



# Responsible Investment Corporate Governance and SRI – Q2 2006

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## Voting profile for Q2 2006

The second quarter is the busiest period of the year for company General Meetings. Annually, Newton votes at some 1,600 General Meetings. About half of these occur in the second quarter. The quarter includes the meetings of UK companies with calendar financial years, as well as the majority of Japanese companies that, traditionally, hold their AGMs in the last week of June.

Historically, in order to exercise voting rights at meetings of German companies, shareholders would have been blocked from trading their shares. The blocking period was from the

time of the exercising of voting rights until the meeting had closed. Given this restriction, only in exceptional circumstances did Newton exercise its clients' voting rights at German meetings. However, Germany adopted the European Commission's directive on the easing of cross border voting. Shareholders of German companies are now able to exercise their voting rights without being restricted from trading. Newton now votes actively on all German company meetings.

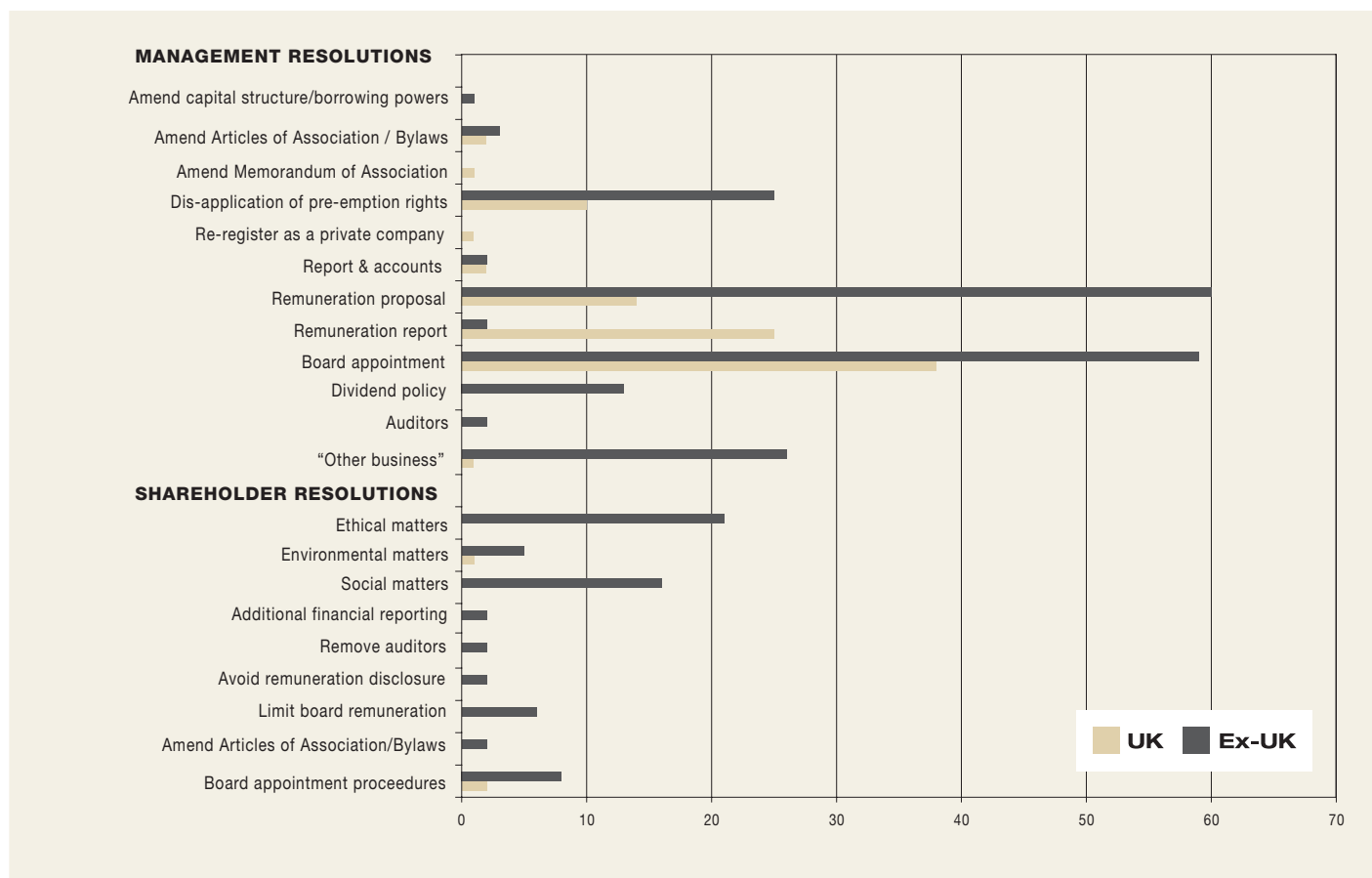
The table below summarises the exercise of voting rights during the second quarter of 2006.

<b>Complete voting summary – Q2 2006</b>	<b>Total</b>	<b>UK</b>	<b>Ex-UK</b>
<b>AGMs</b>			
Voted in favour of all resolutions	486	244	242
Voted against one or more resolutions	174	43	131
Took no action	80	0	80
Abstained	1	0	1
	<b>741</b>	<b>287</b>	<b>454</b>
<b>EGMs</b>			
Voted in favour of all resolutions	91	60	31
Voted against one or more resolutions	2	1	1
Took no action	8	0	8
Abstained	1	1	0
	<b>102</b>	<b>62</b>	<b>40</b>
<b>Court Meetings</b>			
Voted in favour of all resolutions	5	4	1
Voted against one or more resolutions	0	0	0
Took no action	0	0	0
Abstained	0	0	0
	<b>5</b>	<b>4</b>	<b>1</b>
<b>Totals</b>	<b>848</b>	<b>353</b>	<b>495</b>
<b>Voted in favour</b>	<b>582</b>	<b>308</b>	<b>274</b>
<b>Voted against</b>	<b>176</b>	<b>44</b>	<b>132</b>
<b>Took no action</b>	<b>88</b>	<b>0</b>	<b>88</b>
<b>Abstained</b>	<b>2</b>	<b>1</b>	<b>1</b>
<b>Totals</b>	<b>848</b>	<b>353</b>	<b>495</b>

## Breakdown of resolutions voted against during Q2 2006

In a number of instances, shareholder approval was sought for identical and, seemingly, routine resolutions. Many were consistent with the letter of the law but the spirit of good corporate governance was ignored. Examples of some of these

routine resolutions included seeking shareholder approval for “other business”, the dis-application of shareholders’ pre-emption rights over an acceptable level and the granting of retirement bonuses to independent non-executive directors.



## UK Companies

### Aegis PLC – AGM – 14/06/2006

Groupe Bollere, the company’s largest shareholder controlling 29% of the issued share capital, proposed two resolutions seeking the election of two of its nominees to the company’s board. The proposed board members would be representatives of Groupe Bollere. It should be noted that Groupe Bollere is also a material holder of Havas, a direct competitor of Aegis. Also, Havas and Groupe Bollere share the same Chairman. Therefore, it could be argued that Groupe Bollere was seeking to potentially disadvantage current shareholders of Aegis and to control the company without paying an appropriate takeover premium to shareholders of Aegis. Newton supported the management of Aegis by way of voting against the two shareholder-proposed resolutions.

### Alizyme PLC – AGM – 27/06/2006

The company’s remuneration arrangements allow for share option awards to be exercised after three years if the company’s share price growth exceeds that of the FTSE All Share. However, should this not be achieved, re-testing of the performance condition is permitted over the remaining life of the share option awards. Given the ability to re-test and the limited performance condition, Newton instructed votes against the company’s remuneration report.

### Amvescap PLC – AGM – 27/04/2006

Newton was concerned with the robustness of the company’s remuneration policy. It was felt that the award of a US\$9m bonus to the chairman, who was also CEO until August 2005, was excessive. Newton considered that the explanation

proffered by the company did not justify the award. It was stated, by the company, that the bonus was granted following a difficult period when the chairman had to fend off a hostile bid and recruit a Chief Executive. Newton also considered that the company's earnings growth targets, governing the vesting of share-based awards, was not challenging. Votes were instructed against the resolution seeking shareholders' approval of the remuneration report.

#### **Arm Holdings PLC – AGM – 25/04/2006**

The company proposed a new Deferred Annual Bonus (DAB) plan. Newton was concerned that the earnings growth targets, governing the matching of deferred shares, was not sufficiently stretching. However, the proposed DAB was felt to be more appropriate than the company's previous arrangement, which simply provided a doubling of any deferred shares irrespective of performance achieved. Subject to shareholders approving the proposed new DAB, the company would not make any further awards under its Share Option Scheme. Newton had concerns with the Share Option Scheme due to awards automatically vesting after seven years, irrespective of performance. Despite being a vast improvement on the existing incentive arrangements, Newton instructed votes against the new DAB and the remuneration report. A member of the remuneration committee, who was seeking re-election to the board, was also voted against.

#### **BPP Holdings PLC – AGM – 20/04/2006**

Newton instructed votes against a resolution that sought approval of "Other Business". The unknown content of this resolution meant that Newton had to exercise a level of prudence by voting against its approval. It should not be expected that shareholders will blindly approve such resolutions.

#### **Brixton PLC – AGM – 10/05/2006**

The company proposed a new Share Matching Plan, which would provide a 2:1 match should the three pre-determined performance conditions be achieved. The proposed performance conditions were absolute Total Shareholder Return (TSR), relative TSR and relative performance to a property index. Newton was not comfortable with the proposed use of absolute TSR as a performance condition and felt that the relative TSR measure should be underpinned by a financial metric. Whilst Newton was comfortable with the use of relative performance to the Total Property Return index as a performance measure, the actual targets were not considered to be challenging. These performance conditions were also proposed for a new Long-Term Incentive Plan. Newton remained unconvinced that the proposed performance conditions would generate returns to shareholders commensurate with the executives' likely rewards. Votes were instructed against the two proposed remuneration plans, the remuneration report and two members of the remuneration committee, who were seeking re-election to the board.

#### **Burren Energy PLC – AGM – 24/05/2006**

The company's bonus arrangement provides for a percentage of the company's profit to be distributed. However, there is no minimum profit level that needs to be achieved in order for bonuses to be awarded. Additionally, the Long-Term Incentive Plan can allow individuals to be rewarded for the sale of a business or for returning cash to shareholders, which is not necessarily consistent with improving the company's long-term performance. Finally, all members of the remuneration committee have varying levels of affiliation with the company and are, therefore, not deemed to be independent. Votes were instructed against the remuneration report and two members of the remuneration committee, who were seeking re-election to the board.

#### **Carnival PLC – AGM – 20/04/2006**

The company's remuneration practices were not considered to be in line with the creation of shareholder value. Significant awards of restricted shares, up to seven times an individual's base salary, vest after five years, irrespective of the company's performance. Additionally, all US-based non-executive directors enjoy routine awards of share options. Generally, where companies are not suffering from cash flow or profitability issues, Newton believes that the independence of non-executive directors should not be compromised by being in receipt of share options. Newton voted against the re-election of five non-executive directors. These were all members of the audit and the remuneration committees and were in receipt of share option awards. The above reasons also led to votes being instructed against the resolution seeking shareholder approval of the company's remuneration report.

#### **Corporate Services Group PLC – AGM – 09/06/2006**

Many elements of the company's Long-Term Incentive Plan (LTIP) were considered to be of sufficient concern to warrant instructing votes against the company's remuneration report. The company failed to disclose the performance conditions that would govern the vesting of awards made under its LTIP. If the undisclosed performance conditions are not achieved, re-testing is permitted. The awards are subject to three one-year performance periods rather than one three-year performance period. Furthermore, special accelerated vesting occurs if the company goes through a change in control.

#### **Evolution Group PLC – AGM – 25/05/2006**

The proposed Performance Share Plan was not felt to be in shareholders' best interests, given that the performance condition was only based on absolute share price growth. Also, investors' value could be diluted by up to 23%. The proposed annual awards would vest if the shares reached certain pre-determined prices over any 60 day period within the three-year performance period. This, effectively, is a scheme providing for re-testing and one that could either incentivise or disincentivise recipients for market momentum rather than for the actual performance of the company. Votes were instructed against the proposed plan and, also, against a member of the remuneration committee, who was seeking re-election to the board.

#### **Guinness Peat Group PLC – AGM – 13/06/2006**

The board failed to appoint any independent non-executive directors to its audit and remuneration committees. Instead, these key committees consisted of the non-independent chairman and an executive director. The company is listed on the Alternative Investment Market, where companies are not subject to the same demands as companies with a full UK listing. However, given the company's size, Newton felt that shareholders should be afforded the comfort of independent non-executive directors representing their interests. Therefore, votes were instructed against the resolutions seeking shareholder approval of the remuneration report and the company's financial statements & statutory reports.

#### **Graphite Enterprise Trust PLC – AGM – 25/05/2006**

Newton did not support the re-election of a non-executive director due to the fact that he was the chairman of an unquoted company, which was held in the company's portfolio.

A further resolution, seeking to issue the company's treasury shares, was also voted against. In receiving approval of the resolution, the company would be able to issue shares at a discount to their market value, whilst dis-applying the pre-emption rights of existing shareholders.

#### **Hanson PLC – AGM – 26/04/2006**

Newton voted against the resolution to receive and adopt the company's report and accounts. This decision was based on the company's poor disclosure of Social, Environmental and Ethical matters. For the full voting rationale, please refer to the SRI Activity log on page 37 of this report.

#### **Highway Insurance Holdings PLC – AGM – 10/05/2006**

At the company's EGM in December 2005, Newton voted against the proposed new Performance Share Plan (PSP). The company failed to satisfy investors concerns and implemented the plan as it intended. Therefore, at the AGM, votes were instructed against the resolution seeking shareholder approval of the company's remuneration report. Below is the rationale for why Newton voted against the PSP at the earlier meeting:

"...Newton felt that the allocation of high up-front awards for the first two years of the plan was inappropriate. The use of absolute growth in returns to shareholders, as a performance condition, could allow for awards to vest for underperformance. Additionally, the remuneration committee exercised its discretion by changing the performance targets that would mean all historic share option awards would automatically vest. Finally, it was proposed that a transitional bonus be awarded to compensate for the lack of a long-term incentive arrangement being in place for 2005. The level of this transitional bonus was 50% greater than prior arrangements."

#### **Inchcape PLC – AGM – 11/05/2006**

The award of guaranteed bonuses to an executive director of the company led to votes being instructed against the resolution seeking shareholder approval of the company's remuneration report.

#### **LogicaCMG PLC – AGM – 17/05/2006**

The company's proposed new share based incentive awards were felt to be inappropriate. First, the proposals would significantly enhance the value of recipients' awards, while no explanation was provided as to why this was necessary. Secondly, the performance condition that would govern vesting under the three proposed plans was not considered to sufficiently stretching to warrant the size of the awards. The remuneration report, the three proposed remuneration plans and two members of the remuneration committee, who were seeking re-election to the board, were voted against.

#### **Millennium & Copthorne Hotels PLC – AGM – 04/05/2006**

The chairman of the company received a transaction-based cash reward of 26 times his annual fee. Generally, Newton does not approve of transaction-based rewards, especially for a company's chairman. In this case, the chairman owns the company that controls 53.8% of Millennium & Copthorne. Votes were instructed against the remuneration report. Additionally, three members of the remuneration committee, who were seeking re-election to the board, were also voted against.

#### **Morgan Sindall PLC – AGM – 25/04/2006**

The remuneration committee decided to make an ex-gratia payment to the company's CEO in recognition of "record results and outstanding performance". Newton considered that this payment was unnecessary, given that the CEO would be sufficiently rewarded by way of his participation in the company's long-term incentive arrangements. Given the lack of rationale or consultation with shareholders, the resolution seeking shareholder approval of the remuneration report was voted against.

#### **Morrison (WM) Supermarkets PLC – AGM – 25/05/2006**

During the year, the company's CEO received a salary increase of 33%. This significantly enhanced his termination arrangement, which in itself, did not accord with best practice. In June 2005, a decision was made to increase the CEO's notice period from 12 months to 24 months. This is a significant breach of the Combined Code on corporate governance. It was also noted that, following the recruitment of a replacement and subsequent handover period, the CEO would receive twice his salary, profit share and certain other benefits. Following the cessation of his employment, the CEO agreed to work on a consultancy basis for 12 months at an agreed market rate. Newton felt that the termination package awarded to the CEO was not an appropriate use of shareholders' funds. Votes were instructed against the resolution seeking shareholder approval of the remuneration report.

#### **Nestor Healthcare Group PLC – AGM – 27/04/2006**

The recommendation of the Combined Code on corporate governance and Smith's guidance on the composition of a company's audit committee clearly excludes the board's chairman from membership. The company has failed to review this situation. Therefore, votes were instructed against his re-election to the board.

#### **NEXT PLC – AGM – 17/05/2006**

The company proposed two new share-based incentive arrangements, a Performance Share Plan and a Risk/Reward Investment Plan.

The Performance Share Plan (PSP) would provide awards to participants at a level twice that of the previous PSP, whilst retaining the same performance conditions. This did not seem to accord with best practice in this area, which suggests that performance conditions should be commensurately stretched with the increased level of award.

The Risk/Reward Investment Plan was first put to a shareholder vote last year. Newton remains concerned with the plan for the same reasons given in July 2005 – “The company’s executives could be rewarded with up to 16 times their own investment in shares for absolute share price appreciation. For such substantial levels of share matching, Newton would expect performance conditions that incentivise management to improve the underlying financial performance of the company. The Risk / Reward Investment Plan, as structured, would reward or penalise participants solely on share price movement, which may be merely a function of market momentum.”

