

Pensioenfonds PNO Media
Engagement report

Q4
2009

Q4

This report contains a summary of the responsible ownership activities undertaken by EOS on behalf of its clients. It covers significant themes that have informed some of our intensive engagements with companies over the past quarter. The report also provides information on our voting decisions and the steps we have taken to promote global best practice, improvements in public policy and collaborative work with other shareholders.

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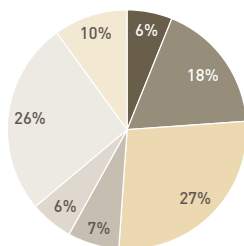
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Engagement by region

Over the last quarter we engaged with 101 companies held in PNO Media's portfolios on a range of 256 social, environmental and governance issues. EOS' holistic approach to engagement means that we will typically engage with companies on more than one issue simultaneously. The engagements included in these figures are in addition to our discussions with companies around voting matters.

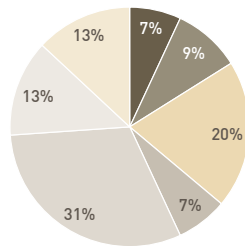
Americas

We engaged with 29 companies over the last quarter.



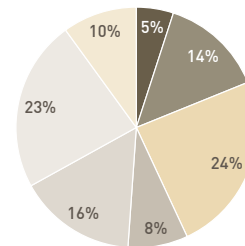
Asia

We engaged with 20 companies over the last quarter.



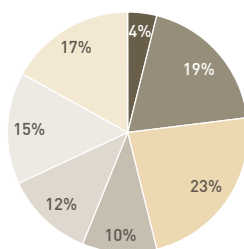
Europe

We engaged with 34 companies over the last quarter.



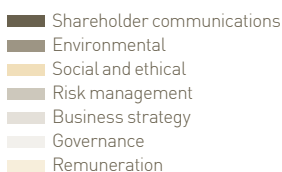
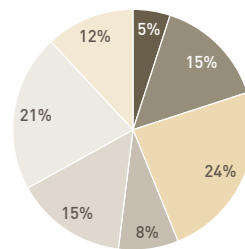
UK

We engaged with 18 companies over the last quarter.



Global

We engaged with 101 companies over the last quarter.

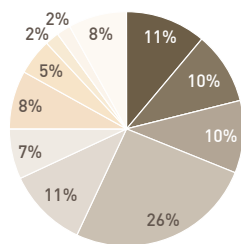


Engagement by issue

A summary of the issues on which we engaged with companies over the last quarter is shown below.

Social and ethical

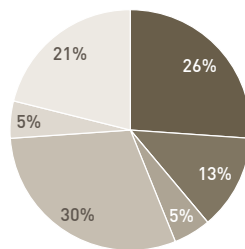
Social issues featured in 24% of our engagement over the last quarter.



- Employee relations
- Community relations
- Health and safety
- Supply chain
- Operations in troubled regions
- Corporate culture
- Political risk management
- Bribery and corruption
- Licence to operate
- Other ethical
- Other social

Environmental

Environmental issues featured in 15% of our engagement over the last quarter.



- Climate change/carbon intensity
- Water stress
- Oil sands
- Forestry
- Biodiversity
- Other environmental

Other engagement

Business strategy featured in 15% of our engagements over the last quarter.

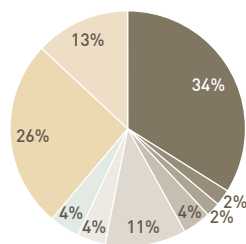
Remuneration featured in 12% of our engagements over the last quarter.

Risk management featured in 8% of our engagements over the last quarter.

Shareholder communications featured in 5% of our engagements over the last quarter.

Governance

Governance issues featured in 21% of our engagement over the last quarter.



- Board structure
- Committee structure
- Related party transactions
- Conflicts of interest
- Succession planning
- Poison pill
- Voting rights - not 1 share 1 vote
- Separation Chair/CEO
- Other governance

Governance: Business strategy and board structure

Strategic engagements

Many of EOS' most successful engagements combine discussions of business strategy and structural governance issues.

Statistics

Number of companies engaged with on strategic matters this quarter:	200
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Africa/Middle East	11
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Americas	47
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Asia	44
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Europe	64
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UK	34
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Number of significant steps forward in strategic/governance engagements this quarter:	15
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Africa/Middle East	2
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Americas	4
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Asia	2
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Europe	4
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UK	3
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Includes only companies which in this quarter have made substantive strategic or major governance changes.

Overview

EOS' holistic approach to engagement combines discussions on business strategy and risk management, including social and ethical risks, with structural governance issues. Our engagements fill the gap left by the investment industry's tendency to focus on the short-term. The result of this tendency is that management too often goes unchallenged in its approach to the long-term future of its business and there is minimal pressure for change. EOS assesses and engages with underperforming companies from a long-term perspective, asking questions which encourage management and boards to think afresh to overturn long-running periods of underperformance. This proven approach is often successful in adding value or ending destruction of value.

