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Material 4

# **Japan Financial Services Agency The Council of Experts Concerning the Stewardship Code**

**Presentation by  
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## Discussion Topics

- **Governance of institutional investors**
- **Vote disclosure**
- **Company engagement**
- **Role of asset owners**



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## International Corporate Governance Network

Established in 1995, ICGN's mission is to promote effective standards of corporate governance and investor stewardship to advance efficient markets and sustainable economies worldwide.

Our objectives are to:

- **Influence** policy by providing a reliable source of investor opinion on governance and stewardship
- **Connect** peers at global events to enhance dialogue between companies and investors around long term value creation
- **Inform** debate through knowledge and education to enhance the professionalism of governance and stewardship practices



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# Influencing policy

## ICGN Global Governance Principles

The ICGN Global Governance Principles, first published in 2004, is the ICGN's primary standard for well governed companies and investors alike. This flagship document was significantly revised in 2013 when we included standards – not only for companies – but also for investors. In doing so, the ICGN recognises the importance of aligning a shared responsibility between companies and investors in protecting and generating long-term value.



## ICGN Global Stewardship Principles

The ICGN Global Stewardship Principles provide a framework to help investors, particularly those with globally diversified portfolios, integrate stewardship responsibilities as part of their overall investment approach. Seven core principles address the key stewardship activities of company monitoring, engagement and voting supported by robust stewardship policies and processes.





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## 1. Governance of investors

### Foundations of effective stewardship

“Investors should keep under review their own governance practices to ensure consistency with the aims of national requirements and the ICGN Principles and their ability to serve as fiduciary agents for their beneficiaries or clients.”

- Time horizons for delivering value
- Independent oversight
- Ethics and conduct
- Capacity and experience
- Investment chain
- Conflicts of interest
- Appropriate remuneration

*Principle 1, ICGN Global Stewardship Principles*

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## 1.1 Governance of investors

### ICGN position on independent oversight

“Investors should be overseen by governance structures that act independently and without bias to advance beneficiary or client interests. This may involve the need to separate or ring-fence investment activities for clients from the investor’s own commercial pressures. Such governance structures should be subject to periodic independent review as consistent with good corporate governance practice. This includes the conduct of regular internal evaluations and periodic third party led evaluations, to ensure they meet expectations of accountability and effectiveness. The way in which individuals are appointed to serve on the governing body should be disclosed.

*Guidance 1.2, Principle 2: ICGN Global Stewardship Principles*



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## 1.2 Governance of investors

### ICGN position on capacity and experience

"Investors to have the appropriate capacity and experience to effectively oversee and manage their stewardship obligations (particularly in terms of monitoring, voting and engagement) in the interests of beneficiaries or clients. This includes devoting time and training for decision-makers along all parts of the investment chain, particularly co-ordinating with fund managers, to exercise stewardship and fiduciary duties. It can also include delegating to governance specialists to guide governance policies and voting."

*Guidance 1.4, Principle 1, ICGN Global Stewardship Principles*

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## 1.2(a) Governance of investors

### Anecdotal evidence from Florida SBA

“We attempt to balance our limited resources with the most significant and material governance concerns among owned companies. We rank global markets by the SBA’s size of investment, individual company performance (both short and long-term time frames—1,3,5, and 7 year timeframes), and also by governance factors. This results in staff spending virtually all of their time on pension investments of the largest size, lowest relative performance, and relatively-poor governance practices. As Japan is our second largest country by size of equity investment value, we naturally have focused on several Japanese companies.”

*Michael McCauley, Florida State Board of Administration, USA*





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## **1.2 (b) Governance of investors**

### **ICGN position on investor collaboration**

“Investors should be open to collaborating with other investors (both domestic and overseas) to leverage the voice of minority investors and exert influence where required, with investee companies. Investors should respect individual market regulations relating to acting in concert and market manipulation and be prepared to form or join investor associations to promote collective engagement.”

*Guidance 4.5, Principle 4: ICGN Global Stewardship Principles*



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## 1.3 Governance of investors

### ICGN position on conflicts of interest

“Investors should have robust policies to minimise or avoid conflicts of interest and such policies address how matters are handled when the interest of clients or beneficiaries diverge. Investors should rigorously review their investment activities and their client interests to identify and appropriately manage real or potential conflicts of interest.....Such conflicts of interest should be disclosed, along with remedies to mitigate them.....”

