

Annual Governance and Proxy Voting Report 2011

Corporate governance continued to garner media attention in 2011 with executive remuneration grabbing headlines along with fraud scandals such as that at Olympus. A year on from the implementation of the Dodd-Frank Act in the US and the UK Stewardship Code, attention remains on the role that asset management companies play in responsible investment and stewardship of companies.

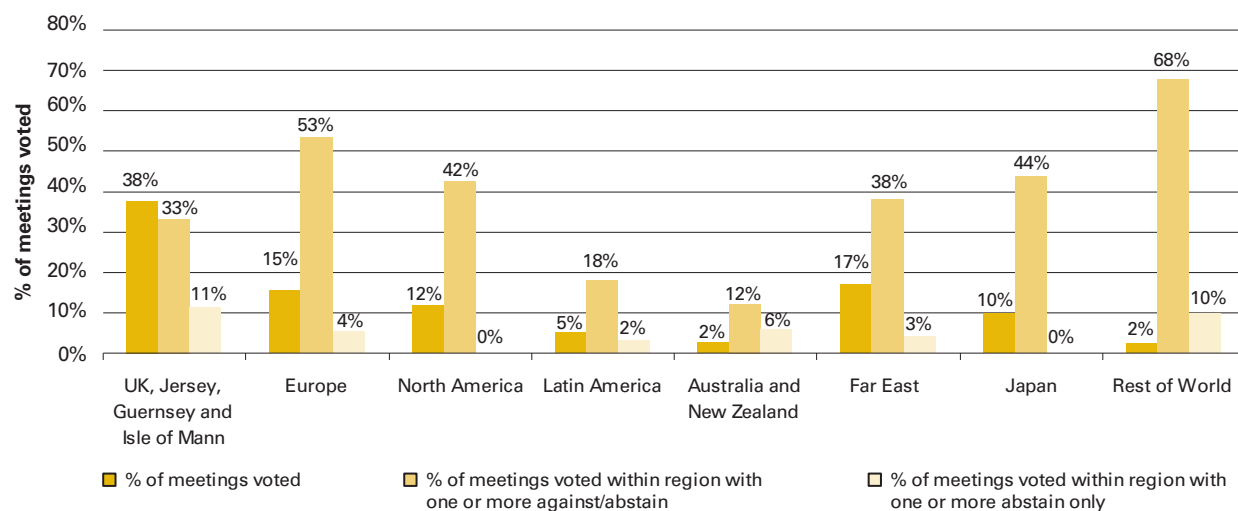
Threadneedle is fully compliant with the Stewardship Code and we have attended a number of updates from the Financial Reporting Council on the Code. We concur with the view that 2011 has brought about noted improvements in the discussion of the broader risk agenda, succession processes, reputational concerns and board composition and capabilities. Board effectiveness and diversity was a principle theme in 2011 that we expect to gain momentum in 2012. We note that many UK companies, following the Davies review, and pre-empting any potential European legislation enforcing gender quotas, are introducing formal plans to increase female representation on the board. Alongside this we find a greater willingness, particularly in Europe and the UK, to discuss board diversity in the wider context of skills, experience and geographical background.

A key tool for exercising active and responsible ownership is shareholder voting. During 2011 we voted at 1942 annual general and extraordinary meetings across our funds and regions. Threadneedle currently practice proxy voting in 50 markets globally representing most of its investment regions. However, for certain markets and product vehicles legal and logistical barriers remain. We work with industry bodies that lobby law-making institutions to take into account these barriers when amending or establishing new rules and regulations.

We aim to be as transparent as possible to the general public about how we vote and what our rationale is. Our main focus will always be the interest of our clients, who receive tailored and detailed reports throughout the year. Our website has links to Threadneedle’s company-wide corporate governance policies, which will shed light on what we apply as best practice guidance.

Vote Summary by Geography

The UK is our largest voting region, representing 38% of all meetings voted. The Far East follows with 17% of all meetings voted, Europe accounts for a further 15%, followed by North America at 12%, Japan with 10%, Latin America at 5%, with Australia, New Zealand and the rest of the world making up the remaining 5%.



Overall we voted against management or abstained on voting on one or more resolution at 39% of the 1942 meetings voted. The majority of meetings with votes against management were in the UK although this accounts for only a third of meetings voted overall in that market. We note a significantly higher incidence of dissent in Europe with 53% of meetings resulting in a vote against management or an abstention, likewise we observe a high frequency of dissent votes in North America (42%), the Far East (38%), Japan (44%) and Rest of the World (68%). The high frequency of against votes in the ‘Rest of the World’ category is primarily due to the inclusion of the Cayman Islands, Bermuda and South Africa in this category.

The lower frequency of against votes in the UK, together with the high level of abstentions, is owed in part to the on-going dialogue that we have with UK companies. Given our ease of access to UK companies and the relationships that have been built through engagement activities, as well as their pro-active highlighting of issues prior to voting, we find that we can more readily support proposals on a comply-or-explain basis. As responsible stewards we are proactively reassessing our engagement process to allow for a more even spread of engagement across our markets.

