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Dear Catherine

The UK Corporate Governance Code and Stewardship Code consultations

I am writing on behalf of Lane Clark & Peacock LLP in response to the consultation on the proposed revisions to the UK Corporate Governance Code and the UK Stewardship Code, issued on 5 December 2017.

Lane Clark & Peacock LLP ("LCP") is a specialist consulting firm with over 600 personnel in the UK and Europe, including 110 partners. We have offices in London, Winchester and Ireland.

The provision of actuarial, investment and pensions administration advice, benefits, and directly related services, is our core business. About 90% of our work is advising trustees and employers on all aspects of their pension arrangements, including investment strategy. The remaining 10% relates to insurance consulting and business analytics. We provide investment advice to pension schemes with assets under management totalling around £115bn, of which approximately 6% (or £7bn) is invested in listed UK equities.

We are supportive of the Financial Reporting Council's work to promote the long term success of companies, thereby benefiting companies, investors and the economy as a whole. We welcome the chance to comment on the framework for reform of the Stewardship Code in particular.

Our responses to the consultation questions are attached as Appendix 1 in relation to the UK Corporate Governance Code (Q4 only) and Appendix 2 in relation to the UK Stewardship Code.

In summary, we suggest the following changes in relation to the UK Stewardship Code:

- more explicit emphasis on promoting the long term success of companies and the economy as a whole;
- greater recognition of the interests of wider stakeholders (such as customers, suppliers, the community and the environment) to ensure that corporate activity is sustainable;
- recognition of the importance of remuneration and other management incentives in achieving long term sustainable outcomes;
- acknowledgement of signatories' differing roles in the investment chain, and hence their differing opportunities for stewardship (for example, the role of asset owners in overseeing asset manager stewardship); and
- a move towards signatories reporting on outcomes rather than disclosing their processes.

We are happy for our comments, which represent the collective view of a number of people within LCP, to be attributed to LCP. We hope that our response is helpful and if you have any questions, or would like to discuss anything further then please contact me.

Yours sincerely

+ Prepared as an attachment to an email at 14:28 on 28 February 2018

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UK Corporate Governance Code

We have answered question 4 only below, since our expertise lends itself more to answer the questions relating to the UK Stewardship Code. We believe that our answer to this question supports our responses to those questions (as set out in Appendix 2). Our answer to this question is as follows:

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?

We believe that there should be more emphasis on environmental and social issues in the UK Corporate Governance Code, reflecting their importance to long-term sustainable corporate performance.

We also believe that there should be explicit reference to climate-related risks and opportunities in the UK Corporate Governance Code, mirroring a new reference in the UK Stewardship Code (see Q29). An easy and comprehensive way of including climate considerations in the Codes would be to encourage companies and investors to follow the Task Force on Climate-related Financial Disclosures' reporting recommendations.

We would also support encouragement for companies to explain how their business strategy supports achievement of the UN SDGs, since we believe that a company is more likely to have a long-term sustainable future if it is providing goods or services that are consistent with these internationally-supported policy objectives.

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?

Yes, there should be explicit guidance on the differing expectations of direct investors, indirect investors and service providers (distinguishing between those who assist investors with high-level matters such as manager selection and those who assist with detailed aspects of stewardship such as voting recommendations). However, we believe that there should only be one code. Separating the Code may lessen its impact and lead to inconsistencies.

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?

Some areas of the Code could be strengthened by indicating best practice expectations, where there is consensus on what best practice is. These might include approaches in the use of voting advisory services and stock lending. However, stewardship practices are evolving and there are many areas where such consensus does not exist and may not be desirable. These may include many aspects of monitoring and engaging with investee companies. Different organisations could demonstrate good stewardship in different ways depending on how they operate. Moreover, being too prescriptive may stifle progression to better approaches.

On the whole, we believe that the Code shouldn't be prescriptive regarding best practice. A better way to promote best practice would be to provide examples of good practice. We suggest the FRC collates views on, and examples of, current best practices by convening groups of signatories and by engaging with relevant bodies (such as the Investor Forum, the Pensions and Lifetime Savings Association (PLSA) and the Principles for Responsible Investment (PRI)).

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?

The tiering exercise provides valuable information on the quality of signatories' stewardship disclosures, and provides an incentive for laggards to improve, so we would not want that replaced. However, we don't believe that this is an effective way to highlight best practice because of the large number of Tier 1 signatories. Moreover, it focuses on disclosures rather than policies or outcomes. As noted in our response to Q18, we believe providing examples of good practice would be a better approach.

This could be taken further and an award system introduced, which incentivises organisations to move towards best practice. Given the diversity of good stewardship practices, such a system might identify a small number of "gold standard" investors (perhaps ten) who are judged to demonstrate good practices, rather than singling out one investor as "the best".

Although there are inevitably costs associated with tiering signatories and identifying good practices, we note that this is likely to reduce costs for asset owners seeking to compare asset managers on their stewardship practices and may be more cost-effective for the market as a whole. We further note that tiering should not be a one-off exercise, but requires periodic review to ensure that signatories' disclosures are keeping pace with evolving stewardship practices.

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

We believe that there should be alignment between the two Codes, so that the Stewardship Code incorporates all the relevant themes included in the UK Corporate Governance Code and vice versa. For example the focus on culture and diversity that is suggested for the UK Corporate Governance Code should be reflected in the UK Stewardship Code.

