ICMA AMIC Response to FRC Consultation of the UK Corporate Governance Code

The ICMA Asset Management and Investors Council (AMIC) was established in March 2008 to represent the buy-side members of the ICMA membership. ICMA is one of the few trade associations with a European focus and both buy-side and sell-side representation. AMIC welcomes the opportunity to respond to the FRC’s consultation on the UK Corporate Governance Code and the Stewardship Code and will do so mainly from a debt investors’ perspective as ICMA’s main focus is on debt instruments.

1. Do you have any concerns in relation to the proposed Code application date?
No, January 2019 is fine from our perspective.

2. Do you have any comments on the revised Guidance?
While we support the FRC’s suggested changes to the guidance, we think that an additional element could be added: a reference to the need to consult bondholders as one of the stakeholders. We believe bondholders should be explicitly recognised among the stakeholders, because of our contribution to the sustainable success of companies. While larger debt investors typically have opportunities and channels to actively engage, small and mid-sized institutions are usually excluded from meaningful dialogue and left with the simple choice of divesting their stake, if that is possible.

We believe it would be useful to design better channels to articulate bondholder concerns and interests and to encourage management to take these into account.

Therefore, we suggest adding a reference in Provision 5 of Section 1, which currently only mentions shareholders, that would ask firms to also engage and consult with other stakeholders such as bondholders.

3. Do you agree that the proposed methods in Provision 3 are sufficient to achieve meaningful engagement?
While AMIC has no particular views on how engagement with the workforce should be achieved, some of our members agree with the principle that this is a helpful provision in the revised code. Another part of our membership, however, considers that the proposed methods are limiting and would favour a more open approach, allowing them to engage with the workforce through other mechanisms than those described in Provision 3.

4. Do you consider that we should include more specific reference to the UN SDGs or other NGO principles, either in the Code or in the Guidance?
While sustainability considerations by companies is essential for their viability on the long term, a specific reference to a set of principles such as the UN SDGs may not provide companies with the flexibility to integrate ESG and/or wider stakeholder considerations, as appropriate or relevant to their sector and operating framework.

5. Do you agree that 20 per cent is ‘significant’ and that an update should be published no later than six months after the vote?
As debt investors without voting rights, we have no particular view on the 20% threshold suggestion.
6. Do you agree with the removal of the exemption for companies below the FTSE 350 to have an independent board evaluation every three years? If not, please provide information relating to the potential costs and other burdens involved.

Yes, as investors we value information on companies and value standards of governance, while recognising that there is a burden involved for those companies. Therefore a ‘comply or explain’ approach is preferred.

7. Do you agree that nine years, as applied to non-executive directors and chairs, is an appropriate time period to be considered independent?

We broadly agree but suggest that appropriate flexibility is retained, such as comply or explain. In some cases, tenures longer than nine years are more helpful than mandatory rotation.

8. Do you agree that it is not necessary to provide for a maximum period of tenure?

A maximum is probably fine to provide in the code, as long as there is sufficient flexibility to allow exceptions where the situations warrant it.

9. Do you agree that the overall changes proposed in Section 3 of the revised Code will lead to more action to build diversity in the boardroom, in the executive pipeline and in the company as a whole?

It is hard to predict whether these changes will deliver diversity, but it is a start and as debt investors we support the measures.

10. Do you agree with extending the Hampton-Alexander recommendation beyond the FTSE 350? If not, please provide information relating to the potential costs and other burdens involved.

While we do not have strong views on this, we do generally support increased transparency on diversity within firms, which should not be restricted by firm size.

11. What are your views on encouraging companies to report on levels of ethnicity in executive pipelines? Please provide information relating to the practical implications, potential costs and other burdens involved, and to which companies it should apply.

As debt investors we support the promotion of diversity, provided sufficient flexibility is allowed for companies to comply.

12. Do you agree with retaining the requirements included in the current Code, even though there is some duplication with the Listing Rules, the Disclosure and Transparency Rules or Companies Act?

Yes, we agree with retaining these requirements despite the duplication.

13. Do you support the removal to the Guidance of the requirement currently retained in C.3.3 of the current Code? If not, please give reasons.

We have no particular views on the removal of the requirement to make available the terms of reference of the audit committee.
14. Do you agree with the wider remit for the remuneration committee and what are your views on the most effective way to discharge this new responsibility, and how might this operate in practice?

Yes, we support the wider remit - as bondholder we support a sustainable remuneration policy that takes numerous stakeholders into account for the long-term success for the company.

15. Can you suggest other ways in which the Code could support executive remuneration that drives long-term sustainable performance?

No.

16. Do you think the changes proposed will give meaningful impetus to boards in exercising discretion?

Yes, it is a helpful start.

17. Should the Stewardship Code be more explicit about the expectations of those investing directly or indirectly and those advising them? Would separate codes or enhanced separate guidance for different categories of the investment chain help drive best practice?

