now the allocation of loyalty votes or dividends. It is also likely that the Directive may require all listed companies incorporated in the EU to have a “Say on Pay Policy” vote.

Another area for proposed action is enhancing issuer disclosures and shareholder rights on related party transactions. It initially proposed requiring shareholder votes on certain types of related party transactions, in order to help protect shareholders from potentially abusive deals. However, companies across Europe have been successful in watering down many of the requirements.

The Directive is also likely seeking to address perceived concerns with what they call “proxy advisors” (i.e. companies like Manifest who provide research or voting guidance to institutional investors), relating to the transparency of methodologies used for producing voting guidance for clients and potential conflicts of interest.

9.4 Red Lines Voting Initiative: Association of Member Nominated Trustees (AMNT)

A separate but relevant development related to the provisions about fund manager performance evaluation in the Shareholder’s Rights Directive has been the launch of the “Red Lines Voting Initiative” by the Association of Member Nominated Trustees. The aim of this initiative is to better equip AMNT members in holding their fund managers to account for their voting on issues where companies fall short of the governance “Red Lines” of their policy, which are yet to be announced. The initiative is virtually identical in concept to the vote monitoring Avon undertakes with this report.

9.5 Pre-Emption Group Revised Guidance

The Pre-Emption Group has now released updated guidance on the factors to take into account when considering whether to disapply pre-emption rights. <https://frc.org.uk/News-and-Events/FRC-Press/Press/2015/March/The-Pre-Emption-Group-publishes-a-revised-Statement.aspx>

Manifest welcomes the March 2015 improved guidance particularly with regard to the explicit inclusion of “cash box placings”. Manifest has tracked use of this dilutive capital raising mechanism since 2005. Our records reveal that a total of £2.7bn has been raised by 39 different companies using cash box placement over this period.

Quite how effective the revised guidance will be at stopping companies from using this method of share issuance is yet to be seen. The ABI (one of the Pre-Emption Groups members at the time) wrote to companies in February 2009 warning that the pre-emption principle was being eroded through the abuse of cash-box placings. Since that date this mechanism has been used more than 20 times by companies to which the ABI issued its warning. Key amendments to the 2008 Statement of Principles include:

- Clarification of the scope of the Statement, making it clear that it applies to both UK and non-UK incorporated companies whose shares are admitted to the premium segment of the Official List of the UK Listing Authority. Companies whose shares are admitted to the standard segment of the Official List, to trading on AIM, or to the High Growth Segment of the London Stock Exchange’s Main Market are encouraged to adopt the Statement.
- Clarification that the Statement applies to all issues of equity securities that are undertaken to raise cash for the issuer or its subsidiaries, irrespective of the legal form of the transaction, including, for example, “cashbox” transactions.
- Flexibility to undertake non-pre-emptive issuance of equity securities in connection with acquisitions and specified capital investments, consistent with existing market practice.
- Greater transparency on the discount at which equity securities are issued non-pre-emptively.

9.6 Japanese Stewardship Code

February 2014 saw the publication of the Japanese Stewardship Code. The working group which put it together included institutional investors, representatives of companies, as well as academics and representatives of government departments.

A part of the “Abenomics” policy, the aim of the code is to make the Japanese market more amenable to foreign investment, and thereby enabling Japanese companies to better harness the positive input from foreign investment perspectives to further enhance the growth of the Japanese economy as a whole.

It sets out the roles and responsibilities of both sides of the stewardship role – investors and companies. As regards investors, it distinguishes between asset managers and asset owners (who may outsource their asset management to asset managers), highlighting the formers' role as being to "contribute to the enhancement of corporate value of investee companies through day-to-day constructive dialogue with them" and that of the latter as being to "disclose their policies on fulfilling their stewardship responsibilities and ... aim to assess the asset managers in line with the Code, not placing undue emphasis on short-term performance".

The code is also rightfully careful to point out that although voting is a vital part of engagement and stewardship, it is no substitute for constructive dialogue.

The main principles are very similar to the UK Stewardship Code – including the use of comply or explain. The encompass publicly disclosing a policy, management of conflicts of interest, monitoring of portfolio companies, having strategies for engagement and voting as well as disclosure of the latter, reporting of policy implementation to clients and the acquisition of adequate company knowledge to fulfil their Code responsibilities.