Given the above, and the fact that bonuses remain pensionable, Newton voted against the resolutions seeking shareholder approval of the remuneration report, the two proposed share-based incentive plans and, also, against two members of the remuneration committee, who were seeking re-election to the board.

#### **Northern Rock PLC – AGM – 25/04/2006**

The company operates a deferred share scheme whereby shares can be awarded, to the value of short-term cash bonuses, and released after three years should real average annual growth in earnings exceed 3%. Newton did not consider this performance condition to be sufficiently stretching to warrant the vesting of nil-cost share awards. Newton voted against the remuneration report and two members of the remuneration committee, who were seeking re-election to the board.

#### **Partygaming PLC – AGM – 04/05/2006**

Newton instructed votes against the resolution seeking shareholder approval of the company’s remuneration report. Two members of the remuneration committee, who were seeking re-election to the board, were also voted against. These two non-executive directors were also seeking to be re-elected to the board’s audit committee. Newton considered that their independence was compromised by the fees they had received in relation to the company’s Initial Public Offering, last year. The company’s Share Option Plan also caused concern. Awards vest on a quarterly basis, from the date of grant, irrespective of performance.

#### **Persimmon PLC – AGM – 20/04/2006**

At the company’s EGM, in January this year, Newton voted against the proposed Synergy Incentive Plan. The incentive plan was a transaction-based plan that would reward management for achieving synergy cost savings resulting from a proposed acquisition. Should certain cost savings be realised, the plan would provide for awards to individuals of up to 10 times their base salary. The awards could equate to c.20% of any synergy cost savings achieved. Newton considered this to be excessive and felt that the scheme could encourage radical cost savings that may be to the detriment of the company’s long-term performance. Newton, voted against the company’s remuneration report and two members of the remuneration committee, who were seeking re-election to the board.

#### **Psion PLC – AGM – 19/05/2006**

Votes were instructed against the resolution seeking shareholder approval of the company’s remuneration report. Despite the company’s intention not to make any further awards under its Share Option Scheme, Newton was sufficiently concerned with its structure, and with the proposed replacement Plan, to warrant voting against the remuneration report. The existing scheme allows for significant vesting for simply achieving mediocre performance and, should the performance condition not be achieved after the initial three-year vesting period, performance conditions may be re-tested.

It was proposed that the above scheme be replaced with a new Portfolio Long-Term Share Plan. Newton did not consider that the earnings targets, governing vesting of awards, were challenging. Newton was also uncomfortable with the level of discretion that would be afforded to the remuneration committee. If the committee consider it to be appropriate, performance conditions may be removed. This is tantamount to retaining the re-testing provisions that caused shareholder concern with the Share Option Scheme. Finally, the company proposed that shares awarded under other previous schemes would not be included in new dilution calculations. This is a fundamental breach of best practice.

In addition to voting against the remuneration report and proposed Plan, Newton voted against a member of the remuneration committee, who was seeking re-election to the board.

#### **Rank Group PLC – AGM – 26/04/2006**

Support was not given to the resolution that sought shareholder approval for the company to amend its Articles of Association. In accordance with changes to the UK Companies Act, that came into effect in April 2005, the amendment would allow the company to indemnify its directors. However, the proposed amendment would also allow the company to indemnify its auditors. Newton does not consider the indemnification of auditors to be in shareholders’ best interests.

#### **Reckitt Benckiser PLC – AGM – 04/05/2006**

Newton considers that the remuneration arrangements at the company are excessive in light of the relatively undemanding performance conditions that govern the vesting of very substantial Long-Term Incentive awards. Votes were instructed against the remuneration report. The company also proposed a new long-term incentive arrangement. However, given that this was broadly similar to the existing arrangements, Newton also voted against the proposed plan.

#### **Rentokil Initial PLC – AGM – 18/05/2006**

Newton had various concerns over the company's remuneration arrangements.

In the recruitment of a new CEO, last year, the company made a one-off award of cash and shares to compensate for awards foregone from the previous employer. However, awards provided at the previous employer had vested on his departure.

The company proposed, and sought shareholder approval, to replace its existing Share Option Scheme with a new Performance Share Plan (PSP). Newton felt that the earnings growth performance condition, governing the vesting of the proposed PSP awards, was not sufficiently challenging. Newton was also concerned that the Total Shareholder Return performance condition was not underpinned by a financial metric.

Votes were instructed against the remuneration proposal, the remuneration report and two members of the remuneration committee, who sought re-election to the board.

#### **Royal Dutch Shell PLC – AGM – 16/05/2006**

A shareholder-proposed resolution was voted against. The resolution related to concerns at the company's loss of production, its environmental costs and its reputational risks. For the full rationale behind Newton's voting decision on this resolution, please refer to the SRI Activity log on page 37 of this report.

#### **Seaperfect PLC – EGM – 14/06/2006**

Newton does not usually register abstentions on resolutions. In the case of Seaperfect's resolutions, neither support nor rejection of the resolutions appeared to offer a satisfactory outcome for shareholders. These resolutions sought to re-register the company as a private company and to reflect this in the company's Memorandum of Association and in its Articles of Association. Given that the company has not been quoted on a recognised exchange for over 10 years, Newton felt that becoming a private company could alleviate some of the costly regulatory burdens. However, this would mean Newton's clients having a shareholding in an even more illiquid company. The company stated its reason for seeking to become a private company as enabling it to return funds to shareholders. However, if the company failed to return funds to shareholders, Newton's clients would be left with a non-tradeable shareholding, whilst having less protection than before.

#### **Shire PLC – AGM – 21/06/2006**

Votes were instructed against the resolution seeking approval of the remuneration report. The company's Share Option Scheme continues to provide for performance conditions to be re-tested should they not be achieved at the end of the initial performance period. The company provided little justification for this deviation from well-established best practice. Additionally, the company increased executive directors' maximum bonus potential by c. 55% without providing any evidence that increased awards would be subject to the achievement of more demanding performance conditions. Newton also instructed votes against three members of the remuneration committee, who were seeking re-election to the board.

#### **Spectris PLC – AGM – 17/05/2006**

Individual awards were made under the company's Share Option Plan at a rate of between 2.3 times and 2.7 times an individual's base salary. This is in conflict with the company's remuneration report, which states that "...grants may be made up to an annual maximum exercise value of two times base salary..."

Given the company's deviation from its publicly stated policy, together with an award of a guaranteed bonus to the newly appointed CEO, Newton instructed votes against the company's remuneration report.

#### **Venture Production PLC – AGM – 07/06/2006**

A total of four resolutions were voted against. These included the re-election to the board of two members of the company's remuneration committee, the remuneration report and a separate resolution seeking shareholder approval of a new Long-Term Incentive Plan (LTIP).

In relation to the proposed new LTIP, Newton considered that vesting of awards for achieving threshold performance was too high at 150% of individuals' base salaries. Additionally, Newton was not convinced that providing individuals with free unconditional shares was the best use of shareholders' funds.

#### **Xstrata PLC – AGM – 09/05/2006**

Whilst the remuneration committee had made some positive changes to the company's remuneration structure over the year, Newton still felt unable to support the company's remuneration report. Vesting of awards made under the Long-Term Incentive Plan would be subject to the achievement of certain levels of cost savings. This was not considered to be an appropriate performance condition, given the danger of cost reductions being undertaken for short-term personal benefit without consideration of the longer-term interests of the company. Newton voted against the resolution that sought shareholder approval of the remuneration report.

### Yule Catto & Co PLC – AGM – 18/05/2006

The company failed to alter the representation of the board in favour of its shareholders by appointing independent non-executive directors. Newton considers it to be highly important that a board of such a company should be shaped in a way that can protect and enhance shareholder value. Therefore, Newton voted against three non-independent non-executive directors who were seeking re-election to the board.

Newton also instructed votes against the proposed new Performance Share Plan (PSP) and a member of the remuneration committee, who was seeking re-election to the board. Part of any awards made under the proposed PSP would vest for achieving absolute levels of Total Shareholder Return, without the need for improving the underlying financial performance of the company. Also, half of any awards made would vest in the event of a change in control, irrespective of achieving the pre-determined performance conditions.

## Dis-application of Pre-emption Rights at UK Companies

During the past quarter, there has been progress in relation to protecting shareholders' pre-emption rights in the event of a company issuing new shares. On the 15th May 2006, the Pre-emption Rights Group produced guidance for companies and investors in relation to this matter. The guidance supports Newton's view that acceptable justification must be given to shareholders should a company seek to issue more than 5% of its issued share capital, without first offering the shares to existing shareholders. Without this level of protection, existing shareholders could face unacceptable levels of dilution to their holdings.

At the meetings listed below, Newton voted against the resolution seeking shareholders' authority to dis-apply pre-emption rights.

Company	Meeting type	Date	Level of dis-application sought
Baillie Gifford Shin Nippon PLC	AGM	27/04/2006	10%
Barr (A.G.) PLC	AGM	22/05/2006	10%
Bioprogress PLC	AGM	20/06/2006	10%
Finsbury Technology Trust PLC	AGM	06/04/2006	10%
M.P.Evans Group PLC	AGM	13/06/2006	10%
Peter Hambro Mining PLC	AGM	22/06/2006	20%
Sterling Energy PLC	AGM	15/06/2006	20%
SVM Global Fund PLC	EGM	18/05/2006	10%

## Ex-UK Companies

The report on voting with regard to ex-UK companies is split into four sections. The second, third and fourth sections deal, respectively, with Japanese companies, shareholder approval of "other business" and dis-application of pre-emption rights. The first section covers all other ex-UK resolutions where Newton has voted against or registered an abstention on behalf of its clients.

### Abbott Laboratories – AGM – 28/04/2006

Newton voted against a shareholder-proposed resolution that requested the company to provide a bi-annual report on its political donations. This report should disclose information relating to the amount, the business rationale and identification of the person or persons who participated in making the decision to contribute or donate. Newton felt that the requested report,

which would contain a high level of disclosure, would not provide meaningful information to shareholders or be a useful employment of shareholders' funds. In addition, the company already describes its oversight function of political donations and has committed to improving disclosure in its annual report.

### Allergan Inc – AGM – 02/05/2006

Newton voted against a proposal seeking to increase the number of shares that may be awarded under the company's non-executive director share option plan. Newton considers it inappropriate for non-executive directors to be rewarded with share options, given the conflicts of interests that may arise. Therefore, as this proposal was seeking to augment the non-executive share option plan, Newton instructed votes against the proposed amendments.

**Allgreen Properties Ltd – AGM – 28/04/2006**

The company sought shareholder approval to increase the number of shares that may be awarded under its Share Option Scheme. The proposed limit would be 15% of the company's issued share capital. The proposal was in line with recent changes to the Singapore Exchange's listing rules, where, historically, the limit was 5%. However, Newton felt that the proposed level would lead to an excessive distribution of shareholders' wealth to the company's executives. It was also thought that the Share Option Scheme was not sufficiently well structured for a company of its size and nature.

**Allied Irish Banks Plc – AGM – 26/04/2006**

The company sought shareholder approval for a special one-off payment to a director following his loss of office. The company failed to provide any rationale for this payment. Therefore, Newton instructed votes against the proposal and, also, against three members of the remuneration committee, who were seeking re-election to the board.

A shareholder of the company proposed two resolutions at the company's AGM. The proponent sought to remove the company's auditors and to appoint himself to the company's board of directors. On both of these proposals, Newton supported management and instructed votes against the resolutions. It is understood, from the company, that the proponent was dismissed from the company a number of years ago and has a history of attending and attempting to disrupt the company's AGM.

**The Allstate Corporation – AGM – 16/05/2006**

Fundamentally, Newton is against the awarding of share options to non-executive directors. However, it is appreciated that, in certain circumstances, it may be appropriate for non-executive directors to be rewarded with shares. Even by just having a share price performance condition, Newton considers that non-executive directors' judgement could be clouded and lead to decisions being approved that may not be in shareholders' best interests. Votes were instructed against the chairman of the compensation committee, who was seeking re-election to the board and against the proposed Share Option plan.

**Altria Group Inc – AGM – 27/04/2006**

Newton declared a conflict of interest, by way of a long-standing business relationship with Altria. In such cases, the advice of the voting services used takes precedence (see page eight of Newton's Responsible Investment – guidelines and procedures). This policy meant that Newton instructed votes against all seven of the shareholder proposed resolutions. These were numbered three-to-nine. These resolutions requested for the company to: 3) provide for an independent chairman; 4) adopt the ILO's standards; 5) inform African Americans of the health risks associated with menthol cigarettes; 6) establish fire safety standards for cigarettes; 7) adopt an animal welfare policy; 8) support legislation to reduce smoking; 9) provide information on second-hand smoke.

**Ameren Corporation – AGM – 02/05/2006**

A shareholder submitted a resolution requesting that the company publish a report, within six months of the annual meeting, on the advantages and disadvantages of applying for an extension to the operating license at its Callaway facility. At the time of this request, the company had twenty years remaining on a forty-year licence and has until 2019 to submit a renewal application to the Nuclear Regulatory Commission (NRC). Newton was in agreement with the company that it would be premature to submit a renewal application at this time. Also, applying for an operating license extension at such an early stage could impair the company's ability to accurately consider all the factors that may develop over the remaining life of the license. Newton did not believe that the proposal warranted shareholders' support at this time.

**American Express Co – AGM – 24/04/2006**

Newton voted against three of the four shareholder proposed resolutions at the company's AGM.

The proponent of one of these resolutions sought for the board to take the necessary steps to cease future awards of share options. Newton considered that the board's compensation committee is best placed to recommend, for shareholder approval, the use of share options, should it feel they are an appropriate form of incentive.

A further shareholder requisitioned resolution requested the company to remove reference to sexual orientation in its statement on Equal Employment Opportunity. The proponent believes that individuals engaging in homosexual activities are subject to greater health risks and does not believe that the company should have to pay benefits based on an individual's personal decisions to engage in, what he believes to be, risky behaviour. The company stated that it considers its policy on non-discrimination to be valuable to the company on many levels. Also, in adhering to the proponent's request, the company may be at risk of violating certain state and city laws.

The final shareholder requisitioned resolution, which Newton voted against, proposed that the company amend its bylaws to provide for the reimbursement of reasonable expenses incurred by a shareholder in the proposing election of directors to the company's board. Newton considers that the proposal of nominees to a board is a key role of a well-constituted nomination committee. While Newton supports the right of shareholders to propose resolutions, it was felt that the reimbursement of expenses to shareholders might result in a proliferation of resolutions not in the best interests of all shareholders. It is also felt that the proposal would encourage shareholder nominees, which may not necessarily, be in the best interests of the other shareholders and the company.

**Apache Corp – AGM – 04/05/2006**

Two members of the company's compensation committee were seeking re-election to the board. Newton did not consider the individuals to be sufficiently independent to represent shareholders' interests, especially given their proposed election to the board's compensation committee. Both nominees have a transactional relationship with the company. One has been a member of the board for 10 years, the other for 25 years. The nominee, who had been a board member for 25 years, was proposed as chairman of the company's compensation committee. The resolutions seeking the re-election of these non-executives directors were voted against.

**Banco Santander Central Hispano – AGM – 16/05/2006**

Votes were instructed against the re-election of one of the company's non-executive directors. It was considered that, given his membership of the compensation committee, he should be seen as truly independent of the company. However, the nominee is the non-executive chairman of an affiliated company, he receives a separate consultancy fee in addition to his non-executive fees and has been a board member for 18 years.

The company also sought shareholder approval to amend its Bylaws, which included changing individuals' board terms from three years to five years. Newton voted against the proposed amendments as it was felt that this would lead to an unnecessary deterioration in shareholders' powers.

**Bank of Philippine Islands – AGM – 06/04/2006**

No information was provided for three resolutions for which shareholder approval was sought. These resolutions concerned the declaration of a dividend, bonuses to the company's directors and for shareholder approval of "any other business" that may be raised at the company's AGM. Given the unknown content of these proposals, Newton instructed votes against each of these three resolutions.

**BASF AG – AGM – 04/05/2006**

Included in the proposed amendments to its Articles of Association, the company sought to change the process for removing members from its supervisory board. If passed, the removal of a supervisory board member would require 75% of votes cast, as opposed to a simple majority. Newton felt that this provided too much protection for the members of the supervisory board. Votes were instructed against the proposed amendment.

**BCE Inc – AGM – 07/06/2006**

A shareholder requisitioned a resolution seeking for the company to convert to an Income Trust. In doing so, the proponent stated that the company would distribute 90% of its annual free-cashflow to shareholders. Newton considered that the proposal would overly restrict the company's ability to invest in its rapidly changing market. Votes were instructed against the shareholder proposed resolution.

**Bunge Ltd – AGM – 26/05/2006**

The company proposed to amend its bylaws by deleting the requirement for the board to obtain approval by at least 66% of votes cast should it wish to extend or adopt a new anti-takeover mechanism. Approval would revert to a simple majority. Newton felt the proposed reduction in shareholders' rights would unnecessarily shift the balance of power away from shareholders and towards the board. Therefore, votes were instructed against the proposed amendment.

**Carnival Corp – AGM – 20/04/2006**

The company's remuneration practices were not considered to be aligned with the creation of shareholder value. Significant awards of restricted shares, up to seven times an individual's base salary, vest after five years, irrespective of the company's performance. Additionally, all US-based non-executive directors enjoy routine awards of share options. Generally, where companies are not suffering from cash flow or profitability issues, Newton believes that the independence of non-executive directors should not be compromised by being in receipt of share options. Newton voted against the re-election of five non-executive directors. These were all members of the audit and the remuneration committees and were in receipt of share option awards. The above reasons also led to votes being instructed against the resolution seeking shareholder approval of the company's remuneration report.

