

## Financial Reporting Council Consultation on a Stewardship Code for Institutional Investors

### Royal London Asset Management Response

#### General Comments

We strongly believe that any Stewardship Code must be principles based and we would like it to remain as close as possible to the ISC Code published in 2009 which we believe contained much to be commended. Any code should avoid the idea that there are instant solutions to governance issues or that a proscriptive approach would in any help advance the cause of better shareholder engagement or improved oversight of company management.

It is our experience that good governance has the characteristics of being long term in nature, is cumulative in effect over time and that it can be both time consuming and difficult. Therefore any Stewardship Code needs to reflect these realities and should not be overly detailed or compliance driven. We are also of the opinion that it is an attractive feature of the UK that different institutions adopt varied approaches towards corporate engagement within different investment processes. It is essential that we accommodate those varied approaches while allowing the market to evolve best practice as a means of improving overall company oversight. By adoption of this approach we believe that over time more investors can be encouraged to become involved and that we can embrace the many overseas investors who now own UK company shares. We foresee a significant risk that an overly proscriptive approach will not advance the cause of improved engagement activity but instead will lead to many institutions effectively retreating behind third party agencies as has happened in other countries.

It is our view that the best way of ensuring this progress is through an investor led proportionate approach to corporate engagement and the new Stewardship Code. Therefore while we support the FRC having oversight of the Code we believe that its content and future evolution should remain with the ISC.

Given that almost all UK investors will also have investments in overseas markets we would recommend that the Stewardship Code should recognise that scale of resources that would be required in order to undertake the same level of activity in other markets may not be appropriate but that investors should make best efforts to apply the same principles in those jurisdictions wherever possible. Similarly if we are to encourage overseas holders of UK stocks to have greater involvement within the UK it should be recognised that a lesser degree of verification would be reasonable.

Consistent with our recommendation for the continued significant involvement of the ISC in the Stewardship Code we believe that the individual institutions that sign up to the Code should be listed on the ISC website.

Overall we see the development of the Stewardship Code as being a potentially significant step in encouraging a greater emphasis within the UK upon long term investment, through the encouragement of a wider universe of institutional shareholders in genuinely value creative

shareholder activity. Our comments reflect this aim and we strongly believe that any Code should be judged against this objective.

### **Objectives of the Code**

We believe that the code should be implemented on a comply or explain basis both as to adoption by the institution but also in terms of how they individually apply the provisions of the Code given their particularly circumstances.

While the Code should encourage high quality activity and transparency in reporting it should be left to the institution to determine how best to achieve this rather than the Code setting rigid 'model' approaches to the internal workings of an institution or in reporting externally. Any commentary on institutional activity with respect to engagement should be framed in terms of overall market progress rather than singling out individual institutions. These institutions will all be reporting on their activity through to their clients and these should be in a good position to judge on the quality, effectiveness and reporting of the company oversight.

### **Coverage of the Code**

We believe that a similar approach should be adopted to the introduction of the Code as was the case when the various elements of the Combined Code were introduced. In particular we would suggest that implementation of the Code should be phased in rather than as one big-bang. This reflects the fact that the various elements of the Code do represent a fairly large scale increase in expectations for many institutions and therefore it would be better as a means of encouraging improvements in overall best practice and coverage if this could be addressed over a reasonable period of time. Again we would caution that an overly ambitious introduction of the Code could encourage retreat from engagement rather than spurring on involvement, which would strongly act against one of the prime drivers behind the adoption of the Stewardship Code which is to increase the amount of actively engaged longer-term focused shareholders..

Again similar to previous corporate codes we would suggest that the next full review of the Stewardship Code should take place in three years time which would allow for an overall increase in activity to be meaningfully observed and would prevent institutions being presented with a too quickly changing target to aim for. Hence we envisage that corporate oversight activity should be allowed to continually evolve towards improved standards.

### **Reporting & Monitoring Against the Code**

Our expectation is that over time as client demand and interest grows and assessments of best practice evolve we will see industry practice improve in terms of the detail and transparency through which institutional investors report. This will allow clients to properly assess the institution is applying its policy on corporate engagement. In addition through the public disclosure of an institutions policies that companies will be able to gain a greater understanding of the approach and expectations of investors in this area.

We believe that any disclosures should be made against the Codes provisions on a comply or explain basis which would be consistent with the way in which the current Combined Code is applied to company disclosures. We would not recommend that certain standards are imposed upon investors

as we would see this as counterproductive to genuine improvements in best practice and/or could dissuade institutions from actively utilising the Code.

In the debate as to whether disclosures should be at the firm or fund level we would strongly come down in support of the former approach. Reporting on a fund basis would be extremely onerous and we do not believe that it would lead to any particular benefit. Reporting by individual institutions should make reference of the fact that the way in which the overall approach to governance is applied could differ between certain funds dependent upon their specific mandate or investment approach. Indeed these differences should be highlighted to actual and prospective clients of the firm.

We would encourage the FRC to propose that there be a single survey, such as that currently undertaken by the IMA, which would help in the monitoring market activity. The alternative is of a plethora of competing surveys which compile an incomplete picture if only a minority of institutions complete them.

The ISC Code did propose that an independent audit of the institutions practices and procedures relating to engagement activity could form part of the annual AAF 0106 exercise. We would endorse such an approach as we believe it would provide credible independent verification.

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30<sup>th</sup> March 2010