Adherence to the FRC's Stewardship Code

At 30 September 2014

THE
INVESTMENT
ASSOCIATION
MAKING INVESTMENT
BETTER

June 2015

The Investment Association
65 Kingsway, London, WC2B 6TD

T +44 20 7831 0898
F +44 20 7831 9975
W theinvestmentassociation.org

June 2015

For enquiries please email The Investment Association at **enquiries@theinvestmentassociation.org**

CONTENTS

	About this report	2
	Foreword	3
1	Key Findings	4
2	Profile of respondents	8
3	Policies	11
4	Structure and resources	13
5	Monitoring and engagement	19
6	Quality of engagement	24
7	Practical examples	29
8	Voting	33
9	Reporting	36

APPENDICES

1	Steering Group members	39
2	Respondents to the questionnaire	40
3	Markets and proportions of shares voted	42

ABOUT THIS REPORT

Over the last five years The Investment Association has worked with the Financial Reporting Council (FRC) to monitor adherence to the FRC's Stewardship Code (the Code). The FRC issued the Code in July 2010 and a revised version in September 2012[1]. The Code operates on a 'comply or explain' basis and aims to enhance the quality of engagement between institutional investors and companies. It sets out good practice on engagement with investee companies, which includes monitoring companies, entering into a dialogue with boards and voting at general meetings.

The Code is directed in the first instance to institutional investors, Asset Owners and Asset Managers with equity holdings in UK listed companies, and then to Service Providers[2].

This is the fifth report on adherence to the Code and looks at the activities that support institutional investors' commitment in practice. It summarises the responses to a questionnaire sent to 288 signatories as at 30 September 2014. The past four reports covered the periods to 30 September 2013, 2012, 2011 and 2010, respectively.

In summary, the questionnaire requested details of:

- the type of respondent and assets managed/ owned (Section 2)
- the policy statement (Section 3)
- structure and resources, including the use of proxy voting agencies and the integration of stewardship into the investment process (Section 4)
- how monitoring is prioritised and markets and issues engaged on (Section 5)
- the quality of engagement (Section 6)
- practical examples of engagement with specific companies (Section 7)
- voting including whether voting records are publicly disclosed (Section 8)
- reporting to clients, including the frequency and content, and whether an independent opinion on voting and stewardship processes is obtained (Section 9).

During the course of this exercise a Steering Group chaired by the FRC's Director of Corporate Governance provided direction and independent oversight. The members of the Steering Group are set out in Appendix 1. The collation of the individual submissions that support the report has been reviewed by Ernst & Young LLP.

The Investment Association would like to thank all respondents for their contributions and the members of the Steering Group who gave their time.

1 See here for more details.

2 Broadly defined, Asset Managers act as agents and manage investments on behalf of their clients. They can be independent or owned by banks, insurers etc. Asset Owners are the underlying beneficial owners of assets and often outsource the management of those assets to Asset Managers. They include pension funds, insurance companies, charities etc. Service Providers offer services such as processing voting instructions, providing research and making voting recommendations. They do not hold equities for investment purposes and, where relevant, they are presented separately in this report. Thus, unless otherwise stated, references to "respondents" are to Asset Managers and Asset Owners only.

FOREWORD

THE STEWARDSHIP CODE WAS INTRODUCED IN 2010 AND FIVE YEARS ON WE WANT TO TAKE STOCK OF WHAT HAS BEEN ACHIEVED AND WHAT IMPROVEMENTS CAN BE MADE. THIS REPORT SHOWS HOW SIGNATORIES TO THE CODE ARE UNDERTAKING AND DEVELOPING THEIR STEWARDSHIP RESPONSIBILITIES.

We are encouraged that many investors and companies approach engagement openly and constructively. Engagement is about purposeful dialogue, constructive discussion over the longer term and, ultimately, about building trust.

Over the five years there has been an increase in the quantity and quality of engagement. Most encouraging is that almost 90 per cent of investors are satisfied with the outcome of their engagement. Those that are completely satisfied are able to effect change. Whilst the focus of the engagements outlined in this report unsurprisingly was remuneration, investors continued to state that other areas were more important, including corporate performance, culture and strategy and board leadership. Consequential changes were not always made after engagement occurred, but many companies were believed to be more responsive and engaged.

The report shows an increase in the resource devoted to stewardship analysis and activity. If engagement is to be undertaken on a longer term basis, both investors and companies need to ensure that their activities are appropriately resourced.

We have also seen a significant increase in voting activity and formal integration of stewardship factors in the broader investment analysis. Companies and investors prioritise their engagement activities by focusing on particular holdings or on particular issues.

Unfortunately the report shows a decrease in respondents notifying companies in advance of votes against or abstentions. Companies find this information very useful in their voting process and in further engagement with their investors. We encourage all investors to notify their companies in advance of their intentions in order to build an open dialogue.

For the first time, companies subject to the detailed case studies were asked to provide a response to the feedback given by investors. Extracts of the responses are in this report, but responses are detailed in full in 'Detailed Practical Examples', providing a wealth of information on the depth of engagement undertaken by companies and investors. It details frank disclosures and discussions and I urge companies and investors to note these insightful examples.

We are encouraged by the improvements we have seen over the past five years but realise the establishment of a culture of stewardship will take time. There is more to be done. The investment landscape is changing. Investors have increasingly global portfolios and this may have an impact on their engagement. At the same time, many UK companies are confronted with a greater proportion of overseas ownership. The globalisation of investment will continue, and we need to consider ways to meet the challenges this represents.

Asset owners, as the providers of capital, play a vital role in monitoring the actions of asset managers. Disappointingly, the report shows a drop in the number of mandates referring to stewardship, although there has been a significant increase since the first report. Asset owners will be subject to the proposed requirements of the Shareholder Rights Directive, so harnessing their influence is important.

The Stewardship Code has helped to build engagement in the five years since it was introduced. We look forward to responding to the challenges that remain by building better engagement to benefit companies, investors and the economy as a whole.

Let me thank The Investment Association for undertaking this survey, the Steering Group members for giving their time and the signatories who responded.

Sir Winfried Bischoff

1 KEY FINDINGS

PROFILE OF RESPONDENTS (SECTION 2)

More respondents and stabilising response rate. 130 out of 288 signatories responded – the largest number since the first exercise in 2010. This gave an overall response rate of 45 per cent – a slight increase from the 42 per cent in 2013 and 43 per cent in 2012. This is much less that the initial 67 per cent response rate when the questionnaire was sent to 75 signatories on the Code's introduction in 2010.

Make up of respondents broadly consistent year on year. Most respondents were Asset Managers: 92 Asset Managers managing £675 billion of UK equities responded in 2014 (2013: 82 and £708 billion). Thirty respondents were Asset Owners that owned £29 billion of UK equities (2013: 27 and £38 billion). Eight were Service Providers (2013:5).

Holdings of UK equities decreased but global equity holdings increased. Respondents' holdings in UK equity holdings decreased to £704 billion in 2014 from £746 billion in 2013. Their holdings in global equities increased to £2.8 trillion in 2014 from £2.7 trillion in 2013. There has been a steady decrease in the average size of respondent in terms of assets managed/owned since 2010.

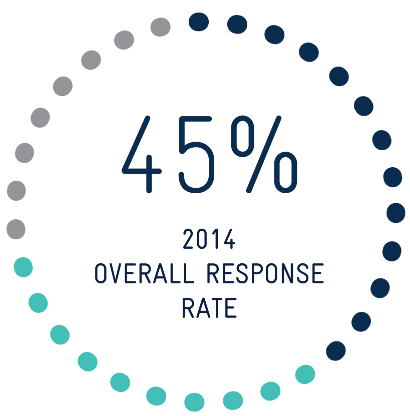
POLICIES (SECTION 3)

Principle 1 of the Stewardship Code requires signatories to *"publicly disclose their policy on how they will discharge their stewardship responsibilities"* while Principle 2 requires that they have *"a robust policy on managing conflicts of interest in relation to stewardship which should be publicly disclosed".*

All respondents have a public policy statement. In this context, 88 per cent of respondents also have a public conflicts of interest policy, an increase from 82 per cent in 2013 but lower than 94 per cent in 2012 and 96 per cent in 2011.

Fewer reviewed and made changes to their statement. Eighty-three per cent reviewed their policy statement in 2014 with 45 per cent making changes. This is a decrease from the 90 per cent that reviewed with 67 per cent making changes in 2013 when respondents were reflecting the 2012 revisions to the Code.

Fewer mandates to Asset Managers refer to stewardship. The proportion of Asset Managers where mandates refer to stewardship decreased to 74 per cent from 83 per cent in 2013. However, this is an increase from the 71 per cent in 2012; 65 per cent in 2011; and 66 per cent in 2010.



STRUCTURE AND RESOURCES (SECTION 4)

Most respondents conduct engagement and voting in-house. In this respect, the proportion that conduct all or some engagement in-house remained stable at 78 per cent compared to 2013. The proportion that vote all or some holdings in-house decreased to 73 per cent from 76 per cent in 2013. Again this is indicative of smaller respondents on average.

Where outsourced, external providers are monitored. Monitoring of external providers is mostly through a combination of periodic reports and meetings. All Asset Owners that outsource engagement refer to it by including it either in the Request for Proposals or in the mandate, with the majority addressing it during the manager selection process.

Significant increase in in-house resource. Where stewardship is in-house, the resource responsible for stewardship has increased significantly. In 2014 there were 2,090 individuals involved in stewardship which compares to 1,703 in 2013; 1,311 in 2012; 1,268 in 2011; and 769 in 2010. Over 80 per cent of respondents complement this resource with proxy voting or other advisory services which is described in their policy statement – an increase from 78 per cent in 2013. Section 4 provides more details on how proxy voting and other advisory services are used.

Stewardship is formally integrated into the investment process and significantly more portfolio managers/analysts involved. Consistent with prior years, 86 per cent of respondents that involve stewardship specialists have formal integration arrangements. At the same time there are more portfolio managers/analysts involved in stewardship where the head count increased by over 300 compared to an increase of 10 for the dedicated specialists. In addition, more respondents involve portfolio managers and analysts in all voting decisions: 37 per cent in 2014 as compared to 27 per cent in 2013.

MONITORING AND ENGAGEMENT (SECTION 5)

The Code requires signatories to monitor their investee companies and establish clear guidelines as to when and how they will escalate stewardship.

A variety of approaches to monitoring investee companies. The majority, 80 per cent, of respondents combine direct contact with the company and in-house and third-party research. Over half also contact other investors and stakeholders.

Engagement is prioritised and more engage with actively managed holdings. Thirty-five per cent of respondents engage with all their holdings (2013: 34 per cent) and 22 per cent engage when there are significant issues (2013: 26 per cent). However, significantly more engage with actively managed holdings: 16 per cent in 2014 compared to eight per cent in 2013.

Most engagement around board remuneration but corporate performance the most important. Most engagement was around board remuneration which reflected the introduction of the binding vote in 2014 and extensive outreach by companies. This was followed by corporate performance and then board leadership. It also contrasts with the issues that respondents considered the most important, which in descending order were: corporate performance; board leadership; culture and strategy; board and committee composition. Remuneration was fifth (fourth in 2013).

More engagement overseas, but less with other asset classes. Engagement overseas increased particularly in Western Europe (84 per cent compared to 81 per cent in 2013) and the US and Canada (76 per cent compared to 73 per cent in 2013) albeit it decreased in Central and Eastern Europe, and Japan. However, engagement with asset classes other than equities decreased. For example, 20 per cent engaged with private equity holdings as compared to 24 per cent in 2013, and 40 per cent with fixed income holdings compared to 41 per cent in 2013.

Fewer respondents attend AGMs as a matter of policy. The proportion of respondents that have a policy not to attend AGMs increased: 53 per cent as compared to 37 per cent in 2013 and 2012.

QUALITY OF ENGAGEMENT (SECTION 6)

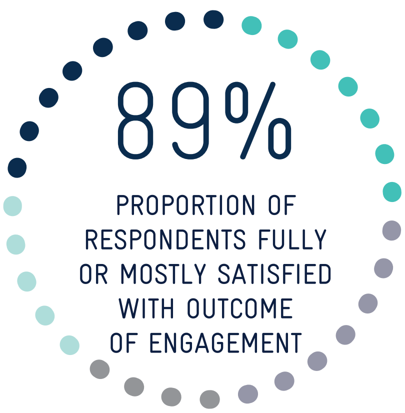
For the first time this year, respondents were invited to comment on the quality of the engagement, the dialogue with companies and the method of communication that was most effective, and the value of collective engagement.

Broadly the quality of the dialogue is the same but respondents expect to engage on a wider range of issues in 2015. Almost two thirds considered that the quality of the dialogue was the same as in 2013. Some expect remuneration to be less of an issue in 2015, given that remuneration polices are approved for three years, and they expect this to allow them to engage on a wider range of issues. For the quarter of respondents that considered the dialogue had improved from 2013, this was because companies were more responsive largely driven by the introduction of the binding vote on remuneration policy.

Direct contact the most effective means of communication. Over 80 per cent found direct contact and one-to-one meetings to be the most effective type of communication. However, about 20 per cent consider that a formal letter can often be one of the best means of securing change.

