

# CORPORATE GOVERNANCE



## CONTENTS

- 03 Introduction
- 04 Corporate Governance at LGIM
- 07 Structure and Accountability of the Board
- 11 Remuneration
- 16 Accountability and Audit
- 17 Shareholder Rights and other voting policies
- 19 Corporate Governance Engagement
- 20 Voting Process
- 20 Socially Responsible Investment Policy
- 24 Appendix





## INTRODUCTION

### What is Corporate Governance?

---

Corporate governance is “the set of processes, policies, laws and institutions affecting the way a company is directed, administered or controlled. Corporate governance also includes the relationships among the many stakeholders involved and the objectives for which the company is governed. The principal stakeholders are the shareholders, management and the board of directors. Other stakeholders include employees, suppliers, customers, banks and other lenders, regulators, the environment and the community at large.”

At Legal & General Investment Management (LGIM), our aim is to maximise shareholder value by promoting integrity in business

As at 31 March 2008 LGIM has £297 billion of funds under management and is one of the UK's largest asset managers. LGIM's holding of equities accounts for around 5% of the total capitalisation of the FTSE All-Share Index. We aim to use our position as a major shareholder to help shape the UK stock market into being a premier brand for investing. We expect all companies listed in the UK stockmarket and those seeking a listing, regardless of their domicile, to demonstrate the highest standards of corporate governance.

We believe companies that demonstrate good corporate governance and have policies for a sustainable business model will generally deliver shareholder value. Though our engagement and voting policies we aim to exert major influence on the companies in which we invest to drive best practice and reduce the risk of corporate failure.

Our policies on corporate governance build on the Combined Code and incorporate many features of the guidelines issued by the Association of British Insurers (ABI) guide on Executive Remuneration and on Responsible Investment Disclosure.

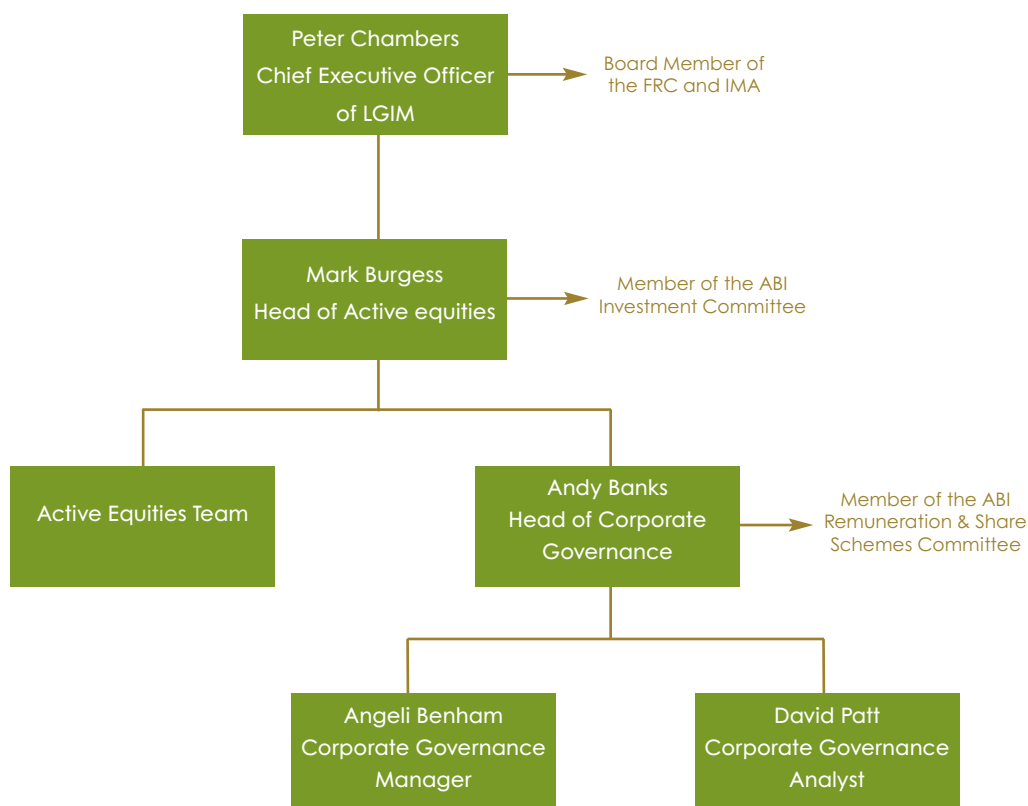
Our links with the Financial Reporting Council, the Investment Management Institute, as well as our membership of both the ABI Investment Committee and the Remuneration and Share Schemes Committee enables the team to draw on different sources of information.

LGIM is committed to supporting the Institutional Shareholders Committee's “Statement of Principles and Responsibilities for Institutional Shareholders and their Agents”, as well as their framework on voting disclosure. Clients receive a quarterly report covering both engagement and voting activity.

In 2007, LGIM met with over 1000 UK companies. Over 100 of these meetings were held to specifically discuss governance issues. In 2007 we consulted our major clients to gain their views on the public disclosure of voting and in January 2008 our website was updated to provide information on the voting instructions for the funds managed on behalf of Legal & General Assurance Society.

The following pages set out Legal & General's approach to being a force for good in governing the companies in which we invest.

## CORPORATE GOVERNANCE AT LGIM



### The Team

The Corporate Governance Department is headed by Andy Banks who is responsible for monitoring and developing LGIM's Corporate Governance Policy.

