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FRC consultation on UK Corporate Governance Code and Stewardship Code

## WWF-UK RESPONSE

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## INTRODUCTION

- WWF-UK welcomes the opportunity to submit comments to the FRC's consultation on review of the Corporate Governance Code and to the initial consultation on the future direction of the Stewardship Code (where full consultation will follow mid-2018)

- WWF-UK – the UK arm of the global WWF Network, one of the world's largest environmental organisations – seeks to build a future where people and nature thrive. We see finance as a key lever to influence sustainable outcomes and appropriate corporate framework as crucial to driving the transition to a sustainable, resource-efficient and low-carbon UK economy.

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## OVERALL RESPONSE

- We welcome the FRC's move to review the Corporate Governance Code, and the future plan to review the Stewardship code. We especially support the emphasis on long-term sustainability and consideration of wider stakeholders.

- We believe it is important to consider the two codes together, so that the expectations from the Boards and the investors are aligned. Clarifying the roles of different actors along the investment chain in the Stewardship Code is also important. The Stewardship Code should be more explicit on this, and separate best practise guidance should be issued.

- The Stewardship Code should require its signatories to demonstrate how they are considering their long term sustainability and covering this in their stewardship activities.

## POINTS ON SPECIFIC QUESTIONS – CORPORATE GOVERNANCE CODE

*Q.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?*

- The revised Code should explicitly refer to the SDGs and the underpinning philosophy: a holistic approach to contributing to society, economy and environment delivered through collaboration between all stakeholders.
- This should be represented in both the Code and the Guidance – with the guidance providing the underpinning detail.
- The Code should have more explicit reference to the environment and the SDGs are a key mechanism to do this.
- It must be highlighted that SDGs are not just a tool for managing risk and reputation, but the framework offers a route to drive business innovation and value creation.

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

- Executive pay/reward should not be linked to unsustainable business practices over the long-term e.g. bonuses for increased exploitation of fossil fuel reserves by oil companies.

## POINTS ON SPECIFIC QUESTIONS – FUTURE DIRECTION OF THE UK STEWARDSHIP CODE

Q.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?

- The Stewardship Code should be clear about the obligations of different actors along the investment chain, but separate codes are not necessary.
- Intermediaries (asset managers, investment advisors and service providers) should follow the steer of the ultimate asset owner on stewardship practises. The asset owner should have a clear policy on stewardship and expect any intermediaries they engage to follow this policy.
- Rather than separate codes, guidance by type of investor (targeted specifically to asset owners, asset managers, investment advisors or service providers) should be issued separately. This should include detailed examples and case studies of best practise for each type of investor.

Q.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?

- Yes, and there are no areas in which this would be inappropriate as the 'explain' element allows signatories to explain non-compliance.

- In general the code should be more explicit about its expectations from its signatories. To help companies achieve best practise, providing best practise guidance and case studies specific to the different actors (asset owners, asset managers, investment advisors and service providers) would be helpful.

- Best practise will demonstrate a stewardship policy embedded in investor's company culture with internal buy-in and Board level support, timely execution and assessment, as opposed to top down compliance/reporting exercise.

- The code states that "*the investors are required to demonstrate effective stewardship in line with their specific investment objectives, while also seeking to secure long-term value by enhancing the quality of engagement between investors and companies to improve long-term risk-adjusted returns to shareholders"*. More detailed guidance on how to demonstrate the commitment to long-term value creation and best practise examples of this would be welcome (see question 22)

- Also more guidance on how to cover all relevant stakeholders within their stewardship activities, not just shareholders, is necessary (see question 24).

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

- Tiering practise should be renewed each year to keep the momentum in improved practise and disclosure, and remove signatories who are not complying to a required standard. Only such public ranking will create a 'race to the top'.

- To help companies achieve best practise, providing best practise guidance and case studies specific to the different actors (asset owners, asset managers, investment advisors and service providers) would be helpful.

- FRC could also offer periodic workshops or training days to the signatories of the code.