*Guidance 1.6, ICGN Global Stewardship Principles*



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## **1.3 (a) Governance of investors**

### **LGIM Conflicts of interest identification**

“Where do conflicts of interest potentially arise?”

- A large number of our clients are trustees of pension schemes that are associated with the companies in which LGIM invests
- Legal & General Group plc might try to influence LGIM’s activities on Corporate Governance, rights issues, takeovers etc
- Depending on the asset class (e.g. equities/fixed income), the investment strategies for active/index and funds are very different particularly in terms of the number of stocks held and the time scale for holding investments
  - The department receives and processes a great deal of “inside”, or price-sensitive information relating to a company’s activity, such as management succession, financing, or M&A activity.

LGIM owes each of its clients a duty of care and loyalty with respect to all services undertaken for clients, including proxy voting. LGIM places its clients’ interests ahead of its own and must cast proxy votes in a manner consistent with the best interest of its clients.”



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## **1.3 (b) Governance of investors**

### **LGIM Conflicts of interest mitigation**

- The team is structured and supported to minimise potential and perceived conflicts of interest. The team reports directly to the Chief Executive of LGIM and its activities are monitored and supported by two Non-Executive Directors. This acts as a safeguard and ensures we are able to engage on any topic, wherever needed, to achieve the best outcome for all clients.
- The LGIM Corporate Governance Committee, which includes the two Non-Executive Directors, meets quarterly to monitor LGIM's activities.
- Treat confidential material appropriately
- Train new front office staff in conflicts of interest
- If in doubt refer upwards to a Director, the CEO of LGIM, or NED's of LGIM (H)
- Have a register of conflicts which are reported to LGIM (H)
- L&G Group plc shares are held by Swiss Re for the benefit of LGIM pooled funds as they cannot be held directly. These shares are voted independently of LGIM
- For shares directly held by trusts and segregated funds, LGIM will seek clients' informed direction on voting



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## **1.3 (c) Governance of investors Room for improvement...**

“We recognise that stewardship activities may give rise to conflicts of interest. Where such conflicts arise, arrangements will be made to ensure that decisions are taken in the long term interest of clients. We monitor potential conflicts of interest with a member of staff dedicated to this function.”

*UK Stewardship Code Signatory*



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## **2.1 Voting disclosure**

### **ICGN position on vote disclosure**

“Investors should regularly disclose their actual voting records publicly on their website as well as directly to clients. Voting records should indicate whether resolutions were cast for, against or abstained.”

*Guidance 5.3, ICGN Global Stewardship Principles*

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## 2.2 Voting disclosure: BMO voting record on Schroders

#	Proposal	Mgt Rec	Vote
<b>Management proposals</b>			
1	Accept Financial Statements and Statutory Reports	For	For
2	Approve Final Dividend	For	For
3	Approve Remuneration Report	For	Against
<b>Notes:</b> We are concerned with regard to the significant quantum of annual bonus awards made during the year and the overall structure of remuneration at the company. The remuneration report is not considered to warrant support.			
4	Elect Rhian Davies as Director	For	For
5	Re-elect Michael Dobson as Director	For	Against
<b>Notes:</b> Retiring CEOs should not assume the role of the Chairman as it may impact a proper balance of authority and responsibility between executive management and the board.			
6	Re-elect Peter Harrison as Director	For	For
7	Re-elect Richard Keers as Director	For	For
8	Re-elect Philip Mallinckrodt as Director	For	For
9	Re-elect Massimo Tosato as Director	For	For
10	Re-elect Robin Buchanan as Director	For	For
11	Re-elect Lord Howard of Penrith as Director	For	For
12	Re-elect Nichola Pease as Director	For	For
13	Re-elect Bruno Schroder as Director	For	For
14	Reappoint PricewaterhouseCoopers LLP as Auditors	For	For
<b>Notes:</b>  Companies that have had the same auditor for a period of over 10 years should consider a plan or tender process for bringing in a new auditing firm.			
15	Authorise the Audit and Risk Committee to Fix Remuneration of Auditors	For	For
<b>Notes:</b>  Companies that have had the same auditor for a period of over 10 years should consider a plan or tender process for bringing in a new auditing firm.			
16	Authorise EU Political Donations and Expenditure	For	For
17	Authorise Issue of Equity with Pre-emptive Rights	For	For
18	Authorise Market Purchase of Non-Voting Ordinary Shares	For	For
19	Authorise the Company to Call General Meeting with Two Weeks' Notice	For	For



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## **3.1 Company engagement**

### **Proactive and reactive**

- Proactive approach: formal planning process using sophisticated spreadsheets showing size of holdings, geography, investment ranking, voting concerns and so on.
- Reactive approach: responding to sudden change and deal with the issue within a limited timeframe .
- Local investor networks can encourage constructive engagement, e.g., UK Investor Forum, Australian Council of Superannuation Investors





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## 4.1 Role of asset owners

### ICGN position on delegation of responsibilities

“Asset owners cannot delegate their fiduciary responsibilities and where they are unable to exercise stewardship over investee companies directly, they should ensure that their asset managers are undertaking these activities on their behalf through contracts or by other means.”