Business strategy is also a key feature of other engagements such as those highlighted elsewhere in this report. We are generally most successful in achieving change on environmental, social and other matters where we lead the conversation from a business perspective and focus on these issues as risks to the company's strategic positioning. Companies can become locked into historic patterns where they are overdue for refreshment and new perspectives on the board. Injecting new thinking at the head of the company – an independent chair or change of CEO – is frequently the key to unlocking change and driving renewed operational performance, creating long-term value for shareholders.

Engagements on governance and business strategy may require a series of meetings over months and years. It takes time for board changes to generate the business and strategic changes which improve long-term performance.



Highlighted sample engagements

We met with both the chair and SID from a major company from **Africa/Middle East** to discuss participation in further industry consolidation and succession planning. On consolidation we gained agreement that the company had paid generous premiums in the past and firmly encouraged greater discipline in any future deals, and discussed the details of how synergies will be effectively driven out of any transactions. We tested the issue of succession planning, a key concern at the company, and urged the board not to surprise the market and to mount a full external search for candidates, laying out our concerns about simply appointing insiders.

We began to see some progress in our ongoing engagement with a large company in the **Americas**. We met with a series of senior representatives at its headquarters and discussed a range of governance and strategic matters. In particular we discussed the combined roles of chair and CEO and won the first indication that this structure might not always be the best for the company; we flagged a way for it to approach the issue sensitively whilst also giving shareholders some confidence of change. We also highlighted our favoured response to the company's major underperforming business unit, and while we did not gain specific undertakings for change we believe that over time this will now be addressed.

We continued our engagement with a significant retailer in **Asia** on strategy, remuneration and governance matters. We tested the company's overseas expansion strategy, and questioned how possible it is to extend the company's brand successfully into other markets. We also talked through the immediate challenge of bringing certain regional operations into profit. On pay, given a lack of disclosure on performance criteria, we challenged the company on the extent to which management incentives are linked with the strategy and the creation of long-term shareholder value. We also highlighted succession planning for the CEO as a concern for investors, and probed the process for identifying and developing internal talent and that for attracting high potential individuals to the company.

We continued to press a major manufacturer in **Europe** with regard to significant related party transactions. We spoke with both the company itself and a major shareholder to gain reassurance that the relevant deals are being structured in such a way that they do not disadvantage minority shareholders, and strongly urged further disclosures on the structure of the deals and the fairness of the pricing for them. We also called for further detail on how the company effectively manages the ongoing conflicts of interest which it faces in its operations, and sought some oversight by independent directors of this area. Our public stance on this controversial issue was sufficient to wring some concessions from the company.

We met with the chair of a leading **UK** company with regards to succession planning and strategy. We were particularly keen to discuss governance given an apparently botched senior appointment which needed to be rapidly reversed. We talked through the prior process – which seems to have been rushed – and the qualities of the new candidate, who seems rather more appropriate for the role. On strategy, we questioned the structure of the business which does not seem sustainable and which includes some significantly underinvested activities; we pressed for changes as and when markets allow, and discussed capital structure and the need for the company to generate sufficient cashflow for its investment needs as well as maintaining the dividend.

Environmental: Copenhagen and beyond

Engaging policy makers and companies on climate change

EOS works on behalf of institutional shareowners with significant holdings in a broad range of companies. As such, EOS works to encourage public policy solutions which minimise the costs of climate change and maximise related opportunities across our clients' portfolios.

Statistics

Number of companies engaged with	79
Reassurance gained	33
Number of companies where substantive change sought	46
Number of these showing progress so far	19

'EOS publicly called for the world's politicians to put into place an institutional framework which places genuine constraints on carbon emissions.'



Overview

Beyond the potential macroeconomic impacts, EOS continues to be concerned about the effects of climate change and climate policy on its clients' investments. Companies are likely to be affected by regulatory and fiscal measures directed at reducing greenhouse gas emissions, and consumer or public pressure to take action on climate change. The costs for carbon intensive companies, in particular, are unlikely to diminish in the foreseeable future and those with low carbon energy mixes will be best positioned in the long-term.

In the build up to the United Nations negotiations in Copenhagen, along with 180 other institutional investors, EOS publicly called for the world's politicians to put into place an institutional framework which places genuine constraints on carbon emissions, driving higher carbon prices which, in turn, will change behaviours. In EOS' view the longer the world waits to take action the more the costs of climate change will rise. Any delay in reducing emissions significantly increases the risk of severe climate impacts as it locks in more carbon-intensive infrastructure and development pathways. EOS urged boldness from the climate change negotiators in order to send a strong signal to capital markets and help encourage carbon prices to be built into investment decisions by companies and institutions, so that the global economy can begin to develop into a low carbon economy in a cost-effective and efficient way.

EOS set out the three key elements investors require from policy makers. Firstly, a long-term global target for greenhouse gas emission reductions. This is essential to give investors and portfolio companies confidence about the future direction of climate policy and facilitate a smooth transition from the current policy framework that ends in 2012. Secondly, measures that support the development of an effective global carbon market, including ambitious caps, fair and efficient allocation of allowances and links between different trading schemes. Thirdly, the recognition that a strong carbon price is not enough to deliver the scale of change required. EOS called for additional support for energy efficiency and low carbon technologies, funding for adaptation to help manage the unavoidable climate change impacts and measures to reduce deforestation and promote afforestation.



