



Best Practice Principles for Governance Research Providers

19th December, 2013

Dear Sir, Madam,

Investor Relations Society response to the Public Consultation on Best Practice Principles (BPP) for Governance Research Providers

Thank you for giving us the opportunity to take part in the above consultation. I am pleased to enclose The Investor Relations Society's response.

The Investor Relations Society's mission is to promote best practice in investor relations; to support the professional development of its members; to represent their views to regulatory bodies, the investment community and government; and to act as a forum for issuers and the investment community. The Investor Relations Society represents members working for public companies and consultancies to assist them in the development of effective two way communication with the markets and to create a level playing field for all investors. It has over 670 members drawn both from the UK and overseas, including the majority of the FTSE 100 and much of the FTSE 250. As such, through our members, we have direct experience of working with proxy agents both in the EU and globally.

The development of the proxy advisory industry in Europe in recent years is a key issue for investor relations practitioners and listed companies more generally. The trend of a growing industry is a feature that we consider is likely to continue. We understand that nearly all institutional investors subscribe to one or more proxy advisers, and that in the case of all but contentious resolutions, or in corporate actions, institutional investors will regularly follow the recommendations of the research provider. Therefore, we support this review of the industry that this consultation undertakes. We believe there is a role for proxy advisers in providing external research support to diversified investors, and that proxy advisers offer significant savings in cost and time to investors. However, investors should not cite resourcing issues as a reason for implementing passive investment strategies.

Given the regularity with which many of our members report issues of factual inaccuracies and/or selective use of information by proxy agencies, combined with unreasonably short deadlines to respond, we are not confident that proxy advisers always provide robust and adequately informed judgments in guidance to their clients. We consider that on certain sensitive areas these advisers are not always sufficiently versed with the nuances of company policy issues, and we would encourage them to engage more directly with corporate issuers.

Our primary recommendation in this submission rests on our objective to promote open and honest market interaction between investors and companies. To this end, we encourage proxy agencies to engage more directly and openly with corporate issuers to enhance dialogue. The current relationship is in many cases adversarial which is not in the interests of an open market.

On behalf of our members (issuers and their advisers), we have summarised our key concerns regarding the governance research industry as follows:

- **Evident factual inaccuracies and overall lack of fact checking by governance research providers**
- **The lack of accountability and transparency over proxy advisory decisions with potentially significant implications for issuers**
- **Apparent lack of direct and open dialogue between companies and governance research providers**
- **No right to response - issuers are either unable to comment on the factual accuracy of proxy research or given insufficient time to respond**
- **Lack of discretion applied by investors with an increasing blanket acceptance of proxy advisor recommendations**

We address these points in our response to your consultation questions below. Please note we have responded to the summary questions on page 25 at the back of the document, which differed to the questions in the main document under each of the three principles.

1. What are your views about the principles development process?

The IR Society very much applauds the work of The Drafting Committee of the BPP and welcomes this discussion on the activities associated with governance research services, and the goal for the industry to develop standards. We understand the Committee has

considered ESMA's conclusions from their 2012 consultation on the European proxy advisory industry, which we also welcome.

Our members view transparency as being at the heart of best practice investor relations with a company's Board providing the lead and the IR team acting as a conduit to and from the capital markets. We support the current disclosure and transparency regime and the principles of universal, proactive and prompt dissemination of information to shareholders to ensure a fair investment market. As such, we are concerned when third party organisations exercise influence over essential governance issues affecting companies, without demonstrating the sort of transparency and accountability that issuers are themselves obliged to provide by the current regulatory regime. Therefore we would seek clarification that the principles' development process has taken into account the perspective of the corporate issuer in mind in the drafting.

2. Respondents are welcome to express their expectations regarding the review and monitoring of the principles. As the on-going governance of the principles has yet to be determined, the committee particularly welcomes suggestions by stakeholders as to how a representative feedback mechanism can be implemented.

We strongly believe there is a need for a forum or professional industry body (e.g. Investor Relations Society, ESMA), which can represent corporates and with whom issuers can feel comfortable lodging legitimate concerns or issues regarding the governance research industry. Our concern is that the BPP mechanism doesn't appear to engage with corporates on their issues and is too inward-looking. The perspective of the proxy agencies is focused on themselves rather than on the fundamental principle of market openness and integrity.

Despite recent media attention in support of the governance research providers, a recent poll of our members has shown that 84% have been presented with reports on their companies prepared by proxy advisers which contained incorrect, inaccurate or otherwise misleading information.

