UKSIF

13th July 2012

Email: codereview@frc.org.uk

Chris Hodge
Financial Reporting Council
Fifth Floor
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Dear Chris,

Revisions to the UK Stewardship Code – Consultation

Thank you for the opportunity to comment on your proposed revisions to the Stewardship Code.

UKSIF has always strongly supported the introduction of the Stewardship Code. High quality stewardship is essential for long-term wealth creation and protection as well as to meet the broader interests of society and so protect the continuing “licence to operate” of asset owners and their agents.

We welcome the decision of the Financial Reporting Council (FRC) to reinforce the Stewardship Code without making any fundamental changes; we believe that giving the Stewardship Code time to settle down and evolve gradually over time is the correct course of action.

We also broadly welcome the proposed changes to the Stewardship Code, many of which are in line with suggestions outlined in UKSIF’s previous response to the FRC’s “Consultation on a Stewardship Code for Institutional Investors” in April 2010.

We are grateful to you for briefing UKSIF members on your consultation at an UKSIF seminar held on the 22nd May 2012. Feedback from our members at this event has fed into our response to this consultation, and we have also based our submission on our previous response to the FRC’s “Consultation on a Stewardship Code for Institutional Investors” in April 2010 as well as our September 2010 submission to the consultation on “CP10/15: Disclosure of Commitment to the Stewardship Code Principles (COBS)” and our response to the Kay Review of UK Equity Markets and Long-Term Decision Making in November 2011, which examined stewardship issues.

The two ‘tests’

We generally welcome the additional clarification proposed to the first three introductory sections of the draft revised code, although we would recommend actually placing the ‘Principles’ – the de-facto ‘definition’ of the Stewardship Code – on page 1 instead of page 8 as we believe that it would aid further clarity in what is meant by stewardship, its purpose and how it relates to governance.

We also believe that the FRC has succeeded in enhancing the existing Code without adding unnecessary detail.

Stimulating Asset Owner demand

We are pleased to see that the proposed changes recognise that asset owners have been slower than originally anticipated in signing up to the Code; although aware that regulation can only achieve so much, we have always believed that the implementation of the Stewardship Code must harness the power of asset owners and change investment industry culture i.e. it must combine regulatory power with the "remunerative" power of asset owners and the "normative" power created by market commentators and civil society.

In particular, the Code's success will depend on genuine demand from pension funds and other asset owners which create commercial drivers for high quality implementation; it has been a recurring theme amongst the feedback from our asset manager members that it is easier to justify effective implementation of the Stewardship Code if there is a commercial incentive to do so from their asset owner clients.

Therefore, while pleased to see recognition of the importance of encouraging asset owner demand in the proposed revisions to the Code, we believe that more could be done in this regard; for instance, we believe that it is particularly important that The Pensions Regulator (TPR) should encourage adoption of the Stewardship Code by pension funds.

Clarification of terminology

We welcome the decision to clarify the terminology used in the original code, particularly replacing the words "institutional investor" with either "asset manager" or "asset owner" where a statement in the Code refers to only one type of firm. We also agree that the respective responsibilities of asset owners and asset managers have been correctly described in the proposed changes.

Conflicts of interest

We believe that how a signatory reports its management of conflicts of interests is a key part of good stewardship; we are therefore pleased to note the changes to Principle 2 of the Stewardship Code and agree that this will encourage fuller disclosure.

We agree that it is desirable to use the term "effective" in the Principle's first paragraph and in the guidance.

However, there are some areas where we would suggest further improvements and these have been set out below.

The role of Environmental, Social and Governance (ESG) factors in good stewardship

We feel that the proposed changes are a 'missed opportunity' to draw out more clearly the environmental, social and governance (ESG) risks that can be posed to businesses and monitoring of which are a key part of good stewardship; we believe that there are additional opportunities and challenges for responsible owners resulting from climate change, resource management and social sustainability drivers and that there is a clear business case for long-term responsible investment approaches.

With this in mind, UKSIF would recommend the following changes:

To Principle 1 of the Stewardship Code:

"Stewardship activities include monitoring and engaging with companies on matters such as strategy, performance, risk **– including risks associated with environmental and social factors -,** remuneration and corporate governance as well as voting. Engagement is purposeful dialogue with companies on those matters as well as on issues that are the immediate subject of votes at general meetings."

Similarly, to paragraph 4 of the introductory section 'Stewardship and the Code':

"For investors, stewardship activities include monitoring and engaging with companies on matters such as strategy, performance, risk **– including risks associated with environmental and social factors -,** remuneration and corporate governance as well as voting. Engagement is purposeful dialogue with companies on those matters as well as on issues that are the immediate subject of votes at general meetings."

The role of service providers, including proxy voting agencies, research agencies and investment consultants

We strongly support measures to encourage agents of institutional investors to commit to the spirit of the Code, although we see this as a significantly lower priority than client support for the Code.

However, we would recommend that the revised Stewardship Code recognise the fact that institutional investors use not only proxy voting agencies but also environmental, social and governance (ESG) research agencies in support of their stewardship activities. The Code should therefore more explicitly support commitment by these agencies within its scope.

UKSIF would suggest the following changes:

Under 'Application of the Code', paragraph 2:

"The Code is directed in the first instance to institutional investors, by which is meant firms that may be considered asset owners and/or asset managers. The Code also applies, by extension, to service providers ~~such as proxy advisors and investment consultants.~~ **who contribute to the stewardship processes that institutional investors employ, through the provision of research, analysis or opinion.**

Under 'Application of the Code', paragraph 5:

In particular, the disclosures should, with respect to conflicts of interest, address the priority given to client interests in decision-making; with respect to collective engagement, describe the circumstances under which the signatory would join forces with other institutional investors to ensure that boards acknowledge and respond to their concerns on critical issues and at critical times; and, with respect ~~to proxy advisors, how the signatory makes use of their advice.~~ **service providers, how the signatory makes use of their services.**

Application to a broader range of asset classes

We welcome the fact that the proposed revisions would recognise the need for the Stewardship Code to be applied to a broader range of asset classes, in line with current industry trends. However, we feel that the proposed changes to the Code do not go far enough in ensuring that signatories do so. We therefore suggest the following changes:

Under 'Application of the Code', paragraph 11:

"Institutional investors with several types of funds or products need to make only one statement, but ~~are encouraged to~~ **should** explain which of their funds or products are covered by the approach described in their statements. Institutions ~~are also encouraged to~~ **should also** disclose whether they adopt a stewardship approach with regard to other asset classes in which they invest, including corporate debt.

The UK Sustainable Investment and Finance Association (UKSIF)

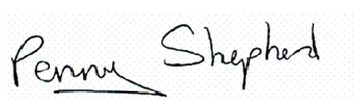
The UK Sustainable Investment and Finance Association (UKSIF) supports the UK finance sector to be a global leader in advancing sustainable development through financial services. We promote and support responsible investment and other forms of finance that advance sustainable economic development, enhance quality of life and safeguard the environment. We also seek to ensure that individual and institutional investors can reflect their values in their investments.

UKSIF was created in 1991 to bring together the different strands of sustainable and responsible finance nationally and to act as a focus and a voice for the industry. UKSIF's 260+ members and affiliates include pension funds, institutional and retail fund managers, banks, financial advisers, research providers, consultants and non-governmental organisations. For more information about UKSIF, please visit www.uksif.org.

UKSIF supports long-term responsible investment and ownership. It focuses its corporate governance support on the interface between governance on the one hand and social, environmental and ethical issues on the other.

We trust that our comments will prove to be self-explanatory but please do get in touch if you would like any further clarification.

Yours sincerely,



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