Issues and companies

At the Conference of the Parties meeting itself, EOS participated in a series of high level side-events in Copenhagen including a dinner organised by the UN Finance Initiative and Institutional Investor Group on Climate Change with a number of key negotiators from the European Union, Germany, Indonesia, and the Republic of Korea. In addition to pressing for the three key elements of a global deal outlined above, it also encouraged the design of public finance mechanisms which could leverage private sector capital to support the emergence of low carbon economies by sharing the early stages of investment risk.

After many months of negotiations, on 18 December 2009, 140 countries backed the 'Copenhagen Accord'. Beyond a non-binding commitment to hold emissions below two degrees Celsius, the Accord lacked any medium or long-term emission reduction targets that could mobilise additional private investment for low carbon technologies. In addition, the negotiations shed little light on the level of support for adaptation, clean technology, Reduced Emissions from Deforestation and Degradation (REDD) or much-needed practical reforms of the Clean Development Mechanism (CDM). Indeed, the carbon markets were perhaps the biggest casualty of Copenhagen with no tightening of the EU cap or any further clarity on the institutional framework to drive a global price on carbon.

More positively, the Accord signalled that all the world's major emitters are willing to contribute to the transition to a low carbon global economy, with commitments from Brazil, China, India, Japan, South Africa, the European Union and the United States, among others. Industrialised countries that have emissions targets for 2008-2012 under the Kyoto Protocol must now commit to quantified economy-wide emissions targets for 2020. In addition, funding will rise from US\$30 billion in 2010-2012 to US\$100 billion annually by 2020 to support developing countries to mitigate emissions and adapt to climate change. Importantly, this funding will come from a wide variety of sources including private capital and alternative sources of finance.

Beyond Copenhagen, it is anticipated that negotiators will seek to build on the existing Accord to reach a legally binding treaty with emission reduction targets in December 2010, when the 16th Conference of the Parties will be held in Mexico. In the meantime, EOS will focus on the potential impact of legislative developments to introduce a federal cap-and-trade scheme in the USA. By winning agreement on transparent action from key major developing economies

including China, President Obama has helped strengthen the case for climate change legislation reinforcing the 'endangerment findings' by the Environmental Protection Agency. EOS is in discussions with the Coalition for Environmentally Responsible Economies (CERES) to leverage their resources in this area as we increase our engagement activity with US companies on climate change issues.

EOS has not been waiting passively for the development of a binding global treaty. On the contrary, we are determined not to continue with business as usual. Prudence and our clients' fiduciary duty to prevent long-term destruction of shareholder value, compels us to increase our efforts to engage carbon exposed companies and encourage them to effectively mitigate the financial impacts of climate change. Indeed the International Energy Agency has estimated that every year of delaying a global agreement on climate change adds US\$500 billion to mitigation costs for the energy sector alone.

EOS continues to target those companies operating in sectors and countries with a high exposure to existing and planned environmental regulations including surface and air transport, power generation, construction, clothing and food retail and real estate. In particular, EOS has ongoing engagements with those companies which have (i) a high level of direct and indirect carbon emissions compared to the average for their sector; and (ii) insufficient disclosure of the material financial risks associated with climate change and how those risks and opportunities relate to long-term business strategy.

In most cases EOS' objective is to encourage companies to take a long-term view on the price of carbon when making major capital expenditure decisions. EOS has sought to actively persuade major listed companies to consider long-term investments in cost-effective alternative technologies as we believe this will put them at a competitive advantage. Among the companies particularly exposed in this area are: American Electric Power (US), Exxon (US), WalMart (US), Enel (IT), Drax Group (UK), International Power (UK), Easyjet (UK), Associated British Foods (UK), Arriva (UK), Balfour Beatty (UK), Sainsbury (UK), Tesco (UK), RWE (Germany), Hochtief (Germany), Veolia (FR), Carrefour (FR), Bouygues (FR), Lafarge (FR), Grupo Ferrovial (ES), Ryanair (Irl), Hyundai Motors (SK), Nissan Motor (JP), Toyota (JP), Takeda Pharmaceutical (JP), Kenya Airways (Kenya), Canadian Oil Sands Trust (Canada), CNOOC (China/Hong Kong), China Mobile (Hong Kong/China), ArcelorMittal (Luxembourg), Sasol (South Africa).

Social and Ethical: Electronics industry sourcing of minerals from the Democratic Republic of Congo

EOS has undertaken a programme of engagement with electronics companies on the issue of minerals sourcing from the eastern regions of the Democratic Republic of Congo.

Statistics

Number of companies engaged with	15
Reassurance gained	9
Number of companies where substantive change sought	6
Number of these showing progress so far	2

'So called 'conflict minerals' can turn up in a wide array of electronic products such as smart phones, MP3 players, and laptop computers amongst others.'