Our members report they have serious concerns that proxy advisors do not correct inaccuracies or do not do so in a timely manner and cite the quality of service being provided by the proxy industry as the main focus of their concern. This is a crucial point in transactions where timetables are compressed. Therefore, in order to represent the views on both sides of the industry (corporates and proxy services), there needs to be a representative body that both sides can respect and whose judgments will carry authority, and where issues can be heard and resolved accordingly.

3. Please share your views on the practicality of a comply-or-explain approach to the principles.

To reiterate our above point, in order for the BPP Group to implement these draft principles most effectively, we need a formal representative body that the industry will respect and listen to. The market needs reassurance that this process has been correctly administered and that there is an official channel of communication and application of these principles. All UK listed companies adhere to the principle of 'Comply or Explain', to which The Investor Relations Society adheres. With a recognised professional body in place, we feel that applying 'Comply or Explain' through the implementation of governance research industry standards would be beneficial for both issuer and investor.

4. Could the effectiveness of the principles be further enhanced? Please elaborate and provide specific examples and/or suggestions.

Please see our responses to the specific questions regarding Principles One, Two and Three.

5. Do you think that Principle One will help the market to better understand the different kinds of services and approaches that participants operate? If not, please explain.

In Principle One: Service Quality, it states that 'signatories aim to offer services that are delivered in accordance with agreed client specifications'. We note there is no reference to the factual accuracy on issuer information that we strongly believe governance research providers should seek to achieve. While 'client specifications' need to be agreed, accurate corporate information must be at the heart of the issue; institutional investors need factually correct research reports to form a sensible and reasonable investment judgement.

In addition, we feel the word 'aim' in Principle One does not demonstrate that research providers need to adhere to a strict policy that they should be providing accurate information. No advisory body should "aim" to provide an acceptable service – providing honest and robust analysis must be at the heart of everything a proxy advisory undertakes.

We support the proposal that signatories should disclose their research policies and guidelines, and we would like to see that a process is put in place to ensure that research providers are validated and verified to ensure they are carrying out the highest quality service on behalf of their clients. Final reports issued publicly should be reviewed and approved by experienced agency staff, in addition to the author/researcher. It is not apparent

that such quality controls are currently in place at all proxy agencies. Further transparency on the personnel that carry out the research e.g. qualifications and experience would also be welcomed by the issuers.

We feel strongly that dialogue with issuers needs to improve, and regular communication between proxy advisers and issuer IR teams should be encouraged. Current practices cannot be allowed to continue unchecked and we feel strongly that the increasingly adversarial engagement process is detrimental to open investment dialogue and the quality of the corporate governance process between issuers and investors.

Furthermore, we feel it is very important that sufficient time is allowed for IR departments to respond to proxy adviser communications and that in general, issuers have the right to reply to the reports produced by proxy advisers. Research providers should bear in mind that IROs are typically in meetings or on calls, when they are not travelling on roadshows. To give a timeframe of twenty-four hours for responding to challenges, as frequently happens, is clearly not sufficient and does not allow issuers a realistic opportunity to respond.

In conclusion we support Principle One and the call for increased accuracy in reports and improved transparency in the process. To be clear, while issuers do not wish to argue with the research providers' judgement on the issues of corporate governance, there is a desire for an overall improvement in the degree of basic accuracy of information and in the management of timing for review and response.

6. Do you see any issues of service quality that are not addressed in this section? If so, please provide examples and specific information on the purpose and merits of any additional disclosures.

As previously mentioned, following a recent poll of our IR Society members, we note that 84% of respondents have been presented with reports on their companies prepared by proxy advisers containing incorrect, inaccurate or otherwise misleading information. In addition, over 64% of companies were given 2 days or less to respond to these reports - 39% state that proxy advisory firms typically give only 1-2 days to respond to reports, with 25% saying they are given fewer than 24 hours. Many also remarked that not only will some proxy advisers refuse to engage with issuers, but also request payment for access to the research report. This is a situation which must improve.

7. Do you think the disclosure of the research policy, voting guidelines and research methodologies will enable stakeholders to determine how signatories consider local market conditions? If not, please provide reasons.

We understand that the Committee has yet to finalise the specific details of the monitoring and review process, with the first review of the Principles taking place in autumn 2014. In our view, the proposed timeframe for this review by the Committee needs more immediacy. This is over a year away and we would ask if proxy agencies would be able to work to a more realistic timetable.

8. Please express your views on the scope and content of the proposed research-related disclosure under this principle with respect, to:

a. Research policy

b. Voting guidelines

c. Research methodologies

See answer above.