9.7 UK's Investor Association Updates to Executive Pay Guidelines

In June 2014 the Association of British Insurers (ABI) Investment Department merged with the Investment Management Association (IMA) to create the Investment Association (IA). The ABI's Remuneration Guidelines have been a long standing feature of the UK's corporate governance landscape and so, not unsurprisingly, the IA has now published its own guidance on the role of shareholders and directors in relation to remuneration.

The only change of substance to the guidelines is reference to the emergent issue of "Allowances" which have been used by some banks to circumvent the EU cap on variable pay. As with the ABI guidance, the best practice outlined by the IA is a very broad church. What may surprise some investors is that the IA best practice appears tolerant of remuneration practices which post crisis regulatory initiatives are trying to tackle.

A comparison of attitudes apparent in the recent Prudential Regulatory Authority (PRA) Consultation paper (CP 15) towards a range of issues serves to illustrate the point. The PRA is proposing a minimum clawback period of 7 years for executives whom are classed as material risk takers under its rules and this extends to 10 years for senior managers in some circumstances. The IA is silent with regard to the period which shareholders should expect vested variable pay to be reclaimable by a company.

The PRA takes the view that deferral periods for variable pay should be longer than current minima whilst the IA explicitly tolerates 3 years as a minimum performance period for variable pay awards.

Pay for Performance

In an unequivocal statement the PRA assert that there is too much reliance on metrics based on short term revenue or profit such as RoE, EPS and TSR whilst the IA guidance explains how best to measure TSR when it is used as a metric. With regard to buy-outs (the practice by which a recruiting company buys out "forfeited" awards of an executives former employer) the PRA proposes four solutions including the banning of buy-outs.

Principles, not Prohibitions

The IA guidance doesn't countenance a prohibition of buy outs (actually the guidance doesn't countenance a prohibition of anything) but suggests that buy outs should take account of performance period remaining and performance achieved (in effect the application of malus by the new employer).

Guidance For Remuneration Committees

In its covering letter to remuneration committee chairs, the IMA outlined four focus areas which are of concern to investors:

- Amounts and gearing of variable pay: Basic salary should not exceed inflation or the increase for the general workforce and any increase to maximum variable pay should be clearly explained.

- Threshold performance: Despite the proportion of awards vesting being low this can still lead to substantial amounts being paid.
- Length of performance/holding period: Performance periods for long term incentives should be no less than three years, preferably longer.
- Retrospective changes to performance conditions: There should be no adjustments to take account of “adverse” exchange rate movements.

Standards Clash for Financials?

For listed financial companies (which include many IA members) there may be a concern about “Standards Clash” as the IA guidelines are a supplement to the PRA’s bright line regulations. The IA guidelines don’t address this scenario. It therefore remains to be seen whether engagement by IA members who are subject to the PRA pay code with companies who are not subject to the code will start to reflect the apparent asymmetry in attitudes towards executive pay.

UK Executive Pay Guidelines – PRA vs. IMA

| Guidance Source >> | PRA/FCA Oct 2014 CP 15 | IMA Remuneration Guidance |
|------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Issue | Applicable to financial companies including some IMA members (PRA designated investment firms) | Applicable to all companies including financial companies |
| Clawback | Proposes minimum clawback period of 7 years for material risk takers and 10 years for senior managers in some circumstances | Silent on period during which shareholders should expect vested variable pay to be reclaimable by a company |
| Long term Incentive Pay Characteristics | A means of retaining staff | Exists to reward the successful implementation of strategy |
| Performance Periods | The PCBS took the view that deferral over two or three years was insufficient to take account of the timescales over which material business issues can come to light. It is the view of the PRA and FCA that deferral periods should generally be longer than current minima. | The performance period should be clearly linked to the timing of the implementation of the strategy of the business, which should be no less than three years and shareholders would generally prefer longer. |
| Performance Measures | The PRA share this concern that there is too much reliance on metrics based on short term revenue or profit such as RoE, EPS and TSR. | Where TSR relative to an index is used remuneration committees should satisfy themselves that recorded TSR is a genuine reflection of underlying financial performance |
| Buy Outs (recruiting company buys out “forfeited” awards) | Proposed 4 options: a) banning buy-outs b) maintaining unvested awards c) applying malus to bought out awards d) reliance on clawback | Compensating executives for the forfeiture of awards from a previous employer should generally be on a comparable basis, taking account of performance achieved or likely to be achieved the proportion of performance period remaining and the form of the award. |