Overview

This engagement was prompted by concerns over the continuing link between multinational corporations which source minerals mined in the militia-dominated eastern Democratic Republic of Congo and armed rebel groups responsible for human rights violations.

So called 'conflict minerals' can turn up in a wide array of electronic products such as smart phones, MP3 players, and laptop computers amongst others. Consumers in the United States, Europe, and Asia are the ultimate end-users of these conflict minerals and are inadvertently fuelling the ongoing abuses of human rights in the DRC through the purchase of these electronics products. EOS believes that the use of conflict minerals in these products can result in significant reputational risks. EOS has engaged with global consumer electronics companies to ensure that their policies on supply chains are transparent and sufficiently robust to address these risks.





Issues and companies

During the fourth quarter of 2009, EOS launched a collaborative engagement initiative with other UN PRI signatories on the issue of minerals sourcing from the Democratic Republic of Congo. This engagement programme will target major electronic companies in North America, Europe and Japan.

The Democratic Republic of Congo has been the scene of some of the deadliest conflict since World War II and remains among the most dangerous places in the world to live, in significant part because of the international demand for electronic products that requires minerals found in the eastern Congo. Whilst eastern Congo is a complex crisis – fuelled by tensions over land, rights, identity, regional power struggles, and the fundamental weaknesses of Congo as a state – the trade in conflict minerals remains one of the key drivers of the conflict. The same armed groups that reap enormous profits from the mineral trade in eastern Congo regularly commit human rights abuses as they jockey to control the region's most valuable mines, transportation routes, and opportunities to impose extortionary 'taxes' on those involved in this trade. This violence is also hampering the establishment of the civil society in the region and ensures local people remain in poverty.

While it is difficult to determine the full extent to which militia groups profit from these minerals it has been estimated that in 2008 alone armed groups in Congo earned approximately \$185 million from the trade. The three main minerals in question are tin, tantalum, and tungsten which are used in nearly all types of electronic products including mobile phones, MP3 players, and laptop computers.

The link between armed groups and the mineral trade has been well documented by numerous international organisations, including, most recently, the United Nations. The UN panel recommended due diligence in the international minerals supply chain as an effective strategy to cut off support to the Congolese rebels derived from these mining activities.

This is a particularly timely issue due to the recent introduction of the Congo Conflict Minerals Act in the US Senate designed to stem the flow of money from the mineral mines which help fuel the civil war in the Congo. If passed, companies will be required to track and disclose the country of origin of minerals used in common electronic products. The US Congress has also initiated a strong bipartisan effort to curb the conflict minerals trade. Both Senate and House bills on this issue represent a significant step toward conflict-free cell phones and laptops by setting up a system of audits and minerals-tracing mechanisms.

Clearly any link in a company's supply chain which has the potential to facilitate the breach of fundamental human rights is not only unacceptable as a matter of policy and principle but also is damaging to a company's reputation and the value of our clients' investment.

EOS is encouraging electronics companies to play a significant role in combating the trade in conflict minerals in eastern Congo by publicly disclosing their supply chains for components containing tin, tantalum, and tungsten by working with relevant organisation and industry peers to develop robust and internationally accepted mechanisms to verify the origin of these minerals and promote responsible and sustainable mining practices.

Examples of companies which have been named by NGOs concerned about the minerals trade are: Motorola (US), Hewlett-Packard (US), Apple (US), Dell (US), SanDisk (US), IBM (US), Intel (US), Microsoft (US), Research in Motion (Canada), Nokia (Finland), Philips (Netherlands), Sharp (Japan), Panasonic (Japan), Toshiba (Japan), Canon (Japan).

Governance: Board leadership

Focus: Separation of Chair and CEO

The recent financial turmoil has highlighted the need for companies to effectively mitigate a variety of risks. Good governance through independent board leadership is core to building effective checks and balances within organisations. The current emphasis on this fundamental principle of good governance stems not only from a challenging economic environment and the need to rebuild trust among investors, and safeguard the long-term interests of shareholders. Having an independent chair is critical to effective oversight of management and to reduce unnecessary risks. The board will therefore fulfil its duties to shareholders more effectively if the roles of chair and CEO are separate.

Statistics

Number of companies engaged with	15
Reassurance gained	0
Number of companies where substantive change sought	15
Number of these showing progress so far	3

'The separation of the roles of chair and CEO is a cornerstone of sound governance.'



Overview

The separation of the roles of chair and CEO is a cornerstone of sound governance. As recently demonstrated at some of the worst-hit financial institutions and in the past by corporate scandals like Enron, combining the role of chair and CEO can contribute significantly to company crises.

EOS recognises that local practice and company specific contexts are important. Without being a panacea, a non-executive independent chair enhances the effectiveness of the board, and therefore strengthens the confidence of the markets in the company. Most codes of best practice worldwide embrace this principle, including the Cadbury report (<http://www.ecgi.org/codes/documents/cadbury.pdf>).

Whilst the separation of roles is required in numerous markets, such as Germany, other jurisdictions leave this open for companies to decide. It has recently become a dominant practice in some markets like the UK and Canada and is gaining support in other key markets, including the United States. However, in practice the concentration of power on boards is still an issue in the United States, Switzerland and France. In France, recent governance reshufflings have resulted in a very worrying step backwards in numerous companies. As a consequence EOS is giving particular focus to this issue in 2010.



