

Response from **Professor Carol Adams PhD CA FAICD, Professor of Accounting, Durham University Business School, UK** and Swinburne Business School, Melbourne, Australia on the:

UK Financial Reporting Council (FRC) Consultation on Draft Revised Stewardship Code

1st March 2019

Thank you for the opportunity to respond to the Draft Revised Stewardship Code at <https://www.frc.org.uk/consultation-list/2019/consulting-on-a-revised-uk-stewardship-code>. I responded to the initial questions that were included in the Corporate Governance Code consultation in January 2018 and strongly supported making references to the Sustainable Development Goals and the sustainable development issues (or Environmental, Social and Governance [ESG] issues) that have made the goals necessary. I am pleased to see that such references have been included as relevant to serving the interests of clients and beneficiaries.

My research has demonstrated that consideration of ESG risks and opportunities is essential to maximising long term value creation for companies and hence investors and their beneficiaries (see Adams, 2017a¹ and 2017b²). I recently gave evidence to the Australian Senate Inquiry on the SDGs where a number of investors, their representative bodies and stakeholders gave evidence regarding current investor initiatives concerning the SDGs. This is an increasing focus of asset owners and asset managers.

Two organisations I've worked with, Cbus (an Australian Superannuation fund) and Baillie Gifford (a global asset manager) have developed leading approaches to the SDGs which include following the steps set out in Adams (2017b). On the basis of their Impact Report for their Positive Change Strategy, Baillie Gifford have been involved in the better reporting stream of the UK Government's Implementation Taskforce on Impact investing³.

I applaud recognition in your consultation documents of the relevance to investors of the Sustainable Development Goals and the recommendations of the Financial Stability Board's Task Force on Climate related Financial Disclosure (TCFD). Key global standard setters are providing guidance to companies on responding to the Sustainable Development Goals (SDGs) and make explicit reference to the existence of sustainable development issues in the external environment which pose a risk to a company's ability to create value for shareholders and other stakeholders in the long term (see Adams, 2017b).

Please find below my response to your consultation questions.

¹ Adams, CA, (2017a) Conceptualising the contemporary corporate value creation process, *Accounting Auditing and Accountability Journal* 30 (4) 906-931 <http://dx.doi.org/10.1108/AAAJ-04-2016-2529> Also available [here](#)

² Adams, C A (2017) *The Sustainable Development Goals, integrated thinking and the integrated report*, IIRC and ICAS. Read [here](#).

³ See <https://www.grow-impact-investing.org/>

Q1. Do the proposed Sections cover the core areas of stewardship responsibility? Please indicate what, if any, core stewardship responsibilities should be added or strengthened in the proposed Principles and Provisions.

Yes, they do.

Q2. Do the Principles set sufficiently high expectations of effective stewardship for all signatories to the Code?

Given that practice with respect to climate change and other ESG risk and opportunities is still emerging and that there are many laggards, the Principles should explicitly require asset owners and asset managers to disclose their stewardship objectives with respect to them. This will assist in reducing risk to beneficiaries.

Q3. Do you support 'apply and explain' for the Principles and 'comply or explain' for the Provisions?

Yes. This will require asset owners and asset managers to carefully think through the Principles and Provisions and justify any non-application or non-compliance. Overall, this will lead to better practice.

Q4. How could the Guidance best support the Principles and Provisions? What else should be included?

The assessment mechanisms detailed in paragraph 60 will be particularly important in supporting compliance with the Principles and Provisions. It will be important to ensure that adequate resources are allocated to implement them.

Q5. Do you support the proposed approach to introduce an annual Activities and Outcomes Report? If so, what should signatories be expected to include in the report to enable the FRC to identify stewardship effectiveness?

Yes.

A key content element should be the processes of identifying and monitoring key ESG risks and opportunities and sustainable development issues impacting on their portfolio/ Fund.