Collective engagement helps achieve critical mass. In most cases, collective engagement was seen as a way to achieve critical mass, thus allowing small investors access to companies. It was also viewed as a way to signal to companies that concerns are widely shared. However, some respondents stressed that achieving consensus was critical for collective action to be effective.

Respondents broadly satisfied with engagement. Almost 90 per cent were satisfied with the outcome of their engagement. Those that were completely satisfied were able to effect change whereas others noted that although companies were more responsive than in prior years, this did not necessarily result in changes.



PRACTICAL EXAMPLES (SECTION 7)

To see how stewardship works in practice, respondents were invited to describe how they engaged with specific companies during the year. The companies concerned were AstraZeneca plc, Experian plc, GlaxoSmithKline plc, Sports Direct plc, and Standard Chartered plc. The responses are summarised in Section 7 and an in depth analysis on objectives, outcomes, and how respondents voted on particular resolutions at AGMs is set out in the separate document 'Detailed practical examples'. This document also includes many quotes from respondents and, for the first time, comments from the companies concerned.

Engagement covers a variety of issues. For each company, the main objectives were as follows:

- GlaxoSmithKline – where 38 respondents mainly sought to address concerns over bribery allegations and culture.
- AstraZeneca – where 30 respondents engaged primarily on Pfizer's takeover bid that was withdrawn.
- Standard Chartered –where 29 respondents engaged mainly on directors' remuneration and governance.
- Experian – where 25 respondents engaged mainly on succession and the Chief Executive taking over as Chairman and strategy.
- Sports Direct – where 15 respondents engaged over remuneration and board independence.

As objectives vary, so do the channels of communication. For GlaxoSmithKline and Sports Direct, most contact was with the Chairman while for AstraZeneca it was with the Executive Directors. For Experian and Standard Chartered most contact was with Investor Relations and the Chair of the Remuneration Committee, respectively.

Collaboration helpful except where a lack of consensus. More respondents collaborated with other investors when engaging with GlaxoSmithKline and Sports Direct (13 and nine, respectively) although several collaborated in respect of AstraZeneca and Standard Chartered (eight each). This collaboration was helpful in that respondents found that other investors shared their concerns. Where it was not particularly helpful, it was mainly down to lack of consensus on the course of action or the desired outcome not being achieved.

The majority of respondents achieved their objectives. In every case, over half of the respondents considered that the quality of the engagement was good in that the companies were open to discussion even if they did not make any changes as a result. The exception was Sports Direct where some felt that the presence of a dominant shareholder weakened their position as minority shareholders.

VOTING (SECTION 8)

Principle 6 of the Stewardship Code states that investors should *"seek to vote all shares held"* and the Guidance requires that they *"disclose publicly voting records"*.

A significant increase in voting activity. The proportion of respondents that vote all shares in UK companies increased to 84 per cent from 78 per cent in 2013 while there were similar increases in all other regions including Europe, and USA and Canada.

An increase in the disclosure of voting records. The proportion of respondents that publicly disclose their voting records increased to 68 per cent from 66 per cent in 2013 and 65 per cent in 2012. Of these, three quarters disclose all votes – up from 62 per cent in 2013 – with over half including the rationale behind their decision.

Decrease in respondents that notify companies in advance of votes against or abstained. This dropped to 39 per cent in 2014 compared to 47 per cent in 2013 – the Guidance to Principle 6 states that it is good practice to do so.

REPORTING (SECTION 9)

Principle 7 requires that institutional investors *"report periodically on their stewardship and voting activities"* and the Guidance states that Asset Managers should *"obtain an independent opinion on their engagement and voting processes"* and disclose publicly the existence of such assurance.

Nearly all respondents report to clients or beneficiaries on their stewardship and voting activities. However, 90 per cent of respondents in 2014 report to clients compared to 94 per cent in 2013. Ten per cent do not report at all – an increase from one per cent in 2013.

Mixed views on the benefit of an independent opinion on stewardship and voting. The proportion of respondents that obtained an independent opinion on both their voting and engagement processes in the last 12 months was similar to last year at 18 per cent (2013: 17 per cent) while that for voting only, decreased to 18 per cent (2013: 21 per cent) (no respondent addressed engagement only in 2014). Two thirds of those that obtained an independent opinion make it publicly available. The proportion of respondents that did not obtain an independent opinion and have no plans to do so increased to 53 per cent from 45 per cent in 2013. Of these, 41 per cent have some or all of these processes reviewed by internal audit and 20 per cent have plans to do so within the next 12 months.

2 PROFILE OF RESPONDENTS

TYPES OF RESPONDENT

The questionnaire was sent to 288 institutional investors that had signed up the Code as at 30 September 2014[3] – 200 Asset Managers, 76 Asset Owners and 12 Service Providers. Overall, 130 responded – the largest number of respondents since the first exercise in 2010. This gave a response rate of 45 per cent, the highest in three years (Table 1). Whilst the response rate increased for Service Providers (67 per cent in 2014 compared to 42 per cent in 2013) and Asset Managers (46 per cent in 2014 compared to 41 per cent in 2013), for Asset Owners, the response rate decreased to 39 per cent from 42 per cent in 2013, even though three more responded – see Table 2.

There was a marked decrease in the value of respondents' holdings in UK equities, amounting to £704 billion in 2014 compared to £746 billion in 2013 and £733 billion in 2012. Asset Managers held £675 billion accounting for 30.4 per cent of the UK equity market – an average of £8.6 billion per Manager compared to an average of £10.1 billion in 2013 and £10.8 billion in 2012. Asset Owners held £29 billion or the equivalent of 1.3 per cent of the UK equity market – down from £38 billion in 2013 and £31 billion in 2012 (Table 2).

In this context, the Investment Association's Asset Management Survey[4] reported that during 2013-2014, asset managers reduced their holdings in UK equities. This is also consistent with the increasing ownership of UK companies by overseas investors previously documented in the ONS share ownership survey[5]. Moreover, although respondents' UK equity holdings decreased, their total holdings in global equities increased to £2.8 trillion in 2014 from £2.7 trillion in 2013.

It should also be noted that as Asset Managers could be managing Asset Owners' holdings, some of the assets reported in Table 2 may relate to the same holdings and be double-counted. Service Providers do not hold equities for investment purposes.

TABLE 1: TYPES OF RESPONDENT AND RESPONSE RATE

	No. of questionnaires sent					Percentage response rate				
	2014	2013	2012	2011	2010	2014	2013	2012	2011	2010
Asset Managers	200	198	177	128	58	46	41	41	45	71
Asset Owners	76	64	52	34	12	39	42	44	59	58
Service Providers	12	12	12	10	5	67	42	58	50	40
Total/overall rate	**288**	**274**	**241**	**172**	**75**	**45**	**42**	**43**	**48**	**67**

TABLE 2: TYPE OF RESPONDENT AND UK ASSETS MANAGED/OWNED

	No. of respondents					UK assets managed/owned (£ billion)[6]				
	2014[7]	2013	2012	2011	2010	2014	2013	2012	2011	2010
Asset Managers	92	82	73	58	41	675	708	702	668	590
Asset Owners	30	27	23	20	7	29	38	31	31	15
Service Providers	8	5	7	5	2	n/a	n/a	n/a	n/a	n/a
Total	**130**	**114**	**103**	**83**	**50**	**704**	**746**	**733**	**699**	**60**

3 As at 30 September 2014 there were 296 signatories to the Stewardship Code of which eight did not receive a questionnaire because each had two entities that were signatories.

4 Investment Management Association, Asset Management in the UK 2013-2014, September 2014, Pages 21-22.

5 Office for National Statistics, Ownership of UK quoted shares, 2012.

6 The 2014 figures exclude 14 Asset Managers and 3 Asset Owners that were unable to provide this figure. For three respondents the value of UK equities was taken from the IMA Asset Management Survey 2013-2014 and for six respondents from the Adherence to the FRC's Stewardship Code survey 2013, adjusted for movements in the FTSE All Shares Index.

7 One respondent previously categorised itself as an Asset Manager but as an Asset Owner in 2014.

The sample of signatories that respond varies from year to year which may affect the comparability of results. However, there is a core sample of institutional investors that consistently respond every year. Almost two thirds of the 130 respondents in 2014 also responded in 2013 and almost half responded in the last three years. A little over a quarter of the 2014 respondents responded in each of the five years since 2010 (see Table 3).

The Guidance to **Principle 1** states that *"the stewardship responsibilities of those whose primary activities are related to asset ownership may be different from those whose primary activities are related to asset management or other investment-related services"*.

Not only the type but also the structure of respondent can affect how stewardship is conducted. For example: whether an asset manager manages its parent's assets or is independent and only manages those of a third party; whether an asset owner is a pension fund, charity or other type of owner; and the type of service a service provider offers. Thus Asset Managers were asked for details of their parent company (Table 4), Asset Owners for the type of ownership (Table 5), and Service Providers for the type of service provided (Table 6).

These distinctions should be borne in mind when reading this report but are not necessarily clear-cut. For example, one respondent classified as an Asset Owner manages its own and third party assets, and provides corporate governance services to others (an overlay service).

ASSET MANAGERS

Similar to 2013, over a half of the Asset Managers are independent, 14 per cent are owned by an insurer and 10 per cent by an Asset Owner. Nine per cent of Asset Managers are owned by retail or investment banks and nine per cent have "Other" types of parent such as another asset manager or a legal partnership (Table 4).

TABLE 3: RECURRING RESPONDENTS

	No. of respondents				Per cent of 2014 respondents			
	2014-2013	2014-2012	2014-2011	2014-2010	2014-2013	2014-2012	2014-2011	2014-2010
Asset Managers	64	49	42	30	70	53	46	33
Asset Owners	18	13	8	3	60	43	27	10
Service Providers	3	2	2	1	38	25	25	13
Total	**85**	**64**	**52**	**34**	**65**	**49**	**40**	**26**

TABLE 4: ASSET MANAGERS – PARENT

	No. of respondents				Per cent of respondents			
	2014	2013	2012	2011	2014	2013	2012	2011
Retail bank	5	3	3	3	5	4	4	5
Investment bank	4	4	7	3	4	5	10	5
Insurer	13[8]	15	13	14	14	18	18	24
Independent	53[9]	43	35	27	58	53	48	47
Asset Owner	9[10]	11	9	5	10	13	12	9
Other	8	6	6	6	9	7	8	10
Total	**92**	**82**	**73**	**58**	**100**	**100**	**100**	**100**

8 One respondent's ownership is divided between its staff and two insurance companies.

9 Fifteen are owned by an independent company.

10 Two are occupational pension schemes and one is a foundation owned by Swiss pension funds.

ASSET OWNERS

Similar to prior years, the majority of Asset Owners are pension schemes. However, this year there was a marked increase in the proportion of public pension schemes which accounted for 40 per cent of Asset Owners, up from 30 per cent in 2013, and a decrease in the proportion of occupational pension schemes to 43 per cent from 56 per cent. For the two "Other", one is a life company platform for UK pension schemes and the other an independent self-managed scheme (see Table 5).

SERVICE PROVIDERS

The number of Service Providers that responded increased to eight in 2014 from five in 2013. Half of these are proxy voting agencies – with one specifying that it is a *"corporate governance research provider"* – and the other half are consultants (Table 6).

Service Providers do not manage nor own equities and so a number of questions did not apply to them or were approached from a different viewpoint. Where relevant, Service Providers' responses are reported separately in this report from those of Asset Managers and Asset Owners.

TABLE 5: ASSET OWNERS – TYPE

	No. of respondents				Per cent of respondents			
	2014	**2013**	**2012**	**2011**	**2014**	**2013**	**2012**	**2011**
Occupational pension scheme	13	15	11	8	43	56	48	40
Public pension scheme	12	8	8	7	40	30	34	35
Private pension scheme	1	–	–	2	3	–	–	10
Charity/foundation	2	2	2	1	7	7	9	5
Other	2	2	2	2	7	7	9	10
Total	**30**	**27**	**23**	**20**	**100**	**100**	**100**	**100**

TABLE 6: SERVICE PROVIDERS - TYPE

	No. of respondents				Per cent of respondents			
	2014	**2013**	**2012**	**2011**	**2014**	**2013**	**2012**	**2011**
Proxy voting agency	4	3	6	3	50	60	86	60
Consultant	4	2	1	2	50	40	14	40
Total	**8**	**5**	**7**	**5**	**100**	**100**	**100**	**100**

3 POLICIES

PUBLIC POLICY STATEMENT

Principle 1 of the Stewardship Code requires signatories to *"publicly disclose their policy on how they will discharge their stewardship responsibilities"*. The Guidance specifies that this policy *"should disclose how the institutional investor applies stewardship with the aim of enhancing and protecting the value for the ultimate beneficiary or client"* and *"should reflect the institutional investor's activities within the investment chain, as well as the responsibilities that arise from those activities"*.