9. For additional potential signatories only: Does the Guidance provide you with the information necessary to properly apply Principle One? If not, would you prefer further Guidance? Please explain. Does Principle Two address the relevant issues or considerations relating to potential conflicts of interest in the provision of governance research? If not, please explain.

No comment, question not applicable.

10. Do you agree with the proposed conflict management and mitigation procedures? If not, please explain why and what additional measures you would propose.

As a Society we are not aware that potential conflicts of interest within the governance research industry are high on the discussion agenda with corporate issuers. Although there is a potential for conflicts of interest in practice if a governance research agency is providing advisory and voting services while advising listed companies on corporate governance issues, there should be complete and total separation of these two businesses. Many businesses within the capital markets have to manage conflicts of interest e.g. investment banks, and have no difficulty doing this; so we see this as a matter of course for the governance research industry too.

11. Do you agree with the proposed approach on disclosure of material conflicts? If not, please explain.

No comment.

12. For potential additional signatories only: Does the Guidance provide you the information necessary to properly apply Principle Two? If not, what additional Guidance do you need?

No comment, question not applicable.

13. Please express your views on the scope and content of the proposed policy disclosure under this principle with respect to:

a. Issuers; and

b. Media and the public

We are currently unaware of any disclosure policies in place with respect to communication with corporate issuers, the media and other stakeholders, and so it would therefore be helpful for signatories to be explicit in their communications approaches. The Society welcomes BPP's proposals on this important issue, and agrees with the suggested scope of which the policy should cover as set out in principle three. Some proxy agencies actively court publicity for their reports, and we believe this should happen in conjunction with clear regulatory guidelines.

14. Are there any other aspects of issuer-related dialogue that should be taken into account? If yes, please elaborate and provide specific examples and/or suggestions.

The Society accepts that research providers have an important role to play and on behalf of our members, our goal is to encourage a more open and engaged dialogue between the issuer and the governance research agency. A good example of where this model exists already can be seen in issuer dialogue with market participants such as the sell-side analysts, ratings agencies and industry analysts, interaction with whom is very much encouraged by regulators and occurs on a daily basis. All of these stakeholders have a role to play in investment decision-making. Given their influence, inaccurate reports from them can and do have a disproportionate effect on a company's market valuation. To avoid this therefore, it is routine for analysts to submit their draft research documents to the issuer for fact checking and comments on general accuracy (but not on their investment opinions) prior to publication, thus avoiding any distortions from inaccurate information. We would therefore strongly urge governance research providers to follow suit, by engaging in open dialogue and looking to build longstanding relationships with the corporate issuers. While we understand some governance research providers are happy to meet with corporates, this is far from common, and there appears to be little follow-up with the company post-meeting in order to establish robust channels of communication.

15. Are there any other aspects of media and the public dialogue that should take into account? If yes, please elaborate and provide specific examples and/or suggestions.

We would welcome a published disclosure policy covering research providers' communication with the media. The onus should be on anyone communicating with the media to ensure that any information disclosed is factually correct and verified. It cannot be overestimated how damaging published misleading or inaccurate information can be, and how time-consuming the efforts are on behalf of the issuer to undo factually inaccurate information in the market once published.

16. For additional potential signatories only: Does the Guidance provide you with the information you need to properly apply Principle Three? If not, where would you prefer further Guidance?

No comment, question not applicable.

17. In addition to comments on the specific questions addressed in the remainder of this Consultation Document, views are invited on the general approach taken by the Committee and the general features of the Principles.

We commend the Best Practice Principles Group on the steps taken to address a Code of Conduct for the governance research industry. We would, however, like to reiterate that we consider it unbalanced that issuers face a great regulatory burden regarding the timely provision of accurate, verified and, in large measure, audited information, and as a result we welcome the move to create best practice guidance for the proxy advisory industry.

18. Do you feel that the Principles meet the policy principles set forth in ESMA's Final Report? If not please explain.

We agree with ESMA's final report and feedback on the proxy advisory industry and agree that the introduction of binding measures would not be justified. However we support proposals for a coordinated effort of the proxy advisory industry to improve transparency and disclosure, as outlined in our responses above.

19. Do you have any other comments that the Committee should take into account when finalising the Principles?

No further comments.

In summary, we understand there is a role for proxy advisers and commend the efforts undertaken by BPP to develop an industry standard. However, we would welcome a

thorough review of current practices to ensure that all parties are satisfactorily addressed in a transparent and accountable way.

We hope you find these comments useful and please do not hesitate to contact me if you have any further questions.

Kind regards

A handwritten signature in black ink, appearing to read 'E Burdett', with a horizontal line underneath.

Emma Burdett

Chair of The Investor Relations Society's Policy Committee

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