Activities and Outcomes Reports should also discuss the process by which asset owners/ managers are engaging with companies in which they invest on: material ESG risks and opportunities; and, contributions to, or negative impacts on, achievement of the SDGs.

Activities and Outcomes Reports should also discuss how asset owners/ managers plan to improve their stewardship in the future in order to ensure continued improvements and adaptation of their investment approach to changing circumstances – particularly with regard to social and environmental risks.

Q6. Do you agree with the proposed schedule for implementation of the 2019 Code and requirements to provide a Policy and Practice Statement, and an annual Activities and Outcomes Report?

Yes.

Q7. Do the proposed revisions to the Code and reporting requirements address the Kingman Review recommendations? Does the FRC require further powers to make the Code effective and, if so, what should those be?

Publishing leaders and laggards as per para 72 and thematic reviews as per para 73 is important and should be resourced so it can occur annually.

Excellence is stewardship cannot occur without reference to ESG / sustainable development issues. By including such considerations in the revised Code, the FRC has raised the bar. Some of the responses from pension funds to the UK Government's Green Finance Inquiry indicated that assessment of this (for example, by the mechanisms in paras 72 ad 73) is sorely needed⁴.

Q8. Do you agree that signatories should be required to disclose their organisational purpose, values, strategy and culture?

Yes, as this has an influence on approach to stewardship. Ideally this should already be disclosed in other reporting and can be cross referenced to avoid duplication.

Q9. The draft 2019 Code incorporates stewardship beyond listed equity. Should the Provisions and Guidance be further expanded to better reflect other asset classes? If so, please indicate how?

Asset managers should be encouraged to disclose differences in approaches to stewardship across funds and asset classes.

Q10. Does the proposed Provision 1 provide sufficient transparency to clients and beneficiaries as to how stewardship practices may differ across funds? Should signatories be expected to list the extent to which the stewardship approach applies against all funds?

Signatories should be required to disclose significant differences in stewardship approach across funds. Some funds focus on particular SDGs or address particular ESG risks and opportunities and it is important to overall improvements to stewardship that this is known and shared.

Q11. Is it appropriate to ask asset owners and asset managers to disclose their investment beliefs? Will this provide meaningful insight to beneficiaries, clients or prospective clients?

Yes and yes. Given concerns about stranded assets and long term non-financial risks, it is particularly appropriate to expect asset owners and asset managers to disclose their investment beliefs with respect to climate change and other sustainable development or ESG risks and opportunities. Research demonstrates that they influence long term value creation (see Adams, 2017a⁵).

Q12. Does Section 3 set a sufficiently high expectation on signatories to monitor the agents that operate on their behalf?

It appears to.

⁴ The contrast between responses is highlighted at <https://drcaroladams.net/pension-funds-adopt-strikingly-different-approaches-to-climate-change-risk/>

⁵ Adams, CA, (2017a) Conceptualising the contemporary corporate value creation process, *Accounting Auditing and Accountability Journal* 30 (4) 906-931 <http://dx.doi.org/10.1108/AAAJ-04-2016-2529> Also available [here](#).

Q13. Do you support the Code's use of 'collaborative engagement' rather than the term 'collective engagement'? If not, please explain your reasons.

Yes, as long as it is defined. Given the importance of ESG issues to long term beneficiaries, and the relative newness of integrating ESG issues into investment approach and strategy, there should be an explicit requirement to engage on ESG risks and opportunities and the SDGs that companies materially impact on or contribute to.

Q14. Should there be a mechanism for investors to escalate concerns about an investee company in confidence? What might the benefits be?

Yes. This might result in corrective action which reduces risks to beneficiaries.

Q15. Should Section 5 be more specific about how signatories may demonstrate effective stewardship in asset classes other than listed equity?

Yes.

Q16. Do the Service Provider Principles and Provisions set sufficiently high expectations of practice and reporting? How else could the Code encourage accurate and high-quality service provision where issues currently exist?

They appear to.

regards



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