**Caterpillar Inc – AGM – 14/06/2006**

The company proposed a new Long-Term Incentive Plan, for which it sought shareholder approval. Newton felt that the proposed total dilution to existing shareholders, on a fully diluted basis, of c.14.5% was an excessive transfer of value away from the company's shareholders. Newton also disagreed with a provision that would allow for early vesting of awards in the event of a change in control. Over the past three years, the average annual number of shares awarded under share based incentive schemes was 2.3% of the company's issued share capital. Newton felt that the proposed plan was not sufficiently well-structured to justify such high levels of awards. Votes were instructed against the proposed plan.

**Celesio AG – AGM – 27/04/2006**

The company's largest shareholder proposed a resolution requiring the company to desist from disclosing the remuneration of individual members of the management board. This proposal was in direct conflict with best practice in this area and also against the recommendations of the recent German Corporate Governance Code. Newton voted against this shareholder requisitioned resolution.

**Chevron Corporation – AGM – 26/04/2006**

Shareholders of the company submitted a resolution requesting that the company report on the potential environmental damage from its drilling in protected areas. Specifically, the proponents were concerned over the biodiversity issues surrounding the company's operations in Alaska. Newton noted the company's participation in the Energy & Biodiversity Initiative and the Convention on Biological Diversity & World Conservation Forum. It was also recognised that the company currently discloses its operational and environmental policies on biodiversity. The company also stated that its decision to operate in protected areas is taken on a case-by-case basis and only where government has legally authorised the operations. Newton did not consider that support for this resolution was warranted.

A shareholder proposed resolution requested the company to report, bi-annually, on its political contributions. It was requested that the report detail information on the amount of each contribution, identify the person or persons in the company who participated in making the decision and the rationale for each contribution. Newton voted against this resolution due to the company's established disclosures and policies on this matter.

A shareholder proposed resolution requested the company to reduce the use of animals in the testing of its products. The company stated that the limited amount of animal testing, which is all outsourced, is required by law and is carried out in a manner that meets or exceeds applicable regulations. The company also stated that any testing is carried out by qualified laboratories, which are all accredited with the American Association for the Accreditation of Laboratory Animal Care. Newton voted against the shareholder proposed resolution.

Finally, a fourth shareholder proposed resolution was voted against. This resolution would require the company to report on the costs associated with the remediation of sites in Ecuador. The requested report would cover the period from 1993 to 2005. The company has made numerous public legal filings and has communicated certain matters on its website relating to the remediation of sites in Ecuador. The company felt that, in disclosing the requested information, its legal position would be weakened in relation to ongoing litigation. Chevron's exposure to the remediation costs was a result of its merger with Texaco in 2001. Texaco was a minority partner in an oil consortium, along with the Ecuadorian government.

**China Petroleum & Chemical Corp – AGM – 24/05/2006**

The company sought shareholder approval to issue Commercial Paper up to an amount equivalent to 10% of its net assets. It was also proposed that the board would determine all matters relating to such an issue. Given that no comfort was provided to shareholders that any issuance would be in their best long-term interests, Newton instructed votes against the proposal.

**Citigroup Inc – AGM – 18/04/2006**

The proponent of a shareholder requisitioned resolution sought for the board to take the necessary steps to cease future awards of share options. Newton considered that the board's compensation committee was best placed to recommend, for shareholder approval, the use of share options should it feel they are an appropriate form of incentive. Newton voted against the resolution.

As raised at last year's AGM, a shareholder proposed resolution requested the company to report, bi-annually, on its political contributions. It was requested that the report detail information on the amount of each contribution, identify the person or persons in the company who participated in making the decision and the rationale for each contribution. Newton voted against this resolution due to the company's established disclosures and policies on this matter.

Newton instructed votes against a resolution that requested the company to provide, publicly on its website, a list of all charitable contributions. Whilst requesting full disclosure of charitable contributions, it seemed that the proponent was seeking for the company to stop making contributions to certain charities. Newton was comfortable with the company's current policy and disclosures surrounding charitable contributions.

The final shareholder requisitioned resolution, that Newton voted against, proposed that the company amend its bylaws to provide for the reimbursement of reasonable expenses incurred by a shareholder in proposing the election of directors to the company's board. Newton considers that the proposal of nominees to a board is a key role of a well-constituted nomination committee. While Newton supports the right of shareholders to propose resolutions, it was felt that the reimbursement of expenses to shareholders might result in a proliferation of resolutions not in the best interests of all shareholders.

**Colgate-Palmolive Co – AGM – 04/05/2006**

Newton instructed votes against the resolution seeking shareholder approval to award 2,600 shares, annually, to the board's non-executive directors. Making such awards to non-executive directors may not be in shareholders best interests, in that recipients' may be hindered in their ability to exercise independent judgement.

**Comdirect Bank AG – AGM – 04/05/2006**

Votes were instructed against the election of a proposed new non-executive director. Newton did not consider it appropriate for the Chief Investment Officer of the company's major shareholder to be nominated to the company's supervisory board. Newton was not confident that he would act in the best interests of all shareholders.

#### **CRH PLC – AGM – 03/05/2006**

One of the proposed nominees for re-election to the company's board was a director of a company in which CRH held a 45% stake. Given the relationship between the two companies, Newton felt uncomfortable with the nominee being a member of the audit committee. Votes were instructed against his re-election.

#### **DaimlerChrysler AG – AGM – 12/04/2006**

One of the company's shareholders proposed two resolutions at the company's AGM. The resolutions requested that shareholders authorise special audit reports of the company's Smart brand and, also, the company's Maybach brand. According to the proponent, both of the businesses have been suffering losses, with little prospect for improvement, since inception. The company's supervisory board stated that there is no indication of undue external influence, irregularities or violations of the executive directors in exercising due care and diligence in the decisions to develop and produce both brands. The supervisory board went on to state that it did not consider such an audit to be justified in any way. Newton did not support the shareholder's proposals given that there has been no clear evidence of misconduct and the new CEO, appointed in January this year, has initiated a restructuring and consolidation programme at the company.

#### **Dow Chemical Company – AGM – 11/05/2006**

Certain Dow Chemical shareholders submitted a proposal requesting the company report to shareholders on new initiatives that address specific health, environmental and social concerns associated with the Union Carbide India toxic release, which occurred in Bhopal, India, in 1984. Dow Chemical stated that, prior to its February 2001 acquisition of Union Carbide, it conducted a liability assessment and concluded that there would be no outstanding liability in relation to Bhopal. In 1998, the Indian government stated that it would take responsibility for managing any clean-up or remediation work required on the site. Newton believes the company has been open and transparent. Newton voted against this shareholder proposal.

Certain Dow Chemical Shareholders filed a proposal requesting that the company review its internal controls relating to potential adverse impacts associated with genetically engineered (GE) products. Newton instructed votes against this resolution. Factors considered included the current conflicting studies regarding the possible effects on wildlife, the environment and humans with regard to genetically engineered products. There is also a process, established by the federal government, for reviewing and approving GMO products for commercial marketing. The company provides detailed information on biotechnology, responsible uses of certain products and information on policies and controls related to GE products. Furthermore, the company is committed to engaging with interested shareholders on GE matters. Though it is prudent for a company to thoroughly evaluate its processes and increase disclosure of "off-balance sheet risk", Dow Chemical has already taken significant steps in this direction.

A shareholder requisitioned resolution requested that the company establish an independent panel to provide a report on

the extent to which the company's products cause or exacerbate asthma. Newton voted against this resolution. The additional reporting requested by the resolution would largely duplicate existing disclosure. Newton felt that a more appropriate forum for this matter would be the public regulatory agencies, which are tasked with creating policy on these issues. Newton believes that the company's current disclosures provide shareholders with adequate information to evaluate the risks associated with investing in the company. To minimise all chances of any biased results, it is important that any such study and report be completely independent of Dow Chemical. It was also noted that hazardous chemicals are heavily regulated in the US and EU.

A further shareholder proposed resolution was voted against. The resolution requested the company to report on the implications of adopting a policy to reduce the danger of potentially catastrophic chemical releases. Government regulation and legislation, to a large extent, already address many of these concerns. Dow Chemical also provides information on its policies and procedures with regard to chemical safety and security on its website. Management systems and controls, which the company has in place to mitigate risk to employees and the public, are also discussed. There is also a concern about releasing information that includes proprietary details about the company's security policies and procedures.

#### **Drillisch AG – AGM – 26/05/2006**

A resolution was proposed that requested the company not to disclose the remuneration arrangements in place for members of its management board. This proposal was in direct conflict with best practice in this area and also against the recommendations of the recent German Corporate Governance Code. Newton voted against this resolution.

#### **eBay Inc – AGM – 13/06/2006**

Newton instructed votes against a resolution requesting shareholder approval for the company to reserve additional shares for making awards under its Equity Incentive Plan. Newton felt that the proposed level of dilution was excessive at c.15% of the company's issued share capital. Newton also considered it inappropriate for the board's non-executive directors to be recipients of share-based incentive awards, especially when they were members of the board's remuneration and audit committees. Furthermore, the company has a history of making excessive share awards. On average, over the last three years, the company has made annual share-based incentive awards representing 3.3% of its issued share capital. This is not a sustainable policy.

#### **Exxon Mobil Corp – AGM – 31/05/2006**

Historic and current remuneration arrangements at the company led to Newton instructing votes against all five members of the compensation committee, who were seeking re-election to the board. Long-term incentive rewards are included as part of individuals' pension calculations. This "double dipping" led to the departing CEO receiving a \$98 million retirement package. Additionally, the CEO received an annual grant of 525,000 restricted shares, which would vest after four years, irrespective of performance. Similar arrangements have been put in place for the company's new CEO.

A shareholder of the company requested, by way of a shareholder resolution, that the board adopt a certain policy when recruiting chairmen for the compensation, audit and nomination committees. Despite disagreeing with the company's remuneration arrangements, Newton felt that the board's recruitment policy for its directors more than adequately addressed the issues raised by the proponent. Votes were instructed against the resolution.

Two resolutions proposed by separate shareholders were similar in nature. The first sought for public disclosure, in the national press, of the company's political donations, whilst the second shareholder proposed resolution sought disclosure of the company's charitable contributions. Newton noted that the company discloses detailed information, on its website, concerning its policies and contributions in relation to political and charitable expenditure. Newton did not consider that these resolutions warranted shareholder support.

#### **General Electric Co – AGM – 26/04/2006**

A shareholder requisitioned resolution proposed that the board should, on an annual basis, nominate one of the company's retirees for a position as non-executive director of the company's board. The proponent believes that the substantial number of shares held by the 205,000 retirees warrant the election of a retiree to the board and that the candidate would bring to the board unique perspectives and a better balance. Newton does not consider it appropriate for one shareholder group to be advantaged over another and that nominations to the company's board is a key role that should be conducted by the board's nominations committee. Newton voted against this shareholder proposal.

#### **The Home Depot Inc – AGM – 25/05/2006**

Three main reasons led to Newton voting against the four members of the company's compensation committee, who were seeking re-election to the board. First, the committee has re-priced underwater share-option awards, which fundamentally undermines the nature of long-term incentive arrangements. Secondly, special one-off remuneration arrangements have been put in place unnecessarily. Thirdly, the committee has failed to implement a shareholder requisitioned resolution, which has received a majority support from shareholders, for the past two years. This resolution sought to limit executives' service agreements. The company has also been the subject of much criticism over its remuneration practices.

#### **Honeywell International Inc – AGM – 24/04/2006**

A new share option plan was proposed for the sole participation of the board's non-executive directors. Individuals' annual awards would be limited to 10,000 shares, which equates to US\$432,200 as at the time of the AGM. Newton failed to see the necessity for compromising non-executive directors' independence by awarding them share options. Therefore, votes were instructed against the resolution seeking shareholder approval of the Non-Employee Director Omnibus Stock Plan.

Newton also voted against a resolution proposed by one of the company's shareholders. The proponent requested that the company report to the public of the dangers associated with

consuming fish or water from the Onondaga Lake. It was also requested that the company report to shareholders on the implementation of this policy. The company has accepted responsibility for the remediation of the lake, which was polluted by Allied Chemical prior to its acquisition by Honeywell. Whilst Newton recognises the importance of this matter, it was considered that the requested investigations would be better carried out by an independent third party.

#### **Hong Kong Exchanges and Clearing Ltd – AGM – 26/04/2006**

Five nominees were proposed for two available seats on the company's board. Two of the nominees were incumbents of the board, whilst the remaining three were nominees proposed by shareholders of the company. Newton was not convinced that any of the three shareholder nominees would prove to be significantly better for the creation of long-term shareholder value than the two incumbent nominees. Given the cumulative voting arrangements, Newton registered abstentions against the three shareholder nominees and instructed votes in favour of the two incumbents.

#### **Intel Corp – AGM – 17/05/2006**

Newton voted against the resolution seeking shareholder approval of a new share incentive plan and against three members of the compensation committee, who were seeking re-election to the board. On a fully diluted basis, covering all the share-based incentive arrangements, the company's shareholders would be excessively diluted by up to 15.4%. It was also proposed that non-executive directors participate in the plan. Given the size of the company and its level of profitability, together with the company's history of awarding high levels of share incentive arrangements, Newton did not consider the proposal to be in shareholders' best interests.

#### **International Business Machines Corp – AGM – 25/04/2006**

By way of a shareholder proposed resolution, it was requested that the company establish an independent committee to evaluate and report to shareholders on the risk to IBM's brand name from its outsourcing of jobs to offshore locations. The proponent is concerned that the level of outsourcing is having a negative effect on the morale of the American population. Newton is comfortable that the company's decision to outsource jobs forms part of its considered strategy to maximise shareholder value. Votes were instructed against the resolution.

A shareholder proposal requested the company to report, bi-annually, on its political contributions. It was requested that the report detail information on the amount of each contribution, identify the person or persons in the company who participated in making the decision and the rationale for each contribution. Newton voted against this resolution due to the company's established disclosures and policies on this matter.

**Johnson & Johnson – AGM – 27/04/2006**

Newton instructed votes against a shareholder proposed resolution that requested the company to prepare, and make publicly available on its website, a list of all charitable contributions. Whilst requesting full disclosure of charitable contributions, it seemed that the proponent was attempting to stop the company making contributions to certain charities. Newton was comfortable with the company's current policy and disclosures surrounding charitable contributions.

**JPMorgan Chase & Co – AGM – 16/05/2006**

The proponent of a shareholder requisitioned resolution sought for board to take the necessary steps to cease future awards of share options. Newton considered that the board's compensation committee is best placed to recommend, for shareholder approval, the use of share options, should it feel they are an appropriate form of incentive. Newton voted against the resolution.

A further shareholder requisitioned resolution requested the company to remove reference to sexual orientation in its statement on Equal Employment Opportunity. The proponent believes that individuals engaging in homosexual activities are subject to greater health risks and does not believe that the company should have to pay benefits based on an individual's personal decisions to engage in, what the proponent considers to be, risky behaviour. The company states that it considers its policy of non-discrimination is valuable to the company on many levels. Also, in adhering to the proponent's request, the company may be at risk of violating certain state and city laws.

**Lifestyle International Holdings Ltd – AGM – 26/04/2006**

The company proposed a resolution seeking shareholder approval of a grant of share options to a managing director of the company. The total award would be equivalent to almost 1% of the company's issued share capital. Given that the proposed recipient owned 63.8% of the issued share capital of the company, Newton did not consider it appropriate to make such a large one-off award. Votes were instructed against the proposal.

**Merck & Co Inc – AGM – 24/02/2006**

A shareholder requisitioned resolution requested the board to take the necessary steps to cease future awards of share options. Newton considered that the board's compensation committee is best placed to recommend, for shareholder approval, the use of share options should it feel they are an appropriate form of incentive. Newton voted against the resolution.

**Merrill Lynch International Investment Funds – AGM – 20/06/2006****Japan Opportunities/UK/Asian Tiger Bond/  
US Flexible Equity/Global /European Opportunities/  
US opportunities**

No information or comfort was given in relation to two resolutions for which shareholder approval was sought. The resolutions concerned the approval of directors' remuneration and of "any other business" that may be raised at the company's AGM. Newton instructed votes against these two proposals due to the lack of information or comfort offered to shareholders.

**Monster Worldwide Inc – AGM – 07/06/2006**

The shareholder requisitioned resolution, proposed at the company's AGM, requested the company to increase the diversity of its board. It was detailed that this should be achieved by ensuring women and minorities are considered for board positions, whilst publicly committing to a timetable for implementing such a policy. The company has a publicly available statement on diversity, has recently appointed a Chief Diversity Officer and addresses the issues surrounding diversity in the charter pertaining to the nominations committee. The proponent's concerns are already largely covered by the company. Additionally, it was felt that a strategy of committing to a timetable could have an adverse impact on recruitment of the most able candidates. Newton did not feel it appropriate to support such a resolution.

**Motorola Inc – AGM – 01/05/2006**

Over the past three years, the company has made awards of share-based incentives equating to 2.7% of issued share capital per annum. This level of dilution to shareholders' value is considered to be excessive, especially for a company with a market capital of more than US\$50 billion. The company sought shareholder approval for proposed overall dilution from all share-based incentive plans to be increased to c.14% of its issued share capital. Also of concern was the ability for non-executive directors to participate in the proposed new Omnibus Incentive Plan. Newton voted against the proposed Plan.

**Newfield Exploration Co – AGM – 04/05/2006**

Where a company has limited cashflow, it may be deemed appropriate for non-executive directors to be rewarded with share-based remuneration. However, in the case of Newfield Exploration, Newton failed to understand the need to increase the size of the annual awards of restricted stock that is provided to the company's non-executive directors. Votes were instructed against the resolution that sought shareholder approval of the amendment to the non-executive directors' share plan.

