<u>Report on the UK Corporate Governance Programme</u>
<u>April 2010 – March 2011</u>

This paper describes the broad trends seen in corporate governance during the period 1st April 2010 to 31st March 2011.

The Funds use Institutional Shareholder Services Inc (ISS) (formerly known as Research, Recommendations and Electronic Voting Ltd) advice, incorporating the views of the National Association of Pension Funds (NAPF). In the majority of cases votes were cast in line with ISS guidelines, however, in certain instances an alternative course of action was taken.

The main areas of concern for the Funds were remuneration reports and re-election of directors. Fund Managers continue to engage with investee companies where a vote has been cast against the company and is out of line with the ISS vote recommendation.

On 41 occasions during the period under review the Funds voted against at least one proposal at investee companies' Annual General Meetings (AGM) (22.4% of the total). This is broadly in line with the previous year when, between 1st April 2009 and 31st March 2010, the Funds voted against management on 40 occasions (20%). The Funds also voted against two Extraordinary General Meeting (EGM) resolutions.

The Funds voted against the remuneration report on 21 occasions in 2010/11. This is in line with the previous year (2009/10). Whilst the annual vote on the remuneration report remains advisory, ISS and the wider shareholder community continue to scrutinise companies with perceived shortcomings in corporate governance. For a number of years BAPIML has been highlighting executive remuneration as an area of concern. The Funds continue to communicate this message to management by voting against non-compliant resolutions. During the period under review one of the more controversial aspects of remuneration has been excessive base salary increases. Following a year in which most companies had implemented a pay freeze, those that appeared to be awarding management "catch-up" salary increases were not looked upon favourably and consequently the Funds voted against such resolutions where it was deemed appropriate.

In the case of a small distribution company, the Funds voted against the remuneration report in line with ISS's recommendation. There was a resounding vote of no confidence in the remuneration committee as 61% of shareholders voted down the resolution. The remuneration committee had recommended a 14.6% increase in the Chief Executive Officer's (CEO) basic salary to £532,875, due to his personal contribution in the 18 months preceding the review. The committee explained that upon his appointment to the board on 1st January 2008, his salary was set at the lower quartile of market data with the intention of moving his pay closer to market median at the next review. Whilst this was deferred in January 2009, we expected the company to show restraint and not propose a catch-up award following market benchmarking, particularly as the financial performance of the company had since deteriorated. During 2009 the company's total shareholder return (TSR) had declined, basic earnings per share amounted to a loss of 9.7 pence and the company paid no dividend.

At an industrial company's AGM, the remuneration report received significant shareholder scrutiny. The Funds voted against the remuneration report in line with ISS; nevertheless, on this occasion the resolution was passed by a narrow margin (50.7% in favour). In spite of the challenging economic environment the Chief Executive and the Chief Financial Officer were awarded their maximum allocation of shares under the long-term incentive plan. The CEO's maximum annual bonus potential was also increased from 100% to 150%. During this period, however, the company reported an overall loss for the financial year 2009, suspended its dividend payment and launched a £240m rights issue. There were also large-scale job losses across the group (20% of the workforce). Whilst the company advised that any payment to the CEO as part of his annual bonus plan in excess of 100% will be channelled into shares and deferred for three years subject to a claw-back provision, the Funds believe that the company should have shown greater restraint.

During the period under review, there have been a number of instances where companies proposed supernormal inflationary increases in base salaries. In the case of an asset management company excessive, salary increases and the potential for uncapped annual bonuses resulted in the Funds voting against the remuneration report in line with ISS's vote recommendation. The magnitude of the increase in the fixed salary element proposed by the remuneration committee was between 25% for the CEO, rising to 40% for other executive directors. Such significant increases are particularly problematic in an industry where the performance-related element of pay is also high. Since the onset of the financial crisis the FSA have been working on new guidelines which were released in January 2011 and as a result of this ISS are now encouraging the company to review its uncapped annual bonus policy. BAPIML have long held the view that uncapped bonuses are not aligned with the long term interests of shareholders, as excessive awards could adversely impact the financial performance of a company. Whilst the remuneration report was approved at the AGM, it attracted a 29% opposition.

ISS continue to highlight the re-election of Non Executive Directors (NED) where they have concerns about directors' independence. The Funds use the voting service to highlight potentially controversial re-elections and make the voting decision on a case by case basis. Fund managers pay particular attention to any unique experience that Non Executive Directors might offer, whilst recognising the important principle of true independence. During the period under review the Funds voted against the re-election of Non Executive Directors on 25 occasions compared to 23 over the same period last year.

During the reporting period, three companies had shareholder- requisitioned resolutions. In all cases the Fund managers sided with incumbent management and voted against the proposal.