Furthermore, the preface to the Code states: *"The FRC expects signatories of the Code to publish on their website, or if they do not have a website in another accessible form, a statement that:*

- *describes how the signatory has applied each of the seven principles of the Code and discloses the specific information requested in the guidance to the principles; or*
- *if one or more of the principles have not been applied or the specific information requested in the guidance has not been disclosed, explains why the signatory has not complied with those elements of the Code."*

Given that only those that had committed to the Code were invited to complete the questionnaire, all respondents have a public policy statement on how they discharge their stewardship responsibilities. For eight respondents – four Asset Managers and four Asset Owners (2013: four and two, respectively) – the policy statement is on the FRC's website as opposed to their own. In this context, the FRC analysed the policy statements of a randomly selected sample of 50 signatories in 2014 and concluded that *"not all are reporting against all seven principles of the Code. For those who do report against all the principles the depth of statements continues to vary considerably[11]"*.

CONFLICTS OF INTEREST POLICY

It is institutional investors' duty to act in the interests of their clients and/or beneficiaries and **Principle 2** of the Stewardship Code requires them to *"have a robust policy on managing conflicts of interest in relation to stewardship which should be publicly disclosed"*. The Guidance clarifies that conflicts could arise when voting on matters affecting a parent company or a client. It also specifies that *"the policy should also address how matters are handled when the interests of clients or beneficiaries diverge from each other"*.

Eighty-eight per cent of respondents disclose publicly their conflicts of interest policy – 24 per cent as a standalone document and 64 per cent within or referenced in their policy statement. Although this is an increase from 82 per cent in 2013 it is lower than in 2012 and 2011 at 94 and 96 per cent, respectively (see Table 7).

Eleven per cent, that is 13 respondents, do not publish their conflicts of interest policy. However, eight clarified that they make it available to existing and potential clients on request and two include it in investment consultants' due diligence process. One respondent is currently finalising its conflicts of interest policy following an organisational change and one stated that *"it is not expected to be a contentious issue and is not considered relevant to [its] client base"*[12].

TABLE 7: PUBLIC CONFLICTS OF INTEREST POLICY

	Per cent of respondents			
	2014	**2013**	**2012**	**2011**
Standalone	24	19	12	6
Within or referenced in Code statement	64	63	82	90
Not public	11	15	6	4
No response	1	3	–	–
Sample size	**122**	**109**	**96**	**78**

Five of the Service Providers have a conflicts of interest policy which is public, two as a standalone document and three within or referenced in their policy statement. Of the three Service Providers that do not disclose their conflicts of interest policy one discloses it to all clients, one has a policy but it does not address stewardship as its *"position in the investment chain ... does not pose material conflicts of interest around stewardship"* and one did not specify why its policy is not public.

[11] FRC, Developments in Corporate Governance and Stewardship 2014, January 2015, Page 20.

[12] One respondent did not clarify why its conflicts of interest policy is not public.

REVIEWING AND UPDATING POLICY STATEMENTS

The preface to the Stewardship Code states that *"signatories are encouraged to review their policy statements annually, and update them where necessary to reflect changes in actual practice"*.

Eighty-three per cent of respondents reviewed their statement during the past year and 45 per cent made changes (Table 8). This is a decrease from 2013 when respondents were more likely to review and update their statements to reflect the amendments made to the Stewardship Code in 2012.

The changes this year mainly involved minor amendments such as updating the language following an organisational change. Others introduced more substantial changes to reflect:

- disclosure of voting records;
- updated conflicts of interest policy;
- obtaining an independent external opinion on engagement and voting processes;
- collective engagement;
- communication with investee companies.

TABLE 8: STATEMENT REVIEWED

		Per cent of respondents	
	2014	**2013**	**2012**
Reviewed			
Changes made	45	67	29
No changes made	38	22	48
	83	90	77
Not reviewed	16	9	23
No response	1	1	–
Sample size	**122**	**109**	**96**

Five of the Service Providers reviewed their statements during the year and one updated it to reflect an organisational change.

ASSET MANAGERS' CLIENT MANDATES

In its report of developments in Corporate Governance in 2014, the FRC stated that one of the areas of focus for 2015 and 2016 would be *"generating demand from asset owners for stewardship work by fund managers[13]"*.

In this context, Asset Managers were asked whether they make their institutional clients aware of stewardship and how many of their mandates refer to stewardship.

Eighty-four of the 92 Asset Manager respondents have institutional clients of which 85 per cent make their clients aware of stewardship.

The proportion of Asset Managers for which all or some of their client mandates refer to stewardship decreased to 74 per cent in 2014 from 83 per cent in 2013. However, this partly reflects the relatively large proportion of respondents that did not answer this question in 2014 (Table 9). Adjusting for this, the decrease is less pronounced to 84 per cent in 2014 from 88 per cent in 2013.

TABLE 9: MANDATES THAT REFER TO STEWARDSHIP

			Per cent of respondents		
	2014	**2013**	**2012**	**2011**	**2010**
All clients	40	44	30	29	10
Some clients					
Three quarters	10	16	11	4	
Half	9	11	8	10	
A quarter	15	12	22	22	
	34	39	41	36	56
None	14	11	28	28	29
No response	12	6	1	7	5
Sample size	**92**	**82**	**73**	**58**	**41**

[13] Page 17

4 STRUCTURE AND RESOURCES

STRUCTURE AND OUTSOURCING

Institutional investors may conduct stewardship in-house or outsource it fully or partly. This is not relevant for Service Providers which are excluded from this section.

The preface to the Stewardship Code states that *"institutional investors may choose to outsource to external service providers some of the activities associated with stewardship"* and adds that *"they cannot delegate their responsibility for stewardship. They remain responsible for ensuring those activities are carried out in a manner consistent with their own approach to stewardship."*

The proportion of respondents that carry out engagement fully or partly in-house remained at 78 per cent with 22 per cent of respondents – 22 Asset Owners and five Asset Managers – outsourcing all engagement. However, there has been a decline in the proportion of respondents that vote all or some of their shares in-house, which was at 73 per cent compared to 76 per cent in 2013. Twenty-seven per cent of respondents – 22 Asset Owners and 11 Asset Managers – outsource all voting. Most commonly engagement and voting are outsourced to an external investment manager (see Table 10).

Where respondents outsource all voting or engagement, they monitor the external parties that undertake these activities on their behalf. The majority, about two-thirds, monitor through a combination of periodic reports and meeting with the external parties concerned (see Table 11)[15]

TABLE 11: MONITORING OF EXTERNAL PARTIES

	Per cent of respondents	
	Voting 2014	**Engagement 2014**
Periodic reports	27	26
Meetings	3	4
Both of the above	67	67
Other	3	4
Sample size	**33**	**27**

TABLE 10: HOW STEWARDSHIP IS CONDUCTED[14]

	Per cent of respondents					
	Voting 2014	**Engagement 2014**	**Voting 2013**	**Engagement 2013**	**Stewardship 2012**	**Stewardship 2011**
All in-house	63	70	63	71	68	82
Partly in-house	10	8	13	7	15	
Outsourced	27	22	24	22	17	18
External investment manager	12	11	11	11	8	12
Overlay service provider	9	3	8	6	9	6
Both	4	5				
Other	2	2	5	5		
Sample size	**122**	**122**	**109**	**109**	**96**	**78**

14 The option "Some in-house" only became available to respondents in 2012, and outsourcing to "other" in 2013, and "both" in 2014.

15 The two respondents that answered "other", one for voting and one for engagement, did not specify how they monitor third parties.

Most commonly, it is the trustees that monitor outsourced engagement (ten respondents compared to five in 2013) with portfolio managers and analysts monitoring for six respondents (2013: seven respondents) and investment consultants for three respondents (2013: three respondents). For only one respondent the monitoring is undertaken by a stewardship specialist. Others use different combinations, for example:

- *"fund officers, pensions committee and investment panel..."*
- *"pension fund officers"*
- *"... management team (including portfolio managers and ESG specialists)".*

Specifically, the 22 Asset Owners that outsource all engagement were asked how they address stewardship. Fifty per cent refer to it in their request for proposals, 59 per cent in the mandate and 86 per cent address it during the manager selection process (Table 12). This is consistent with results from the NAPF's Engagement Survey which reported that 51 per cent of its pension fund respondents set out their expectations with respect to stewardship in mandates[16].

Encouragingly, each of the 22 Asset Owners refers to engagement in at least one way and over a third refer to it in all three ways. This is particularly important as Asset Owners will ultimately drive Asset Managers' stewardship (the NAPF's Survey showed that fewer investment consultants raise the issue of stewardship with their pension fund clients than previous years[17]).

TABLE 12: ADDRESSING ENGAGEMENT WHEN OUTSOURCED

		Per cent of respondents 2014
Request for proposals (RFPs)		50
Manager selection process		86
Mandates		59
	At least one	100
	All three	36
Sample size		**22**

With the exception of section 8 on voting, those that outsource all engagement are excluded from the remainder of this report which focuses on the 95 respondents that carry out all or some of their engagement in-house. Section 8 on voting focuses on the 87 respondents that carry out all or some of their voting in-house.

16 NAPF, Engagement survey: pension funds' engagement with investee companies, November 2014, Page 19.

17 Page 14

RESOURCES

There was again a large increase in the headcount responsible for stewardship in 2014 although smaller than that in 2013. There were 387 more individuals involved compared to 2013 and this increased average headcount to 22 per respondent compared to 20 in 2013 (see Table 13).

Portfolio managers and analysts make 83 per cent of this resource. Dedicated specialists account only for 11 per cent but play a role for almost 60 per cent of respondents.

INTEGRATION INTO THE INVESTMENT PROCESS

Engagement on strategy and performance may often be handled by the portfolio managers/analysts, with specialists handling particular aspects such as corporate governance and SRI. At times, this dual approach can give rise to questions as to whether those conducting stewardship represent the views of the portfolio managers responsible for the investment and how stewardship is integrated into the investment process. Indeed, in the FRC's report on developments in Corporate Governance in 2014, it was stated that companies that participated in the GC100 survey *"highlighted concerns with the low level of integration*

TABLE 13: PRIMARY RESOURCE RESPONSIBLE

		Headcount *No. of respondents* **2014**	**2013**	**2012**	**2011**	**2010**
Portfolio managers/analysts with dedicated specialists looking at general policy	Portfolio managers	544	398	221	81	57
	Specialists	22	20	22	16	3
	Others	4	5	7	4	–
	No. of respondents	*8*	*7*	*11*	*3*	*2*
Both portfolio managers/analysts and dedicated specialists	Portfolio managers	805	745	547	640	469
	Specialists	195	173	170	166	94
	Others	22	23	35	24	–
	No. of respondents	*45*	*38*	*37*	*36*	*24*
Dedicated specialists only	Specialists	3	17	40	29	38
	Others	–	4	8	6	–
	No. of respondents	*2*	*6*	*4*	*3*	*4*
Others		59	23	10	2	–
	No. of respondents	*4*	*4*	*4*	*1*	–
Total headcount where specialists and others have a role		1,654	1,408	1,060	968	661
	No. of respondents	*59*	*55*	*56*	*43*	*30*
Portfolio managers/analysts only	Portfolio managers	378	270	224	284	108
	Others	58	25	27	16	–
	No. of respondents	*36*	*30*	*23*	*18*	*8*
Total	Portfolio managers	1,727	1,413	992	1,005	634
	Specialists	220	210	232	211	135
	Others	85	80	87	52	–
Overall total headcount		**2,090**	**1,703**	**1,311**	**1,268**	**769**
Overall total no. of respondents		***95***	***85***	***79***	***61***	***38***
Average headcount		**22**	**20**	**17**	**21**	**20**

of corporate governance teams". The FRC noted that clear communication from investors is important *"as trust between investors and companies can otherwise be needlessly eroded"* and it encourages investors to *"consider ... the involvement of portfolio managers"*[18].

The Guidance to **Principle 1** states that the statement *"should describe arrangements for integrating stewardship within the wider investment process"*.