**Norsk Hydro ASA – AGM – 09/05/2006**

A shareholder proposed resolution sought to prohibit the president and CEO from participating in any future bonus schemes. The proponent failed to provide any information to support the proposal. Therefore, Newton voted against the shareholder's proposal.

**Nortel Networks Corporation – AGM – 29/06/2006**

A trust company, holding Nortel Network's shares, proposed a resolution requesting the establishment of a "pay-for-superior-performance" standard. Whilst Newton appreciated the objectives of the resolution, it was felt that they would be overly restrictive and could demotivate executives. It was also noted that the company's compensation committee had made some positive changes helping to align the interests of the company's executives with the long-term interests of the company's shareholders.

**Northern Star Mining Corp – AGM – 15/06/2006**

Shareholders were asked to re-approve a share option plan that would allow the company to award 10% of its issued share capital on a rolling basis. Newton considered this to be

excessive, especially when the average annual award of share options over the past three years has been 9.9%. In addition to voting against this resolution, Newton also instructed votes against the resolution seeking shareholder approval for the company to re-price underwater share option awards. Newton believes that the re-pricing of share option awards undermines the principle of incentivising directors through options and the related requirement for share price appreciation.

By way of two resolutions, the company sought shareholder approval to authorise and issue an unlimited number of shares in the company. The company failed to provide any assurances as to the intended use of any such issuance. Given the lack of comfort provided by the company and its track record of making high share option awards, Newton voted against the two proposed resolutions.

Shareholders were also asked to approve an anti-takeover mechanism. The proposal was for an old style plan that would only be renewed every eight years. Of most concern was the discretion that would be afforded to the board, which would allow it to waive any third party bids without, first, gaining shareholder approval. Votes were instructed against this protectionist measure, which was not considered to be in the best long-term interests of shareholders.

Finally, Newton voted against a resolution that sought approval of "Other Business". The unknown content of this resolution meant that Newton had to exercise a level of prudence by voting against its approval.

#### **Occidental Petroleum Corp – AGM – 05/05/2006**

A shareholder of the company requisitioned a resolution which would limit managements' individual remuneration to a maximum of \$500,000 per annum. Whilst Newton understood and appreciated the proponent's concerns surrounding escalating remuneration arrangements, it was considered that adopting such a policy would put the company at a competitive disadvantage when seeking to attract and motivate management. Votes were, therefore, instructed against the shareholder proposed resolution.

#### **Parkway Holdings Ltd – AGM – 12/04/2006**

The company sought shareholder approval to increase the number of shares that may be awarded under its Share Option Scheme. The proposed limit would be 15% of the company's issued share capital. The proposal was in line with recent changes to the Singapore Exchange's listing rules, where, historically, the limit was 5%. However, Newton felt that the proposed level would lead to an excessive distribution of shareholders' wealth to the company's executives. It was also thought that the Share Option Scheme was not sufficiently well structured for a company of its size and nature.

Newton also voted against a resolution that sought approval of "Other Business". The unknown content of this resolution meant that Newton had to exercise a level of prudence by voting against its approval.

#### **PepsiCo Inc – AGM – 03/05/2006**

Two similar resolutions were proposed by separate shareholders. The first sought for public disclosure, in the national press, of the company's political donations, whilst the second shareholder proposed resolution sought disclosure of the company's charitable contributions. Newton noted that the company discloses detailed information, on its website, concerning its policies and contributions in relation to political and charitable expenditure. Newton did not consider that these resolutions warranted shareholder support.

#### **PetroChina Company Ltd – AGM – 26/05/2006**

The company requested shareholder approval to issue up to 20% of the company's issued share capital, whilst dis-applying existing shareholders' pre-emption rights. As the company did not provide any comfort as to why shareholders should accept such a level of dilution, Newton voted against the resolution.

Newton also voted against a resolution that sought approval of "Other Business". The unknown content of this resolution meant that Newton had to exercise a level of prudence by voting against its approval.

#### **Pfizer Inc – AGM – 27/04/2006**

A Pfizer shareholder submitted a resolution requesting a report from the company relating to the measures it takes to keep price increases on its most prescribed drugs below the annual rate of inflation. The shareholder disputes the company's claim that price increases of its main prescribed drugs have been below the inflation rate in the US. Pfizer has implemented several programmes to assist accessibility to its drugs. The company's website provides information on discounts, subsidies and assistance programmes relating to this matter. Newton voted against this shareholder proposed resolution.

Newton voted against a shareholder proposed resolution that requested the company to provide a bi-annual report on its political donations. This report should disclose information relating to the amount, the business rationale and identify the person or persons who participated in making the decision to contribute or donate. Newton felt that the requested report, which would contain a high level of disclosure, would not provide meaningful information to shareholders or be a useful employment of shareholders' funds. In addition, the company has an established policy on political donations, which is publicly available.

Two further resolutions, proposed by shareholders, were voted against. These resolutions requested the company report on the welfare of the animals it uses for testing and to justify its funding of animal testing, whilst also requesting that the company support non-animal testing methods. Newton believes that the company's current policies address the proponents concerns. Therefore, votes were instructed against each of these resolutions.

**PNC Financial Services Group Inc – AGM – 25/04/2006**

The company's proposed Incentive Award Plan raised various concerns. Newton instructed votes against its approval. The dilution to shareholders under the plan would be c.11%, with total dilution of c.17% under all the company's share-based remuneration arrangements. This was considered to be excessive, especially when the company has a history of awarding c.2% of its share capital, on an annual basis, by way of share based incentives. The annual limit of shares to an individual in any single year was also considered to be inappropriate at 2 million shares (equivalent to US\$138.7 million as at the time of the AGM). Further concern resulted from the proposed inclusion of non-executive directors as participants in the Plan.

**QBE Insurance Group Ltd – AGM – 07/04/2006**

Newton instructed votes against two resolutions that sought shareholder approval of the issue and granting of shares pursuant to the company's Long-Term Incentive Scheme. Awards under the Scheme are made on the basis of the company's prior year's Return on Equity, with no forward looking performance conditions needing to be achieved for awards to vest. This policy is inconsistent with the remuneration guidelines in Australia, which state that executive incentive plans should be designed so that recipients are incentivised to create "materially improved company performance in terms of medium-to-long term growth of the company and resulting shareholder value".

**Raffles Medical Group – AGM – 21/04/2006**

The company sought shareholder approval to issue shares and grant of options in relation to the Raffles Medical Group (2000) Share Option Scheme. Newton was concerned at the potential for the company to issue 15% of its issued share capital by way of share-based incentive arrangements. Additionally, the Scheme provides for non-executive directors to be awarded share options. Newton instructed votes against the resolution.

**Reynolds American Inc – AGM – 03/05/2006**

Newton instructed votes against two resolutions that were proposed by certain shareholders of the company.

The first resolution requested that the company initiate and oversee independent research on individuals that begin smoking the company's flavoured cigarettes. If the findings from the research show that 20% of the individuals that started smoking these cigarettes were youths, the proponents requested that the company cease global operations to test, develop and market these cigarettes. Whilst the proponents' concerns may be legitimate, Newton does not believe that the company is best placed to conduct independent research into this matter. Government or non-affiliated bodies would more appropriate to conduct the requested independent investigations relating to this issue.

A further shareholder proposed resolution requested that the company support legislation to reduce and eliminate smoking in public areas and, also, to support legislation for tax increases on cigarettes. It makes little sense for the company to adopt such a strategy, whilst it operates within the parameters defined by legislation.

**Simon Property Group Inc – AGM – 11/05/2006**

The company proposed an amendment to its Omnibus Stock Plan that would allow for automatic grants to the company's non-executive directors. It was also proposed that the chairmen of the audit and compensation committees receive additional grants over those received by other non-executive directors. Newton believes that the award of share-based incentives to independent non-executive directors can undermine their ability to act in the best long-term interests of shareholders. This is especially the case when the individuals chair the two board committees where it is crucial that its members are independent of the company. Given the above, and the company's good profitability, which allow the payment of cash fees, Newton voted against the proposed amendment to the Omnibus Stock Plan.

**Singapore Technologies Engineering – AGM – 31/03/2006**

The company provided no rationale in relation to its resolution that sought shareholder approval to issue 20% of its share capital, whilst dis-applying the pre-emption rights enjoyed by existing shareholders. Newton felt that the potential level of dilution was excessive and instructed votes against the resolution.

The company also looked for shareholder approval to increase the number of shares that may be awarded under its Share Option Scheme. The proposed limit would be 15% of the company's issued share capital. The proposal was in line with recent changes to the Singapore Exchange's listing rules, where, historically, the limit was 5%. However, Newton felt that the proposed level would lead to an excessive distribution of shareholders' wealth to the company's executives. It was also thought that the Share Option Scheme was not sufficiently well structured for a company of its size and nature.

**Target Corporation – AGM – 17/05/2006**

Newton believes that the company's current disclosures surrounding political contributions provides a sufficient level of insight in to the company's policies and procedures on this matter. Therefore, votes were instructed against the shareholder proposed resolution that requested the company report in more detail on its political contributions and the decision-making process behind each contribution.

**Techpacific Capital Ltd – AGM – 26/04/2006**

Newton instructed votes against the company's request for shareholder approval to issue shares, whilst dis-applying the pre-emption rights enjoyed by its exiting shareholders. Newton felt it to be excessive that existing shareholders could be diluted by up to 20%.

Concern surrounding excessive dilution to shareholders was also the key reason for Newton voting against five further resolutions. These resolutions sought to make share option awards to the company's executive directors. The company operates under a policy that allows dilution under share-based compensation arrangements to reach up to 30%.

### **TeliaSonera AB – AGM – 27/04/2006**

The three shareholder proposed resolutions were voted against.

The first of these resolutions requested the company to hold General Meetings at the same time in both Stockholm and Helsingfors. The proponent failed to provide any rationale for this request.

Newton felt that the other two resolutions related to matters best left to the discretion of the management. It was requested that the board seek to allow shareholders to purchase the company's shares at a discount to their trading value. It was also requested that the company pay compensation to the Juvenile Diabetes Fund and to the Management team of Sonera Corporation.

### **Time Warner Inc – AGM – 19/05/2006**

At the time of the AGM, the company had a market capitalisation of US\$73 billion and was generating profits of US\$4.3bn. Given the size and profitability of the company, Newton considered it excessive for the company to seek shareholder approval to reserve 15.6% of its share capital for share based incentive awards. Over the last three years, the company has made annual share based incentive awards of between 1.5% and 2.5% of its issued share capital. Newton felt that the structure of the proposed Stock Incentive Plan did not warrant the intended grant levels. Votes were instructed against the proposed plan and, also, against three members of the compensation committee who were seeking re-election to the board.

### **Toreador Resources Corporation – AGM – 09/05/2006**

It was proposed, for shareholder approval, that additional shares be reserved for the granting of further awards under the 2005 Long-term Incentive Plan. Newton instructed votes against this proposal. Annual awards, over the last three years, have averaged 2.4% of the company's issued share capital. Also, the plan provides for vesting of awards to be at the discretion of the compensation committee. Two members of the compensation committee, who were seeking re-election to the board, were voted against. These nominees were both related to senior employees of the company.

### **Toronto Dominion Bank – AGM – 30/03/2006**

A shareholder requisitioned resolution requested that the company include, in its annual report, the financial statements of its subsidiaries that are domiciled in tax havens. The financial market in Canada is heavily regulated and the company states that it is in full compliance with all national and international laws developed to detect and deter tax evasion, terrorist activity and organised crime. The company also has policies and procedures in place to address any inappropriate activity. Newton understands that countries adopt differing tax regimes in order to attract and retain investment and that companies should be able to take advantage of these regimes when establishing legitimate tax planning strategies. It should also be noted that the company highlights the locations, within its annual report, of all its principle activities. Newton did not consider that this shareholder requisitioned resolution warranted support and, therefore, votes were instructed against the proposal.

Newton voted against a second shareholder proposed resolution. This resolution requested that the company not recruit directors if they had been implicated in any judicial proceedings that resulted in a finding of unethical activity or behaviour. The proponent's suggested prohibition policy appeared to be very broad. Individuals would not necessarily need to be named in a case of unethical conduct to be prohibited from being recruited, but simply have been a director of a company found to be operating unethically. Newton considers that a well structured and well resourced nomination committee is best placed to oversee the recruitment of a company's directors. It should also be noted that the company has certain policies and procedures in place that address ethical conduct.

### **United Overseas Land Ltd – AGM – 19/04/2006**

The company sought shareholder approval to increase the number of shares that may be awarded under its Share Option Scheme. The proposed limit would be 15% of the company's issued share capital. The proposal was in line with recent changes to the Singapore Exchange's listing rules, where, historically, the limit was 5%. However, Newton felt that the proposed level would lead to an excessive distribution of shareholders' wealth to the company's executives. It was also thought that the Share Option Scheme was not sufficiently well structured for a company of its size and nature.

A further resolution was also voted against. The company did not justify its request to dis-apply existing shareholders' pre-emption rights in the event of a new issue of shares, which could be up to 20% of the company's issued share capital. 20% dilution of existing shareholders' value was felt to be excessive where no commitments or comfort was provided to shareholders relating to the company's intended use of any capital raised.

### **United Technologies Corp – AGM – 12/04/2006**

A shareholder proposed resolution requested that the company impose term limits on non-executive directors to six years. Given the company's commitment to refresh board membership, Newton felt it inappropriate to support such a restrictive resolution.

A shareholder proposed resolution, that Newton voted against, requested the company to review its conduct and policies relating to foreign sales of weapons related products and services. Newton felt that the company's disclosure of such matters addressed many of the proponents concerns without divulging commercially sensitive information. Moreover, the company's sales of military equipment are closely monitored by the government.

### **Ventiv Health Inc – AGM – 14/06/2006**

The company proposed a new Long-Term Incentive Plan, for which it sought shareholder approval. Newton's main concern with the Plan was the overall dilution to shareholders' value. The Plan was not considered to be sufficiently well structured to warrant the award of 16.6% of the company's issued share capital. For share-based incentive awards, over the last three years, the company has made average annual grants equating to 3.2% of its issued share capital. In addition, non-executive

directors were specifically mentioned as intended recipients of the proposed incentive awards. Newton instructed votes against the proposed Plan.

#### **VeriSign Inc – AGM – 26/05/2006**

Newton voted against the resolution seeking shareholder approval for the company to increase the number of shares available for making awards under its Long-Term Incentive Plan. On a fully diluted basis, under all the share-based incentive arrangements, the company's shareholders would be excessively diluted by up to 20.5%. Newton did not consider the Plan to be sufficiently well structured to warrant the proposed level of dilution.

#### **Volkswagen AG – AGM – 03/05/2006**

The German code on corporate governance discourages the bundling of resolutions when a company is seeking to elect directors to its board. Instead, it recommends that a separate resolution be proposed for the election of each director. However, Volkswagen ignored this recommendation and proposed a bundled resolution for board elections. One of the proposed nominees was the CEO of Porsche, whilst another was an executive of Porsche. Porsche held 21.3% of the Volkswagen's shares. Given the lack of independent non-executive directors on the company's board and its key committees, Newton voted against the single resolution that sought to elect five nominees to the company's board.

#### **Wal-Mart Stores Inc – AGM – 02/06/2006**

A Wal-Mart shareholder submitted a proposal that requested that the company issue quarterly reports on its progress towards the implementation of Controlled Atmospheric Killing (CAK) at its suppliers' operations. Newton did not feel that shareholder support was warranted due to Wal-Mart's support for animal welfare guidelines released by the Food Marketing Institute (FMI). The FMI works with its counterparts to promote best practice for each species that will strengthen food quality and safety and ensure animal well-being at every step of the production process. Wal-Mart does disclose its general policy on animal welfare and appears to be taking steps to support animal welfare in its supplier relationships. Therefore, producing a quarterly report outlining progress on implementing CAK at suppliers operations could be burdensome for the company without providing meaningful information to shareholders. Votes were instructed against this proposal.

#### **Wells Fargo & Company – AGM – 25/04/2006**

Newton instructed votes against the re-election to the board of four non-executive directors who were relatives of the company's employees. Each of these four nominees were either members of the remuneration or audit committees, where it is important for members to demonstrate their independence.

A shareholder proposed resolution requested that a report be prepared comparing the cost of loans, highlighting any disparities that might exist due to race or ethnicity. Newton instructed votes against this resolution. The company is subject to stringent fair lending laws and it makes lending decisions based on credit risk, not racial or ethical data. The company also offers advice and support to individuals with regard to managing their own credit problems.

#### **Williams-Sonoma Inc – AGM 23/05/2006**

Newton voted against the resolution seeking shareholder approval for the company to increase the number of shares available for making awards under its Long-Term Incentive Plan. On a fully diluted basis, under all the share-based incentive arrangements, the company's shareholders would be excessively diluted by up to 13.5%. Also of concern was the proposed automatic grants of share options to the board's non-executive directors. Newton did not consider the Plan to be sufficiently well structured to warrant the proposed level of dilution. Votes were also instructed against three members of the compensation committee, who were seeking re-election to the board.

#### **Woodside Petroleum Ltd – AGM – 11/04/2006**

The company sought shareholder approval for its remuneration report. Newton was concerned that full vesting of long-term incentive awards would occur in the event of a change in control, performance conditions can be re-tested for two further years should awards not vest after the initial three year period and a third of awards automatically vest irrespective of performance achieved. In addition, service contracts of executives are 18 months, rather than the 12 months as suggested by best practice. Newton instructed votes against the company's remuneration report.