He is supported by Angeli Benham and David Patt who are involved with the execution of the policy and the daily considerations of corporate governance matters. These responsibilities include:

- weekly revision of contentious voting issues raised by corporate governance bodies;
- implementation of LGIM's voting process;
- remuneration consultations;
- generation of information for client reports; and
- production of in-house research on corporate governance topics

The Corporate Governance Department is also involved with examining issues relating to Socially Responsible Investment (SRI).

## Links with Active Equities

---

When considering corporate governance matters, the Department engages with the Active Equities Team who provide a valuable source of information when analysing the performance of companies.

This enables the Department to take into account a Company's operational circumstances before reaching a final decision.

There is a procedure whereby the Corporate Governance Department meets with the Active Equities Team on a weekly basis to discuss any corporate governance concerns. These are then investigated and will generally result in a meeting being held with the Company to discuss the matter.

In addition, the Head of Active Equities, Mark Burgess, hosts an internal weekly Corporate Governance meeting in which contentious remuneration and voting issues are raised and a final decision is taken on the subject.

## Association with Regulatory and Trade Bodies

---

LGIM has extensive ties with a number of different bodies that are concerned with the generation and regulation of policies that shape the governance landscape in the UK market.

Mark Burgess is a member of the ABI's Investment Committee which determines specific policies relating to the functioning and regulation of investment business in the UK and EU.

The Head of Corporate Governance, Andy Banks, is a member of the ABI's Remuneration and Share Schemes Committee which produces annual guidelines on executive remuneration and reviews individual schemes proposed by companies.

In addition, LGIM's Chief Executive Officer, Peter Chambers, is a Non Executive Director of the Investment Management Association whose remit is to "foster the good reputation of the industry and to promote a legal, tax and regulatory environment which is appropriate for the needs of asset managers and their customers." Peter is also a Non Executive Director of the Financial Reporting Council which is the UK's independent regulator responsible for promoting confidence in corporate reporting and governance.

On a fortnightly basis, the Corporate Governance Team and the Head of Active Equities meet with the Chief Executive Officer of LGIM, to discuss and examine policies that impact UK companies. In these meetings, the Chief Executive Officer is also updated on the activity of the Corporate Governance Department.





## Conference 2

## STRUCTURE AND ACCOUNTABILITY OF THE BOARD

Every company should be headed by an effective Board, which is collectively responsible for the success of the company.

### Board of Directors

---

Members of the Board have the most important task of setting the strategy and direction for the business and ensuring the necessary financial and human resources are in place to enable their strategy to be implemented.

The Board collectively has a duty of care to its employees and shareholders and should ensure that effective controls are put in place to enable risks to be assessed and managed. They should decide upon the core values for the business and ensure these are understood throughout the company.

The Board should comprise a number of executive and non-executive directors but should not be so large as to be unwieldy. The size of the Board should be appropriate for the size of the company. No individual or small group of individuals should be able to dominate the board's decision taking.

The Board should meet regularly throughout the year and the Chairman should hold separate meetings with the non-executive directors. The non-executives should have at least one meeting per year without the Chairman present. Every company should establish a Nominations Committee, Remuneration Committee and an Audit Committee. The Remuneration and Audit Committees should comprise independent non-executive directors.

LGIM believes it is important for directors to seek outside appointments to other boards as this will help broaden their knowledge and will enable them to provide more input into Board discussions. However, when taking up outside appointments an executive should be mindful of the time commitment required to exercise his duties both within the company and that of any other Board.

Non-executive directors should have access to independent professional advice at the company's expense when required in discharging their normal duties as directors. They should also have access to the Company Secretary who is responsible for ensuring that Board procedures are complied with. Under the direction of the Chairman, the Company Secretary should ensure that there is a good flow of information within the Board and the committees. The Board as a whole should decide on the appointment or removal of the Company Secretary.

### Chairman and Chief Executive

---

There should be a clear division of responsibilities between the running of the Board and the executive responsibility of the running the company's business. No one individual should have un-fettered powers of decision making.

LGIM believes that the role of the Chairman and the Chief Executive are separate roles that require different and distinct skills and experience. Therefore, they should be held by two separate people. The Chairman should be independent at the time of appointment and should have the responsibility of leading the Board, setting the agenda for Board meetings and ensuring the directors receive accurate and clearly



written information in time for meetings. LGIM believes the Chairman should set aside sufficient time to hold regular meetings with the non-executive directors to discuss the performance of the executive directors and the company.

The Chairman is also responsible for ensuring directors receive a comprehensive induction to the company on joining the Board and ensure training is available on an on-going basis. They should encourage the directors to continually update their skills and knowledge. LGIM expects directors' training to include all aspects of social, environmental and ethical risks faced by the business.

The Chairman's role has generally been part-time. However, the rapidly changing economic times that corporate Britain faces requires a Chairman at the helm that is able to devote more time to the business and has the strength of character to challenge the executive directors and safeguard the position of shareholders. It is important that they are supportive of their management team, but this should not lead to complacency in allowing a management team to continue, if they are destroying value for shareholders. The Chairman should be available to meet with shareholders and should effectively manage concerns raised by investors.

The Chief Executive should have the responsibility of executing the strategy agreed by the Board and lead the business.

We believe that the Chief Executive should not normally go on to become the Chairman. There are two main reasons for this. A hands-on Chief Executive may often find it difficult to become a hands-off Chairman. Secondly, this may make it difficult to appoint a successor.