Fifty-one, i.e. 86 per cent, of the 59 respondents that involve specialists and others (Table 13) have formal arrangements for integrating them in the investment process of which 42 describe these in their policy statement. Several respondents gave further details, for example:

- *"Portfolio managers are responsible for all voting decisions and engagement. Dedicated specialists provide general information on best practice and handle proxy voting instructions."*

- *"... [Asset Manager established] a group of employee representatives (mainly analysts and fund managers across asset classes and regions) supporting [its] goal of becoming a fully integrated investment company weaving environmental, social and corporate governance (ESG) considerations into [its] investment processes. The [group] represents the enablers of the RI integration strategy. The [group] meets regularly. Specific performance indicators linked to the integration strategy are embedded in all [group] objectives and therefore reflected in annual compensation. ..."*

- *"... the [corporate governance] team provide the UK equity team with their views on company corporate governance performance including appointments, board structure and executive compensation (particularly compensation performance targets). This is often done ahead of company meetings. [Asset Manager] is a member of the IMA [The Investment Association] investment committee and actively participates in the collective engagement that is facilitated by this body. Both a member of the corporate governance team and the UK equity team would typically participate in meetings with companies via this forum. Similarly, meetings with companies may involve only members of the [corporate governance] team, only members of the UK equity team or participation by both teams. On contentious voting issues the process is for the [corporate governance] team to make a voting recommendation to the respective analyst/ fund manager that covers the stock, the head of appropriate equities team and the Chief Investment Officer. All parties are then required to formally indicate if they support or reject the [corporate governance] team recommendation and their reasons why. The final decision rests with the Chief Investment Officer."*

- *"Investment teams must complete ESG checklists for all stocks that they hold, which include an assessment of associated ESG risks. These form the basis for the inclusion of ESG issues as part of the monitoring discussions held with investee companies."*

- *"Environmental, social and governance factors are considered as part of our investment process. The investment team is supported by the corporate finance team who provide specialist support for all ESG issues and senior members of the corporate finance team participate in investment team meetings. Members of the corporate finance team also have access to all company meetings."*

- *"Each of our portfolio managers and investment teams develops their own investment approach or approaches, respectively, whereby stewardship-related considerations are integrated into their research and decision-making processes to the extent that these issues may affect the long-term success of a company and investment returns. [Asset Manager] also has a dedicated ESG team that focuses on stewardship and provides our investment teams with tailored resources and information in order to the integration of support stewardship into the investment process."*

- *"... The Head of Corporate Governance reports directly to an Investment Management Committee which helps to ensure that our research is of value to the investors and integrated into the investment decision-making process. All of our investment teams are located on one floor ... and our Corporate Governance Team sit in the centre of this floor, so are physically as well as philosophically integrated."*

Of the nine respondents that do not include integration arrangements in their policy statement, four intend to do so within the next year, two provide information to current and prospective clients on request, one makes a judgement on a case-by-case basis according to what is in the clients' best interests and for the remainder, it is a matter of keeping the statement succinct.

[18] Page 19

In terms of voting decisions, only two per cent of respondents do not involve portfolio managers/analysts. Thirty-seven per cent involve them for all voting decisions and 31 per cent for controversial decisions and/or votes against (Table 14). The 'other' use a variety of criteria, such as: the vote is controversial and the holding in the company is above a given threshold; corporate actions are involved; there is an actively held position; or there is a history of engagement with the company in question.

Moreover, for the majority of respondents dedicated specialists and portfolio managers/analysts attend meetings with investee companies together. For 52 per cent of respondents this happens sometimes and for 27 per cent often. Encouragingly there has been an increase in the proportion of respondents for whom portfolio managers and specialists always attend meetings together – to seven per cent in 2014 from three per cent in 2013.

TABLE 14: INTEGRATION INTO THE INVESTMENT PROCESS

	Per cent of respondents 2014	2013
Portfolio managers/analysts involved in voting decision		
All voting decisions	37	27
Controversial voting decisions and/or against	31	40
None of the voting decisions	2	4
Other	30	29
Dedicated specialists attend investee company meetings with portfolio managers/analysts		
Always	7	3
Often	27	33
Sometimes	52	51
Never	14	13
Sample size	**59**	**55**

SERVICE PROVIDERS

Institutional investors often supplement their resources with service providers that process their voting instructions, provide research, make voting recommendations or offer other customised services. The Guidance to **Principle 6** of the Code requires institutional investors to *"disclose the use made, if any, of proxy voting or other voting advisory services"* and to *"describe the scope of such services, identify the providers and disclose the extent to which they follow, rely upon or use recommendations made by such services"*.

Eighty-two per cent of respondents describe how they use such services in their policy statement – up from 78 per cent in 2013. Where this is not the case, some respondents disclose it in another public document or they did not consider it applicable as they do not use such services or if they do, it is only to process voting instructions. One respondent intends to include it when it updates its statement and another does not consider the disclosure cost effective or that it would make an impact given its small size.

Seventy-six per cent of respondents use at least one service provider to process voting instructions, down from 83 per cent in 2013 and 86 per cent in 2012 with the majority using only one. Accordingly, there was an increase in the proportion of respondents that do not use such services to process instructions – 21 per cent compared to 17 per cent in 2013 and 13 per cent in 2012 (see Table 15).

TABLE 15: SERVICE PROVIDERS THAT PROCESS VOTING INSTRUCTIONS

No. of providers	Per cent of respondents 2014	2013	2012	2011	2010
Three +	2	–	2	–	4
Two	10	14	10	13	10
One	64	69	74	64	67
None	21	17	13	17	15
No response	3	–	1	6	4
Sample size	**95**	**85**	**80**	**64**	**48**

Similar to past years, just over three quarters of respondents – 79 in total – receive research from service providers with the majority using one provider (see Table 16).

TABLE 16: SERVICE PROVIDERS THAT PROVIDE RESEARCH

No. of providers	Per cent of respondents 2014	2013	2012
Three +	10	9	12
Two	24	25	26
One	43	44	40
None/No	21	22	21
No response	2	–	1
Sample size	**95**	**85**	**80**

Sixty-seven of the 79 that receive research also receive voting recommendations. Only one per cent always follow these whereas 79 per cent do not necessarily follow the recommendations in that they make their own assessment. Nineteen per cent of respondents sometimes follow the recommendations without carrying out their own assessment (see Table 17). In which case, several clarified that they do not follow recommendations when:

- their holding is above a defined threshold or part of an active investment strategy;
- there aren't any conflicts of interest between the respondent, the investee company and its clients;
- the recommendation is to vote against.

Moreover, two respondents tend to override recommendations following engagement with a company.

TABLE 17: RECOMMENDATIONS FOLLOWED

No. of providers	Per cent of respondents 2014	2013	2012	2011	2010
Not necessarily					
>Four	1	–	–	–	8
Four	1	2	7	7	–
Three	3	3	3	6	8
Two	14	19	15	11	13
One	57	15	21	16	18
Not given	3	–	–	–	–
	79	39	46	40	47
Sometimes					
>Four	–	–	2	9	–
Four	–	2	–	7	3
Three	–	–	–	–	–
Two	3	3	–	24	16
One	16	51	50	16	31
Not given	–	–	2	–	–
	19	56	54	56	50
Always					
One	1	5	–	4	3
Sample size	**67**	**59**	**58**	**55**	**38**

Of the 14 respondents that always or sometimes follow recommendations without their own assessment, five do so based on the provider's standard voting policy and nine on a tailored policy specific to them.

5 MONITORING AND ENGAGEMENT

MONITORING

Principle 3 states that *"institutional investors should monitor their investee companies"* and the Guidance adds that the aim should be to *"identify at an early stage issues that may result in a significant loss in investment value".*

Respondents were asked to provide details about how they approach monitoring which in most cases involves a combination of direct contact with investee companies and reviewing in-house or third-party research. Moreover, over half of respondents monitor through their contact with other investors or stakeholders (see Table 18).

These results are corroborated by the ShareAction survey of asset managers where it reported that *"79% of survey respondents mentioned that they use a range of internal and external data sources and that they have direct contact with investee companies[19]"*.

TABLE 18: MONITORING APPROACH

	Per cent of respondents 2014
Direct contact with investee companies	91
In-house research	85
Third-party research	82
Contact with other investors/stakeholders	57
Other	2
Sample size	**95**

The most common approaches to monitoring among Service Providers are in-house research (four) and contact with other stakeholders (four). Three contact companies directly, and another three use third-party research.

PRIORITISATION

Principle 4 requires that institutional investors *"establish clear guidelines on when and how they will escalate their stewardship activities"*.

In the past, respondents indicated that a lack of resources was a significant barrier to stewardship. This was reiterated in the more recent ShareAction survey where most respondents cited resource constraints as *"a barrier to conducting stewardship[20]".*

As a consequence, institutional investors need to prioritise which companies and issues they engage on.

Similar to 2013, over one third of respondents engage with all their investee companies whereas about a quarter prioritises those companies where there are significant issues. A larger proportion prioritises actively managed holdings – 16 per cent compared to eight per cent in 2013 (see Table 19).

As regards the "other", the majority use a combination of factors with some considering how responsive the company had been to engagement in the past. To quote:

- *"Our integrated stewardship practices reflect both our material long term investments and the ethical priorities of our clients. As such our approach prioritises our largest holdings, companies where we have identified concerns and also the ethical priorities of our clients."*
- *"Our decisions to engage are made on a case-by-case basis and depend on the materiality of the issue, the responsiveness exhibited by the company to past communications, and our assessment of whether such engagement is in the best interests of our clients."*
- *"[We prioritise] member directed engagement queries (e.g., cluster munitions, tobacco companies etc.); remainder is delegated to third party provider (LAPFF)."*

[19] ShareAction, Responsible Investment Performance of UK Asset Managers: The 2015 ShareAction Survey, January 2015, page 11.

[20] Page 12. Other cited barriers were: *"challenges and costs in obtaining adequate corporate access; regulatory uncertainty in obtaining adequate corporate access; lack of demand by clients; lack of receptiveness to engagement by investee companies".*

TABLE 19: PRIORITISATION OF ENGAGEMENT

	Per cent of respondents 2014	Per cent of respondents 2013
All holdings	35	34
Actively managed holdings	16	8
Overweight holdings	1	5
When there are significant issues	22	26
Delegated to manager/overlay service	0	2
Other	23	23
No response	3	2
Sample size	**95**	**85**

In general Service Providers contact companies as needed and for research purposes. For example, one engages with companies *"on a 'required' basis, mainly to gather additional information and clarification of public documents. [Service Provider] also engages with companies on request from clients, and in respect of a range of issues. Companies also seek engagement and consulting with [Service Provider] to discuss remuneration and other governance issues ahead of an AGM or GM."*

The issues that are most frequently addressed are set out in Table 20 while Table 21 sets out the issues respondents consider are the most important.

Remuneration gives rise to the most engagement. This was also the case in previous years[21], although 2014 was marked by the introduction of the binding vote on remuneration policy[22]. According to the NAPF survey this *"was accompanied by a tidal wave of companies consulting with their investors"* and resulted in over three quarters of its respondents seeing more engagement seeking to bring about *"changes to executive remuneration[23]"*.

That said, in its report of developments in Corporate Governance the FRC stated that *"many companies ... would welcome more engagement from investors on other substantive issues[24]"*. In this context, corporate performance, although not specifically mentioned in prior years, is the second most frequently addressed issue followed by board leadership.

TABLE 20: MOST FREQUENTLY ADDRESSED ISSUES

	Ranking[25] 2014	Ranking[25] 2013
Remuneration	1	1
Corporate performance	2	–
Leadership - Chairman/CEO	3	3
Culture and strategy	4	2
Board and committee composition/succession	5	4
Capital structure, including equity issuance	6	10
Environmental/social issues	7	7
Merger and acquisitions	8	6
Corporate actions and restructuring	9	5
Risk management/appetite	10	8
Reporting, audit and audit tendering	11	9
Health and safety	12	–
Sample size	**66[26]**	**68**

Respondents consider corporate performance is the most important issue to engage on, followed by board leadership, culture and strategy and board and committee composition. Remuneration is now slightly less important and is fifth but capital structure, including equity issuance, has increased in importance and is now sixth (see Table 21).

21 IMA, Adherence to the FRC's Stewardship Code 2013, May 2014, Page 24.

22 See here for more details.

23 Page 28.

24 Page 17.

25 The two issues "Corporate performance" and "Health and safety" were not available in 2013.

26 Twenty-nine respondents did not provide any information regarding the most frequently addressed issues.

TABLE 21: MOST IMPORTANT ISSUES

	Ranking 2014	2013
Corporate performance	1	–
Leadership - Chairman/CEO	2	2
Culture and strategy	3	1
Board and committee composition/succession	4	3
Remuneration	5	4
Capital structure, including equity issuance	6	9
Environmental/social issues	7	8
Risk management/appetite	8	7
Merger and acquisitions	9	5
Corporate actions and restructuring	10	6
Reporting, audit and audit tendering	11	10
Health and safety	12	–
Sample size	**69**[27]	**72**

Contrary to expectations[28] following the introduction of the Competition and Markets Authority's[29] measures to increase competition within the audit market, there was no change in the reporting, audit and audit tendering in the most frequently addressed or in the most important issues. However, it is one of the three most frequently addressed issues for four respondents and is considered one of the three most important issues for six respondents.

For five Service Providers the top five issues are identical to those for Asset Managers and Asset Owners.

[27] Twenty-six respondents did not provide any information regarding the issues they consider to be most important.

[28] IMA, Adherence to the FRC's Stewardship Code 2013, May 2014, Page 25.

[29] Previously the Competition Commission.

ANNUAL GENERAL MEETINGS

The Guidance to **Principle 3** states that as part of their monitoring, institutional investors should seek to *"attend the General Meetings of companies in which they have a major holding, where appropriate and practicable"*.

A little over half of respondents never attend Annual General Meetings (AGMs) as a matter of policy which is a large increase from 37 percent in 2013 and 2012. Only three per cent attend whenever possible, an increase from two per cent in 2013, and 11 per cent where they have a major holding and/or where appropriate and practicable – a decrease from 29 per cent in 2013 (see Table 22).