#### **Yahoo! Inc – AGM – 25/05/2006**

The company proposed a number of amendments to its non-executive directors' share option plan. Only in exceptional circumstances would Newton support the granting of share-based incentives to non-executive directors. Shareholders require non-executive directors to act independently of management. Votes were instructed against the proposed amendments to the Plan. Votes were also instructed against three members of the compensation committee, who were seeking re-election to the board.

#### **Yukos Oil – AGM – 21/06/2006**

Newton instructed votes against all eleven resolutions proposed by the company at its AGM. The company failed to provide any information relating to the proposed resolutions. Given the company's chequered history and the need to regain shareholders' confidence, Newton would expect the company to be open with disclosure of fundamental information. Without such information, shareholders are unable to exercise voting rights in an informed and intelligent manner.

## Japanese Companies

Many Japanese companies proposed a number of common resolutions, which Newton viewed as contentious. These included:

### (a) Retirement bonuses to departing independent non-executive director, as designated by the company

Shareholder approval was sought to award retirement bonuses to retiring directors. One of the proposed recipients was designated, by the company, as an independent non-executive director. Newton considers this method of payment to non-executive directors to be inappropriate. The non-executive's ability to exercise independent judgement could be adversely affected. Votes were instructed against this resolution.

### (b) Determine dividend allocation

Amongst the proposed amendments to the company's Articles of Association was a request for the board to determine the allocation of income. This would include the payment of dividends to shareholders. If approved, shareholders would not be able to vote on the approval of the company's dividend policy or submit shareholder proposals relating to the allocation

of income. Whilst it is uncommon for Newton to oppose a company's income allocations, Newton was concerned that the proposal could lead to unacceptable dividend policies, going forward. Newton voted against the resolution proposing to amend the company's Articles of Association.

### (c) Appointment of non-independent statutory auditor

Shareholder approval was sought for the appointment of an internal statutory auditor, who Newton considered to be affiliated to the company. Internal auditors are privy to market sensitive information that requires them to act in the best long-term interests of the company. Therefore, it is essential for such nominees to be viewed as independent of the company and its directors. Votes were instructed against the proposed appointment of non-independent internal statutory auditors.

The following companies, at their AGMs, included resolutions relating to the categories shown above. In addition, any further comment shown beneath the company indicates that there were other contentious issues.

Category	Company
(a)	<b>Acom Co. Ltd – AGM – 22/06/2006</b>
(a)	<b>Fuji Television Network Inc – AGM – 29/06/2006</b>
(a),(b),(c)	<b>Godo Steel Ltd – AGM – 29/06/2006</b>
(b)	<b>Honda Motor Co Ltd – AGM – 23/06/2006</b>
(b)	<b>JS Group Corp – AGM – 22/06/2006</b>
(c)	<b>Jupiter Telecom – AGM – 28/03/2006</b>
(c)	<b>Lawson Inc – AGM – 26/05/2006</b>
(c)	<b>Matsui Securities – AGM – 25/06/2006</b>
(a),(b),(c)	<b>Matsushita Electric Works Ltd – AGM – 23/06/2006</b>
(a)	<b>Mitsubishi Estate Co. Ltd – AGM – 29/06/2006</b> Votes were also instructed against the proposed election to the board of the company's president. The nominee was forced to resign as president following charges made against him for conspiracy to conceal facts and the violation of laws relating to real estate transactions.
(a)	<b>Mitsubishi Heavy Industry Ltd – AGM – 28/06/2006</b> Newton also voted against the resolution seeking shareholder approval of the share option plans for the company's directors. One of the proposed option plans would provide for the award of deeply discounted awards, which could vest almost immediately following the grant date. Additionally, given the lack of disclosure, Newton assumed that the awards would vest irrespective of performance.

<b>Category</b>	<b>Company</b>
(a)	<b>Mitsubishi UFJ Financial Group – AGM – 29/06/2006</b>
(a),(c)	<b>NEC Electronics Corp – AGM – 27/06/2006</b> The company also sought shareholder approval for it to reduce its capital reserves. Newton voted against this resolution due to the company’s failure to provide any details relating to the proposal.
(a)	<b>Nippon Express Co. Ltd – AGM – 29/06/2006</b>
(b)	<b>Nippon System Development Co Ltd – AGM – 29/06/2006</b>
(a),(c)	<b>Nippon Telegraph &amp; Telephone Corp – AGM – 28/06/2006</b>
(a)	<b>Nissan Motor Co Ltd – AGM – 27/06/2006</b>
(b)	<b>Nomura Research Institute – AGM – 23/06/2006</b> Newton also voted against the resolution seeking shareholder approval of share option plans for the company’s directors. One of the proposed option plans would provide for the award of deeply discounted awards, which could vest almost immediately following the grant date. Additionally, given the lack of disclosure, Newton assumed that the awards would vest irrespective of performance.
(b),(c)	<b>NS Solutions Corp – AGM – 27/06/2006</b>
(a),(c)	<b>NTT DoCoMo Inc – AGM – 20/06/2006</b>
(a),(b)	<b>PanaHome Corp – AGM – 29/06/2006</b>
(a)	<b>Promise Co Ltd – AGM – 20/06/2006</b>
(a)	<b>TakeFuji Corp – AGM – 29/06/2006</b>
(a)	<b>Terumo Corp – AGM – 29/06/2006</b>
(b)	<b>Yamato Holdings Co Ltd – AGM – 28/06/2006</b>
	<b>Sharp Corp – AGM – 22/06/2006</b> The company proposed a number of changes to its Articles of Association. Most of the proposed amendments were not contentious, with the exception of the request to increase the company’s authorised share capital. The company explicitly stated that one purpose of the increase would be to enable it to issue shares as part of any take-over defence plan. This authority would, in effect, deter any potential hostile bids. Votes were instructed against the bundled resolution that sought approval of various changes to its Articles of Association.

## Other Business

The companies below all included a resolution at their meetings entitled “other business”. For each company below, this was the only resolution that Newton considered to be sufficiently against shareholders’ best interests to warrant voting against.

Company	Meeting type	Date
Advanced Info Service PCL	AGM	24/04/2006
AXA World Funds II – Far East Equities	AGM	18/05/2006
Ballard Power Systems Inc	AGM	10/05/2006
Bangkok Bank Public Co Ltd	AGM	12/04/2006
Bank of Ayudhya Public Co Ltd	AGM	27/04/2006
Bougainville Copper Ltd	AGM	02/05/2006
CTCI Corp	AGM	23/06/2006
High Tech Computer Corp	AGM	02/05/2006
First Bangkok City Bank	EGM	24/05/2006
Great Quest Metals Ltd	AGM	26/05/2006
Investcom LLC	AGM	05/06/2006
PTT Public Co	AGM	20/03/2006
Sur American Gold Corp	AGM	22/06/2006
Vina Concha Y Toro SA	AGM	25/04/2006

Shareholder approval was sought for the company to conduct “other business” that may arise at its General Meeting. Open-ended resolutions of this type, with no additional supporting information or shareholder protection measures, are generally considered to be unhelpful by institutional investors and other shareholders who vote by way of proxy. No explanation of this resolution or the motivation behind the proposal was disclosed. Therefore, Newton instructed votes against the resolution seeking shareholder approval of “other business”.

## Dis-application of Pre-emption Rights at Ex-UK Companies

In the UK, the Pre-emption Rights Group has issued a guidance note to companies and investors where companies seek to issue more than 5% of their share capital without recognising the pre-emption rights of existing shareholders. Above 5%, consultation should be undertaken and adequate justification given.

The following table shows companies, outside of the UK, held by Newton's clients, that sought to dis-apply pre-emption rights, whilst failing to justify the requests.

Company	Meeting type	Date	Level of dis-application sought
Cnooc Ltd	AGM	24/05/2006	20%
China Merchants China Direct Investments Ltd	AGM	30/05/2006	20%
China Mobil (Hong Kong ) Ltd	AGM	18/05/2006	20%
China Netcom Group Corp Ltd	AGM	16/05/2006	20%
DBS Group Holdings Ltd	AGM	30/03/2006	20%
Hengan International Group Co Ltd	AGM	08/05/2006	20%
Hutchison Telecommunications Intl Ltd	AGM	16/05/2006	20%
Hutchison Whampoa Ltd	AGM	18/05/2006	20%
Melco International Development Ltd	AGM	17/05/2006	20%
MLP AG	AGM	31/05/2006	19%
Pacific Basin Shipping Ltd	AGM	07/04/2006	20%
Quester VCT	AGM	20/06/2006	10%
Sinotrans Ltd	AGM	29/05/2006	20%
Swire Pacific Ltd	AGM	11/05/2006	20%
Telefonica SA	AGM	20/06/2006	20%
Television Broadcasts Ltd	AGM	24/05/2006	

# Examples of engagement – Corporate Governance Q2 2006

## **UK Software & Computer Services company – April 2006**

**Contact: Senior Non-Executive Director**

Last year, the company split the roles of chairman and CEO. While the then chairman/CEO became CEO, an interim chairman was appointed. The company identified a preferred nominee for the permanent position of chairman. The company's senior non-executive director sought Newton's views. From discussions relating to the nomination committee's search and selection process, Newton was confident that the proposed candidate would be a positive addition to the company's board. Newton's main concern was with the age of the proposed nominee. However, assurances were given that the proposed chairman would be committed for two terms (6 years).

## **Thai Bank – April 2006**

**Contact: Executive Vice President of Accounting**

Of concern was a resolution proposed at the company's AGM that sought shareholder approval of "Other Business". Newton understands that the approval of "Other Business" is a routine request at Thai AGMs and that, historically, no significant business has been raised under this resolution at this company's AGMs. However, given that shareholders voting by way of proxy would not know the content of the resolution, it would not be in our clients' best interests to support such a request. The company understood Newton's concerns but stated that it would not be able to remove the item from this year's AGM agenda.

## **Canadian Pharmaceutical & Biotechnology company - April 2006**

**Contact: Finance Director**

The company sought to amend its share option plan. Included as intended recipients, on a discretionary basis, would be the board's non-executive directors. Newton raised this issue with the company, together with other remuneration related matters. Newton was concerned that awarding share-based incentives to non-employee directors can compromise their independence. Newton accepted the argument that the limited free-cash flow, generated by the company, is best invested in the company's operations. It was explained that non-executive directors receive a nominal fee for attending board meetings and that additional compensation is provided by way of non-performance based share options. Newton considered this to be an appropriate method of recruiting and retaining non-executive directors in an environment where fees are rising rapidly. Dilution of shareholder value, by way of issuances of share options, together with payments in the event of a change in control, were also discussed. The company provided Newton with certain levels of comfort in relation to these matters.

## **Hong Kong General Financial company – April 2006**

**Contacts: Non-Executive Directors and board nominees**

There were five candidates seeking appointment to the company's two non-executive director board seats. Newton discussed the attributes and agendas of the candidates with the company and, also, with the proposed nominees. Two of the candidates were existing board members seeking re-election, whilst three were nominated by the company's shareholders. Newton felt that it was important to support the election of two candidates who would be able to contribute, meaningfully, to the success of the company and provide an independent view that would be in the best long-term interests of shareholders. Newton felt that one of the shareholder proposed nominees would only be using the appointment to the board as a learning exercise and for career advancement. Given the challenges faced by the company in a complicated and politically sensitive market, it was considered that only individuals of sufficient calibre, expertise and knowledge should be appointed to the board. Following extensive discussions, Newton favoured the two nominees proposed by the company's management.

## **UK Media company – April 2006**

**Contact: Company Secretary**

The company proposed changes to the performance targets governing the vesting of awards made under its Long-Term Incentive Plan and Share Option Scheme. Newton expressed concern that the earnings targets were not sufficiently challenging. It was also suggested to the company that the proposed Profit Before Tax (PBT) performance conditions should be disclosed. The company was only willing to disclose the PBT target that would initiate the vesting of awards. The PBT target required for maximum vesting to occur would not be disclosed due to the company deeming it to be commercially sensitive. The company stated that the remuneration committee would review the setting of appropriate targets, which govern the vesting of share options and long-term incentive awards.

### **UK Support Services company – May 2006**

**Contact:** Chair of the Remuneration Committee

Discussions were had with the company concerning the proposed performance conditions which would be used for the next award of restricted shares. The company did not make any awards in 2005 but it did provide for higher than usual awards in 2004. It was the company's intention to introduce Earnings Per Share (EPS) targets. It was suggested to the company that the EPS measure be more stretching and vesting be subject to a secondary performance measure of relative Total Shareholder Return (TSR). Newton queried various elements of the plan, including potential dilution to existing shareholders and the sourcing of shares. It was confirmed that normal dilution limits will be adhered to and vesting awards would be satisfied with newly issued shares. The company stated that in calculating EPS, one-off distortions would be stripped out, including the effects of any share buy-backs. The company agreed that it would provide additional detail in its remuneration report relating to the discretion afforded to the remuneration committee when assessing the vesting levels of awards.

### **UK General Industrial company – May 2006**

**Contacts:** Chair of the Remuneration Committee  
Company Secretary  
Broker

Detailed discussions were had with the company in relation to a proposed remuneration scheme, which it was seeking approval of at its AGM. Whilst Newton did not feel comfortable with some aspects, the scheme was considered to be of a significantly better structure than the CEO's contractual arrangements, which the company would have been obliged to satisfy. Newton expressed its concern in relation to the use of absolute Total Shareholder Return growth that would govern the vesting of Performance Share Plan awards. Newton was also concerned with the discretion afforded to the remuneration committee in the event that the performance conditions are not met.

Newton stated that it would support the company's proposal but only on the basis that the proposal was better than existing arrangements and that it would be significantly detrimental to shareholder value should the CEO resign. However, Newton indicated that it would not expect to see the same structure in place when it comes to making the next set of awards. Should the long-term incentive arrangements not be improved, it would be Newton's intention to vote against the remuneration report and any members of the remuneration committee seeking re-election to the board.

### **Taiwanese Technology Hardware & Equipment company – May 2006**

**Contact:** Investor Relations

At the company's AGM, various resolutions were proposed that sought shareholder approval of changes to the company's procedures, guidelines and Articles of Association. However, no information relating to the proposed amendments was disclosed. The company stated that it was acting in accordance with the Taiwan SEC regulations by only providing details ten days prior to the meeting date. Whilst Newton recognised the regulations surrounding such disclosures, it was highlighted to the company that shareholders require the information in advance of this ten-day deadline to enable votes to be exercised in an informed and timely manner.

### **UK Food Producer – June 2006**

**Contact:** Company Secretary

The company requisitioned an EGM to seek shareholder approval to re-register as a private company. This stock was suspended from trading on the London Stock Exchange over 10 years ago. Newton contacted the company and expressed concern that by taking the company private it would lead to a reduction in shareholders' protection. The company secretary stated that the directors of the company had been advised that taking the company private was the best method of maximising distributable reserves. The company secretary also stated that it was the directors' intention to wind-up the whole business and return funds to the shareholders.

### **UK General Retailer – June 2006**

**Contacts:** Chair of the Remuneration Committee  
Human Resources Director

The company sought to adjust the earnings performance targets, which govern the vesting of awards made under the Performance Share Plan. Newton sought and received clarification that the proposed performance conditions would only apply to future awards. Newton considered it sensible that the performance conditions be adjusted and felt that they remained sufficiently challenging.

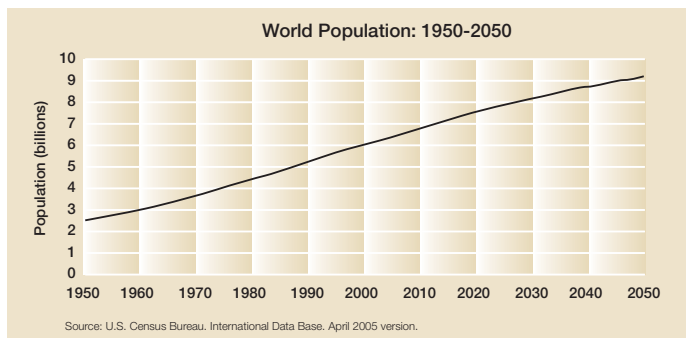
# SRI Focus: Responsible Food Retailing

## Introduction

### Population growth

As the world's population grows, food consumption is increasing globally. Meeting this demand, alongside other necessities such as energy and water, is one of the largest growing sources of pressure on the environment (See Figure 2: UK Food Industry Environmental Impacts).

**Figure 1:**  
**World Population Growth, Actual and Projected, 1950-2050**



### Sustainability of the food industry

How products are grown, processed and transported can significantly affect the environment. It can also have a major impact on the living conditions of people involved in the food production chain. Good long-term management of the natural resources utilised in food production is essential to ensure viability of the sector. For example, the overuse of water resources for crop irrigation can result in depletion of local aquifers; the clearing of forest for agricultural land can result in soil erosion leaving the land infertile. Agriculture must be managed to ensure the sustainability of food resources in the long-term. The challenge of the coming years is to produce enough food to meet the needs of the growing population, while preserving and enhancing the natural resource base so as not to compromise the quality of life of future generations. This is often referred to as sustainability of the food industry.

**Figure 2:**  
**UK Food Industry Environmental Impacts**

#### The UK food industry\* accounts for:

- About 14% of energy consumption by UK businesses and 7 million tonnes of carbon emissions per year;
- About 10% of all industrial use of the public water supply;
- About 10% of the industrial and commercial waste stream;
- 25% of all heavy goods vehicles kilometres in the UK.