Each region has its own specific corporate governance challenges and issues. In Japan for example adequate independent representation on boards remains a contentious issue. In the Far East and 'Rest of the World' categories we note, in our opinion, that independence and transparency is often limited, while capitalisation proposals propose excessive issuance of shares. In the US market we oppose shareholder proposals that are not in our view in the interest of the company or minority shareholders. Following the introduction of the Dodd-Frank Act's 'say on pay' we have also opposed management at a number of meetings regarding the proposed occurrence of disclosure. In Latin America and the rest of the world, the difficulty is often a lack of transparency or the timeliness of proposals, which can mean that we do not have enough information to make a voting decision.

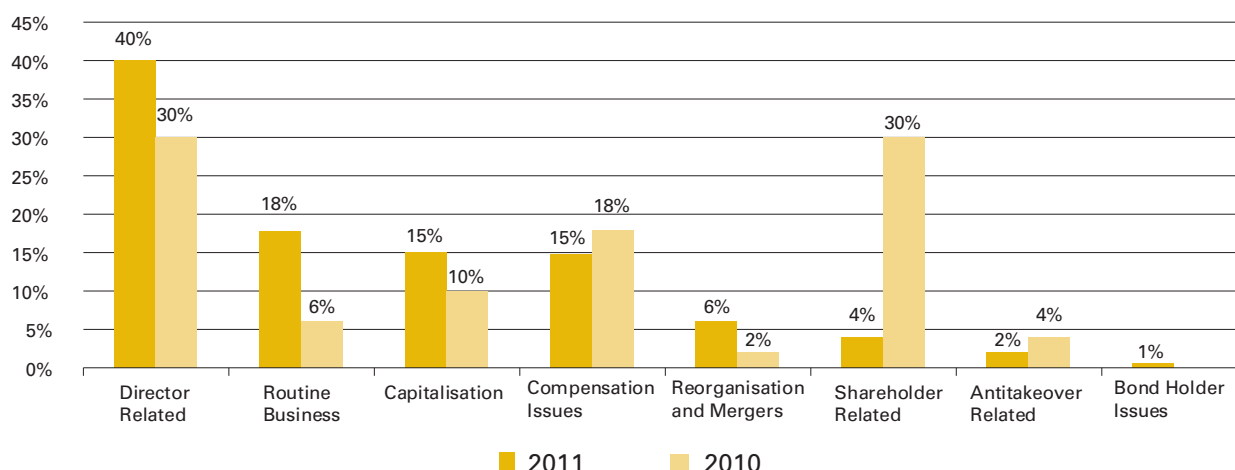
In Europe, we encountered a greater dissent rate than 2010. Trends seen in 2011 by our proxy providers showed that dissent increased in France on director elections, related party transactions, remuneration and share capital increases. Furthermore there has been an increase in anti-take-over concerns in Italy which we consistently oppose, while the Netherlands had more remuneration reports and amendments to articles of association which are sometimes controversial.

Breakdown of Major Reasons for Against Votes

At 39% of all meetings we voted against one or more resolutions, and abstained at 5%. This compares with 2010 when there were only 23% of meetings when we voted against one or more resolutions. Of the resolutions voted against, the majority (40%) were director related. The rest were primarily related to capitalisation, compensation issues and routine business.

Inadequate representation of independent directors, non-division in the roles of Chairman and CEO and non-independence of audit and remuneration committees are the key reasons for our decision to oppose or abstain on a director election. The introduction of new by-laws and approving auditor reports are issues that fall under routine business where we elect to oppose if we do not believe shareholder's interests are being preserved. Compensation and capitalisation remain contentious issues; however we are pleased to note a decrease in anti-takeover related issues in 2011.

Breakdown of Votes Against Management



Corporate Governance Engagement

More than a year on from the implementation of the UK Stewardship Code, we are pleased to report that we are meeting the code requirements and that we are an active investor in 50 markets.

We believe that good governance can have an impact on valuations and as an active shareholder we encourage good governance practices. We regularly meet with companies throughout the year and engage with them on governance issues that we consider important. Following meetings when we have opposed or abstained on resolutions at companies where we have significant holdings we generally send a letter to the management explaining our voting reasons and our discussions with Threadneedle's relevant fund manager. We take into consideration local market practices and the ability of companies to go beyond the minimum requirements set by local law to encourage improvements in governance. Engagement is a two-way effort with many of our companies consulting us as regards changes to remuneration practices as well as providing annual governance updates.

Effective engagement involves complex processes and many factors, such as transparent oversight, strong dialogue, relationship management and the clear communication of outcomes. Threadneedle is seeking to increase its international engagement efforts, and we are thus continually reviewing our engagement processes. In particular we have focused on increasing our engagement efforts in Asia and have this year undertaken a corporate governance study tour with the Asian Corporate Governance Association, as well as attending a number of meetings related to proposed corporate governance legislation changes in Japan.