The 20 per cent 'other' use a combination of factors in deciding to attend AGMs, for example, where there is a major holding and there are specific concerns, or in the case of some it is a way to vote their shares *"at the last moment"*. Moreover, some respondents view it as an opportunity to escalate engagement by making a public statement and reaching out to other shareholders. For example, one respondent stated: *"... it would help send a stronger message to the board and to those attending the meeting and where we feel that our one to one meetings with the company are no longer helping us achieve our objectives".*

TABLE 22: ATTENDANCE AT ANNUAL GENERAL MEETINGS

	Per cent of respondents				
No. of providers	**2014**	**2013**	**2012**	**2011**	**2010**
Whenever possible	3	2	8	2	–
Where have a major holding, and/or where appropriate and practicable	11	29	20	28	38
Where there are specific concerns[30]	11	–	–	–	–
Other	20	31	31	36	35
Never	53	37	37	33	25
No response	3	1	4	1	2
Sample size	**95**	**85**	**80**	**64**	**48**

[30] This option was available for the first time in 2014.

The 42 respondents that attend AGMs as a matter of policy were asked to estimate the number of meetings they attended. Fifty-five per cent attended at least one AGM, up from 48 per cent in 2013. Approximately half of these attended three or more and the rest only one or two AGMs. The proportion of respondents that did not attend any AGM decreased to 26 per cent in 2014 from 38 per cent in 2013 (see Table 23).

TABLE 23: NUMBER OF AGMs ATTENDED

	Per cent of respondents	
	2014	**2013**
Ten +	2	7
Five-Ten	7	15
Four	10	–
Three	5	7
Two	12	13
One	19	7
None	26	38
No response	19	13
Sample size	**42**	**54**

Four of the eight Service Providers never attend AGMs, another delegates attendance to *"the managers it recommends"* and one clarified that it attends AGMS but for *"service operations and employee training"* rather than for engagement purposes. The other two did not respond.

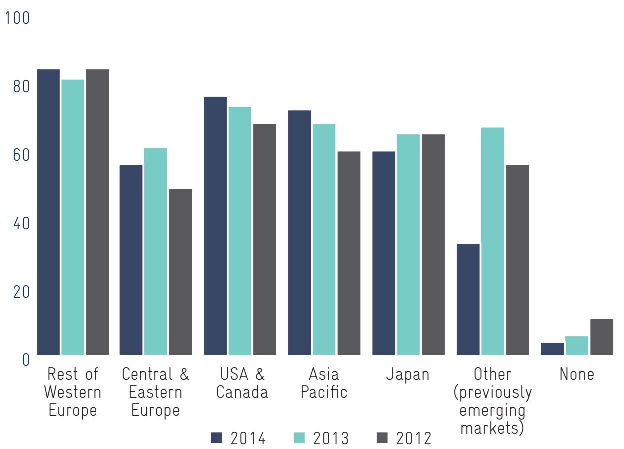
ENGAGEMENT IN OVERSEAS MARKETS AND WITH OTHER ASSET CLASSES

The guidance on the application to the Code explains that *"UK institutions that apply the Code should use their best efforts to apply its principles to overseas equity holdings"*. Furthermore, it clarifies that *"where institutions apply a stewardship approach to other asset classes they are encouraged to disclose this"*.

Charts 1 and 2 show respondents' engagement outside the UK and with asset classes other than equities, respectively.

There was a marked increase in engagement with non-UK equities. The proportion of respondents that engage with Western European equities returned to the 2012 level of 84 per cent – up from 81 per cent in 2013. There was also an increase in those that engage with equities listed in the USA and Canada – 76 per cent compared to 73 per cent in 2013 – and the Asia Pacific – 72 per cent compared to 68 per cent in 2013. At the same time, engagement with Central and Eastern European equities dropped to 56 per cent from 61 per cent and with Japan equities to 60 per cent from 65 per cent. There was also a large decrease in the proportion of respondents that engage with "other" equity although this could be partly due to the re-classification of this category from 'Emerging Markets' (see Chart 1).

CHART 1: ENGAGEMENT WITH COMPANIES LISTED OUTSIDE THE UK



Contrary to the overall increase in engagement with non-UK equities, there was a decrease in engagement with asset classes other than equity. Engagement with fixed income investments decreased slightly to 40 per cent from 41 per cent and with property it remained stable at 21 per cent. However, there was a notable drop in the proportion of respondents that engage with private equity – 20 per cent down from 24 per cent in 2013. Engagement with 'other' asset classes such as hedge funds or infrastructure also fell to 11 per cent from 13 per cent (see Chart 2).

Nevertheless, sometimes engagement with one asset class covers others as well. For example, one respondent explained that although engagement is conducted in respect of its equity holdings, it has *"direct relevance to fixed income and other investors as the focus of our engagements is on risk management, enhanced disclosure and the quality of management and leadership at issuers"* given that there is *"a commonality of interests on these matters between equity and debt investors"*.

CHART 2: ENGAGEMENT WITH OTHER ASSET CLASSES

6 QUALITY OF ENGAGEMENT

The FRC's 2014 report on developments in Corporate Governance observes that: *"on the issue of the quality of engagement, a number of participants in a survey organised by the GC100 ... noted that, on the whole, investors are informed and inquisitive and are generally asking the right type of questions to generate a high quality of debate*[31]*".* However, it notes that the feedback the FRC received from both companies and investors is that *"better quality engagement between them, especially in the context of the new binding vote on remuneration, is required*[32]*"*.

For the first time, respondents were asked to give details on the quality of engagement. In particular, they were invited to comment on the quality of dialogue with companies, the type of communication they found to be most effective, reasons why collective engagement could be constructive, as well as on their general satisfaction with the outcome of their engagement.

QUALITY OF DIALOGUE

Over a quarter of respondents considered that the dialogue improved in comparison to 2013 (Table 24). The main factors driving this were increased awareness around stewardship and companies being more responsive. To quote:

- *"Both companies and asset managers are continuing to appreciate the value of engagement, with more involvement from analysts and portfolio managers as stewardship becomes embedded as 'part of the landscape'. Increased [portfolio manager] attendance has, in turn, led to companies taking engagement discussions more seriously."*

- *"Good governance is more and more becoming standard practice. Companies have therefore [been] becoming increasingly more willing to engage with shareholders."*

Several respondents referred explicitly to the introduction of the binding vote and how this had increased companies' responsiveness to engagement. For example:

- *"Our perception is that UK companies have generally been more receptive and open to engagement. With the binding vote on remuneration this was perhaps a driver of part of this change."*

- *"We have had good quality dialogue with UK companies for many years; however, the outcomes of remuneration consultations have definitely improved with the binding vote."*

- *"We saw a significant rise in pro-active remuneration consultations. This is the result of the new binding pay vote, and the general push from the FRC for companies to engage early and often on matters of significance."*

Despite this increased focus on remuneration, some respondents mentioned that dialogue on other issues had also improved. For example:

- *"While remuneration continued to be the most frequent engagement item, overall there has been much greater emphasis of conversations on long-term strategy and value creation."*

- *"The range of issues for discussion has widened to include audit & risk, diversity on the Board, Cyber risk in addition to succession, company performance & strategy."*

- *"While remuneration continued to be the most frequent engagement item, overall there has been much greater emphasis of conversations on long-term strategy and value creation."*

Overall, the responses indicate that companies' openness to dialogue is crucial. However, one respondent noted that: *"although the level of corporate contact has improved we are increasingly finding that companies are outsourcing engagement to proxy facilitation services or agents prior to meetings, which is detrimental".* Moreover, as one respondent stressed, it is not just companies' responsiveness but its own internal arrangements that are important to improve dialogue: *"... a more experienced team and a more concentrated UK portfolio, [make] it easier to prioritise, integrate and resource engagement activities"*.

No respondent considered the quality of dialogue worse compared to 2013. In fact, the majority (almost two thirds) felt that it was the same in that either it was already of high quality or they face the same challenges, such as lack of direct contact with companies and constrained resources. To quote:

- *"Generally, the same concerns have arisen at companies with whom we engaged last year, and in other sectors where legislative changes were made that impacted issues such as remuneration, the dialogue remained the same because we have yet to see these changes in practice."*

31 Page 18.

32 Page 17.

- *"...There was once again a strong focus on remuneration in the UK. Some consultations were very helpful in explaining how pay supports the company's strategy, others much less so in hoping to tick boxes to get the policy vote passed. Our strong desire is that the amount of time spent discussing bitty remuneration issues decreases and that we are able to spend more time having fuller discussions on issues related to long-term performance and value creation. We hope that now that the remuneration policy votes have been approved we will be able to discuss a wider range of topics over the coming year. On sustainability matters we continue to see the quality and quantity of dialogue increasing, with more companies making the explicit connection to their strategies and long-term success."*

- *"Fund manager meetings with companies continue to be effective and are a significant part of our investment process. ... the subject of remuneration continues to be an area of significant focus, particularly for companies. But we expect this to be of less focus in 2015 as hopefully most companies will not change their executive pay arrangements after having had their policy approved at the 2014 AGM. This should mean that there is more time (for both companies and investors) for better quality engagement i.e. to engage on the wider ESG issues."*

- *"[There is] continued reluctance for most companies to engage directly with investors."*

- *"The quality and extent of our dialogue is constrained by our limited resources."*

TABLE 24: QUALITY OF DIALOGUE WITH COMPANIES COMPARED TO 2013

	No. of respondents 2014	Per cent of respondents 2014
Better	26	27
Same	62	65
Worse	0	0
No response	7	7
Sample size	**95**	**95**

TYPES OF COMMUNICATION

In terms of the type of communication, the vast majority – over 80 per cent – find direct contact to be most effective[33]. In most cases this involves face-to-face meetings with some respondents also using phone calls. For 13 respondents it is not general contact but one-to-one meetings that are most effective. Moreover, respondents prefer to communicate directly with the Chair, senior board members or senior executives. To quote:

- *"The most effective engagement meetings have tended to be with chairman without a specific agenda. Conversations of this nature often provide deeper insights into the culture and workings of the board and help investors explore and better understand the key challenges facing the company and long-term strategies adopted to generate long-term value."*

- *"[Asset Manager] finds face-to-face communication to be the most effective. We also prefer meeting chairmen and other non-executive directors on their own as we think this facilitates more open and constructive dialogue."*

- *"We believe that conducting meetings with investee companies behind closed doors are more effective. We will consider collaborating with other investors where their strategic aims for the company match ours."*

Approximately 20 per cent of respondents prefer to write to companies particularly when it comes to escalating issues. For example:

- *"Face to face meetings were most effective however letters were useful for formal escalation. AGM statements can also be effective."*

- *"Letters directed specifically to management of companies tend to be seriously considered. Companies mostly respond to written correspondence along with an invitation for phone or in person meetings."*

- *"Face to face meetings are essential to build a constructive dialogue but written communication is often most effective at securing change."*

[33] Seventy-seven respondents provided information.

Sometimes, the most effective type of communication depends on the company and the specific issues. To quote:

- *"[Asset Manager] continue[s] to adopt a wide range of engagement methodologies ranging from arranging subject-specific engagement meetings with specialist members of staff at investee companies to structured letter based engagement programmes. The particular engagement methodology that is adopted is specific to the topic and the result that we seek to achieve."*

- *"Direct engagement focusing on each company individually. Looking at each company on a case by case basis. One to one meetings, email engagement and dialogue with portfolio managers."*

Finally, the time invested in preparation and the approach can determine how effective communication is. For example, one respondent stated: *"We have found we have greatest impact where we spend sufficient time analysing the issues, and offering well-considered input that is considered to be constructive."* The same respondent mentioned that where both board and executive members are involved it *"get[s] listened to more carefully"* and that *"speaking with one voice via collective engagements can be powerful"*.

COLLECTIVE ENGAGEMENT

Principle 5 states that *"institutional investors should be willing to act collectively with other investors where appropriate"*. Moreover, the FRC views collective engagement as a way to circumvent the issue of constrained resources that pose a barrier to engagement for both investors and companies[34] and well over two thirds of the respondents to the NAPF survey indicated that they would *"encourage more collaboration amongst their fund managers[35]"*.

Where respondents collaborated effectively with other investors, they were asked to explain why that was. Perhaps unsurprisingly, most described collective engagement as a way to achieve *"critical mass"* that enables even small investors to have access to and engage with a company and a tool to signal to companies that some concerns are widely shared. To quote:

- *"Collective engagement is useful in order to demonstrate to the company that there are concerns that are shared by more than one shareholder. Where we do not have an active holding, participating in collaborative engagement helps [Asset Owner] to share resources with asset managers that are likely to be monitoring the company more closely."*

- *"As a relatively small asset manager, we have found that collaborative engagement can help to attract the attention of senior management."*

- *"Collective engagements bring different angles and views to the table which can be useful to the overall analysis. The company also seems to take the engagement more seriously when there is a group of investors engaging together."*

- *"Collective engagement on the right issues and when managed effectively is an important component of stewardship. Due to our size, we do not have concerns over corporate access. However, in some cases companies justify persisting with a course of action, which we may consider to be value destructive, based upon a lack of consensus in the market. Collective engagement allows the investment community to speak with a single voice of matters of serious concern. ..."*

To ensure collective engagement is effective there needs to be agreement among investors on the issues and ways to engage. For example, respondents stated:

- *"... [Collective engagement] works best when all participants are well prepared and share common concerns."*

- *"Collective engagement can be successful where there are aligned interests of investors. This is very difficult to achieve, even in clear-cut cases of minority shareholder abuse. There remains a reluctance amongst many investor organisations to 'put their head above the parapet' in case this risks drawing unwanted public attention. We have found collective engagement most effective when dealing not with company-specific matters, but regulatory and policy change."*

- *"When investors have the same concern over issues with a company and wish to achieve the same goals, collective engagement works."*

[34] FRC, Developments in Corporate Governance and Stewardship 2014, January 2015, Page 18.