\* The food industry, in this case, refers to the food and drink industry beyond the farm gate. This includes manufacturers, wholesalers, retailers and food service providers.  
Source: DEFRA, Food Industry Sustainability Strategy, April 2006

### Dominance of the food retailers in the food chain

Food retailers can be seen as the gate-keepers of the food chain. Due to their size, global supply chain and role as food providers, the major supermarkets carry significant social and environmental responsibilities. For example, food retailers have the ability to influence:

- the way food is produced through their relationships with suppliers;
- the way food is produced by providing food choices and information that will assist customers in making ethical purchasing decisions should they so choose;
- the way food is consumed by providing food choices and information that will assist customers to adopt healthier and more balanced diets;
- consumer behaviour towards reducing negative impacts on the environment through waste minimisation strategies.

Food retailers also have a responsibility to provide safe and affordable food to consumers.

In the UK, there are 4 major food retailers. These are Tesco, ASDA, Sainsbury's and Morrisons. These four food retailers account for c. 75% of UK grocery sales (see Figure 3: UK Major Food Retailers, Market Share Data). Sainsbury's, as an example, has 752 stores throughout the UK, receives over 16 million customers every week, and sources products directly from 1400 suppliers.

**Figure 3:**  
**UK Major Food Retailers, Market Share**

Food Retailer	% of UK grocery sales
Tesco	31.1
ASDA	16.4
Sainsburys	16.0
Morrison Group	11.3
<b>Total</b>	<b>74.8</b>

Source: TNS Superpanel  
Data as at 21 May, 2006.

## Scope of report

This quarter's SRI focus looks at the role of food retailers as agents to influence positive change.

**Part (I)** of the report details some of the dynamics of the food retailing industry. It looks at the pressures faced by companies as they compete in a highly competitive industry and how this affects behaviour.

## Part (I): Business dynamics of the food retailing industry

The major food retailers often face accusations of procuring food grown anywhere in the world with limited regard for labour conditions, for conservation of the environment or for local suppliers' economic viability. To understand why these accusations occur, it is helpful to consider some of the business dynamics of the food retailing industry and how they drive the behaviour of companies.

- **Price competition dominates the sector**

On a global scale, the sector is highly competitive, mostly because consumers demand low prices. The Institute of Grocery Distribution (IGD) published research in 2005 reporting that the top three factors which consumers cite as influencing their food choice are price, taste and sell by date.

The current economic environment continues to be unhelpful for the retail industry in the UK. Consumers are juggling the impacts of higher interest rates and a weaker housing market, as well as higher oil prices and utility bills. Therefore, to encourage spending, retailers offer lower prices. At the same time, the retailers are facing cost pressures with wage inflation, higher energy prices and rising property costs. This combination of factors puts pressure on margins. As companies have looked for ways to maintain low prices while offsetting rising input costs, supermarkets have faced accusations of preying on other players in the food chain and exerting undue pressure on suppliers.

- **Consolidation to improve buying power**

With pressure on margins, increasing sales, alongside the attendant improvement in buying power, is a way for companies to improve profitability. However, gaining market share in a highly competitive sector is difficult. A way to achieve this is for a company to take over another one. The combined entity, once fully integrated, should be able to manage costs more efficiently by exploiting economies of scale. The combined entity also gains increased buying power, for example, by demanding lower merchandise prices or greater provision of services. The UK food retailing sector has seen significant consolidation over recent years. The merger of Sainsbury and Asda, completed in 2004, concentrated the market into four major players. This has resulted in further pressure on manufacturers, suppliers and farmers to increase flexibility and quality, while simultaneously reducing prices.

**Part (II)** of the report looks at the environmental and social matters that affect the industry. This includes the challenges faced in working towards the sustainability of the industry.

**Part (III)** of the report outlines what the four major UK food retailers are doing to tackle some of the issues discussed in Part (II).

- **Continuous adaptation to respond to changing food consumption patterns**

Understanding the competitive nature of the global food industry means understanding changing consumer preferences and the food industry's efforts to meet these demands. Food markets are constantly evolving, driven not only by changes in consumer preferences, but also by technology, increasing efficiency in the supply chain and prevailing policies and business environments. Retailers themselves can also create demand through the products they offer.

Companies must continuously innovate to keep up with changing trends and to anticipate the next source of demand. A flexible business strategy, including flexibility within supplier operations, is important to be able to respond quickly and efficiently to changing consumer preferences. Modern technology, such as point of sale scanners, provides retailers with first hand information regarding preferences. Companies can interpret this information immediately and position themselves to respond to changing consumer demands.

Some examples of trends driving changing food consumption patterns include:

(i) *Urbanisation*: According to the UNFPA<sup>1</sup>, the proportion of people in developing countries who live in cities has almost doubled since 1960, from less than 22% to more than 40% in 2001. In more developed regions, the urban share has grown from 61% to 76% over the same period.

Part of the reason behind the trend of urban migration is the falling value of food as a commodity. This has resulted in lower economic power for agricultural producers, forcing them to migrate to the cities in search of jobs. In urban areas, there is generally greater food availability as well as higher purchasing power. This is a reflection of higher disposable incomes. Lifestyle changes brought about by urbanisation have resulted in diet changes among consumers worldwide. For example, as urbanisation in developing countries takes place, diets which have traditionally been high in carbohydrate-rich cereals, have increased consumption of meats, fruits, and vegetables.

<sup>1</sup> The United Nations Population Fund (UNFPA) is a subsidiary of the UN General Assembly. The fund provides reproductive health support in response to country requests, helping to integrate population and reproductive health concerns into development initiatives.

As urban food demand rises, food distribution systems must also develop. To meet the growing and changing demand, increasing amounts of foods will need to be supplied from ever more distant production areas. The Food and Agricultural Organisation of the United Nations estimates that, to meet the needs of a growing and increasingly urban population between now and the year 2010, investment in food handling, storage, transport, marketing and processing will need to increase by 25% to the level of US\$43 billion per year.

*(ii) Income growth:* With higher disposable income comes a demand for quality, convenience and variation. For instance, consumers in wealthier countries are increasingly moving their diets toward relatively higher value foods. However, the higher value does not just reflect increases in quantity and nutrients but the value-added service embodied in the products. For example, there is a demand for products that reduce the time required to prepare food for consumption. More recently, Western food retailers have seen increases in demand for organic, ethically sourced and healthy foods. In the developing world, higher incomes have resulted in increased demand for meat products, often leading to the expansion of livestock production.

- **Improved transportation and technology**

Consumer demand for fresh and exotic fruit and vegetables throughout the year, coupled with low transport costs, has led to an increase in long-distance shipping, road transport and air freight. Improvements in technology have enabled real time communication as well as fast and efficient delivery of products. Along with these improvements, global trade in horticulture and processed products has grown.

As imports of food have developed, food retailers have faced accusations that they are increasing their contribution towards global warming. They have also faced pressure resulting from the impacts of increasing imports on local food suppliers.

To some extent, this trend is now reversing as the food retailers respond to consumer concerns. Many of the major supermarkets are now taking action to source more products locally and optimise fuel efficiency to decrease greenhouse gas emissions generated through food transportation.

- **Brand protection**

A company's image is one of its most valuable assets. Brand can directly influence a consumer's purchasing decision. With companies increasingly being held accountable for the practices of their business partners, the working practices of suppliers can give rise to significant operational and reputational risks. Negative reputations gained through poor relationships with suppliers, within a developing country or region, may impact the acceptance of a foreign brand in retailers' home markets. Many major companies now recognise that ethical risk management is an important part of brand management. Responding to social and environmental matters can be a way of gaining customer loyalty and a competitive advantage.

In developed countries, product differentiation, value added, and consumer trust are important considerations for retailers seeking to retain market share. Retailers' brands and ranges can act as a guarantor of product quality and safety. Therefore, many retailers, particularly in Western Europe, have developed private label products that capture these qualities. For example, Tesco's own-brand products do not contain any genetically modified foods. To ensure that their own-brand products meet quality and safety standards demanded by consumers, retailers coordinate and develop relationships with members of their food supply chain. In this way, companies with their own-brand range can influence the behaviour of suppliers.

## **The Office of Fair Trading (OFT) Investigation (UK)**

In May 2006, the OFT referred the market for the supply of groceries by retailers in the UK to the Competition Commission for investigation. Areas that the investigation will focus on include pricing, the supply chain, market concentration, the convenience sector and planning and land use. This is the third investigation into the sector in seven years. The purpose of the investigation is to determine whether any of the areas under scrutiny result in detrimental effects on consumers by distorting competition.

In 1999, the OFT referred the sector to the Competition Commission for investigation over complaints that profits and food prices were unreasonably high in the UK versus Europe and the US. The investigation included assessment of the relationship between supermarket

operators and suppliers. The Competition Commission's findings dismissed claims of over-charging customers and making excessive profits. It was concluded that the industry is broadly competitive. However, as a "secondary concern", the Competition Commission outlined 52 ways in which supermarkets were said to misuse market power. The Competition Commission also found a "climate of apprehension" among many suppliers in their relationship with the main supermarkets. The report, not surprisingly, also showed a significant correlation between market share and the ability of a food retailer to extract better terms from their main suppliers.

The Competition Commission did not impose sanctions but recommended that supermarkets be made to abide by a legally binding Code of Practice on their dealings with

suppliers. The Code of Practice came into effect in March 2002 but was applicable only to the top four supermarkets. By late 2002, it had become clear that the Code of Practice was not producing the desired change in behaviour. In February 2003, the OFT launched a review of the Code. The findings of this review were published in February 2004. The OFT found that supermarket practices had not changed significantly since the introduction of the Code of Practice. It also stated that the position of suppliers had become weaker.

The recently announced investigation is taking place after several takeovers in the convenience store market. This has led to an increased concentration of the market since the last investigation. Planning appears to be an area of considerable concern amongst commentators. Specifically, the investigation will look into whether retailers use property as a barrier to entry by retaining land banks or by acquiring, divesting or developing land

to deter competitive entry. The Competition Commission will also look at whether some retailers pay excessive prices for land to prevent competitors buying it. Alongside this investigation is a separate review on the planning process.

For the investigation into pricing, the OFT will look at local pricing, below-cost selling, price flexing and whether there is any evidence of predatory intent or effects in local pricing decisions. For the supply chain, the investigation will look at the behaviour of grocery retailers towards suppliers and whether it affects their viability in a way that would not happen in an effectively functioning market. A key part of the investigation will also look at how consumers behave.

The full investigation process is likely to take 18-24 months.

## Part (II): Social and environmental matters surrounding the food retailing industry

Consumer concerns about the environmental and social impacts arising from food production and transportation are growing. It is no longer enough for companies only to respond to consumer concerns over food quality and safety in order to preserve brand loyalty or win consumer trust. Rather, firms are increasingly driven to integrate plans for sustainable development of the world's natural resources into corporate strategies and responsibilities. Part (II) of this report looks at some of the specific environmental and social matters that the food industry faces.

### Environmental matters

#### • Energy use and climate change

There is mounting evidence that the world's climate is changing and that the burning of fossil fuels, releasing carbon dioxide into the air, is a principal cause. The increasing levels of carbon are thought to be leading to warmer temperatures and greater unpredictability in weather patterns. Floods, storms and droughts across the world show how vulnerable the planet is to climate extremes and how high the human, environmental and economic costs can be. For the food industry, short-term weather shocks can impact the stability and the price of agricultural and horticultural products. Risk of sporadic or limited supplies can expose the industry to rising prices and reputational damage if consumers associate a company with a degraded environment.

The UK is committed under the Kyoto Protocol to reduce greenhouse gas emissions by 12.5% by 2008-2012, relative to 1990. In addition, the government has set a higher domestic goal of cutting carbon dioxide emissions by 20% by 2010. Energy efficiency will play a large role in achieving these goals. The private and public sectors alike, are expected to contribute; achieving reductions of around 6 million tonnes of carbon a year by 2010.

The food industry is a major energy user, accounting for around 14% of UK energy consumption by UK businesses (excluding the transport and energy industries, as well as the public sector)<sup>2</sup>. By using less energy, companies can cut costs and reduce emissions of carbon. The UK's Food Industry Sustainability Strategy states that the food retail sector could achieve energy savings of up to 25% over 10 years. This could be achieved through improved management and maintenance practices, more efficient refrigeration, more efficient fuel utilisation, improved lighting systems and integrated heating, ventilation and air conditioning.

#### • Sustainable agriculture

Encouraging sustainable agriculture practices could reduce the environmental impact of the food chain. As the food supply chain has spread to developing countries, so too has the use of intensive farming methods such as irrigation, application of fertilisers and pesticides, and battery farming. Such efforts to increase yields carry risks of negative environmental and social impacts, as well as long-term financial costs to farmers. Impacts can include:

- Soil degradation and erosion resulting in reduction of soil fertility and associated loss of income for farmers.
- Water resource depletion and/or pollution resulting in, for example, health and water access issues for local communities.
- Pollution arising from high inputs of chemical fertilisers, pesticides and energy.
- Low quality jobs and poor labour conditions.
- Loss of biodiversity due to degradation of the surrounding environment.

An unsustainable food production system, from both an environmental and socio-economic perspective, is becoming a concern to companies, which associate un-predictable supply chains with higher costs. Over time, pressure for high output at low prices can reduce food quality, damaging brand and company reputations.

Companies can help suppliers to meet sustainable farming standards by encouraging agricultural techniques, which minimise environmental and social costs. Companies can also play a role in assisting the transfer of innovative technology and ideas through their supply chains to help farmers produce higher quality products. This may come about through the development of relationships with suppliers for direct sales of produce through long-term contracts with guaranteed minimum prices. Another example could be to encourage the use of biological pest management techniques to reduce the use of pesticides. Holistic techniques, such as these, result in a higher, more secure income for farmers. They can also result in a reduction of negative environmental impacts, as well as provision of secure, high quality supplies for companies.

- **Food transportation**

Food transportation accounted for 1.8% of total UK carbon dioxide emissions in 2002. Changes within the industry that have occurred in the last fifty years have sparked concern that the external costs associated with the transportation of food are not included in the actual price of the good purchased. External costs include greenhouse gas emissions, air pollution, noise pollution, traffic congestion, accidents and infrastructure. Research commissioned by the Department for Environment, Food and Rural Affairs (DEFRA) has estimated that the external costs of UK food transportation equates to just over £9 billion per year.

These external costs are increasing as a result of:

- globalisation of the supply chain, combined with decreasing transportation costs and improving technology making it economically viable for companies to transport goods over long distances;
- global sourcing enabling fresh produce to be stocked all year round, offering consumers more choice;
- the development of supermarket regional distribution centres leading to an increased use of larger Heavy Goods Vehicles (HGVs) to distribute goods;
- the development of out of town supermarkets increasing shopping trips by car;

The challenge for the industry going forward is to provide efficient distribution of food and drink to consumers that takes due account of the associated environmental and social costs incurred across the life cycle of a product. With the high price of oil, efficient distribution of products will also help to keep input

costs at a minimum. Transporting products more efficiently will reduce carbon emissions and improve commercial performance. Two ways that food retailers can reduce the negative external costs associated with food transportation are highlighted below.

*(i) Efficient fleet utilisation:* By optimising the effectiveness of fleet vehicles both environmental and financial benefits can be achieved. To ensure effective fuel management, the most fuel-efficient vehicles for the job should be purchased. Factors to consider include the most appropriate fuel and the optimal fleet size. Effective route planning can contribute to efficient fleet utilisation, reducing fuel costs and pollution by avoiding unnecessary journeys. This can also help to minimise traffic congestion. Effective route planning can also increase staff time available for productive work. All decisions made in regards to efficient fleet utilisation should consider the overall energy impacts of alternative options.

ASDA's website highlights the issue: "It is obviously in our best interest to keep fleet transport costs to a minimum; fuel is a major part of these costs. In 2005, we made significant progress in reducing road miles through improved vehicle utilisation and a movement from freight to rail."

#### **Guardian article, 27th May 2006**

The Guardian, on May 27th, 2006, reported that Tesco, in an attempt to improve its green credentials, announced plans to move goods off the road and on to the rail network. The supermarket chain plans to start moving non-food products by rail. By the end of this summer, Tesco expects to have this in place for transportation from the Midlands to its main Scottish distribution centre in Livingston. Tesco will be using "purpose-built green trains" imported from Canada, which will replace twenty lorry journeys a day. The company said it would reduce carbon dioxide emissions by about 6,000 tonnes a year, and "make sure goods are transported in the most environmentally friendly way". The initial investment is only £3.2m, but, if it proves a success, the trial may be extended to other routes.

*(ii) Sourcing products locally:* Sourcing from local produce helps to reduce food transportation. Offering locally grown produce means consumers can choose to buy food that is in season or produce that has not travelled large distances. Companies can help to develop relationships with local suppliers by ensuring that buying teams are aware of the opportunities for working with local food producers. Potential suppliers may need assistance with adhering to quality, consistency and volume requirements of supermarkets. Retailers also need to demonstrate their commitment to locally sourced produce by making shelf space available.

- **Waste**

The UK produces around 10 million tonnes of packaging waste every year, most of which is destined for landfill sites. Waste impacts the environment in a number of ways. This includes loss of valuable resources, the need for landfill space and release of methane into the atmosphere from composting waste. Methane is one of the greenhouse gases said to contribute towards climate change. The food industry produces and handles a wide range of wastes. The sector accounts for about 10% of all industrial and commercial waste. Packaging waste is a significant contributor. Some packaging is necessary, for example, that which is required to protect products from damage and contamination. Some products need packaging that is tamper-evident and child-resistant. Packaging can also provide detailed product information. However, much of the waste generated by households starts as food packaging bought from supermarkets. Therefore, the food industry is in a unique position to influence household behaviour, for the better, through packaging design and provision of consumer information. Store-based activity such as waste recycling collection points can help reduce rubbish sent to landfill.

