Universities Superannuation Scheme
Submission to the Financial Reporting Council
Consultation on Revisions to the UK Stewardship Code

16 July 2012

1. Introduction:

USS is the second largest pension fund in the UK with approximately £30billion of assets under management. As a defined benefit scheme, in-house fund manager and asset owner, USS' long-term and universal investor perspective distinguishes us from many other institutional investors.

We take seriously our role as a long-term owner of companies and other assets, and devote substantial resources to oversee and monitor the management of those assets. We believe shareholder engagement and active oversight of our investments is vital for ensuring we deliver long-term and sustainable value for our beneficiaries.

As signatories to the Stewardship Code (the Code) from the outset, we continue to support its concept and welcome the revisions proposed within the April 2012 consultation. In line with the FRC's stance, we believe the Code and its application should continue to evolve to encourage stewardship best practice in a 'race to the top'. A key risk in setting standards for all participants in the industry is that standards could gravitate towards the lowest common denominator. We welcome innovation and the promotion of best practice by the FRC through periodic amendments to the Code.

2. 2020 Stewardship:

USS, along with five other institutional investors (Aviva, Blackrock, Governance for Owners, Ram Trust Services and RPMI Railpen), recently produced a report with Tomorrow's Company on the future of stewardship, *2020 Stewardship* (attached). The purpose of the report is to influence the debate on stewardship and to promote stewardship best practice. The report identifies a number of challenges relating to the quality and quantity of stewardship currently undertaken in the UK market, and recommends four action points to address these challenges (see Box 1 overleaf).

We consider the recommendations are a first step to developing a market-based demand for enhancing stewardship. Enhanced stewardship, and related disclosures, would allow asset owners to better incorporate stewardship into their selection process for fund managers, and help companies to identify those shareholders who are able and willing to engage on a constructive basis.

USS is continuing our involvement with this project, working with other institutional investors to develop further the recommendations identified in this initial March 2012 report. We would encourage the FRC to refer to the recommendations of the *2020 Stewardship* Report in the revised Code with the aim of improving its effectiveness. We also invite the FRC to work with us as we develop and promote the recommendations further.

The working party believes that challenges of stewardship can be addressed by:

- creating a simple **guide to good engagement practice**, in particular to encourage more productive meetings, jointly developed by companies and institutional investors
- companies and institutional investors finding more ways to **seek feedback on the quality of meetings** and over time use this to identify and improve good stewardship. Encouraging institutional investors who are signatories of the UK Stewardship Code to be more transparent about the extent to which they intend to exercise stewardship as part of a product offering
- **a 'Stewardship Framework' against which institutional investors can categorise themselves** which we have developed as a starting point for discussion [see Executive Summary of the report for a draft framework]. Over time, these public statements can be substantiated and ultimately reinforced by the evolution of the AAF 01/06 guidance on internal controls and stewardship. Public statements based on this framework will not only help asset owners compare the stewardship activities of different fund managers and so make more informed decisions. It will also assist companies to identify the stewardship investors on their share register
- companies helping to increase the critical mass of stewardship by **developing a 'Stewardship Profile' of the current extent of stewardship investors on the register and a 'Plan' to achieve an appropriate level.** Each company would report on progress towards this and further develop its investor relations function in areas of 'stewardship relations'. Such plans would need to recognise the important role of passive investors.

Box 1: Key Recommendations from *2020 Stewardship,* Investor Stewardship Working Party, March 2012.

3. Preface to the Code:

Whilst we welcome the revisions proposed in the first three introductory sections, we consider guidance for signatories on their application of the Code and disclosures regarding conformity to the Code could be strengthened further. The Code should be designed to ensure asset owners can differentiate between fund managers and identify 'best in class' in terms of stewardship; and allow companies to identify shareholders on their register who take stewardship more seriously and are willing and able to engage on a constructive basis.

4. Definition of Stewardship:

We welcome the clarifications offered regarding the scope of stewardship activities. However, it should be clear that any list of activities is not exhaustive. For example, we note environmental and social issues and succession are omitted from the list. Conversely 'remuneration' is listed separately, whilst we consider it to be just one aspect of corporate governance. If particular aspects of risk, performance, corporate governance etc. are to be listed, we would encourage the inclusion of, inter alia, environmental issues, social issues and succession planning within the statement.

We welcome the acknowledgment that investors should engage and exercise stewardship across multiple jurisdictions and asset classes. However, we believe this could be taken a step further within the Code by actively encouraging signatories to engage on material issues, irrespective of market or asset class.

Further, we would welcome an acknowledgement that many institutional investors engage on thematic and regulatory issues that may have a more significant effect on a larger number of companies than engagement with individual issuers alone. Information about this type of macro-stewardship would, in many cases, be relevant and appropriate to be included within signatories' statements.

5. Voting:

We support the FRC's guidance regarding disclosure relating to the use of proxy advisory services, and advocated similar disclosure requirements to the European Securities and Markets Authority in their recent consultation on the role of proxy advisory services. We believe it should be the investor's responsibility to satisfy themselves with the processes and policies employed by their proxy advisors to ensure the suitability of any services provided, as with any other service providers appointed.

We continue to have concerns regarding the highly complex and opaque voting chain between the beneficial owner and the issuer. We consider the current structures can lead to potential conflicts of interest and poor quality execution, which, in turn, can act as an impediment to good stewardship and create artificial barriers to investors who seek to vote in an informed and timely manner. At a minimum we expect that all beneficial owners should be able to instruct a proxy to vote at General Meetings. However, in many pooled funds investors are unable to vote the shares attributable to them. We would encourage the FRC to address this issue within the Stewardship Code.

For further information please contact:
Dr Daniel Summerfield, Co-Head of Responsible Investment
Tel: 020 7972 6398 / E-mail: dsummerfield@uss.co.uk