[35] Page 29.

- *"Collective engagement can be useful in certain circumstances; namely when there is an acute issue and there is a relatively small but active and engaged group willing to work together. Large engagement groups involving investors with disparate goals and strategies are often not very effective other than to send a message to the company that investors are generally concerned about an issue."*

Notably, there are still concerns about market abuse and concert party rules. One respondent stated: *"... it should be noted that, as ESG is integrated further into investment processes it is often not possible to ring-fence ESG specialists; collective engagement is becoming more difficult owing to fears surrounding market abuse and breaching concert party rules."*

OUTCOME OF ENGAGEMENT

Almost 90 per cent of respondents were satisfied with the outcome of their engagement in the year ended 30 September 2014 (see Table 25). Twenty-nine per cent were fully satisfied as changes were made as a result of their engagement. To quote:

- *"We have seen an increased awareness in stewardship with a special focus on governance and the implications of the code. Additionally, we have seen an improvement in the understanding of material risks in environmental issues, achieving some reporting transparency on energy efficiency and CO2 footprints."*
- *"We were influential in a number of instances that yielded benefit to the clients."*
- *"As UK investors attached to a US-domiciled parent, we were often overlooked or excluded in the past with regard to company outreach efforts. That is occurring much less frequently now. Overall, our access to company managements and boards improved significantly in 2014."*
- *"Expectations were generally met during the period in our dialogue with investee companies."*

Sixty per cent of respondents were mostly satisfied with the outcome in that companies were more responsive compared to previous years but this did not necessarily always translate into changes. Moreover, although there was constructive engagement on remuneration, respondents were less happy with the outcome on other issues such as strategy. For example:

- *"Our experience in the UK has been that there is good access to board members in companies, and the vast majority of our holdings have either initiated the engagement or they have been very willing to engage with us when we contact them. However, although they are accessible, we have on occasion found it difficult to effect change on crucial matters."*
- *"Companies generally respond with changes to their remuneration policies. Other issues are not as easily changed. A big issue is companies that attempt to greatly shorten notice times for calling meetings. We anticipate corresponding with our companies more on this issue to ensure that our clients are not disenfranchised by this policy."*
- *"Most boards are willing to meet and discuss issues, but the responsiveness of board varies – some listen and respond better than others."*
- *"... Companies have been quite responsive to our requests to engage with them on a variety of strategic, environmental, social and governance issues. There is a growing willingness of non-executive directors to enter into meaningful dialogue about where companies can make improvements. Actual outcomes are mixed, with some companies showing progress and responsiveness to shareholder concerns (particularly around some remuneration consultations), with others showing no interest in initiating change despite repeated attempts by shareholders."*
- *"There were some immediate results on issues of engagement that mainly related to changes around Board composition and remuneration. However, for issues relating to strategy, performance and culture we would need to monitor results over the medium term."*

- *"Whilst we have had success in a number of positive engagements, progress has been hampered selectively by a lack of willingness by other shareholders to engage."*

- *"There is still a disproportionate amount of engagement dedicated to remuneration. While this is not an unimportant topic, we would prefer to see more company chairmen proactively engage their investors on governance matters outside of remuneration, such as strategy. ..."*

Only five per cent of respondents were not satisfied with the outcome of their engagement mainly as their small holding limited the influence they could exert on companies. To quote:

- *"Our holdings do not 'move the dial' for many companies; as a result, although most companies respond, not many follow the course of action we would like to see from them."*

- *"As a relatively small manager we do not have a huge amount of influence and have not engaged heavily with UK listed companies."*

- *"Boards generally respond constructively to our governance concerns but favourable outcomes remain work in progress in many instances."*

TABLE 25: SATISFIED WITH OUTCOME OF ENGAGEMENT

	No. of respondents 2014	Per cent of respondents 2014
Yes	28	29
Mostly yes	57	60
Mostly no	5	5
No	0	0
No response	5	5
Sample size	**95**	**95**

7 PRACTICAL EXAMPLES

To assess how stewardship works in practice, respondents were asked how they escalated matters and engaged on certain issues with particular companies. In more detail, respondents were invited to answer:

- whether they had a holding in the company concerned, if there were any conflicts of interest and how these were addressed, and whether they engaged;
- where they engaged, what their objectives were, what their view of the quality and outcome of engagement was, how many times and whom they engaged with and whether their holding in the company changed as a result of their engagement;
- whether they engaged in collaboration with other investors, and if so, who instigated the collaboration and whether it was effective;
- whether they attended the Annual General Meeting and how they voted on specific resolutions and why.

The companies concerned were:

- AstraZeneca plc
- Experian plc
- GlaxoSmithKline plc
- Sports Direct plc
- Standard Chartered plc.

These examples are summarised below in descending order by the number of respondents that engaged with each. The in depth analysis is set out in the separate document 'Detailed practical examples'. This document is particularly informative as it includes many quotes from respondents bringing the engagement to life. Moreover, it demonstrates the wide variety of approaches used and the importance of an effective dialogue.

In addition, for the first time in 2014, representatives from these companies were invited to comment on their experience of engagement. Where these were provided, they are briefly summarised below and set out in full in 'Detailed practical examples'. Generally, engagement with companies is not within the remit of the Service Providers, but where they did provide details, they are referred to separately in 'Detailed practical examples'

Respondents were also invited to give an example of their engagement with any other company that they would like to highlight, particularly where they considered their engagement made a difference. A brief overview of these cases is set out at the end of 'Detailed practical examples'.

GLAXOSMITHKLINE PLC

In May 2014, GlaxoSmithKline (GSK) became the subject of a criminal investigation by the UK's Serious Fraud Office following allegations of bribery and corruption. Moreover, a profit warning was issued in July 2014 and revenues and the share price declined but despite this, analysts predicted that GSK's dividend would not be affected.

Sixty-one respondents had a holding in GSK and 38 engaged with it – more than any of the other examples. The main concern was the bribery allegations but several respondents also raised succession planning, culture, and performance. For example, one respondent wanted *"(1) an update on performance against strategy; (2) an update on the China bribery issues; (3) an update on a successor for the chairman; (4) to make to company aware of our concerns relating to executive pay and on non-audit fees..."*

Respondents had extensive communication with GSK with a total of 156 contacts – on average five per respondent. This was predominantly with Investor Relations and Executive Directors and was mostly carried out either by portfolio managers or by dedicated specialists.

Thirteen respondents engaged in collaboration with other investors and, in most cases, this involved attending joint meetings with GSK. Almost all considered this effective as it showed that investors shared similar concerns and it allowed better access to GSK.

The quality of engagement was considered on average good as GSK was open to discussion with investors and considered proposed changes even though it could not discuss in detail the bribery case as it was still under investigation at the time. The majority of respondents felt they achieved their objectives but some stressed that engagement is ongoing.

Resolution 4 to re-elect Chairman Sir Christopher Gent received 4 per cent of votes against in the 2014 AGM while only one respondent in the sample voted against it. Respondents explained that showing support would be good for stability particularly while the company was under investigation.

Resolution 17, to re-elect non-executive director Hans Wijers received over 8 per cent of votes against at the AGM while again, only one respondent voted against. The general view was that Hans Wijers was a new appointment and there were no particular concerns.

GSK commented that it *"always seeks to be responsive to engagement opportunities with investors"* and that investor engagement *"by whatever route"* is much appreciated. It also stressed the importance of investors communicating their views and reasons for their decisions before taking action as this helps GSK have the *"full picture"*. Moreover, each year GSK holds formal investor meetings with its largest shareholders and voting advisory firms to discuss corporate governance practices and during 2013-2014 it also held separate investor meetings in the UK and the US to engage with investors on the investigation of the company's business in China.

ASTRAZENECA PLC

In 2014, AstraZeneca became subject to a takeover bid by Pfizer which was eventually withdrawn. The bid attracted considerable attention and shareholder opinion was reportedly divided. AstraZeneca's share price fell notably as an immediate result of the failed bid and, in addition, a number of drug patents are set to expire over the next two years.

Fifty-two respondents had a holding in AstraZeneca of which 30 engaged. The main objective was to discuss the Pfizer bid. For example, one respondent wished to *"understand the process that the management team and board employed when considering the offer from Pfizer; how the board oversaw and approved the strategic plan and implied long-term valuation of the company which was developed in response to the hostile takeover; understand the extent to which the board was acting in the interest of shareholders in relation to other interested stakeholders."* However, several respondents also wanted to address concerns on remuneration as well as operational and strategic issues such as plans for business development.

Respondents contacted AstraZeneca 116 times in total, averaging at over four contacts each. This was primarily with Executive Directors and Investor Relations and carried out mostly by portfolio managers.

Eight respondents collaborated with other investors mainly in order to share information and discuss the Pfizer bid. Five found it effective but the other three did not either because the desired outcome was not achieved or agreement could not be reached on the best course of action.

AstraZeneca's responsiveness to investor concerns was a decisive factor in respondents' assessing the quality of the dialogue as good or average with only three respondents being dissatisfied with it on the basis the company did not justify its actions or that they could not access senior management. Moreover, the majority felt that their objectives were fully or partly achieved. Those that did not, commented that their concerns regarding remuneration remained to be resolved.

Resolution 6 to approve the remuneration report received 38 per cent of votes against at the 2014 AGM while over 80 per cent of respondents voted against it. The main reason was that they did not feel there had been sufficient disclosure and that remuneration was not properly aligned with shareholder interests.

Resolution 5h to re-elect Jean-Philippe Courtois as a director, received 43 per cent of votes against at the AGM which was approximately the same proportion of respondents that voted against it. The main issue was a relatively poor record of attendance the reasons for which had not been properly explained according to some respondents.

STANDARD CHARTERED PLC

In 2014 Standard Chartered reported that its 2013 Group income was down 1 per cent with statutory profit before tax down 11 per cent. In the run up to its AGM, there were investor concerns over the number of non-executive directors and Standard Chartered's remuneration policy.

Twenty-nine of the 50 respondents with a holding engaged with Standard Chartered mainly to address concerns about remuneration and company performance. For example, one respondent's objectives were *"better performance from business, a remuneration policy more closely linked to long term performance, and a succession process for the chairman"*.

There was extensive communication with Standard Chartered – a total of 133 contacts – on average over five contacts per respondent. This was mainly with Investor Relations, the Chair of the Remuneration Committee and Management and was carried out mostly by portfolio managers and dedicated specialists separately.

Eight respondents collaborated with other investors but only half found this effective. The other half either found it difficult for all to agree on a course of action or felt that Standard Chartered could not be persuaded to follow a different approach on remuneration.

A little over one third considered the engagement good because they had access to the company and were able to discuss their concerns. Others felt that issues on governance and particularly around remuneration were not resolved which was also the main reason why most respondents considered the engagement only partly successful.

Over half of respondents voted against Resolution 3, to approve the remuneration policy, compared to approximately 41 per cent of votes against at the 2014 AGM. The main reason was that respondents believed that remuneration was not aligned to long-term performance and disapproved of the addition of further allowances to compensate for the bonus cap.

Resolutions 13, to re-elect the Remuneration Committee Chair and member of the Audit, Board Risk, Nomination, Governance and Board Regulatory Compliance Oversight Committees, Ruth Markland and 19, to re-elect non-executive director and Chair of the Brand and Values Committee and member of the Board Risk, Nomination, Remuneration and Board Regulatory Compliance Oversight Committees, Paul Skinner, received 14 and 11 per cent of votes against at the AGM, respectively. However, the majority of respondents voted in favour of both as they felt that their continued presence would be beneficial in view of the increased turnover at Board level.

Standard Chartered commented that it has a "*comprehensive engagement programme ... covering the investment and governance teams*" and in 2014 alone attended approximately 850 meetings with investors, including 400 institutions. Moreover, it consulted on remuneration with over 50 per cent of its share register and introduced or planned changes on both remuneration *"to address shareholder feedback"* and on the composition of its Board.

EXPERIAN PLC

Prior to Experian's 2014 Annual General Meeting and beginning in autumn 2013, Experian consulted with its shareholders and their representative bodies, to explain its changes to succession planning. Nevertheless, concerns were publicly expressed regarding the Chief Executive Officer, Don Robert, taking over as a Chairman from Sir John Peace and the Chief Financial Officer, Brian Cassin, becoming Chief Executive in turn.

Twenty-five of the 41 respondents with a holding engaged with Experian with main objective of discussing the issue of succession planning. For example, one respondent commented that it had a *"general concern that good CEOs don't always make good Chairman and the risks of not being able to 'let go' of their day to day tasks"*. Other objectives included remuneration, strategy and performance.