Companies and issues

In the current environment, we believe that certain markets need a more systematic approach to promote significant changes towards sound governance. As a consequence, EOS launched this year a series of shareholder resolutions in the United States, initially targeting eight companies. In two of these instances we have co-signed resolutions with labour union funds which hold significant stakes in the companies. EOS will continue its intensive dialogues with these companies ahead of the proposals being presented at AGMs, with a view to negotiating settlements and withdrawing the proposal before the AGM. We are encouraged by the progress we are making and expect to achieve positive outcomes ahead of AGMs in at least some of these cases.

EOS has been actively engaging with companies to split the roles of chair and CEO in difficult times. We have done this at companies in markets where the practice is not prevalent, as well as in a more systematic way where it is more typical to have a combined chair/CEO.

Following the financial turmoil EOS has notably pressed for changes at some financial institutions, for example making gains in the US at Bank of America, where a shareholder proposal on this issue won a majority of support in 2009 which then led to the roles being separated. Changes are easier to bring in the wake of an obvious crisis though they then often come too late. However, in most cases weaknesses had been identified and the engagement started well ahead of the crisis peaking.

EOS recognises that timing is critical and that immediately stripping a chair/CEO of the role of chair may send the wrong message to the market and reduce confidence in the company's leadership structures. In such cases, EOS will press for the nomination of an independent lead director responsible for ensuring a constructive dialogue with shareholders, representing their interests and challenge the chair/CEO when appropriate.

Where there is already a lead director on the board, EOS advocates a strengthening of the role to ensure that the lead director is sufficiently empowered to hold the CEO to account and to liaise with shareholders. EOS then closely monitors the succession planning in order to ensure that the leadership structure changes upon the succession of the current CEO.

In France, a significant number of companies have unexpectedly shifted away from a separation of the roles this year. Related shareholder proposals are not a legal option in this market. We have nonetheless started intensive engagements with selected companies, in some cases with other significant institutional shareholders, to raise our concerns. Our goal is to raise our engagements to the next level and to prevent the change when possible or at least make it transitory. EOS will also publish articles in the press to further raise awareness and share its concerns around this trend.

Finally, we believe that separating chair and CEO roles, though a necessary first step, is not in itself sufficient. Independence is also key for the chair to appropriately fulfil his duties, including challenging the CEO. A former CEO or a significant shareholder can be conflicted and may not be able to act objectively. EOS is therefore also actively engaging with companies where the chair lacks independence. EOS uses a wide array of engagement tools in its approach, from intensive dialogue to letters, sometimes creating or joining shareholders coalitions.

Companies which have had issues in this area include: Valero (US), Freeport McMoran (US), Legg Mason (US), Occidental Petroleum (US), Pfizer (US), John Deere (US), Whole Foods (US), Moody's and McGraw Hill (US), Axa (France), Air Liquide (France), Vinci (France), Veolia (France), Novartis (France).

Governance: Global best practice

Acting in concert regulation in Europe

Building on a successful engagement with German regulators during 2007/2008 on proposed acting in concert legislation, EOS is leading a collective engagement with other investors on this issue in Europe. The goal of this engagement is to encourage the European Commission and a number of Member States to provide further clarity on the concept of acting in concert and its application to cooperation between shareholders, particularly when the aim of the investors working together is not to seek control of a company.

'Lack of clarity in such regulation can hinder the collaborative engagement of institutional investors with companies on ESG issues.'



Overview

The concept of acting in concert defines circumstances in which shareholdings of investors need to be aggregated for disclosure or mandatory bid purposes, is defined in broad and imprecise terms in two European directives. Uncertainty at the European level is further exacerbated by differing interpretations of the concept between EU Member States.

Lack of clarity in such regulation can hinder the collaborative engagement of institutional investors with companies on ESG issues. There is concern among investors that regulators and, indeed, companies will interpret acting in concert rules in a manner that protects particular, vested interests rather than the interests of the shareholders as a whole. This can prevent investors from cooperating constructively in engagement work and presents a barrier to the effective cross border exercise of shareholder rights, which often calls for a dialogue between national and international investors. The ability for investors to work together to leverage their collective power is a key element in their responsibilities as active owners, which is particularly encouraged under principle 5 of the United Nations Principles for Responsible Investment (UN PRI).

This issue has recently gained in prominence due to a number of developments in the UK in 2009 at a government level, to which EOS provided significant input. These included Sir David Walker's review on the perceived barriers to shareholder collaboration, which triggered a dialogue between the FSA and the Takeover Panel. However, in the majority of Member States, interpretations and legal consequences for investors of acting in concert differ significantly. Investors who would like to share information and work together are therefore faced with considerable legal uncertainty. To understand their legal position in a range of situations, they require expensive legal advice. Moreover, even after taking such advice, some legal risks may remain, which may deter investors from carrying out collaborative engagements.