At two large oil companies AGM's, Fair Pensions (shareholder activist group) put forward a shareholder requisition in relation to their Tar Sands campaign. In both instances the Funds voted against the shareholder proposal in line with management and ISS recommendation. At one of the companies the proposal was to approve that the audit committee or a risk committee of the board should commission and review a report setting out the assumptions made by the company in deciding to proceed with its Canadian tar sands project. After engaging with management we believe that the company's response to the issues raised has been satisfactory. They have outlined their assumptions on world energy demand and oil price volatility; they have also provided details on pricing estimates for carbon emissions for its projects and have conducted independent studies on the impact of Steam Assisted Gravity Drainage (SAGD), which suggest that CO_2 emissions thus generated are 5-15% higher than conventional methods. The company made its final investment decision in December 2010 and plan to start production in 2014. The company continues to invest in the search for technological innovations which might further reduce emission levels. The board additionally states that as part of the company's established investment approval process for all projects, they look at numerous factors which include non-financial risk elements such as environmental, social and reputational risk. In April 2011, they also produced a Canadian sustainability report.

Similarly, the other oil company's shareholder proposal was to direct the audit committee or a risk committee of the board, to commission and review a report on the investment risks associated with future Canadian oil sands projects. After engaging with the company, we believe the company's responses to issues raised in the shareholder proposal to have been satisfactory. The company has outlined its assumptions on world energy demand and oil price volatility (citing the International Energy Agency's World Energy Outlook 2009 report), it has also provided details on pricing estimates for future carbon emissions. In its economic assessment, the company assumes a higher CO_2 price than that currently being charged in Alberta. Independent studies have been conducted on the impact of emissions from oil sand based fuels and a report produced by IHS Cambridge Energy Research Associates suggests that on a life-cycle basis, oil sands are around 5-15% more CO_2 intensive than conventional crude oil. The company is, however, continuing to research alternative methods of extraction which it hopes will further reduce emission levels. The company has stated that as part of its established investment approval process for all its projects they look at health & safety as well as environmental impacts.

The Funds continue to vote all shares where practicable at every investee company AGM and EGM.

Originator: **UK Portfolio Manager**
Date: **17th May 2011**

UK Corporate Governance	**1st April 2010 - 31st March 2011**
Total number of AGM's voted	**UK**
Total number of AGM's voted	**183**
Voted FOR on all proposals or voted in line with all management recommendations	142
% of votes for	77.6%
Voted AGAINST on at least one proposal or voted against a management recommendation	41
% of votes against	22.4%
Voted ABSTAIN on at least one proposal	0
% of votes abstained	0.0%
Taken NO ACTION	0
% of votes no action taken	0%
Breakdown of voting on individual proposals	
Number of individual proposals where voted against management in line with RREV recommendation	**51**
Against Directors	31
Against remuneration policy	16
Against Long Term Share Incentive Plan	1
Against Annual Report and Accounts	1
Against LTIP Award	1
Against Approval to issue of equity or equity linked securities without pre-emptive rights	1
Number of individual proposals where voted Against contrary to RREV recommendation to vote for	**1**
Against Directors	1
Number of individual proposals where voted for contrary to RREV recommendation to against	**5**
Approve Tender Bid Requirement	2
Remuneration policy	2
Director Election	1
Number of individual proposals where voted against contrary to RREV recommendation to abstain	**5**
Remuneration policy	5
Number of individual proposals where voted for contrary to RREV recommendation to abstain	**5**
Director Election	3
Remuneration policy	1
Auditor Remuneration	1

Number of shareholder proposals	**3**
Against Shareholder Proposal in line with RREV	2
Against Shareholder Proposal Contrary to RREV (vote for)	1

Total number of EGM's - OGM's voted	**UK**
Total number of EGM's - OGM's voted	**36**
Voted FOR on all proposals or voted in line with all management recommendations	34
% of votes for	94.4%
Voted AGAINST on at least one proposal or voted against a management recommendation	2
% of votes against	5.6%
Voted ABSTAIN on at least one proposal	0
% of votes abstained	0.0%
Taken NO ACTION	0
% of votes no action taken	0%
Breakdown of voting on individual proposals	
Number of individual proposals where voted for contrary to RREV recommendation to vote against	**2**
Capital Raising	2
Number of individual proposals where voted against management in line with RREV recommendation	**6**
Against Long Term Share Incentive Plan	3
Against Approval to issue of equity or equity linked securities with pre-emptive rights	1
Against Approval to issue of equity or equity linked securities without pre-emptive rights	1
Against Establish Prudential as Ultimate Holding Group	1