Where companies are looking to depart from best practice in this regard, we would expect the company to enter into a meaningful dialogue with their major shareholders to explain why they think this is appropriate and in the best interest of investors. This consultation should take place within a reasonable time prior to any public announcement being made. We would expect the company to put the new Chairman up for re-appointment at the next shareholder meeting of the company.

LGIM has in a very small number of cases supported the elevation of the Chief Executive to become Chairman, but this has been with the understanding that it is for a very limited period and we have insisted that a strong independent Deputy Chairman be appointed. The merit for having an Executive Chairman will be considered on a case by case basis. Where a company is in distress there may be a case for having a strong Executive Chairman. However, LGIM strongly believes that this should not be the norm.

## Non-Executive Directors

---

Non-executive directors have a very important part to play in the make up of the unitary Board, and should challenge as well as provide valuable input in the decision making, and development of strategy. They should monitor the performance of the Board and should ensure that proper succession planning processes are in place. In exercising their duty of care to shareholders they must satisfy themselves of the integrity of the financial information and risk controls that are in place. They must ensure that executive remuneration is designed to attract and motivate the right calibre of executives and avoid paying more than is necessary to safeguard shareholders' funds.



Although LGIM expects the non-executive directors to be independent, we also believe that in some cases a non-independent director may prove valuable to a company. In these circumstances we expect the company to fully explain why the non-executive director is not considered independent and why he is valuable to the business. Furthermore, Boards must ensure that at least half of the Board, excluding the Chairman, is comprised of independent non-executive directors. In the case of a small company, we would expect at least two of the non-executives to be independent.

In our view, the factors that affect a director's independence mirror that which is disclosed in the Combined Code . If they:

- have been an employee of the company or group within the last five years;
- have, or have had within the last three years, a material business relationship with the company either directly, or as a Partner, shareholder, director or senior employee of a body that has such a relationship with the company;
- have received or receives additional remuneration from the company apart from a director's fee, participates in the company's share option or performance related pay scheme, or is a member of the company's pension scheme;
- have close family ties with any of the company's advisers, directors or senior employees;
- hold cross-directorships or has significant links with other directors through involvement in other companies or bodies;
- represent a significant shareholder; or
- have served on the board for more than nine years from the date of their first election.

## The Senior Independent Director

---

The Board should appoint one of the independent non-executives directors to the position of Senior Independent Director. The Senior Independent Director should be available to meet with shareholders.

LGIM regard the role of the Senior Independent Director to be critically important. The Senior Independent Director is our key contact when the normal channels of the Chairman, Chief Executive or Finance Director have failed to address our concerns or is considered inappropriate given the circumstances. Given the importance of the role, it is vital that the person is independent and has strength of character to be able to stand up to the executive directors when representing the interests of the company's shareholders. The person who holds the role of Senior Independent Director should be mindful of the time commitment required for the role when taking up outside non executive directorships. LGIM believes the Senior Independent Director should receive additional fees for fulfilling this role.

During 2007, LGIM held meetings with 15 senior independent directors. We also published an article on the role and responsibilities of the Senior Independent Director in our July/August edition of Fundamentals. This can be viewed at: [www.lgim.co.uk/media-centre/fundamentals.shtml](http://www.lgim.co.uk/media-centre/fundamentals.shtml)

Any non-executive director looking to take up a directorship with another company should seek the consent from the Board Chairman in order to avoid the possibility of a conflict of interest. Any possible conflicts should be considered by the whole Board.

## Board Committees

---

LGIM expects all UK listed companies to establish an Audit Committee, a Remuneration Committee and a Nominations Committee. These should comprise at least three independent non-executive directors. Smaller companies should have at least two independent directors as its members. The role of committees are discussed in more detail below.

## Appointments to the Board

---

**There should be a formal, rigorous and transparent procedure for the appointment of new directors to the Board.**

The Nominations Committee should be made up of a majority of independent non-executive directors. LGIM expects the Chairman or an independent non-executive director to chair the Committee.

However, the Chairman should not chair the Committee when it is dealing with the appointment of a successor to the Chairman. The Nominations Committee's main responsibility is to appoint directors to the Board. In doing so, the Committee must be able to demonstrate that a rigorous process had been adopted and that any appointment made was based on merit.

The Nominations Committee should also be involved in making appointments to the next tier of directors as this is a valuable pool of talent for sourcing future Board directors. This would also help to ensure that they fulfil their task of ensuring proper succession plans are in place and maintaining an appropriate

balance of skills and experience within the company and the Board. The Chairman of the Nominations Committee should be answerable to the shareholders if it is felt that proper succession plans had not been in place and as a consequence the Board has had to operate without key directors or where an insufficient number of directors results in Board Committees being improperly constituted.

When appointing a non-executive director to the Board, the candidate should be made aware of the time commitments required and the Committee should satisfy itself that this person can meet these requirements.

## Performance Evaluation

---

**The Board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors.**

LGIM believes that companies should adopt a broad evaluation process that includes the formal appraisal of individual Board members. This should provide the Chairman with sufficient insight as to the level of skills and abilities of those members on the Board, and it should allow him to decide whether new members should be appointed to fill any skills shortage or whether it is necessary to remove any members from the Board. The non-executive directors led by the Senior Independent Director should be responsible for evaluating the performance of the Chairman.

## Re-election of Directors

---

All directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance. The Board should ensure planned and progressive refreshing of the Board.