There were a total of 42 contacts and on average each respondent contacted Experian twice. Contact was mostly by portfolio managers with Investor Relations and the Company Secretary.

There was little collective engagement – only two investors collaborated with others. One entered an agreement to vote the same way and the other sent a joint letter to the company.

Several respondents felt that more could have been done towards improving succession planning but the overall view was that the quality of engagement was good and the dialogue constructive. For example, one respondent stated that "*the Company followed the UK [Corporate Governance] Code guidance of consulting shareholders when considering for the CEO becoming Chairman, and made a clear business case for the proposals."* Accordingly, all respondents but one achieved their objectives.

Resolutions 2 and 3 to approve the remuneration report and policy received respectively 14 and 12 per cent of votes against at the 2014 AGM compared to 16 and 24 per cent of respondents that voted against. Although some felt the remuneration arrangements satisfactory given company performance others considered that the incentive structure could result in too high pay.

Resolution 10, to re-elect Don Robert as a director, received 11 per cent of votes against at the AGM while a much higher proportion of respondents – 24 per cent – voted against and 16 per cent registered an abstention. This was mainly due to concerns about Don Robert's lack of independence whereas those that voted in favour had been reassured given his experience and the independence of the rest of the Board.

Experian commented that it *"undertook a comprehensive engagement process regarding Don Robert's appointment as Chairman"* as required by the Corporate Governance Code and that it found the engagement *"constructive, valuable and informative"*. Moreover, it engaged with investors on remuneration ahead of the 2014 AGM and considered the results of 85.9 per cent and 87.4 per cent of votes in favour of the remuneration report and policy respectively to be positive.

SPORTS DIRECT PLC

A bonus scheme at Sports Direct was subject to some controversy and was finally approved after three unsuccessful attempts in July 2014. Still, due to shareholder dissatisfaction and following discussions with members of the company's Remuneration Committee, founder and director Mike Ashley withdrew from the scheme.

Of the 26 respondents with a holding 15 engaged with Sports Direct, the main objectives being to discuss concerns about remuneration arrangements and the lack of independence on the Board. For example, one respondent commented that its goal was to *"... initiate key governance changes, particularly regarding the leadership and skills on the board, changes to key remuneration decisions, and strengthening internal capacities in the investor relations and company secretarial departments"*.

Respondents contacted Sports Direct 41 times in total – an average of over 3 contacts per respondent – with contact mainly being with the Chairman and the Chair of the Remuneration Committee. This was mostly carried out by dedicated specialists.

Relative to the other case studies, there was considerable collective action with nine out of 15 respondents collaborating with other investors. In most cases, respondents were approached by an established investor group and attended joint meetings with the company. Five did not find the collaboration effective mainly due to the lack of change in the company's approach to governance.

Approximately half of respondents considered the quality of engagement good due to the depth of discussion with Sports Direct but the others were not as satisfied because there was little change and they felt that their position as minority shareholders was particularly weak in the presence of a dominant shareholder. As a result of what they viewed to be poor governance, half the respondents did not achieve their objectives.

Resolution 4, to re-elect the Chairman, Keith Hellawell, received 7 per cent of votes against at the 2014 AGM while about a quarter of respondents voted against it, the main reason being dissatisfaction with the company's governance.

Resolution 5, to re-elect founder Mike Ashley, received just over 13 per cent of votes against at the AGM but all respondents voted in favour of this re-election. This was mainly due to the strong belief in his potential to add value to the company and the robust company performance.

One third of respondents voted against the re-election of the Remuneration Committee Chair, Dave Singleton, while it received about 6 per cent of votes against at the AGM. Respondents cited his connection to the controversial bonus scheme as one of the main reasons for not supporting his re-election.

Sports Direct commented that it *"values constructive dialogue with its shareholders"* and clarified that its Board had an extensive programme of meetings with shareholders in order to discuss the changes it made to the bonus scheme following investor feedback. However, it noted a discrepancy between what was orally agreed with shareholders and the result of the proxy voting and urged investors to *"be clear about who is responsible for voting decisions and to abide by oral commitments given following discussions"*.

8 VOTING

VOTING POLICY AND PROCESSES

Principle 6 states that *"institutional investors should have a clear policy on voting and disclosure of voting activity"*.

Service Providers often execute institutional investors' voting instructions, but as they do not hold equity for investment purposes this section is not relevant to them. Thus this section only addresses those 87 respondents that conduct all or some of their voting in-house.

Forty per cent of the 87 respondents changed their voting policy or processes during the year, an increase from 31 per cent in 2013[36]. The changes varied and included:

- extending voting policies to overseas equities, e.g. one respondent published *"regional specific voting policies for UK, Europe, US & Canada, Emerging Markets, Asia and Japan";*
- increased disclosure around voting, e.g. including the rationale for votes against or clarifying voting policy when there are conflicts of interest;
- extending voting policies to address new issues such as diversity, auditor tenure and non-audit services and the new binding vote on remuneration policy;
- reflecting increased resources or changes in processes, e.g. one respondent is now filtering *"smaller routine voting positions from larger or more problematic matters";*
- minor amendments with two explaining that they reflected regulatory developments for public companies and specifically, the enhanced disclosures on remuneration and the changes in the narrative reporting framework.

VOTING IN PARTICULAR MARKETS

The Guidance to **Principle 6** states that *"institutional investors should seek to vote all shares held"*. In this context, respondents were asked in which markets and what proportion of holdings they endeavour to vote.

Encouragingly, voting activity increased in all markets to reach levels during the 'shareholder spring' in 2012 – see Chart 3 which shows the proportion of respondents that vote all shares in individual equity markets and Appendix 3 which sets out a more detailed analysis of the percentage of holdings voted.

The proportion of respondents that vote all shares held in UK companies increased to 84 per cent from 78 per cent in 2013. There were similar increases in respect of Western Europe – 65 per cent compared to 59 per cent in 2013 – and Central and Eastern Europe – 56 per cent up from 49 per cent in 2013. The largest increase was in respect of the US and Canada where 72 per cent of respondents vote all shares compared to 62 per cent in 2013. Voting in Asia Pacific, Japan and Emerging Markets also increased to 62, 71 and 52 per cent, respectively.

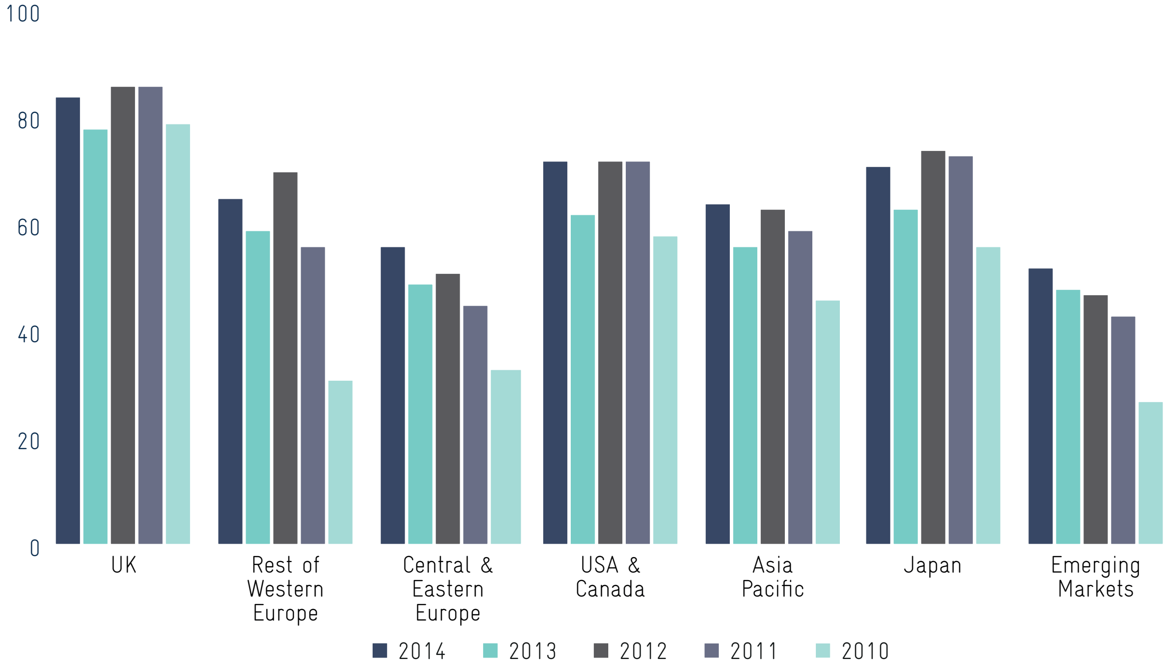
These results are consistent with the NAPF Engagement Survey's findings where *"respondents are exercising their voting rights more and in more jurisdictions[37]"*. It attributes this to a *"general positive momentum ... generated by the Stewardship Code and the accompanying greater emphasis being given to translating the best practice adopted for home market stocks to those from further afield"*. They also add that *"this momentum has been helped further by the introduction of similar Codes such as that in Japan"*.

As regards the percentage of holdings voted, voting is at similar levels as in 2013 for the majority (51-75%), some (25-50%), and few (<25%) holdings. However, the number and proportion of respondents that do not vote any of their holdings decreased in all regions and in some cases was zero.

[36] IMA, Adherence to the FRC's Stewardship Code 2013, May 2014, Page 34.

[37] Page 30.

CHART 3: MARKETS WHERE ALL SHARES VOTED



ADVISING MANAGEMENT

The Guidance to **Principle 6** states that where institutional investors register an abstention or vote against a management resolution it is *"good practice to inform the company in advance of their intention and the reasons why"*.

There is a marked decrease in the proportion of respondents that always or in the majority of instances notify companies in advance of their intention to vote against or abstain – 39 per cent compared to 47 per cent in 2013. At the same time a higher proportion never notifies companies or does so very rarely – 30 per cent up from 25 per cent in 2013. However, 11 per cent of respondents always advise management in arrears which is an improvement from 2013 where no respondents did so (see Table 26).

TABLE 26: ADVISING MANAGEMENT

	Per cent of respondents — Voting against or abstaining on management resolution							
	2014		2013		2012		2011	
	Notify in advance	Notify in arrears	Notify in advance	Notify in arrears	Notify in advance	Notify in arrears	Notify in advance	Notify in arrears
Always	17	11	19	–	20	3	16	2
Majority of instances	22	10	28	13	15	9	23	9
Occasionally	22	36	19	36	29	19	30	20
Very Rarely	14	22	12	22	14	15	16	14
Never	16	15	13	13	18	13	12	13
When not in advance	–	–	–	–	–	11	–	20
N/A as in advance	–	–	–	–	–	24	–	19
No response	9	6	8	15	4	6	3	3
Sample size	**87**	**72**	**83**	**67**	**80**	**80**	**64**	**64**

DISCLOSURE OF VOTING RECORDS

Principle 6 states that "*institutional investors should have a clear policy on voting and disclosure of voting activity*". The Guidance states that "*institutional investors should disclose publicly voting records*".

Just over two thirds of respondents disclose voting records which is similar to the 66 per cent in 2013. In addition, the proportion of respondents that do not disclose also increased slightly to 29 per cent from 27 per cent where more than half of those disclose why this is the case. The majority that do not disclose explained that voting records are either available to clients or on request (see Table 27). The reason that both the proportion of those that do and do not disclose increased is that the proportion of no respondents decreased. If the results are adjusted for this, the proportions are fairly static with 70 per cent disclosing voting information in 2014 compared to 71 per cent in 2013.

Notably, one respondent explained that due to its small size its voting records are "*irrelevant in the greater scheme of things*". Moreover, another commented that "*whilst it is important to engage with companies we see no benefit in publically disclosing the shortcomings we see in the companies we hold*".

TABLE 27: DISCLOSURE OF VOTING RECORDS

	Per cent of respondents				
	2014	**2013**	**2012**	**2011**	**2010**
Disclose voting information	68	66	65	73	65
Do not disclose					
Reason disclosed	14	16	15	14	–
Reason not disclosed	11	10	15	11	–
Commit to publish	–	–	3	2	–
	29	27	33	27	33
No response	3	7	2	–	2
Sample size	**87**	**83**	**80**	**64**	**48**

Of the 59 respondents that disclose voting records, three-quarters disclose all votes, which is a significant increase from 62 per cent in 2013. Over a half of these include the rationale which for 10 per cent includes the rationale for all votes – an increase from 5 per cent in 2013. A quarter of respondents disclose a summary report, down from 38 per cent in 2013 (see Table 28).

TABLE 28: PUBLICLY DISCLOSED VOTES

	Per cent of respondents				
	2014	**2013**	**2012**	**2011**	**2010**
All votes					
Rationale for all	10	5	6	9	
Rationale for against or abstained, and exceptional	12	5	10	6	
Rationale for against or abstained	8	11	8	4	
No rationale	44	40	44	49	
	75	62	68	68	68
Summary report	25	38	32	30	32
No response	–	–	–	2	–
Sample size	**59**	**55**	**52**	**7**	**31**

Similar to past years, when respondents disclose their voting records, the majority – 63 per cent – do so quarterly or less in arrears. Ten per cent publish six months in arrears and 20 per cent annually in arrears. Only five per cent disclose voting records more than one year in arrears (see Table 29).