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

We believe that there should be more explicit references in the Stewardship Code to the purpose of stewardship being to promote the long term success of companies, and in particular that this is done in such a way that the ultimate providers of capital also prosper.

Outcomes are determined by behaviour which is in turn driven by incentives, both short-term and long-term. This is true both for senior company positions, and also within asset managers themselves. Although executive remuneration is often a focus of stewardship activities, there continue to be many cases of high rewards for poor performance and an increasing disconnect between pay levels in the C-suite and the average for the workforce as a whole. Asset managers may be conflicted when engaging with companies on remuneration, given that they themselves are often highly remunerated, and we suspect this is an important barrier to effective engagement on this topic. We therefore believe that asset owners need to take more of a role in this area, holding asset managers to account and perhaps challenging companies directly on this issue. See Q23 for some suggestions on how this could be encouraged further.

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, we think wider stakeholders, ESG factors and social impact should be incorporated, given their importance to the long term success of a company. However, the UK Corporate Governance Code should also do so to ensure consistency (see Q4).

In terms of integrating environmental and social matters into the Stewardship Code, as a minimum, they should be referenced where examples of stewardship topics are presented (such as the opening guidance for Principle 1 which lists "strategy, performance, risk, capital structure, and corporate governance").

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 think it is important that reporting moves towards an emphasis on activities and outcomes, rather than just disclosure of process. It would help if the Stewardship Code set out more specific reporting expectations, particularly around engagement (as reporting is less well developed on engagement than on voting).

We view stewardship reporting as more important for asset managers than asset owners, in part because many asset owners do not have a significant audience for this information. Instead, asset owners should be encouraged to regularly monitor managers' reporting and to hold them to account. This encouragement could be included within the Stewardship Code, although asset owners are more likely to improve their practices in this area if changes to the Code are part of a coordinated approach with other organisations, for example PLSA and the Pensions Regulator (not least because relatively few asset owners are signatories to the Code).

A "gold standard" approach could also work here, identifying signatories that have excelled (see Q19).

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

We support extension of the Stewardship Code to asset classes other than listed UK equities, reflecting the importance of stewardship throughout the investment universe. We believe investors should be encouraged to act in ways that encourage long-term value creation and sustainable investment returns throughout the global economy.

Many of the current principles are appropriate for other asset classes, although the emphasis will vary, and some principles may need modification or additional guidance. For example, property investors can enhance the sustainability of returns by engaging with other stakeholders such as tenants, property managers and local communities.

We believe the Stewardship Code should explicitly encourage investors to engage with policy makers and regulators on matters which support long-term sustainable economic performance. This would include systemic sources of risk, which can be addressed more effectively in this way than by engaging with individual companies. Although investors in some asset classes (eg government bonds) are not able to engage with individual companies, public policy engagement can – and, we would argue, should – be carried out by investors in all asset classes. This might include responding to relevant consultations, signing investor statements of support (for example the those relating to climate change), and dialogue with regulators and policymakers.

In some cases, engaging with investee companies may yield outcomes that contribute to better long-term performance for other investors, with limited direct benefits for the investor in question. This might be the case, for example, where debt holders encourage improved corporate performance that primarily benefits equity holders. This raises a fundamental question about the purpose of the Stewardship Code and whether its focus should be on improving the financial returns to signatories (and their ultimate clients and beneficiaries) or whether it should seek to improve long-term corporate performance in the public interest.

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

The guidance accompanying the ICGN Global Stewardship Principles emphasises a few points that are not explicitly contained within the Stewardship Code, but which we believe are worth consideration are:

- alignment of time horizons for delivering value (section 1.1);
- independent governance structures with disclosure of the criteria used for appointments (section 1.2);
- alignment of remuneration with an appropriate time horizon to encourage good governance and a focus on longer term performance (section 1.7);
- oversight by asset owners of stewardship activities carried out by asset managers on their behalf (sections 2.3 and 2.5); and
- prioritisation of companies for further analysis and engagement (sections 3.2 and 4.1).

In addition, as outlined elsewhere in our response, we support inclusion of:

- engagement with policy makers (section 4.6);
- awareness and mitigation of system-level risk (section 6.3); and
- integration of ESG related risks and opportunities (section 6.4).

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 think that independent assurance should be encouraged for asset managers only. Given that a prescriptive approach to this could be prohibitive for smaller organisations, we believe that independent assurance should be seen as the ideal approach rather than a required approach, but that there should still be an onus on those that do not have the resources to provide independent oversight to instead provide appropriate evidence of internal oversight.

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

We believe that disclosure of the approach to directed voting in pooled funds, and the rationale for that approach, should be encouraged. The Stewardship Code could also ask asset owners to disclose whether they have selected asset managers that allow directed voting.

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

Yes, and this should be multi-faceted diversity, not just one or two dimensions, eg gender diversity.

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

Yes. It should cover risks and opportunities relating to climate mitigation as well as adaptation. As noted in our response to Q4, the Task Force on Climate-related Financial Disclosures' reporting recommendations provide a suitable framework for this. Investors should be encouraged to report on their own approach to climate-related risks and opportunities, as well as engaging with investee companies on this topic.

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?

We support the current approach of disclosing how the investor applies stewardship, rather than defining the purpose of stewardship.

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?

We support better disclosure of variations in stewardship approach between the different funds that an asset manager offers, but there should not be prescriptive guidance. We believe asset managers should be asked to disclose how stewardship is approached across the firm, for example whether a firm-wide policy is used, or whether there are fund-specific or asset-class specific approaches.