The Combined Code requires all directors to be subject to election by shareholders at the first annual general meeting after their appointment and to re-election thereafter at intervals of no more than three years. LGIM believes that where there has been a material role change within the board, major shareholders should be consulted in a timely manner and all shareholders should be given the opportunity to sanction the change at the first general meeting of the company.

Non-executive directors should seek annual re-election if they remain on the Board for more than nine years. Under these circumstances we would expect to see a full explanation in the Annual Report as to why the Board believes it is appropriate for the non-executive director to remain on the Board.

## DIRECTORS REMUNERATION

### Remuneration Committee

---

LGIM expects every UK listed company to establish a Remuneration Committee that is responsible for setting and operating executive remuneration. The Remuneration Committee should comprise entirely of independent non-executive directors. FTSE 350 companies are expected to have a committee that is made up of at least three members. For smaller companies, two members are considered sufficient. The Board's

Chairman is permitted to be a member of the Committee if he was considered independent at the time of his appointment. However, he should not Chair the Committee. The Remuneration Committee should have the authority to appoint its own independent external remuneration advisors to assist them by providing external data and other information. Caution should be exercised when considering benchmark information.

When setting salaries, the Committee should where possible demonstrate consistency by using the same benchmark it uses to measure relative performance. The benchmark group should not be too large or too small as both extremes would produce results that are misleading.

*LGIM will vote against the remuneration report if the Remuneration Committee has no independent non-executive directors or if an executive director is a member.*

### Remuneration Policy

---

When setting remuneration, the Committee should be mindful of the main guiding principle set out in the Combined Code:

Levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose. A significant proportion of executive directors' remuneration should be structured so as to link the rewards to corporate and individual performance.

The Remuneration Committee should also be mindful of the guidelines issued by the Association of British Insurers. LGIM was





involved with the development of these guidelines and expects companies to comply with these guidelines when setting their remuneration policy.

LGIM expects a significant proportion of executive remuneration to comprise performance related pay which is closely aligned with the returns they generate for shareholders. Directors should be encouraged to hold a meaningful interest in the shares of the company they manage. The level of shareholding should be linked to the size of the company and the level of reward that directors receive.

When setting remuneration, the Committee should take into consideration not only the size of the company but also its performance relative to its peers. Directors at underperforming companies should not expect to be paid as highly as those directors working at companies with outstanding performance. The Committee should avoid the use of a wide comparator group that will cause a distortion in remuneration levels.

*LGIM may consider a vote against a remuneration report if there is a persistent disregard to performance when salary levels are set and reviewed.*

## **Basic Salary and Bonus**

---

LGIM expects companies to exercise caution when setting salary levels. The impact of significant pay increases should be carefully considered. If a significant increase is considered necessary due to a promotion, etc, we would expect any increase to be staged over a period of time. We would expect all increases to salary or bonus to be disclosed in the remuneration report. Significant increases should be accompanied by a full explanation.

LGIM has concerns with the rate of increase in board pay witnessed in the past, particularly with the short term bonus. In order to address these concerns LGIM is encouraging companies to select performance targets that are linked to the strategy of the business; and are both meaningful and measurable. We encourage companies to disclose the targets that were set for the bonus earned, to demonstrate to shareholders that targets were challenging.

## Share Schemes

---

In order to align a director's interests with those of a company's long term shareholders, it is vital that a company adopts long term incentives. These should be structured to motivate management to build a sustainable business which generates positive returns to shareholders over the longer term. When setting performance conditions, the Remuneration Committee must pay due regard to the size of potential reward. Upper quartile/decile reward structures should require similar levels of performance for awards to vest in full.

We expect long term remuneration to be linked to the financial performance of the business as well as to the relative performance against a defined peer group. Performance should be measured over a minimum period of three years and should not be re-tested. LGIM may not support a scheme that allows awards to be banked during the performance period. Under these circumstances, we would expect some form of claw-back mechanism should performance subsequently deteriorate.

The use of earnings per share or share price performance as the sole measure of performance should be avoided. However, the Remuneration Committee should satisfy itself that the TSR or another criteria used is a genuine reflection of the company's underlying financial performance and explain its reasoning.

The appropriateness of targets set should be considered at the beginning of each grant and shareholders should be consulted on any significant changes. LGIM does not support retrospective changes to performance conditions.

All schemes should have an individual cap on the potential reward to a participant and this should be disclosed to shareholders in the Remuneration Report.

**LGIM expects companies to be mindful of diluting shareholders' interests and therefore should limit any potential dilution to 10% of the issued share capital over any ten years for all schemes and to 5% in ten years for discretionary schemes.**

*LGIM will generally vote against a scheme or the remuneration report where dilution limits have been breached and there is no indication of how the company intends to rectify the situation.*

On a change of control, LGIM expects all share schemes to continue to require performance conditions to govern the level of vesting. Awards should also be pro-rated to reflect the shorter time that has elapsed. The awards of bad leavers should lapse and those of good leavers should be time pro-rated.

*LGIM will oppose any scheme that permits automatic vesting on a change of control.*

## Service Contracts

---

Contracts should provide for a maximum notice of one year. If the company requires a longer term for recruitment purposes we would expect the notice period to reduce each month until the normal 12 month duration is reached. LGIM does not support change of control provisions within service contracts that enhance contractual terms for loss of office following a change of control.