AMIC is not supportive of more explicit expectations of investors in the Stewardship Code. While we welcome this inception consultation by the FRC, we do not see evidence that the current code has failed, which would warrant a change in concept from the current model. Within our membership there has been divided opinions around whether to maintain one code or create separate codes applying to different categories of the investment chain as there are good arguments to support both options. We believe there are merits in both approaches and at this stage there is not enough information to prefer one over the other. We look forward to engaging with the FRC on this aspect when a more specific consultation on changes to the Stewardship Code is launched.

18. Should the Stewardship Code focus on best practice expectations using a more traditional ‘comply or explain’ format? If so, are there any areas in which this would not be appropriate? How might we go about determining what best practice is?

No, we do not believe that the Stewardship Code should follow a comply or explain model regarding best practices. The tiering exercise is already in place and is in our opinion sufficient to highlight implementation of the Code.

19. Are there alternative ways in which the FRC could highlight best practice reporting other than the tiering exercise as it was undertaken in 2016?

No, as we explain in Question 18, the tiering exercise helpfully highlights best practices in reporting on compliance with the Code.
20. Are there elements of the revised UK Corporate Governance Code that we should mirror in the Stewardship Code?

In line with our response to Question 2 with regard to the UK Corporate Governance Code, we believe that a helpful additional element to the current Stewardship Code would be to specifically refer to bondholders as investors in companies.

21. How could an investor’s role in building a company’s long-term success be further encouraged through the Stewardship Code?

We believe explicitly recognising bondholders in the Stewardship Code would encourage engagement from a wider group of investors in companies. Similarly, as outlined in Question 2 we believe bondholders should also be recognised as a stakeholder in the UK Corporate Governance Code.

22. Would it be appropriate to incorporate ‘wider stakeholders’ into the areas of suggested focus for monitoring and engagement by investors? Should the Stewardship Code more explicitly refer to ESG factors and broader social impact? If so, how should these be integrated and are there any specific areas of focus that should be addressed?

We note that some investors may want to take further steps to engage with wider stakeholders, but firms should also have the flexibility to follow their own judgment and engagement model. Furthermore, it is important to note that we expect that the revised Stewardship Code will reflect the considerations of wider stakeholder groups as part of its implementation of the Shareholder Rights Directive.

With regard to the question whether ESG factors and social impact should be considered more broadly, as noted above, we believe that as a starting point the changes in the Shareholders Rights Directive (SRD) (2017/828/EU) should be implemented in the revised Stewardship Code, in particular new Article 3g on Engagement Policy.

23. How can the Stewardship Code encourage reporting on the way in which stewardship activities have been carried out? Are there ways in which the FRC or others could encourage this reporting, even if the encouragement falls outside of the Stewardship Code?

We believe the current reporting of compliance with the Code is sufficient, subject to adding the changes required by the SRD.

As recognised by the FRC in paragraph 27 of the consultation paper, it may also be pertinent to consider specifically referring to debtholders (as opposed to only "owners") as "investors".

24. How could the Stewardship Code take account of some investors’ wider view of responsible investment?

We believe there are sufficient current reporting possibilities for those investors who take a wider view of responsible investment. This could also become subject to change as a result of the European Commission’s High-Level Expert Group on sustainable finance or the UK Green Finance Task Force, so it would be prudent to await the conclusion of these exercises before taking a view to any further changes.
25. Are there elements of international stewardship codes that should be included in the Stewardship Code?

We have no views on this.

26. What role should independent assurance play in revisions to the Stewardship Code? Are there ways in which independent assurance could be made more useful and effective?

We have no views on this.

27. Would it be appropriate for the Stewardship Code to support disclosure of the approach to directed voting in pooled funds?

The revised SRD will reinforce the existing disclosures by institutional investors and asset managers of their voting activities. We do not believe that the FRC needs to go further than the implementation of the Directive.

28. Should board and executive pipeline diversity be included as an explicit expectation of investor engagement?

As we said in Question 9, we support increased diversity in the boardroom and the levels below, but we also believe that investors should retain flexibility around what approaches and focus to have when engaging with firms.

29. Should the Stewardship Code explicitly request that investors give consideration to company performance and reporting on adapting to climate change?

Like in our response to Question 28, we do not believe that reporting on adapting to climate change needs to be explicitly required in the Stewardship Code, especially in light of the forthcoming implementation of the SRD and any outcomes of the HLEG and UK Green Finance Task Force.

30. Should signatories to the Stewardship Code define the purpose of stewardship with respect to the role of their organisation and specific investment or other activities?

There is no need to further define the purpose of the stewardship an investor undertakes, as organisations wishing to do so can already do it.

31. Should the Stewardship Code require asset managers to disclose a fund’s purpose and its specific approach to stewardship, and report against these approaches at a fund level? How might this best be achieved?

As in Question 30, there is no need to require a purpose and approach to stewardship at fund level, where those companies operating specific funds already do so and most asset managers do not separate their stewardship approach at a fund level.

ENDS

28 February 2018