Reducing waste can also contribute towards minimising costs. Currently the industry carries substantial obligations, linked to EU rules, to undertake or to pay for recovery and recycling of packaging wastes. The challenge for the food industry is to reduce the amount of food and packaging waste that is produced each year, both by the industry itself and by consumers of their products, without compromising food safety. A further challenge is to recycle or otherwise gain value from the waste that does arise.

#### **Financial Times article, 21 June 2006.**

The Financial Times on June 21, 2006, reported that the National Federation of Women's Institutes is "in talks" with retailers in regards to reducing food packaging. This is following the launch of its campaign to reduce excess waste. Supermarkets, including Asda and Tesco, said they would respond to the federation's demands, although they pointed out that some packaging is essential to maintain freshness and keep products clean and safe. The companies stated that they have already been trying to reduce packaging, in part because of the cost benefits. Sainsbury's is already using fully compostable wrap on organic fruits and vegetables in 140 of its stores. The Co-op and Tesco are both in the process of reducing the amount of cardboard used to package their own-brand products. They are also aiming to make all their carrier bags fully bio-degradable, or have already done so. Marks & Spencer is the leader in recycling packaging. The company won the 2005 Tetra Pak Environmental and National Recycling award.

During the quarter, the media reported that the UK supermarket, Waitrose, began efforts to reduce biodegradable waste by selling "ugly" fruit, at a discounted price. "Ugly" fruit is the same as "normal" fruit, albeit, the shape is imperfect.

## **Social matters**

- **Nutrition and health**

The nutritional content of food and its impacts on health is a growing concern to consumers. Poor nutrition is a major cause of ill health and premature death. Cancer and cardiovascular disease, including heart disease and stroke, are the major causes of death in England, together accounting for almost 60% of premature deaths. According to the National Cancer Institute, about one-third of all cancer deaths are thought to be caused by a poor diet. Though the exact links between diet and cancer remain unclear, researchers have found that a diet high in fat increases the risk of cancer, especially colon cancer. Research has also found that a low-fat diet, including lots of fruits, vegetables and whole grains, appears to lower cancer risk.

Unhealthy diets, along with physical inactivity, have also contributed to the growth in obesity. According to the UK Food Industry Sustainability Strategy, 22% of men and 23% of women in England are obese. This equates to a trebling of numbers since the 1980s. Obesity is also a growing problem with children and young people. In England, around 16% of 2-15 year olds are obese. The rise in obesity is occurring on a global scale. The National Cancer Institute reports that nearly one-third of all adults in the US are classified as obese. The World Health Organization (WHO) estimates that the global total of obese people has risen dramatically in the last ten years, from 200 million in 1995 to over 300 million in 2005.

Obesity is associated with health problems including hypertension, heart disease and Type II diabetes. The condition is responsible for an estimated 9,000 premature deaths per year in England. It is estimated that the treatment of ill health from poor diet costs the National Health Service at least £4 billion per year<sup>3</sup>. The surge in obesity and associated conditions has led to growing pressure to reduce fat, sugar and salt in products. It has also led to a tightening of regulations and controls in relation to food marketing, particularly marketing aimed at children.

The food retailers can help to bring lasting improvements to the nutrition and health of people by working in partnerships with Governments and other stakeholders. Offering consumers the choice to buy healthy food or products is key. Making shelf space available for "functional foods" is also important. Functional foods are products enhanced with natural ingredients designed to provide specific health benefits beyond basic nutrition. Products must be supported with information and advice for consumers.

<sup>3</sup> DEFRA: Food Industry Sustainability Strategy, April 2006

### **Financial Times article, 21 June 2006.**

The Financial Times, on June 8, 2006, reported that Disney has begun licensing fresh fruit in European supermarkets in an effort to erase the memory of its former association with MacDonald's. According to the article, Disney branded Satsuma mandarins are available in Tesco. Disney recently decided not to renew a ten-year global promotional contract with MacDonald's. Chairman of Disney Consumer Products, Andy Mooney, explained that the company wanted to be associated with "healthier" areas of the food business.

#### **• Labelling – making informed choices**

Consumers can contribute to their own health and wellbeing through food purchasing decisions. The industry can help to enable healthier choices by providing information and advice on products sold. Clearly and simply labelled food enables customers to make informed decisions. The UK Food Standards Agency (FSA) is currently in the process of adopting consistent and clear standards for information on food. The FSA has recommended a nutritional labelling scheme that uses traffic light colours to show high, medium and low levels of key nutrients. A red logo would signify a high content of salt, sugar or fat. Amber would suggest that moderate consumption is recommended, while green would signify the healthiest options. The system is designed to enable consumers to see, at a glance, which foods can make a positive contribution to a healthy diet and which foods are recommended to be eaten only in moderation or sparingly. Information is based on a set of nutritional criteria for salt, fat and sugar levels. Guidance to portion sizes will also be indicated.

The scheme has received a mixed response from the food retailers. Sainsbury's and Waitrose are bringing in the recommended traffic light coded labels. ASDA is reported to be following. However, six major food suppliers, including Tesco, have rejected the labelling scheme. Instead, they have opted for labels which show recommended guideline daily allowances (GDAs) of nutrients such as fat, saturated fat, sugar and salt. Tesco believes that GDA labels are easy to understand and states that sales data already shows they are leading customers to make healthier choices.

Consumers can make a contribution to achieving sustainable food production through their purchasing decisions. Labelling can help promote sustainable purchases by providing information about the origins of the product and highlighting how far it has travelled.

#### **• Food safety**

Food safety is a primary concern to consumers. Strict cleanliness and food handling rules are enforced throughout the European Union. Maintaining and enhancing public trust and confidence in the safety of the food supply is a top priority. A scare in relation to a food safety matter can cause consumers to react quickly and relatively minor health scares can have a disproportionate impact on sales. Food retailers with international supply chains must be careful to ensure European Union standards are maintained in order to avoid legal action and damage to reputation.

#### **• Ethical trading**

Ethical trade covers a range of practices that promote and protect labour standards, environmental standards and the livelihood of small-scale producers. Growing public interest in the impact of business operations on workers in developing countries has brought ethical trade to the attention of investors and other stakeholders. Practices throughout supply chains that promote and protect labour and environmental standards are increasingly a focus for businesses and shareholders.

There is a potential link between buying pressures and unacceptable behaviour by suppliers. The need to produce goods quickly can lead to excessive working hours in an attempt to meet demand. Issues around flexibility and seasonality can affect a supplier's ability to provide secure and regular employment. The search for lower prices can mean manufacturers want to keep labour costs at a minimum. Cost pressures may also lead to a lack of investment in health and safety measures. Exposure of abuses of workers and/or the environment involved in the production process may present a risk to brand reputation and could influence the purchasing decision of concerned consumers.

Customers want assurance that businesses are responsible, fair and honest. An increasing number of customers want to know that products have been sourced ethically and sustainably. Negative reputations gained through poor relationships with suppliers can directly impact profitability. According to the Co-operative Banks Ethical Purchasing Index, the cost of consumers switching brands for ethical reasons in 2003 was £2.6 billion. 52% of consumers boycotted at least one product in that same period. Two thirds said they would never return to a product once it had been associated with unethical practices.

Managing supply chains to maximise flexibility, efficiency and profitability, while upholding commitments to sustainable business practices, can be a substantial challenge. Some companies have adopted responsible sourcing policies, which aim to meet recognised international standards. Companies can also adopt and uphold best practice ethical trading management systems. Key features of such a system include a Board approved policy, Board level oversight of the implementation of that policy and sufficient resources being allocated to implement their commitment through, for example, stakeholder engagement and staff training.

Last quarter's SRI Focus looked at some of the issues surrounding supply chain management. The report discussed the benefits of responsible sourcing practices and summarised the current multi-stakeholder initiatives and guidelines of best practice for labour standards in the work place. In summary, benefits of responsible sourcing include:

- an increased ability to attract and retain customers;
- an ability to command a price premium for goods produced under fair-labour conditions;
- an increased ability to attract capital;
- a reduction in the risk of trade sanctions;
- enhanced worker productivity;
- a reduction in operational risks.

For more information, please refer to the Q1 2006 Corporate Governance and SRI Report<sup>4</sup>.

A negative aspect of improving standards in the supply chain is that, in some instances, retailers may pass on to their suppliers the costs associated with adhering to certification levels and/or global standards. In some cases it can be argued that suppliers face the costs while supermarkets reap the benefits.

The Fairtrade mark is a consumer label that appears on products as an independent guarantee that disadvantaged producers in the developing world are getting a better deal. Fairtrade products guarantee that developing world farmers are paid a price that covers the cost of production, plus a premium to be spent on community projects. This is often vital in bringing stability to many small suppliers in developing countries.

By stocking Fairtrade products, food retailers can play a role in ensuring that small-scale producers are not excluded from international trade and that all food producers receive fair prices for their products. Tesco introduced their own-brand Fairtrade range in 2004. The Tesco 2006 Corporate Responsibility Review states that in Tesco supermarkets in the UK, one in three customers purchase Fairtrade products.

#### **Comment from Newton's Food Retail analyst: Rosie Bichard**

Having covered the food retail sector for the last four years, I find it remarkable what a major shift in stance on these issues we have seen just in the last twelve months from the leading food retailers – or at least, how seriously they are now being taken. In the past, the focus was all about providing decent quality, but above all cheap food for consumers. Now the debate has clearly shifted and nutrition, organic food, ethical sourcing, recycling, energy conservation and community initiatives have now all come firmly into the mainstream and are being championed by business leaders. Most of this is due to rising consumer interest in these areas, but it is also partly in response to criticism from the media and politicians about issues such as market dominance and treatment of suppliers. Proving that you care has become a key way to reconnect with consumers. It also makes business sense, as categories such as fresh food, organic produce, fair-trade and locally produced foods are showing superior growth and should also represent relatively higher margin areas, and allow the retailer to differentiate their brand and their stores. Retailers who sell the products that consumers want to see on their shelves, at a fair price, and who can prove they are acting responsibly towards the community and the environment should see their business benefit. This should reinforce their attractiveness as investments for our clients, while tying in with the broader themes we consider as part of our long-term investment view.

<sup>4</sup> The Q1 Corporate Governance and SRI Report can be found on [www.newton.co.uk](http://www.newton.co.uk) Hard copies are available on request

## Company commitment

Newton engaged with the UK's four major food retailers to find out how the companies are managing some of the social and environmental matters that the industry faces. Responses are highlighted below. See page 35 for references and glossary of terms.

1. Do you have an ethical sourcing policy?	
Tesco	Yes. Tesco is a founding member of the ETI <sup>1</sup> and uses the ETI Base Code as the standard for its Ethical Trading Policy.
ASDA	Yes. ASDA is a member of the ETI.
Sainsbury	Yes. Sainsbury expects suppliers to conform to its Code of Conduct for Socially Responsible Sourcing. The company is a founding member of the ETI and the requirements of the ETI base-code are incorporated into Sainsbury's own code.
Morrisons	Yes. Morrisons has an ethical trading code but is not a member of the ETI.
2. How do you assess risk in your supply chain?	
Tesco	A risk-based approach is taken to managing labour standards in Tesco's supply chain. Three criteria are used: country risk, industry risk, and supplier risk. Supplier risk is based on the supplier's history with Tesco. Using these three criteria, suppliers are placed into high, medium or low ethical risk categories. For all suppliers, annual reviews in accordance with the SEDEX <sup>2</sup> health assessment forms are undertaken. For high-risk suppliers, as well as the annual review, a third party company carries out annual ethical assessments. For medium risk suppliers, ethical assessments are carried out every two years. 100% of high-risk suppliers are audited. Work on legal compliance, product safety, quality and capability for product development is also undertaken.
ASDA	Information not provided.
Sainsbury	The company undertakes site assessments to monitor compliance with its Code. A third party then audits high and medium risk suppliers. Repeat audits are carried out at various frequencies, depending on the risk level and the findings of previous audits. Sainsbury states, in its 2006 Corporate Responsibility Report, that it is extending monitoring further up its supply chain by auditing selected indirect suppliers. In addition, the company is working with some indirect suppliers to develop monitoring systems. Sainsbury is a founding member of SEDEX.
Morrisons	Information not provided.
3. What do you see as the most significant risks in your supply chain?	
Tesco	Tesco stated that continuity of safe and reliable products is the biggest business risk surrounding the company's supply chain. Ensuring that products are safe for consumption is imperative. The treatment of suppliers is also a key area. It is important the company knows that production is undertaken in a safe environment. Another key concern is the environmental impact of the company's sourcing.
ASDA	Information not provided.
Sainsbury	Sainsbury states that comprehensive mapping of its supply chain is a significant challenge. The challenge often goes beyond 'first tier' suppliers, particularly in primary or commodity areas where there are several tiers in the supply chain.
Morrisons	Information not provided.
4. How do you ensure your buying strategies do not exacerbate poor labour standards in the supply chain?	
Tesco	Mainly through the supplier auditing system. This enables Tesco to see where suppliers are failing to meet standards or methods of best practice. The company stated that where a breach occurs, its initial reaction is not to break the contract. Instead the supplier is asked whether it will work with Tesco to ensure it doesn't happen again. If this is agreed, Tesco will look to find the root cause of the problem and help the supplier to make the changes necessary to prevent the problem occurring again. For suppliers with no desire to improve working conditions, the relationship is likely to end. Tesco also provides technical expertise and knowledge through conferences, events, workshops and producer clubs. Tesco helps suppliers establish quality, environmental and labour standards.
ASDA	Information not provided.
Sainsbury	Sainsbury ensures that its buying teams are aware of the requirements on labour standards and that these are clearly communicated to suppliers at the outset of a trading relationship. If any issues occur, the company works with its suppliers to resolve them, in alignment with the ETI principles.
Morrisons	Information not provided.
5. Have you responded to the Carbon Disclosure Project <sup>3</sup> ?	
Tesco	Yes. In 2005/06 Tesco was the leading food and drug retailer in the CDP Leadership Index.
ASDA	No.
Sainsbury	Yes. All CDP requests have been responded to.
Morrisons	No.

<b>6. What initiatives are in place to reduce greenhouse gas emissions?</b>	
a) Through renewable energy sourcing:	
Tesco	Tesco is aiming to halve, by 2010, the average energy use in all its buildings against a baseline of 2000. The company is also looking to find cost effective ways to reduce emissions by generating energy through renewables and low carbon technology.
ASDA	ASDA's long-term aim is to source 100% of energy from renewable energy.
Sainsbury	Currently, energy supply agreements ensure 10% of electricity is from renewable resources.
Morrisons	Morrisons' policy is to reduce carbon dioxide emissions from energy used for building services through responsible energy sourcing. The company is working with the Carbon Trust <sup>4</sup> and Future Energy Solutions <sup>5</sup> to identify opportunities for improvements in efficiency and to eliminate waste energy.
b) Through improved management and maintenance practices to promote energy efficiency:	
Tesco	Over 2005, Tesco invested £20million in a range of energy-saving schemes that are estimated to save £8.1 million in energy costs, and 58,000 tonnes of carbon dioxide emissions. The company is also establishing a £100 million fund for investment in sustainable environmental technology such as wind turbines, solar panels, combined heat and power, and, gasification.
ASDA	In 2005, ASDA spent £3 million trialling energy efficient technologies in lighting, boiler controls and refrigeration. ASDA aims to continually improve store design to increase efficiency in energy consumption.
Sainsbury	This year, Sainsbury won the Carbon Management City of London Liveable City Award. The group has already delivered carbon dioxide reductions in excess of 20% versus a baseline of 1997/1998. Using 2004 as a baseline, Sainsbury has set a new energy efficiency target to achieve a 5% reduction in carbon dioxide/m <sup>2</sup> , by April 2008. This is a challenging target as most of the major savings have already been made. Sainsbury works closely with The Carbon Trust to understand and improve energy performance.
Morrisons	Morrisons uses Optima, an energy management system, which has monitoring and targeting abilities aimed at reducing energy costs and consumption. 202 of Morrisons' stores are participating in long-term climate change programmes aimed at reducing carbon dioxide emissions associated with food preparation. Good practice guides outlining ways to reduce energy consumption are issued to all stores.
<b>7. What plans do you have to improve efficiency of food transportation?</b>	
Tesco	Tesco is reducing the number of times it delivers to Express stores each week and is improving the way it fills its vehicles. For example, Tesco is working with suppliers to ensure that vehicles do not make unnecessary return trips by travelling empty after making a delivery. The company has invested £2.8 million in double-deck trailers, which carry 67% more products per load. The company encourages suppliers to use these vehicles when making deliveries. Tesco also owns and operates a train that is used to transport goods for sale in Scotland. The train is designed to use both the East and West train lines to ensure delivery if a problem with the tracks is experienced. Tesco is evaluating options to switch lorry loads onto rail in other regions. Tesco also aims, whenever possible, to distribute products by sea freight rather than air.
ASDA	Since 2003, ASDA has been reducing road miles by moving more of its freight to rail. The company is planning to reduce road miles further by shipping 70% of non-food imports to a new import centre that is being developed in the North-East of England. Once opened, the facility will enable savings of two million road miles a year. ASDA participates in the 'factory gate' initiative where the company's own transport is used to collect products from suppliers on their return trip after delivering to stores, thereby maximising utilisation. ASDA has also formed the "Carbon Club" with 11 of its major suppliers. The club aims to identify opportunities to reduce energy consumption and increase energy efficiency in the supply chain.
Sainsbury	Along with targets to improve fuel consumption, reduce road miles and improve vehicle utilisation, Sainsbury is gradually renewing its vehicle fleet and is using this opportunity to switch to more efficient engines. Sainsbury also works in partnership with its suppliers to minimise trips with empty vehicles.
Morrisons	Information not provided.
<b>8. What plans do you have to source more products locally?</b>	
Tesco	Tesco stocks British produce whenever possible. Currently, 97% of fresh chicken, 95% of fresh beef, 92% of fresh pork, and 88% of fresh lamb, is British. All fresh shell eggs and organic milk come from British farms. Products are clearly labelled to show which country food comes from. Tesco is working with British farmers to extend growing seasons so that they can sell more British produce. The group also hosts open days, in every region, offering small suppliers a chance to meet buyers and to gain access to the company.
ASDA	90% of the fresh food sold that can be sourced from Britain, is sourced from Britain.
Sainsbury	Information not provided.
Morrisons	Information not provided.