*LGIM will vote against any service contract that exceeds 12 months.*





## One-off Incentives

---

LGIM has noted a significant increase in the granting of one-off awards. Generally, LGIM would not support the use of one-off awards, because it highlights a weakness in the existing remuneration structure. However, we consider each case on its own merits.

Where schemes are designed to provide directors with a share of any value created for shareholders, LGIM expects any value shared to be in excess of a threshold level of performance. Directors would also be expected to make a personal investment in the shares of the company. This requirement would be in addition to any existing shareholding requirement.

## Remuneration Committee Discretion

---

Where a Committee has exercised its discretion, on more than one occasion, to increase the level of awards that would normally vest, LGIM would expect a full explanation to be provided.

*In the absence of a satisfactory explanation for the exercise of discretion LGIM may vote against the remuneration report.*

## Pensions

---

Pensions are a significant cost and risk for the company. They are also an element of remuneration that are not linked to performance. Therefore, the cost of providing a pension should be taken into account when setting the remuneration package.

LGIM expects pension provisions to be disclosed in full within the Annual Report & Accounts. Any changes to pension benefits should be fully identified and explained.

Companies should not compensate individuals for changes in tax.

The impact of any deficits should be carefully managed as they have become an important factor for consideration in mergers and acquisitions.

LGIM would not support pension enhancement payments at retirement or when a contract is terminated early.

## Chairman/Non-Executive Directors' Fees

---

LGIM expects non-executive directors and the Chairman to be issued with a letter of appointment. The letter should specify an initial term of service.

Directors should expect to receive a fixed fee for their services. We expect additional fees to be paid for those directors who chair any of the Committees and the Chairman of the Board and the Senior Independent Director. Fees may be paid in cash or shares but not in the form of options. Non-executive directors should not receive any other form of performance related pay that may compromise their independence. Directors should not expect compensation for the early termination of their contract.

## Termination Payments

---

The Remuneration Committee should ensure that contracts of employment do not leave any room for payment in the event of failure to perform. Furthermore, contracts should require directors to do all that is necessary to mitigate their loss. In the event that a director's contract is terminated, LGIM would expect any compensation payment to be limited to their contractual entitlements.

In instances of serious corporate failure, we would expect executive directors to sacrifice any bonus entitlement.

## Shareholding Guidelines

---

LGIM expects all FTSE All-Share Index companies to encourage share ownership among its directors and senior executives. We believe that this is an essential part of aligning the interests of executives with those of the company's shareholders.

LGIM expects shareholding guidelines to be linked to the total potential reward offered by a company. As a guideline, LGIM would expect FTSE 350 companies to have a shareholding requirement of at least 2 times base pay.

Directors and senior management of FTSE 100 Index companies who earn a higher level of pay and have a greater opportunity to build up shares in their company should expect to have a higher holding requirement. Research published by Manifest revealed that during the period 2003 to 2007 the total remuneration of FTSE 100 Index companies increased by 208%, while salaries increased by approximately 58%.

Smaller companies should expect to have a holding requirement of up to one times base pay.

## ACCOUNTABILITY AND AUDIT

When preparing financial reports, the Board should present a balanced and understandable assessment of the company's position and prospects. The directors should explain their responsibility for preparing the accounts and state whether they consider the business to be a going concern.

The Board should maintain a sound system of internal control to safeguard shareholders' investment and the company's assets. The effectiveness of the system of controls should be reviewed annually and should cover all material controls including financial, operational and compliance controls as well as risk management systems.

The Board should establish a formal and transparent arrangement for considering how they should apply these principles and for maintaining an appropriate relationship with the company's auditor.

## The Audit Committee

---

LGIM expects every UK listed company to establish an Audit Committee. The committee should comprise wholly of independent non-executive directors, one of whom should have recent relevant financial experience. We expect FTSE 350 Index companies to have three members, while two members is considered sufficient for a smaller company. The Board's Chairman should not be a member of the Committee but may attend the meetings by invitation.

The Audit Committee has the important task of monitoring the integrity of the financial information that flows out from the company, the effectiveness of the internal control processes as well as that of the internal audit function. It should be allowed the responsibility of setting the remuneration for the External Auditor and for making recommendations about their appointment or re-appointment to the Board. The Committee should develop the policy for appointing the External Auditor to carry out non-audit services. This should include the process by which non-audit work is reviewed and approved. Due to the

concerns of maintaining auditor independence, where possible, LGIM would prefer the Auditor was not used to provide significant non-audit services.

## Disclosure

---

LGIM would expect to find the role of the Audit Committee, the authority delegated to it and the work of the committee disclosed within the Annual Report. This should include a review of the whistle-blowing procedures and the independent investigation and follow up of any issues reported. If the company has chosen not to have an internal audit function the reasons for not having one should be explained within the Annual Report. LGIM would expect the Committee to review these reasons annually.

## Non Audit Fees

---

Where the company's External Auditor is used to provide non-audit work we would expect an explanation to be provided in the Annual Report as to how the Auditor independence and objectivity has been safeguarded. Where the fees for non-audit services are very high relative to the fees incurred for audit services we would expect a full explanation to be provided in the Annual Report.

Without a satisfactory explanation, *LGIM may consider voting against the Annual Report & Accounts and the re-election of the Auditor.*

## External Auditor

---

The External Auditor should independently report to shareholders and independently assure the Board on the discharge of its responsibilities.

## SHAREHOLDER RIGHTS AND OTHER VOTING POLICIES

### Dialogue with Shareholders

---

LGIM expects Directors of a company to be available to enter into dialogue based on the mutual understanding of objectives.