TABLE 29: DISCLOSURE OF VOTING INFORMATION IN ARREARS

	Per cent of respondents			
	2014	**2013**	**2012**	**2011**
Quarterly or less	63	65	60	57
Six months	10	11	13	13
One year	20	19	25	28
More than one year	5	4	2	2
Sample size	**59**	**55**	**52**	**47**

9 REPORTING

Principle 7 states that *"institutional investors should report periodically on their stewardship and voting activities"*. The Guidance specifies further that Asset Managers *"should regularly account to their clients or beneficiaries as to how they have discharged their responsibilities"* and that these reports may *"comprise qualitative as well as quantitative information"*. Similarly, Asset Owners are expected to *"report at least annually to those to whom they are accountable on their stewardship policy and its execution"*.

In its 2014 Engagement Survey, the NAPF reported that *"over 80% of respondents reviewed their fund manager's compliance at least annually*[38]*"* and that there was a significant increase in the percentage of their respondents that were very or quite satisfied with the standard of stewardship reporting[39].

This section addresses the 95 Asset Managers and Asset Owners that conduct all or part of their engagement in-house. As shown in Table 30, 90 per cent of respondents report to clients or beneficiaries with approximately three quarters doing so regularly. Most commonly this is quarterly, with the frequency of reporting varying according to the client for 23 per cent. The proportion of those that do not report at all increased from one per cent in 2013 to 10 per cent in 2014 (see Table 30).

TABLE 30: FREQUENCY OF REPORTS TO CLIENTS/ BENEFICIARIES

	Per cent of respondents				
	2014	**2013**	**2012**	**2011**	**2010**
Monthly or more frequently	3	2	3	5	2
Varies according to client	23	27	23	20	31
Quarterly	48	53	50	61	54
Annually	16	12	20	11	11
Do not report	10	1	2	3	–
No response	–	5	2	–	2
Sample size	**95**	**85**	**80**	**64**	**48**

Forty-four per cent of respondents that report to clients and/or beneficiaries include these reports in their performance report.

In terms of content, the FRC noted in its report on developments in Corporate Governance and Stewardship that *"reporting from some signatories continues to improve but most signatories to the Code would benefit from considering ways in which they can be more accountable to their clients and beneficiaries and fully explain their approach to stewardship*[40]*"*.

Forty-six per cent of respondents report on both voting and engagement, slightly down from 48 per cent in 2013. Twenty-eight per cent report on voting, up from 21 per cent in 2013. Only two per cent report on engagement alone, compared to eight per cent in 2013. But for 13 per cent of respondents the reports vary. For example one respondent explained that *"most clients receive vote reports, some also receive summary engagement reports and a few receive detailed engagement reports"*. Some respondents report on both voting and engagement and include a summary of ESG reviews. One respondent also provides updates on *"market trends and developments"* and another adds *"a list of all one-on-one meetings"*.

TABLE 31: CONTENT OF REPORTS

	Per cent of respondents				
	2014	**2013**	**2012**	**2011**	**2010**
Both voting and engagement	46	48	56	53	69
Engagement only	2	8	2	2	2
Voting only	28	21	21	23	17
Other	13	16	15	19	10
No response / do not report	11	7	6	3	2
Sample size	**95**	**85**	**80**	**64**	**48**

INDEPENDENT OPINION

The Guidance to **Principle 7** requires Asset Manager signatories to *"obtain an independent opinion on their engagement and voting processes having regard to an international standard or a UK framework such as AAF 01/06"* and adds that *"the existence of such assurance reporting should be publicly disclosed"*.

38 Page 20.

39 Page 23.

40 Page 17.

In addition, in its report on developments in Corporate Governance and Stewardship, the FRC stressed that *"independent assurance can provide some comfort to clients that signatories are following through on their stated practices"* and the FRC *"welcome[s] this transparency*[41]*"*.

Similar to 2013, 18 per cent of respondents obtained an independent opinion on both voting and engagement within the last twelve months. For 18 per cent the opinion only covered voting whereas none covered engagement alone. Moreover, there was an increase in the proportion of respondents that did not obtain an independent opinion and have no plans to do so – 53 per cent compared to 45 per cent in 2013 (see Table 32).

TABLE 32: INDEPENDENT OPINION ON PROCESSES

	Per cent of respondents				
	2014	**2013**	**2012**	**2011**	**2010**
Both voting and engagement					
Over 12 months	–	–	–	–	–
Within last 12 months	18	17	14	10	6
Ad hoc	–	–	–	–	2
Engagement only					
Over 12 months	–	–	–	–	–
Within last 12 months	–	1	–	–	–
Ad hoc	–	1	–	–	–
Voting only					
Over 12 months	–	1	–	–	2
Within last 12 months	18	21	20	20	36
Ad hoc	–	–	–	–	2
Intend to within the next year	8	9	11	17	10
No, and no plans to do so	53	45	51	48	29
No response	3	5	4	5	13
Sample size	**95**	**85**	**80**	**64**	**48**

[41] Page 22.

The three main reasons an independent opinion was not obtained were that:

- this is covered by an internal audit function;
- it is not considered cost effective;
- clients have not expressed any interest for this.

Moreover, a small number of respondents clarified that they are considering this for the future but are yet to set a specific timeline.

Approximately two thirds of the 59 respondents that obtained an independent report on their stewardship processes disclosed it publicly. Most of those that did not, explained that they either make the assurance available on request or plan to disclose it publicly in the future. One respondent commented that *"there are also sensitivities around disclosing our control process and findings publically as there may be a potential loss of competitive advantage"*.

For the 36 respondents where there is no external opinion, 41 per cent had their process reviewed by internal audit mostly within the last 12 months with 22 per cent covering both voting and engagement up from 15 per cent in 2013. Twenty per cent intend to do so within a year while 32 per cent having no plans for an internal audit – down from 30 per cent in 2013 (see Table 33).

The main reasons for no internal audit review were the lack of an internal audit function (as for 2013) or that it would not be cost effective.

TABLE 33: PROCESSES REVIEWED BY INTERNAL AUDIT

	Per cent of respondents 2014	2013
Yes		
Both voting and engagement	22	15
Engagement only	–	2
Voting only	19	24
Over 12 months	7	13
Within last 12 months	32	26
Not known	–	2
Ad hoc	2	
	41	41
No, but will do in the next 12 months	20	18
No, and no plans to do so	32	39
No response	7	2
Sample size	**59**	**46**

APPENDIX 1

STEERING GROUP MEMBERS

David Styles (Chair)	Financial Reporting Council
Hannah Armitage	Financial Reporting Council
John Dawson	National Grid
Gráinne Delaney	EFAMA
David Jackson	BP plc
Huw Jones	M&G Investments
Leon Kamhi	Hermes Investment Management
Charles King	SSP Group plc
Liz Murrall	The Investment Association
Anastasia Petraki	The Investment Association
Daniel Summerfield	USS

APPENDIX 2

RESPONDENTS TO THE QUESTIONNAIRE

ASSET MANAGERS

7IM
Aberdeen Asset Management
Aberforth Partners
Alliance Trust Investments
AllianceBernstein
Artemis Investment Management
Aviva Investors Global Services
AXA Investment Managers
BAE Systems Pension Funds Investment Management
Baillie Gifford
Baring Asset Management
BlackRock
BP Investment Management
Brewin Dolphin
Capital International
CCLA Investment Management
CFB Methodist Church
City of London Investment Management
Daiwa SB Investments (UK)
Ecclesiastical Investment Management
Edgbaston Investment Partners
Element Investment Managers
Ethos Foundation Switzerland
F&C Investments
Fidelity Investment Managers
First State Investments
Franklin Templeton Investments
GAM (U.K.)
Generation Investment Management
Genesis Investment Management
Goldman Sachs Asset Management International
Gottex Fund Management
GVO Investment Management
Harding Loevner
Henderson Global Investors
Hermes Investment Management
Highclere International Investors
HSBC Global Asset Management (UK)
Impax Asset Management
Insight Investment Management
Invesco Perpetual
Investec Asset Management
J O Hambro Capital Management
JPMorgan Asset Management
Jupiter Asset Management
Kames Capital
Kempen Capital Management (UK)
Kleinwort Benson Investors
Lazard Asset Management
Legal & General Investment Management
Liontrust
Lofoten Asset Management
Longview Partners
M&G Investments
Marshall Wace
Martin Currie Investment Management
MFS Investment Management
Montanaro Asset Management
Morgan Stanley Investment Management
Newton investment Management
Oldfield Partners
Origin Asset Management
PD Capital Management
Pictet Asset Management
Polar Capital
Pyrford International
Rathbone Unit Trust Management
RC Brown Investment Management
River and Mercantile Asset Management
Royal London Asset Management
Russell Investments
S. W. Mitchell Capital
Sarasin & Partners
Schroder Investment Management
Slater Investments
Standard Life Investments
State Street Global Advisors
SVM Asset Management
T. Rowe Price
Taube Hodson Stonex Partners
Tesco Pension Investment
Thomas Miller Investment
Threadneedle Investments
TT International
Turcan Connell Asset Management
UBS Global Asset Management (UK)
UK Financial Investments
Vanguard Asset Management
Veritas Asset Management
Walter Scott
Wellington Management
WHEB Asset Management

ASSET OWNERS

- Alliance Trust plc
- Avon Pension Fund
- BBC Pension Trust
- Bedfordshire Pension Fund
- British Airways Pensions
- British Coal Staff Superannuation Scheme
- BT Pension scheme
- DHL Group Retirement Plan
- Första AP-fonden
- Greater Manchester Pension Fund
- Jaguar Land Rover Pension Trustees
- Lancashire County Council
- London Borough of Bexley Pension Fund
- Marks & Spencer Pension Scheme
- Merchant Navy Officers Pension Fund
- Mobius Life
- Nationwide Pension Fund
- North East Scotland Pension Fund
- Ontario Teachers' Pension Plan
- Pension Protection Fund
- Royal Mail Pensions Trustees
- Société Générale UK Pension Scheme
- Somerset County Council Pension Fund
- Strathclyde Pension Fund
- The Joseph Rowntree Charitable Trust
- The Mineworkers' Pension Scheme
- The Pensions Trust
- The Wellcome Trust
- Universities Superannuation Scheme
- West Midlands Pension Fund

SERVICE PROVIDERS

- ECGS
- Glass Lewis
- Hymans Robertson
- Institutional Voting Information Service
- Lane Clark and Peacock
- Manifest
- Partners Capital
- Towers Watson

APPENDIX 3

MARKETS AND PROPORTION OF SHARES VOTED

NO. OF RESPONDENTS

	UK					Rest of Western Europe					Central & Eastern Europe				
	2014	2013	2012	2011	2010	2014	2013	2012	2011	2010	2014	2013	2012	2011	2010
All	72	64	68	55	38	53	47	54	35	15	40	34	36	25	16
Most (>75%)	9	7	5	6	6	16	14	13	18	18	13	12	13	13	12
Majority (51-75%)	0	2	–	1	1	4	1	–	1	6	2	4	3	1	3
Some (25-50%)	2	1	2	–	–	2	–	1	2	2	1	–	3	3	1
Few (<25%)	0	3	2	1	1	1	8	4	3	2	3	7	5	3	5
None	0	1	–	1	–	0	2	3	2	2	2	3	4	5	6
No equities held	1	1	1	–	–	6	4	3	2	–	15	14	10	8	–
No response	3	4	2	–	2	5	7	2	1	3	11	9	6	6	5
Total	**87**	**83**	**80**	**64**	**48**	**87**	**83**	**80**	**64**	**48**	**87**	**83**	**80**	**64**	**48**

USA & Canada					Asia Pacific					Japan					Rest of the World				
2014	**2013**	**2012**	**2011**	**2010**	**2014**	**2013**	**2012**	**2011**	**2010**	**2014**	**2013**	**2012**	**2011**	**2010**	**2014**	**2013**	**2012**	**2011**	**2010**
57	48	51	41	28	51	41	45	33	22	54	46	52	41	27	41	35	33	24	13
10	9	7	5	8	11	13	12	10	10	6	8	5	5	7	16	13	12	10	13
1	1	2	2	–	0	1	1	4	1	1	1	–	–	1	4	7	7	5	4
2	1	1	1	2	2	–	2	1	2	2	–	1	–	1	1	1	4	3	2
2	5	3	2	2	3	4	3	2	4	2	3	4	5	3	3	4	3	5	4
0	3	2	3	4	2	5	3	2	4	3	5	2	2	4	3	5	4	4	6
8	6	9	7	–	7	10	9	8	–	11	10	10	8	–	8	10	10	8	–
7	10	5	3	4	11	9	5	4	5	8	10	6	3	5	11	8	7	5	6
87	**83**	**80**	**64**	**48**	**87**	**83**	**80**	**64**	**48**	**87**	**83**	**80**	**64**	**48**	**87**	**83**	**80**	**64**	**48**