Our engagement

In 2008 EOS initiated a collaborative high level engagement with national and European legislators and regulators on the subject of acting in concert. EOS' engagement was supported by an impressive number of large institutional investors including a number of PRI signatories.

Through engagement with national regulatory bodies EOS has addressed the uncertainty that the different definitions of acting in concert in the Takeover Bids Directive and the Transparency Directive at the European level presents for institutional investors at a national level. EOS has led collaborative engagements with the regulators of a number of Member States, including the AMF in France, CONSOB in Italy and the CNMV in Spain.

A principle focus has been EOS' engagement with the European Commission with the objective of clarifying the regulation at an EU level, providing a firmer basis for national legislation in this area. We have pushed for the regulation to include an explicit safe harbour for shareholders sharing information or discussing their views on corporate governance issues, particularly regarding voting matters and subsequently acting together, including co-ordinated voting in respect of particular resolutions, provided they are not doing so with a view to gaining control of a company.

In its dialogue and correspondence with the European Commission, EOS has particularly pressed for a clear distinction in the definition between the cooperation of investors with the objective of gaining control of a company, and cooperation aimed at sharing ideas, developing and communicating a common message, and if necessary affecting change at a company. EOS has therefore sought clarity on key concepts used in the Transparency Directive and the Takeover Bids Directive.

The European Commission has acknowledged our concerns and invited EOS to meet with its legal advisers to provide input as long-term shareholders into an official study being conducted to review the Transparency Directive. The Commission's legal advisers commended Hermes for initiating this dialogue with investors. It recognised this was the first time a group of institutional investors had raised the issue of a non-control seeking collective dialogue with companies. EOS will continue the dialogue with the European Commission, leading the UN PRI's response to the forthcoming consultation on the review of the Transparency Directive. The dialogue will also continue with regulatory and government agencies at a national level to influence country-specific regulation. This joint engagement with the UN PRI is leveraging collaboration to promote the interests of long-term shareholders in working together within an appropriate framework to engage with companies on issues with the objective of creating long-term value.

Public policy and best practice

Protecting and enhancing value by promoting better regulation

EOS contributes to the development of policy and best practice on corporate governance, corporate responsibility and shareholder rights to protect and enhance the value of its clients' shareholdings over the longer term.

'Investment institutions are typically absent from public policy debates even though they can have profound impact on shareholder value.'

Overview

EOS actively participates in debates on public policy matters to protect and enhance value for clients by increasing shareholder rights and boosting protection for minority shareholders. This work extends across: company law, which in many markets sets a basic foundation for shareholder rights; securities laws, which frame the operation of the markets and ensure that value creation is reflected in value for shareholders; and in developing codes of best practice for governance, management of key risks and disclosure. In addition to this work on a country-specific basis, we address regulations with a global remit, which are currently in the areas of accounting and auditing standards.

Investment institutions are typically absent from public policy debates even though they can have profound impact on shareholder value. EOS seeks to fill this gap.

By playing a full role in shaping these standards we can ensure that they work in the interests of shareholders rather than being moulded to the narrow interests of other market participants (particularly companies, lawyers and accounting firms, which tend to be more active than investors in these debates) whose interests may be markedly different.





Highlighted sample activities

UN climate change negotiations

We actively participated in the UN-hosted discussions on climate change in both Copenhagen and Cape Town, and were heartened that for the first time there seemed some consciousness in Copenhagen of the need to leverage and involve private investment as part of the step-change which is needed. Issues arising from Copenhagen are discussed elsewhere in this report.

Japanese governance change

We were pleased to note significant developments to enhance investor accountability of Japanese companies with proposed changes to the Tokyo Stock Exchange's listing rules to enhance corporate governance standards, both in relation to independent directors and statutory auditors and in the status of the governance principles. These changes reflect calls we have made over several years and seem to have been catalysed, alongside a general debate in the country on these issues, by the ACGA White Paper which we co-authored. We strongly encouraged these developments, not least through co-writing a formal ACGA statement on this progress which was published towards the end of the quarter.

Access to Medicines

We have continued our engagement with the team revising and redeveloping the Access to Medicines index, which provides an overview of the involvement of major global pharmaceutical companies in making their products and expertise available at appropriate prices to the world's poorest people and nations. We have been able to work with the index staff to give ourselves greater confidence that this round of the process will draw more positive distinctions between different companies, and we have therefore agreed formally to support the initiative for the first time. Also in the quarter we participated in the launch of the Industry-Government Forum on Access to Medicines which seeks to make further strides in making key drugs available to the world's poor.

Further steps on US regulation

We continued to maintain our efforts to encourage regulatory change in the US, both through dialogue with the SEC and with representatives of key legislators.

We have managed to gain access at senior levels with the bodies which will push forward reforms which we regard as necessary to bring US regulatory standards more in line with international best practice. We therefore worked to strengthen their resolve to put into effect the reforms which have already been proposed, not least around making director elections more meaningful and ensuring accountability on pay. In addition to this, we actively attempted to move the debate further forward by raising issues such as Reg FD being used by companies as an excuse that prevents them from entering into effective engagement with involved shareholders.