Q. 20 Are there elements of the revised Corporate Governance Code that we should mirror in the Stewardship Code?

- Yes. The two codes should be consider together in order to align the expectations of shareholders with the duties of boards.
- Both codes should emphasise long-term success, refer to social and environmental issues and reference ESG (whether in the form of references to SDGs, TCFD or otherwise).
- The Stewardship Code should align with s.172 Companies Act duties

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

- The Stewardship Code should explicitly refer to institutional investors' responsibility to invest in a way that promotes long-term sustainability (like the South African code already does).

Q.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?

- Yes, monitoring and engagement by investors should cover the relationships and impacts with wider stakeholders, including environment, in line with the requirements for companies by section 172 of Companies Act and Corporate Governance Code. The obligations on boards by the Corporate Governance Code should align with investors' stewardship expectations by the Stewardship Code.

- The Stewardship Code *"seeks to secure long-term value by enhancing the quality of engagement between investors and companies to improve long-term risk-adjusted returns to shareholders"*. Therefore investors should be required to demonstrate how they are considering their long term sustainability and covering this in their stewardship activities (through relevant ESG factors).

- Environmental and social issues should be specifically mentioned in Principle 1 statement on stewardship and throughout the principles. Alternatively there could be a separate Principle highlighting importance of environmental and social issues for effective stewardship.

- For specific factors - see answer to question 29.

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

- The code should ensure that investors are required to have a sound understanding of the broad range of interests and preferences of their members and beneficiaries, including ESG factors. The code should also require investments are consistent with time horizon of their members and beneficiaries. This would align the UK requirements with the recommendations of the High Level Expert Group on Sustainable Finance to the European Commission.

- There is currently no consensus on definition of responsible, or sustainable, investment. The code should therefore require the asset owners to define their view of sustainable investment.

- The code should also require the asset owners to demonstrate how they integrate their view on long term sustainability in their stewardship activities

- The code should require the asset managers/intermediaries at lower levels to follow the steer of the ultimate asset owner on their view on long term sustainability and how they integrate this in their stewardship activities.

- The code should encourage stewardship to be seen as an integral part of the investment approach rather than a separate compliance exercise.

Q.25 Are there elements of international stewardship codes that should be included in the Stewardship Code?

- Yes, explicit reference to institutional investors' responsibility to invest in a way that promotes long-term sustainability (South Africa), to ESG (Australia, Japan and the Netherlands) and including model policies and detailed guidance on voting (Australia).

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

- The use of the word adapting here is confusing as it could be interpreted as relating to climate change adaption only, rather than mitigation. We will answer this question assuming this was not the intention.

- Climate change is a material risk - as highlighted by the Financial Stability Board's Task Force on Climate-related Financial Disclosure (TCFD) - and therefore should be explicitly referred to in the Stewardship Code. Asset owners should recognise their role in addressing climate change, and their duty to engage with their intermediaries/investee companies on related risks and opportunities.

- We would like the code to explicitly refer to the Paris Agreement and to reporting in line with the recommendations of the TCFD. Providing the required asset level information all along the investment chain is required to also allow the asset owners to do this.

- Similar recommendations for other environmental factors (water, deforestation, pollution and decline in biodiversity) should be incorporated as they become available.

- While the code is principles based, best practise guidance could be issued to provide case studies and examples of ESG factors that should be considered and to show what methodologies and metrics are available.

Q. 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?

- Yes, it would be beneficial for the signatories to define the purpose of stewardship as it relates to their specific activities, rather than just broad commitment to it.

- They should also demonstrate what policies and processes they have in place to carry out their stewardship activities in different parts of their business/for each type of asset they manage/own.

- This would also allow the ultimate asset owners/end investors to assess alignment of intermediaries with their own view on stewardship and investment objectives.

Q.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?"

- Yes, fund's purpose and approach to stewardship should be disclosed as this may differ significantly between different funds managed by the same asset manager.

- This could be disclosed and discussed in the strategic report in the financial statements where the investment objectives, and explanation on how the directors have performed their duty under s172, are already discussed. Alternatively this could be included on the asset manager's website in a separate UK stewardship code report.