9. What plans do you have to reduce packaging waste?	
Tesco	In 2000, Tesco began using reusable plastic crates to replace cardboard boxes and other packaging used to transport and display products. The crates have subsequently been adopted widely in the company's supply chain. Along with the use of these crates, the company has packaging reduction projects such as merchandising units and targets to reduce the weight of packaging used. A "Packaging Strategy Group" also focuses on ways to reduce the impact of packaging. Tesco signed the Courtauld Commitment <sup>6</sup> in 2005.
ASDA	ASDA's packaging policy is to ensure that the weight and volume of packaging is limited to the minimum adequate needed to maintain the necessary level of safety, hygiene and quality for the packed product. In 2005, ASDA signed up to the Courtauld Commitment and is working in partnership with the Government's 'Waste Resources Action Programme' (WRAP) <sup>7</sup> to achieve a shared objective of reducing household waste.
Sainsbury	Sainsbury has a packaging strategy that ensures packaging is fit for purpose while also encouraging a move towards compostable packaging and use of materials that Local Authorities prefer to collect for recycling. Sainsbury aims to reduce overall packaging by 5% by 2010.
Morrisons	One of Morrisons prime objectives is to prevent the generation of waste, wherever possible. Avoidance is preferable to recycling. The type of waste generated is monitored. In addition to complying with the Producer Responsibility (Packaging Waste) regulations <sup>8</sup> , Morrisons is working to find innovative packaging solutions to eliminate or reduce the need for packaging. This is in line with the shared objectives of the Courtauld Commitment.
10. What are you planning to do to improve labelling on food to allow consumers to make more informed purchasing decisions?	
Tesco	Tesco has committed to have Global Daily Allowances (GDAs) on all Tesco own-brand food by the end of 2007.
ASDA	Information not provided.
Sainsbury	In January 2005, Sainsbury launched the "Wheel of Health" labelling system – a colour coded, traffic light system. The labelling system is inline with the FSA recommendations and is currently being rolled out across all own-brand products with the exception of staples and children's products.
Morrisons	Morrisons is currently amending its own brand labelling to include GDAs for energy, protein, carbohydrates, sugar, fat, saturated fat, fibre, sodium and salt.

#### <sup>1</sup> ETI: Ethical Trading Initiative

Founded in 1998, the Ethical Trading Initiative (ETI) is an alliance of businesses, non-governmental organisations and trade unions whose objective is to improve labour standards in supply chains. By signing up, companies agree to conform to high levels of labour standards, including the avoidance of child labour, forced labour, sweatshops, adverse health and safety conditions, and violations of labour rights.

#### <sup>2</sup> SEDEX: Supplier Ethical Data Exchange

Sedex is a web-based system for suppliers to input data on labour standards at their production sites. The system has been designed to allow the sharing of information to prevent companies being audited repeatedly and thus the duplication of information. The development of Sedex has been supported by a group of UK retailers and suppliers, including Geest, Marks & Spencer, Northern Foods, RHM, Sainsburys, Tesco, Uniq and Waitrose.

#### <sup>3</sup> The Carbon Disclosure Project (CDP)

The CDP is a coordinating secretariat for institutional investor collaboration, relating to climate change. Its aim is twofold: to inform investors of the significant risks and opportunities presented by climate change, and to inform company management of shareholders' concerns relating to the impacts of these issues on company value. The project involves sending a request for information to the largest companies in the world and collating responses. In 2006, over 1900 companies were contacted.

#### <sup>4</sup> The Carbon Trust

The Carbon Trust is an independent company funded by the UK Government. The aim of the company is to help the UK move to a low carbon economy by helping business and the public sector reduce carbon emissions and capture the commercial opportunities of low carbon technologies.

#### <sup>5</sup> Future Energy Solutions

Future Energy Solutions is part of AEA Technology. The group is a sustainable energy consultancy that aims to help public and private sector organisations find answers to the growing challenges of sustainable energy, climate change and related environmental issues.

#### <sup>6</sup> Courtauld Commitment

The Courtauld Commitment is a government sponsored initiative with the following objectives:

- To design out packaging waste growth by 2008;
- To deliver absolute reductions in packaging waste by March 2010;
- To identify ways to tackle the problem of food waste.

Thirteen grocery retailers have signed up to the Commitment: Asda, Boots, Budgens, the Co-operative Group, Londis, Iceland, Kwik Save, Marks & Spencer, Morrison's, Sainsbury's, Somerfield, Tesco and Waitrose. The commitment works in partnership with WRAP (the Waste & Resources Action Programme). Those that have signed the Courtauld Commitment also pledge support to WRAP.

#### <sup>7</sup> WRAP: Waste Resources Action Programme

WRAP (the Waste & Resources Action Programme) was established in 2001 in response to the UK Government's Waste Strategy 2000 to promote sustainable waste management. WRAP and the Courtauld Commitment work in partnership.

#### <sup>8</sup> Producer Responsibility (Packaging Waste) regulations

The European Commission Directive on Packaging & Packaging Waste aims to minimise disposal of packaging by setting targets for recycling and recovering packaging waste. From 2001, the Directive targets require that at least 50% of the UK's packaging waste must be re-utilised through recycling and other recovery methods. The UK has implemented the Directive through two sets of Regulations.

- i) The Packaging (Essential Requirements) Regulations 1998 which require that packaging be minimised, that it be capable of recovery and recycling and that it contain only restricted amounts of certain hazardous substances.
- ii) On 1 January 2006 the new Producer Responsibility Obligations (Packaging Waste) Regulations 2005 came into force. The 2005 Packaging Regulations consolidate the original Regulations and incorporate the changes made to the Regulations in 2005 as a result of public consultation.

These Regulations place obligations on all UK companies that have a turnover exceeding £2 million and that handle more than 50 tonnes of packaging per annum.

## Conclusion

Consumer concerns about the environmental and social impacts arising from food production and transportation are growing. Companies are increasingly driven to integrate plans for sustainable development of the world's natural resources into corporate strategies and responsibilities. Due to their size, global reach and role as food providers, the food retailers carry significant social and environmental responsibilities. They are also in a position to influence change through their relationships with suppliers and the information that is provided with products. Consumer behaviour can also be influenced. For example, waste minimisation strategies can help reduce negative environmental impacts. The benefits of being socially responsible include reduction of reputational risk, enhancing brand value, stimulating innovation, improving staff efficiency and morale, and better consumer and community relations. Cost reductions can also be secured through energy efficiency and waste reduction. Retailers should reap tangible benefits if they sell products that consumers want to see on their shelves, at a fair price, and prove that they are acting responsibly towards the community and the environment.

## Next quarter

Next Quarter's SRI Focus will look at some of the social, ethical and environmental matters that surround the pharmaceutical sector.

# SRI Activity

Please note that this activity log shows examples of SRI activity and engagement undertaken over the quarter. It is not an exhaustive list of all engagement. A complete list of how Newton voted on securities during the period is available upon request

## Hanson

### **Subject: Disclosure of social, ethical and environmental considerations**

#### **April 2006**

Newton contacted Hanson regarding the limited level of reporting on Social, Ethical and Environmental (SEE) matters that impact the company. Newton raised the same concern with the company one year ago. Despite this, Newton felt that reporting had not significantly improved. Hanson stated that information on health, safety and environmental performance is already measured and collected. However, the information is not made publicly available. Hanson is planning to improve this going forward, predominantly through offering more information on its website. In response, Newton highlighted to the company what SEE information it would expect from a Construction & Building company. After giving Hanson an opportunity to respond to concerns over the past year, Newton voted against accepting the company's annual report and accounts, based on the limited level of reporting on SEE matters.

## Rank

### **Subject: Disclosure of social, ethical and environmental considerations**

#### **April 2006**

Rank currently produces limited information on its management of SEE matters that can potentially impact its business. Newton considers the company's disclosure to be inadequate given the significant ethical issues that surround the gambling industry. Newton contacted the company in order to gain assurances that it was managing SEE risks and that future reporting would be improved. Rank agreed that reporting on SEE matters should be improved going forward. In 2005, the company underwent an assessment by GoodCorporation\*. The information from this assessment should help Rank to determine what areas of reporting need improvement. Newton outlined its approach to monitoring and recording investee companies' disclosure on SEE matters and how this approach is translated into the exercise of voting rights on behalf of Newton's clients.

## Royal Dutch Shell (RDS)

### **Subject: Shareholder resolution**

#### **May 2006**

RDS held its AGM on May 16th, 2006. The agenda contained a shareholder resolution raised by the Ecumenical Council for Corporate Responsibility (ECCR). The resolution was requisitioned due to concerns surrounding the ability of RDS to successfully manage projects. RDS has recently suffered criticism in relation to cost overruns, drilling delays and poor community relations. These have led, in some instances, to loss of shareholder value. The company's commitment to safety and environmental standards has also been criticised.

Though Newton agreed with the proponents underlying concerns, votes were instructed against the resolution. Certain elements of the resolution seemed impractical and likely to delay the implementation of various worthy projects. Newton believes that the current policies and procedures of RDS, in regards to the management of safety, environment and social performance, already address most of the issues contained within the resolution. However, Newton did acknowledge that there have been situations where the company has failed to meet these standards.

Newton took the opportunity to write to the company, on behalf of its clients, to highlight two suggestions proposed by the ECCR, that it felt warranted further attention. Newton encouraged more use of independent social and environmental impact assessments and greater disclosure of evidence to demonstrate how policies, procedures, and standards on environmental and social matters are enforced at all stages of project planning and operation. This could help to ensure that good intentions are transformed into measurable corporate performance.

\* GoodCorporation provides independent and confidential assessments of business' to help protect reputations and promote responsible business practices.

## **Weir Group**

### **Subject: Disclosure of social, ethical and environmental considerations**

#### **May 2006**

Weir Group has been making small improvements in its SEE reporting over the last five years. However, Newton felt that the level of reporting remained insufficient given the SEE matters that can impact the engineering sector. The company stated that it does collect information regarding health, safety and environmental performance. However, the information is not shared internally or externally. Management is currently looking at key performance indicators for best practice in this area. Going forward, the company hopes to disclose information in line with best practice. Newton outlined its approach to the monitoring and recording of investee companies' disclosure levels on SEE matters and how this approach is translated into the exercise of voting rights on behalf of Newton's clients.

## **Davis Service Group (DSG)**

### **Subject: Disclosure of social, ethical and environmental considerations**

#### **June 2006**

Newton contacted the company given its limited level of reporting on SEE matters. Since May 2005, the company has been performing a detailed review to identify significant SEE risks that might impact on the short and long-term value of the company. Newton requested an update on how this review was progressing and what plans the group has for reporting in 2006 and beyond. Specifically, Newton requested information on what SEE risks the company perceives to be the most important, how policies are integrated into management systems, and how policies are monitored and measured. In response, Davis Service Group provided further information on its corporate social responsibility policies, giving Newton some comfort regarding integration of SEE matters into internal systems and controls. The company also stated that reporting on SEE matters is continuously evolving. Newton encouraged production of future publications that address SEE matters in more detail. Newton also outlined its approach to the monitoring and recording of investee companies' disclosure levels on SEE matters and how this approach is translated into the exercise of voting rights on behalf of Newton's clients.

## **Attendance at corporate responsibility updates**

### **Subject: Investor updates**

Over the quarter, Newton attended investor updates on corporate responsibility for BAE Systems, Akzo Nobel, Statoil, Royal Dutch Shell, Anglo American, O2 and Pearson, Reed Elsevier.

# Company Meeting Log: Q2 2006

During the quarter, Newton analysts and fund managers had individual meetings with the management of 296 companies to initiate or maintain dialogue around financial performance and/or responsible investment matters. The insights gained through this engagement are used when making investment decisions. Meetings were held with the following companies:

3M	Diageo	Lotte Department Store	SAMSUNG Electronics x 2
Acciona	Diagnosticos da America	Lukoil	SAMSUNG Heavy Industries
Accor	Digi	Lundbeck	Samsung Techwin
Acom	DynCorp	Macquarie Korea Infrastructure Fund	Scottish & Southern Energy
Actelion	Earthlink	Macquarie Trust	Scottish Power
Advanced Info Service x 2	Eaton	Makhteshim-Agan	Scuderi
Aeterna Zentaris	Edwards Lifesciences	Man Group	SEEC Media
Agcert	EFG Eurobank	Marshall & Ilsley	Seoul Semiconductor
Air Products	Electra Active	MasterCard	Serono
Alcatel	Elpida	Max Re Capital	Severn Trent
Alcon x 2	Enel	Maxis Communications x 2	Shanks
AllianceBernstein	Erinaceous	Maybank	Sherwin-Williams
Alphatec	Exxon Mobil	McGraw-Hill	Shinhan Financial
aQuantive	Far Eastone Telecom	Medicure	Shire Pharmaceuticals
Ark Therapeutics	Femsa Beer	Melrose Resources	Shoppers Drug Mart
Arpida	First Choice Holidays	Mexichem	Signet
Associated British Foods	FirstGroup	Mitchells & Butlers	Silex
AWG	FKI	Mobile Telesystems	Singapore Telecom
BAA	Flowserve	National City	Sinochem
Babcock & Brown Wind	Fondiaria	National Grid	Sistema
Bachem	Fortune REIT	Neste Oil	SK Telecom x 2
Bank of Central Asia	Freeport-McMoRan	New Star Asset Management	Sykes Enterprises
Banyan Tree	Fullcast	Nextel International	Smith & Nephew
BASF	Gafisa	NHN	Societe Generale
Basilea Pharmaceutica	Gallaher	Nikko Cordial	S-Oil
BATM Advanced Communications	Gazprom	Niko Resources	Sony
BHP Billiton	Genting	Noble	SP Setia
Bio-Treat Technology	Geophysique	Nong Shim	Sprint Nextel
Boeing	Goldcorp	Northern Foods	SQM
Boots/Alliance Unichem	Goodman Fielder	Novatek	Standard Life
Braskem	Grainger	Novo Nordisk	Statoil
Brasil Telecom	Greenhill	NWS Holdings	Stericycle
Bridgewell	Grifols	Oncolytics Biotech	Steris
Brightpoint	Gulfands Petroleum	One Media	Syngenta
British Airways	Halfords	Paddy Power	Tate & Lyle
British Land	Harte-Hanks	Panalpina	Teck Cominco x 2
Britvic	Hengan International	Panin Bank	Tele Norte
BT	High Tech Computer	Parker-Hannifin	Television Broadcasts
Bunge	Hite Brewery	Parkway	Tesco
Burger King	Homex	Partner Communications	Thai Beverage
Bursa Malaysia	Hong Kong Economic Times	Petra Foods	The Restaurant
Cable & Wireless x 2	HORNBACK	Petro-Canada	Tianjin Port Development
Cameco	Humana	PLDT	Timken
Canadian Pacific Railway	Hutchison Telecom International	PNC Financial Services	Tom Group
Canoro Resources	Hyosung	Polyone	Tullow Oil
Carpetright	Hyundai Department Store	Porto Seguro	United
Carphone Warehouse	Hyundai Development	Ports Design	United Overseas Bank
Casino	ICAP	POSCO	Valero
CCU	Imperial Tobacco	Praxair	Venture Production
Champion REIT	Inditex	Principal Financial	Verbund
Chaoda Modern Agriculture	Indosat	Promise	Viacom
Chevron	ING	Provident Financial	Vimpel Communications
China Life Insurance	Intermediate Capital	Prudential Financial	Viridian
China Netcom	International Power	Psvida	Vodafone
Clear Media	Interpublic	Punch Taverns	VT
CNOOC	Interserve	Puricor	Wacom
Coca-Cola FEMSA	Ithaca Energy	QinetiQ	Want Want
Coles Myer	ITW	Rally Energy	Washington Mutual
Compass	Jackson National Life Insurance	Reed Elsevier	Weir
Constellation Brands	Japan Tobacco	Renovo	Williams Companies
Cooper Cos	John Fairfax	Resolution	Wincanton x 2
Cruceil	Kangwon Land	Reynolds American	Wing Hang Bank
Curalogic	KeyCorp	Rockwood	Wolverhampton & Dudley
Daelim Industrial	Kingdom Hotels International	Rohm & Haas	Woongjin Coway
Dalian Port	Kirby	Rowan Drilling	Woori Financial
Datasul	KT Freetel	Royal & Sun Alliance	Workspace
Daum Communications	KT&G	Royal Bank of Scotland	WPP
Debenhams	LG.Philips	Royal Dutch Shell x 2	Xstrata
Denbury Resources	LG Telecom	Ryland	Yamaha
Dentsu	Lojas Americanas	S1	Yell x 2
Deutsche Postbank	Lonmin	SABMiller	Yum! Brands
Deutsche Wohnen	Lonza		

In addition, the analysts and fund managers attended a large variety of external meetings arranged by the companies or by brokers and other research providers.

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