Forest Footprint Disclosure Project

We have continued our extensive efforts in support of this key project, which is attempting to raise greater corporate consciousness of the forestry impacts of corporate supply chains. Deforestation is a crucial issue for climate change, with realistic estimates that it is responsible for perhaps as much as 20% of all greenhouse gas emissions. The FFD Project seeks disclosure from companies as to their indirect impacts on forestry, and we have in this quarter continued to encourage key companies to respond to the Project's questionnaire, as well as working with the Project team to enhance the approach and to help guide the way in which the responses are put to use. The value of this input was recognised this quarter as we were invited to join the Project's steering committee, which we readily agreed to do. We look forward to having further influence on how the Project develops.

Revised ICGN Principles

EOS has provided the chair of the committee which drove the revision of the International Corporate Governance Network's overarching Principles over the last year. This revision has seen some very significant enhancements in the Principles, with a greater focus on corporate culture and boardroom behaviours rather than just structures, as well as the introduction of a section on risk management for the first time. We were pleased when these new Principles were formally launched at the ICGN conference in Washington this quarter.

Public policy and best practice continued

Acting in concert

We believe that we are making significant steps forward in our efforts to address European acting in concert regimes, which in some markets restrict the ability of investors effectively to collaborate in engagement activities. In particular this quarter we met with the European Commission's legal advisers in their consideration of this issue, and were able to highlight the areas of concern and how these might be addressed. We also used the opportunity of a QCA delegation to Brussels to reinforce our concerns about acting in concert directly with senior Commission staff. In addition we had a dialogue with government officials in Australia on this key issue.

Involvement in conflict-affected countries

We continue our efforts as part of a Global Compact working group trying to develop guidelines on company involvement in conflict-affected countries. We are heartened by the involvement in this initiative of a number of companies with very significant exposures in this regard and hope to be able to advance best practice significantly through the development of this best practice guidance.

Enhanced corporate reporting

We continue to promote better corporate reporting. Most notably in the quarter, our efforts around the ICSCA Hermes awards for narrative disclosure came to fruition with the inaugural awards ceremony. We will now seek to generate change out of these awards by writing to all large UK companies with highlighted lessons to learn; we are already using the winning reports as exemplars in our engagements around the world. We also used a CESR (Committee of European Securities Regulators) consultation on XBRL to promote across Europe the more important agenda of better corporate reporting more generally.

Other public policy work this quarter included:

Companies Acts and equivalents

- Australian remuneration – input to Productivity Commission and dialogue with government officials
- Japanese companies act – informal input to the developing process of potential reforms
- Korean poison pills – dialogue with Financial Services Commission to oppose steps to allow pills
- Singapore companies act – dialogue with Ministry of Finance on forthcoming reforms

Securities Laws and Regulations

- Canadian enforcement regime – dialogue with Toronto Stock Exchange on enhancing approach
- Chinese bank regulation – dialogue with Banking Regulatory Commission on risk management

- Hong Kong acceptance of Chinese accounting and auditing – response to consultation
- Hong Kong short-selling disclosure – response to consultation
- Hong Kong rights issues acceleration – response to consultation
- Hong Kong extractives sector listing rules – response to consultation
- Italy related party transactions – response to consultation
- Italy transparency on derivatives holdings – response to consultation
- Qatar governance regime – discussions with MD of Qatar Financial Centre
- UK combined code revision – informal input and response to consultation
- UK non-audit services – informal and formal input to consultation process

Codes of best practice

- OECD Latin America guidance – investor input on OECD White Paper for the region
- Philippines governance code – dialogue with stock exchange
- South Africa King III Code – comments on enhanced disclosure requirements
- US combined roles CEO/chair – speech at Delaware conference alongside key law-maker

Global standards

- IASB agenda – input through members of Standards Advisory Council
- IASB hedge accounting – meeting with IASB members to comment on board's developing thinking
- IASB consolidations – informal response arguing for a rethink on investment vehicles
- IASB revenue recognition – meeting with IASB staff principally to comment on disclosure requirements
- IASB management commentary – response to questionnaire to be fed back to IASB
- IASC Foundation governance – response to consultation on structure of IASB and Foundation itself

Hermes votes at general meetings wherever practicable. We take a graduated approach and base our decisions on annual report disclosures, discussions with the company and independent analysis. We inform companies before we vote against or abstain on any resolution, usually following up such votes with a letter. We maintain a database of voting and contact with companies and if we believe further intervention is merited, we include the company in our main engagement programme.



Hermes votes at company meetings all over the world, wherever its clients own shares.

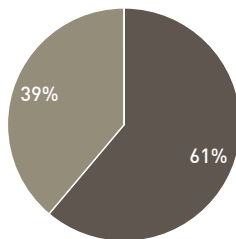
Voting overview

How we voted for PNO Media

Over the last quarter, we voted at a total of 109 meetings around the world, analysing 834 resolutions. At 37 of those meetings we opposed one or more resolutions. We voted with management by exception at three meetings, while we supported management on all resolutions at 69 meetings.

