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Submitted by email to: codereview@frc.org.uk

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Dear Chris

ICSA response to the FRC's Consultation on Revisions to the UK Stewardship Code

Thank you for the opportunity to comment on this important issue. The Institute of Chartered Secretaries and Administrators (ICSA) is the international qualifying and membership body for the Chartered Secretary profession and a recognised authority on corporate governance. Many of our members are company secretaries in public listed companies and are closely involved with the implementation of the Stewardship Code, largely around shareholder engagement with companies.

This involvement gives our community a clear perspective on the value of shareholder engagement and stewardship. We have consulted our network and, in particular, the ICSA Company Secretaries Forum, which includes company secretaries from more than 30 large listed companies from the FTSE 100 and FTSE 250, to formulate this response. However, the views expressed in this response are not necessarily those of any individual members of the ICSA Company Secretaries Forum nor of the companies they represent.

In framing ICSA's response, we wish to make one observation in particular. Since its publication in July 2010, the UK Stewardship Code ("the Code") has not yet achieved its aim of active engagement between companies and investors. We support the Code's objectives and are generally supportive of the proposed amendments; however we are of the view that a Code alone cannot achieve its aims. There needs to be a change of culture and attitude by both investors and companies, and sufficient resources need to be deployed to ensure proper engagement. Unfortunately, in our members' experience, it is still the case today that many investors choose not to engage directly (if at all) with companies, or do so only at a late stage immediately before the AGM. This does not allow companies adequate time to respond before their AGMs.

In the following sections we make some general comments on the proposed revisions to the Code and then we have some specific points on the wording of individual principles and guidance.

1. General points on the proposed revisions to the Code and introductory paragraphs

ICSA supports the proposed changes to the Code and thinks that the new introductory sections are an improvement on the preface to the Code published in July 2010.

1.1 Structure, balance and clarity

We agree that the proposed changes satisfy the two tests set out in paragraph 4 of the consultation document headed 'rationale and summary of the proposed changes'. We think there is no need for the Code to be more prescriptive and agree that the alignment with the UK Corporate Governance Code will improve the understanding of stewardship and the purpose of the Code.

1.2 Definition of stewardship

We agree that the revised definition of stewardship is an improvement and clarifies the role and purpose of stewardship.

1.3 Responsibilities of asset owners and asset managers

We think that the clarification of the different responsibilities of asset owners and asset managers is helpful and will improve the understanding of their respective responsibilities.

1.4 Other proposed changes to the Code

Subject to the comments below, ICSA is supportive of the proposed changes to the Code.

- **Conflicts of interest policies** We support the aim of improving reporting on the management of conflicts of interest. We have some comments on the proposed new wording which are set out at 2.2 below.
- **Collective engagement** We also support the aim of improving Code signatories' understanding of what is meant by 'collective engagement' and have made some suggestions for amendments to the wording of the guidance in 2.5 below.
- **Proxy voting and advisory services** We very much support amendments to the Code to improve disclosure and transparency over the use of proxy advisory services. We are aware of the current EU discussions on the possible policy options for the proxy advisory industry but we do not see regulation as a solution to current problems. We think that it is for institutional investors to use their services appropriately and sensibly. However, we do think that there should be guidelines around the operations of proxy advisory agents and the management of conflicts of interest. We also consider it is inappropriate for these agencies to levy a charge on issuers for providing a copy of their report and voting recommendations.

We have some comments on the wording of the guidance to Principle 6 and these are set out at 2.6 below.

- **Stock lending** We agree with the proposed changes to improve transparency over stock lending and have made comments on the guidance at 2.6 below.
- **Other asset classes** In principle we have no concerns over the revised Code applying the stewardship approach to other asset classes, including overseas equities. In practice, institutional investors holding debt issues are already engaging with investee companies in this way. It is less likely however that there will be substantial levels of engagement by UK based institutions in relation to overseas equities.

- **Assurance reports, signatories' statements, insider information and the role of service providers** These are small but important changes, which we support.
- **Editorial changes** We generally support the proposed editorial changes, subject to our detailed comments below. The proposals to replace the preface with three sections which define stewardship, articulate the relationship with the UK Corporate Governance Code and set out 'comply or explain' are an improvement. The explanation of the relationship with the UK Corporate Governance Code is particularly helpful.

Our detailed comments on the proposed changes to the wording of the principles and guidance are set out below.

2. The Principles of the Code

We generally support the amended wording to the seven principles set out on page 8 of the draft revised Code. However, we have one comment in relation to the suggested amendment to Principle 2 (conflicts of interest). We agree that the word 'robust' is too strong and should be changed, but do not think that substituting the word 'effective' is sufficient. We suggest this be reworded to read '**... have a policy for the effective management of conflicts of interest ...**'

2.1 Guidance on Principle 1 – disclosure of stewardship policy

The guidance seeks to clarify that stewardship is not about socially responsible investment and, to this end, the first paragraph sets out a number of areas that should be monitored. However, **this list omits board composition and succession planning**, which are important issues that should be monitored by investors.