*Guidance 2.3, Principle 2, ICGN Global Stewardship Principles*

“Fiduciary standards require that the client’s interests are put first, that conflicts of interest should be avoided, and that the direct and indirect costs of services provided should be reasonable and disclosed”.

*Kay Report, 2012*



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## **4.2 Role of asset owners**

### **ICGN position on investment mandates**

“Asset owners should clearly incorporate their expectations regarding stewardship practices in the awarding of investment management agreements and in selecting asset managers to ensure that the responsibilities of ownership are appropriately and fully delivered in the interests of their beneficiaries”.

*Guidance 2.4, Principle 2, ICGN Global Stewardship Principles*



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## 4.2 (a) Role of asset owners

### ICGN Model Mandate: key areas

- ensuring that the timescales over which investment risk and opportunity are considered match those of the client;
- setting out an appropriate internal risk management framework so that the risks which matter for clients are managed effectively;
- effectively integrating ESG factors into investment decision-making ;
- aligning interests effectively through fees, pay structures and culture;
- ensuring adherence to the highest standards of stewardship;
- ensuring commission processes and payments reward appropriate research;
- ensuring that portfolio turnover is appropriate to the mandate, in line with expectations and managed effectively; and
- providing appropriate transparency such that clients can gain confidence about all these issues.



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## **4.3 Role of asset owners**

### **ICGN position on stewardship oversight**

“Asset owners should effectively oversee and monitor asset manager stewardship activities and their consistency with the asset owner’s investment beliefs, policies and guidelines. “

*Guidance 2.5, Principle 2, ICGN Global Stewardship Principles*



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## 5. Financial Reporting Council Tiers

- **Tier one** statements provide a good quality description of their approach to conflicts of interest, engagement and resourcing. They generally give good explanations where there's a departure from the principles of the code. There are 140 signatories in Tier 1 (90 managers, 50 owners).
- **Tier two** statements provide more standard reporting with less transparency and weaker explanations. There are 80 signatories in Tier 2 (55 managers, 25 owners)
- **Tier three** statements are of poorer quality and need improvement. There are 30 asset manager signatories in Tier 3. The FRC want to remove poor reporting from the code entirely and are working with Tier 3 signatories to help improve their reporting. After six months, those asset managers that remain in Tier three will be removed from the list of signatories.



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## **Annex 1: ESMA List on shareholder cooperation**

“4.1 When shareholders cooperate to engage in any of the activities listed below, that cooperation will not, in and of itself, lead to a conclusion that the shareholders are acting in concert:

(d) other than in relation to a resolution for the appointment of board members and insofar as such a resolution is provided for under national company law, agreeing to vote the same way on a particular resolution put to a general meeting, in order, for example:

(A) to approve or reject:

- (i) a proposal relating to directors’ remuneration;
- (ii) an acquisition or disposal of assets;
- (iii) a reduction of capital and/or share buy-back;
- (iv) a capital increase;
- (v) a dividend distribution;
- (vi) the appointment, removal or remuneration of auditors;
- (vii) the appointment of a special investigator;
- (viii) the company’s accounts; or
- (ix) the company’s policy in relation to the environment or any other matter relating to social responsibility or compliance with recognised standards or codes of conduct; or

(B) to reject a related party transaction.



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## **Annex 2: Financial Services Authority letter on shareholder engagement**

“We are satisfied that there is no fundamental inconsistency. In the three areas mentioned above [market abuse, disclosure of substantial shareholdings and changes in control rules] we do not believe that our regulatory requirements prevent collective engagement by institutional shareholders designed to raise legitimate concerns on particular corporate issues, events or matters of governance with the management of investee companies. Ad-hoc discussions or understandings of this nature would not, in our view, trigger the restrictions or disclosure rules imposed by our rules.”

*FSA Letter to Institutional Shareholder Committee, 2009*





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