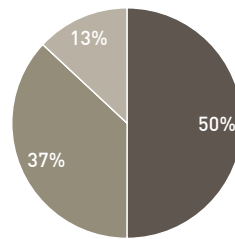
North America

We voted at 33 meetings (332 resolutions) over the quarter.



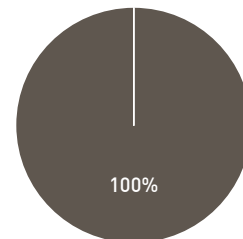
Asia (except Japan)

We voted at eight meetings (69 resolutions) over the quarter.



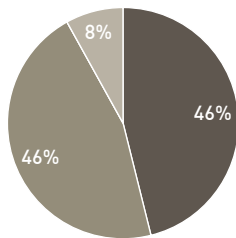
Japan

We voted at one meeting (six resolutions) over the quarter.



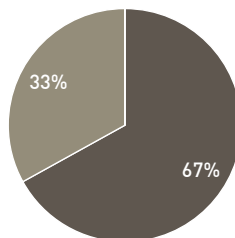
Australia and New Zealand

We voted at 26 meetings (115 resolutions) over the quarter.



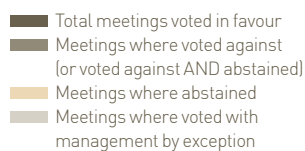
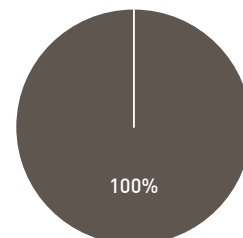
Western Europe

We voted at 27 meetings (159 resolutions) over the quarter.



UK

We voted at 14 meetings (153 resolutions) over the quarter.



What is EOS?

Hermes Equity Ownership Services (EOS) helps institutional shareowners around the world to meet their fiduciary responsibilities and become active owners of public companies. EOS' team of engagement and voting specialists monitor its clients' investments in companies and intervene where necessary with the aim of improving performance. EOS' activities are based on the premise that companies with informed and involved shareholders are more likely to achieve superior long-term performance than those without.

As the largest pension fund in the UK, Hermes' parent the BT Pension Scheme (BTPS), has substantial interests across international markets. Through pooling resource with other like-minded funds to create a stronger and more representative shareholder voice, our joint company engagements are more effective.

Hermes has the largest stewardship resource of any fund manager in the world. Our team includes former CEOs and other board members of public companies, as well as senior strategists, corporate governance experts, investment bankers, fund managers, lawyers and accountants.

The depth and breadth of this resource reflects our philosophy that ownership activities require an integrated and skilled approach. Intervention at senior management and board director level should be carried out by individuals with the right skills and with credibility. Making realistic and realisable demands of companies, informed by significant hands-on experience of business management and strategy setting is critical to the success of our engagements.

Hermes and the BTPS have extensive experience of implementing the United Nations' Principles for Responsible Investment (UN PRI). EOS' Chief Executive Colin Melvin chaired the committee that drew up the original principles, and the current chair is a trustee of the BTPS. This insight enables EOS to help clients who wish to become signatories or have already achieved signatory status to meet the challenges of the PRI.

How does EOS work?

EOS uses a proprietary screening process to determine which companies will benefit from intensive engagement. The first element of this screen looks at the companies' ability to create shareholder value by comparing the weighted average cost of capital with cash returns to investors. The second element assesses the prospects for engagement success. We apply further screens across a range of other metrics including environmental and social issues.

The Hermes Principles set out our basic expectations of companies in which our clients invest. These cover business strategy, communications, financial structure, governance and management of social, ethical and environmental risks. The Principles and their regional iterations guide our intervention with companies throughout the world. Our approach is pragmatic and company and market specific, taking into account individual company circumstances.

We escalate the intensity of our involvement with companies over time depending on the nature of the challenges they face and the attitude of the board towards our intervention. Some engagements involve one or two meetings over a period of months, others are more complex and entail multiple meetings with different board members over several years.

At any one time there are many companies included within our engagement programmes, meaning that significant additional resources are dedicated to these situations. All of our engagements are undertaken subject to a rigorous initial assessment and ongoing review process to ensure that we are focusing our efforts where they can add most value for our clients.

While we are robust in our dealings with companies, the aim is to deliver value to clients, not to seek headlines through campaigns. These can often undermine the trust which would otherwise exist between a company and its owners. We aim to be honest and open with companies about the nature of our discussions and will seek to keep such discussions private. Not only has this proved the most effective way to bring about change, it also acts as a protection to our clients, so that their position will not be misrepresented in the press.

For these reasons, this public report does not contain specific details of our interactions with companies but aims to bring clarity on some of the most important issues relevant to responsible owners today and EOS' related activities in these areas.

We would be delighted to discuss EOS with you in greater detail.

For further information please contact Colin Melvin on 020 7680 2251.

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Hermes Equity Ownership Services

Hermes Equity Ownership Services (EOS) enables institutional shareholders around the world to meet their fiduciary responsibilities and become active owners of public companies. EOS is based on the premise that companies with informed and involved shareholders are more likely to achieve superior long-term performance than those without.