We also suggest that it would be helpful to have greater clarity over the definition of 'engagement'. The first paragraph of the guidance on Principle 1 states that 'Engagement is purposeful dialogue ...' but the wording used in the guidance to Principle 4, which deals with the escalation of stewardship activities, talks about 'intervention' – which is more than 'dialogue'. **It would be helpful to have clarity at the outset if engagement should include both dialogue and, if necessary, intervention.**

2.2 Guidance on Principle 2 – conflicts of interest

The wording in the second line of the third paragraph currently reads '... and publicly disclose an effective policy for identifying and managing ...'. It is difficult to be certain in advance that a policy is effective and we therefore suggest this wording be amended to '**... and publicly disclose a policy for the effective identification and management of ...**'

2.3 Guidance on Principle 3 – monitoring of investee companies

We think it is unfortunate that the reference to 'active dialogue with boards' has been removed and replaced with a reference to 'effective monitoring', which does not require engagement and does not provide an opportunity for boards to respond. In our introductory comments we have highlighted the importance of changing behaviours as, without effective engagement, the Code alone cannot achieve its aims. **We therefore suggest that the wording 'active dialogue with boards' be retained** and that the importance of active dialogue with the company be emphasised in the Code.

The fourth bullet point under the second paragraph in this section includes the wording that institutional investors should seek to 'satisfy themselves that the investee company's board and committees adhere to the spirit of the UK Corporate Governance Code ...'. We have concerns over the use of the word 'spirit' in this section as this might suggest a requirement

to 'comply' with all code provisions. This would undermine 'comply or explain' and tend towards a 'box ticking' approach. **We suggest that 'spirit' be replaced with 'principles'** as all companies are required to adhere to these.

The fourth paragraph in this section refers to institutional investors identifying at an early stage problems that may result in a significant loss. We would suggest that identifying issues when they have already become problems is too late. Institutional investors should endeavour to identify issues that could result in loss at an earlier stage, before the issues become problems and before any consequential loss is significant. We therefore propose amending this wording to '**... issues that may result in loss ...**'.

2.4 Guidance on Principle 4 – escalation of stewardship activities

We have no comments on the guidance to Principle 4 other than to suggest that the list of topics where institutional investors may have concerns should include board composition and succession planning (as we suggest for Principle 1).

2.5 Guidance on Principle 5 – collective engagement

The second paragraph of this section refers to collective engagement when risks posed threaten to destroy significant value. As in the guidance to Principle 3 above, we think that focussing on issues only when they threaten to destroy *significant* value is too late and we therefore suggest this should read '**... threaten to destroy value ...**'.

The third paragraph of this section refers to institutional investors '**... indicating their readiness to work with other investors ...**'. However, a statement on this would not provide important information on an institutional investor's degree of readiness to work with other investors. We therefore suggest this wording be revised to '**... indicating the extent of their readiness to work with other investors ...**'.

We also think that the deletion of the last paragraph in the guidance on Principle 5 is unfortunate. Whilst accepting that collective engagement, conflicts of interest and insider information are dealt with separately in the Code, we think that it is helpful for institutional investors to be reminded that they should have due regard to these issues when involved in collective engagement.

2.6 Guidance on Principle 6 – disclosure of voting policy and activity

The first paragraph of this section states that voting by institutional investors '**should not automatically support the board.**' We are concerned that there is a presumption that institutional investors vote in this way. Our members' experience is that, where institutional investors are not giving proper consideration to their voting, it is more likely that they will vote mechanistically on the recommendations of proxy voting agencies. We would therefore suggest that this second sentence of the first paragraph be removed or that it be replaced with the wording '**They should not automatically support the board or recommendations of proxy voting agencies.**'

The second paragraph gives guidance around institutional investors informing the company in advance of their intention to abstain or vote against a resolution. In our members' experience the issue facing companies is the timeliness of these notifications to companies, which frequently come at such a late stage it is impossible for companies to engage in dialogue with the relevant investors. We would therefore suggest amending the last sentence of this paragraph to read '**...inform the company in advance of their intention and the reasons why, giving sufficient time to allow the company to respond.**'

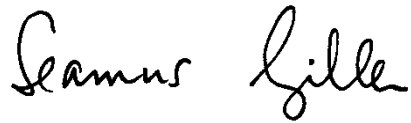
The last paragraph in this guidance appears to be aimed at the issue of voting on shares that are subject to stock lending and we think that this should be made clear. We suggest that the wording be amended to read 'Institutional investors should disclose their approach to stock lending and recalling lent stock, **and the effects on such stock being voted.**'

2.7 Guidance on Principle 7 – records of voting activity

We have no comments on the guidance to Principle 7 and are happy with the wording.

We would be glad to expand on any of these points should you like to discuss any of them further.

Yours sincerely

A handwritten signature in black ink that reads "Seamus Gillen". The signature is written in a cursive, flowing style.

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