LGIM has regular contact with companies on matters including strategy, succession, and remuneration. During the course of the year, our equity team will have regular contact with the Chief Executive and Finance Director of companies. In addition, the Corporate Governance Team will meet with the Chairman, Senior Independent Director, and at times the Chairman of all the Board Committees. We also have meetings with key directors responsible for social, environmental and ethical issues within companies.

### Pre-emption

---

Pre-emption is the right conveyed by law to shareholders to be offered any new issue of shares, pro-rata to their existing holdings, before these shares are offered to non-shareholders.

LGIM believes that pre-emption is a fundamental right for shareholders to protect their investment in a company. Its importance is such that it is incorporated in the Companies Act 2006 and the UK Listing Rules.

A general authority to issue shares with pre-emption rights, under section 80 of the Companies Act 1985, should be limited to one third of their issued share capital. A company whose capital requirements are greater will need to seek a fresh authority from shareholders. In these circumstances shareholders would expect a full explanation.



Any company looking to obtain an authority to issue shares without pre-emption rights under section 95 of the Companies Act 1985 is required to use a special resolution. An authority to disapply pre-emption rights should be limited to 5% of their issued share capital or 7.5% over a three year period. These limits were set by The Pre-emption Group and are considered market practice.

An investment trust may request an authority to issue up to 10% of the issued share capital so long as any issue is at a premium to their net asset value. The re-issue of treasury shares should be at a premium to net asset value.

Any requests that exceed these guideline limits will be considered by assessing the business case for the issue, the size and stage of development, the sector in which it operates, the governance of the company and other financing options open to the company.

*LGIM would be minded to oppose any resolution that will potentially have a large dilutive effect on shareholder interests.*

### **Share Buy Backs/Dividends**

---

LGIM will support a share buy back policy that delivers shareholder value.

LGIM expects a company to have a clear policy to grow its dividends and to return surplus cash to shareholders in the most efficient way.

### **Mergers & Acquisitions**

---

LGIM will normally support any plan that will create shareholder value. In a contested takeover, LGIM will aim to meet with both parties at least once before making a decision. In a majority of cases we will

support management but support may not be given in circumstances of poor performance or a very full price is offered. Anti-takeover provisions (poison pills) should be avoided.

### **Shareholder Requisitioned Resolutions**

---

LGIM will generally support management unless the resolution addresses concerns that LGIM considers material and discussions have failed to resolve the issue

### **Political Donations**

---

LGIM will only support resolutions that authorise payments under the Political Parties, Elections and Referendums Act, if the company has clearly stated that donations will not be made to political parties. The maximum amount should be appropriate for the size of the company.

### **Bundled Resolutions**

---

LGIM expects unrelated matters to be tabled as separate resolutions to allow shareholders to consider each on its own merits.

### **Rule 9 Waiver**

---

Rule 9 of the Takeover Code requires any person(s) who acquires an interest in shares, which when taken together with their existing shareholding and collectively with that of any concert party is in aggregate over 30% of the issued share capital but less than 50%, to make a general offer to the remaining shareholders to acquire their shares for cash at a price that is equivalent to the highest price paid during the previous twelve months prior to making the offer.

Share buy backs can trigger Rule 9 where there is a dominant share holder on the company's share register. LGIM strongly

objects to share buy backs being utilised to allow management with a significant interest in the company’s shares to increase their holding in this way without having to pay a premium to remaining shareholders.

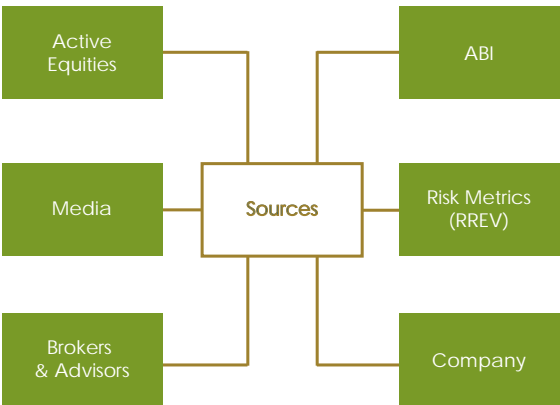
*We will therefore generally oppose any requests for a Rule 9 waiver where the interested party has a holding in excess of 35% of the issued share capital.*

**Borrowing Powers**

Boards should consider carefully the level of debt necessary to operate the business and maintain an efficient balance sheet.

LGIM believes that in doing so, management should not ignore the importance of maintaining a healthy level of interest cover that is relevant for the business.

**CORPORATE GOVERNANCE ENGAGEMENT**



LGIM’s engagement stems from a number of sources. Both the ABI and RREV produce reports on forthcoming meetings highlighting any areas of concern. If LGIM believes these concerns are material, we will either contact the company in writing for an explanation or we will request a meeting with a member of the Board.

Weekly meetings with the Active Equities Team are used to identify companies with poor performance, corporate governance concerns, as well as sectors where issues may arise in the future. This is then used as a basis for further analysis and engagement.

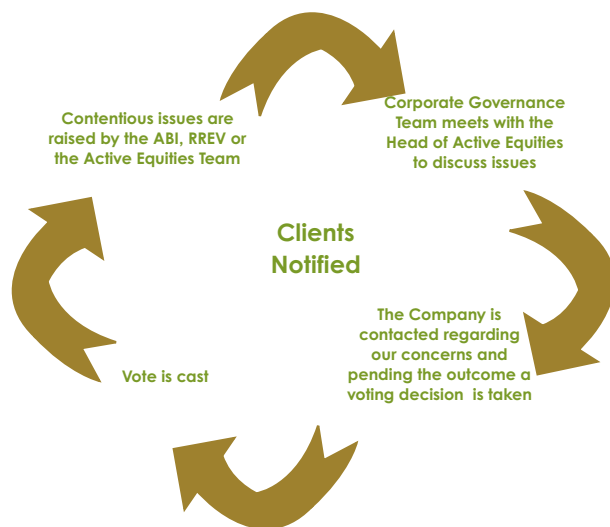
As one of the largest investors in the FTSE All-Share Index, we expect companies to contact us on corporate governance matters including Board changes, changes to remuneration and strategy. In accordance with the “comply and explain” regime we expect a company to consult with us on any proposed departures from the recommendations of the Combined Code and best practice. We also welcome early discussions with companies that are looking to raise additional capital or who are considering other corporate actions.

Brokers and advisors contact us to find out our views on a possible corporate transaction or a resolution that has been tabled at a forthcoming general meeting for shareholders. LGIM expects any consultation to be a two-way process.

The media is a useful source of information and can have a major impact on the reputation of a company. LGIM makes extensive use of the financial media such as Regulatory News Service for its research.

During 2007, LGIM’s corporate governance team engaged with 102 companies. Of these, 52 were with the Chairman and 15 were with the Senior Independent Director. In addition, we held meetings with 28 companies to discuss social, environmental and ethical issues affecting their business.

## VOTING PROCESS



LGIM provides its clients with a valuable service in exercising their voting rights. A majority of clients have allowed LGIM to exercise its judgement when voting their shares. Others have given express instructions to follow the voting advice of specific voting information providers.

LGIM takes its duty to vote seriously. A weekly meeting is held with the Head of Active Equities to decide how to vote. Any highly contentious issues will be discussed with the Chief Executive Officer of LGIM before votes are submitted. Where LGIM intends to abstain or oppose a resolution, the company will be notified in advance to allow further discussion.

### Voting Disclosure

LGIM's clients receive quarterly reports that contain details of voting and engagement activity.

In 2008, LGIM began to publicly disclose the voting decisions for the funds it manages on behalf of Legal & General Assurance Society. These can be found on the Corporate Governance section of the Legal & General Investment Management website.

## SOCIALLY RESPONSIBLE INVESTING

LGIM believes that directors who are committed to running their company in the long-term interests of shareholders should manage the relationship with their employees, customers and suppliers. They should also consider what impact their business has on the environment and society as a whole and endeavour to reduce any negative impacts.

High standards of business conduct as well as a responsible approach to social, environmental and ethical issues makes good business sense and can enhance shareholder value. Conversely, poor management of these issues presents a risk to the reputation and value of the business.

As a Group, Legal & General recognises its own duty to behave responsibly in conducting its business activities and towards those whom its actions affect. LGIM's socially responsible investment team aims to influence the companies in which it invests to do the same.

### Socially Responsible Investment Policy

LGIM launched its first ethical trust in 1999. We also helped the Association of British Insurers to draw up their guidelines which was published in 2001. In 2007, these guidelines were revised to take account of the EU Accounts Modernisation Directive and the Companies Act 2006 as well as building on experience of reporting evidenced over the previous five years.

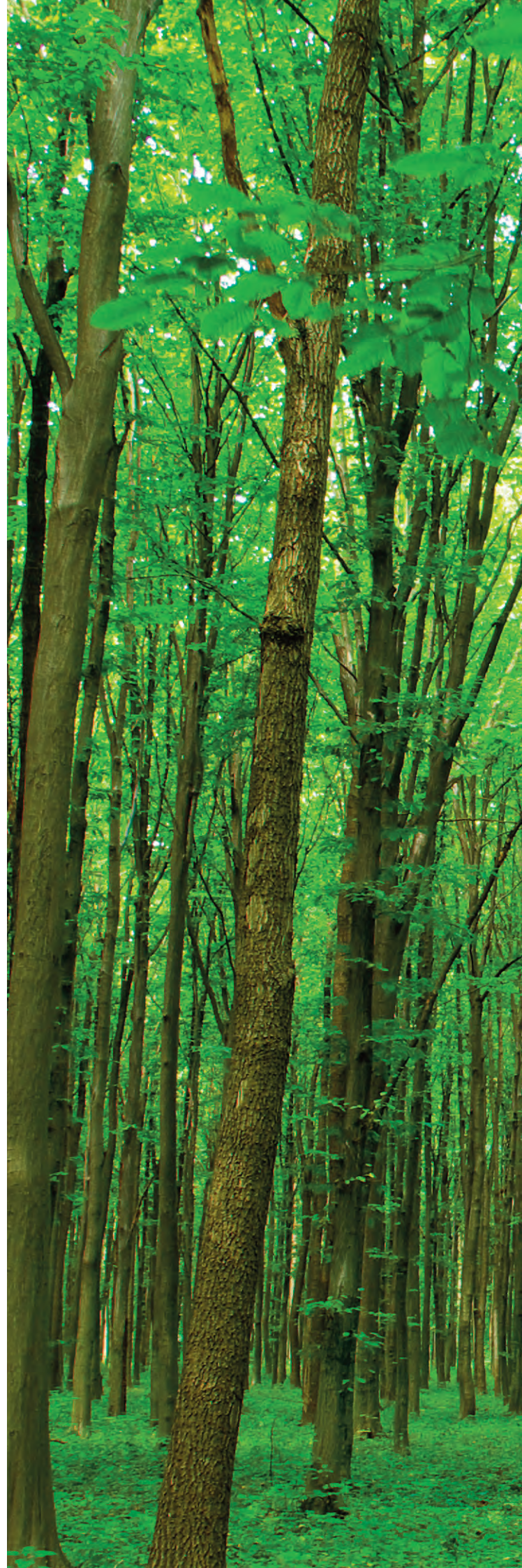
These guidelines require companies to provide disclosures within the Annual Report as follows:



- As part of its regular risk assessment procedures, the Board takes account of the significance of environmental, social and governance (ESG) matters to the business of the company
- The Board has identified and assessed the significant ESG risks to the company's short and long-term value, as well as the opportunities to enhance value that may arise from an appropriate response
- The Board has received adequate information to make this assessment and that account is taken of ESG matters in the training of directors
- The Board has ensured that the company has in place effective systems for managing and mitigating significant risks, which, where relevant, incorporate performance management systems and appropriate remuneration incentives

With regard to policies, procedures and verification, the Annual Report should:

- Include information on ESG-related risks and opportunities that may significantly affect the company's short and long-term value, and how they might impact on the future of the business
- Include in the description of the company's policies and procedures for managing risks, the possible impact on short and long term value arising from ESG matters. If the Annual Report and Accounts states that the company has no such policies and procedures, the Board should provide reasons for their absence
- Include information, where appropriate using Key Performance Indicators (KPIs), about the extent to which the company has complied with its policies and procedures for managing material risks arising from ESG matters and about the role of the Board in providing oversight



- Where performance falls short of the objectives, describe the measures the Board has taken to put it back on track
- Describe the procedures for verification of ESG disclosures. The verification procedure should be such as to achieve a reasonable level of credibility

With regard to the Board, the company should state in its remuneration report:

- Whether the remuneration committee is able to consider corporate performance on ESG issues when setting remuneration of executive directors. If the report states that the committee has no such discretion, then a reason should be provided for its absence
- Whether the remuneration committee has ensured that the incentive structure for senior management does not raise ESG risks by inadvertently motivating irresponsible behaviour

LGIM expects the companies in which it invests to demonstrate awareness of the impact of social, environmental and ethical risks to their business.

We believe companies should establish, and be able to provide evidence of, appropriate risk management systems for identifying, managing and mitigating any risks or creating value from any opportunities. Policies and procedures and key performance indicators (KPIs) should be set for managing risks and opportunities, and these should be disclosed to investors. LGIM recognises that companies face different challenges according to the nature of their business and their particular circumstances, and we take this into account in our evaluations.

Companies should accept responsibility for the environmental impacts of their activities and endeavour to set their policies and procedures to reduce these risks where viable. They should do all that is necessary to comply with all environmental laws and regulations.

Climate Change – the operations of all companies, to varying degrees, have an impact on the environment and climate change. LGIM expects companies to do what they can to reduce their impact on climate change and this should be reported to shareholders.

Environmental impact assessments should be carried out when considering acquisitions. This should include biodiversity impact assessments.

Human Rights - LGIM expects companies to respect internationally recognised labour rights and provide a safe working environment for their employees and contractors. They should ensure that their operations do not violate internationally recognised human rights standards. Policies and guidelines on human rights and business ethics should be developed and disseminated within the organisation.

## Engagement

---

As part of our engagement process, we review company Corporate Social Responsibility (CSR) reports as well as their web content. We also have access to independent research provided by Ethical Investment Research Services (EIRIS).



In company meetings we pay particular attention to those issues which are most relevant to the company or the sector in which it operates. We monitor the statements made by management and question them if there is anything of concern.

In addition, where events come to light that indicate an apparent breach in the fiduciary duties of management or a failing within risk controls, LGIM will request a meeting with the company to discuss our concerns.

LGIM participates in a number of collaborative investor initiatives aimed at promoting best practice in the handling of social, environmental and ethical matters. We are a signatory to the Carbon Disclosure Project, the ABI's ClimateWise programme and the Investors' Statement on Transparency in the Extractives sector.

## Ethical Investment

---

LGIM provides:

- The Legal & General Ethical Trust, which aims to match holdings in the bespoke Ethical Investment Research Service filtered FTSE 350 Index (excluding investment trusts)
- The Ethical UK Equity Index Fund that aims to track the sterling total return of the FTSE4Good UK Equity Index (including re-invested income) to within +/-0.5% pa for two years in three
- The Ethical Global Equity Index Fund that aims to track the total return of the FTSE4Good Global Equity Index to within +/-0.5% pa for two years in three





The FTSE100 and FTSE350 are calculated by FTSE International Limited ("FTSE"). FTSE does not sponsor, endorse or promote this product.

Legal & General Investment Management Limited is authorised and regulated by the Financial Services Ltd. "FTSE™", "FT-SE®" and "Footsie®" are trade marks of the London Stock Exchange Plc and The Financial Times Limited and are used by FTSE International Limited ("FTSE") under licence. "All-Share" is a trade mark(s) of FTSE.

Legal & General Investment Management  
One Coleman Street  
London EC2R 5AA

Telephone +44 (0)20 3124 2000  
Facsimile +44 (0)20 3124 2526

[www.lgim.com](http://www.lgim.com)

January 2009