



December 19, 2013

Prof. Dr. Dirk Andreas Zetsche, LL.M.
Chair, Drafting Committee of the Best Practice Principles for Governance Research Providers Group

Sent by email to: consultation@bppgrp.info

Dear Prof. Zetsche:

Re: Public Consultation on Best Practice Principles for Governance Research Providers

We are writing in response to the Governance Research Providers Group's (GRPG) public consultation on the draft Best Practices Principles (BPP) for the proxy voting advisory industry.¹ We commend the GRPG for seeking stakeholder input on the development of industry principles.

With approximately C\$5 billion in assets under management, NEI Investments' approach to investing incorporates the thesis that companies integrating best environmental, social and governance (ESG) practices into their strategy and operations will build long-term sustainable value for all stakeholders and provide higher risk-adjusted returns to shareholders. As a Canadian investment management company, we have experience as a client of several of the major proxy voting advisory firms.

Proxy voting advisors provide important facilitation services for investment institutions in fulfilling our investment stewardship responsibilities. Proxy voting platform and vote disclosure services are essential to us, and proxy research is extremely useful, especially for international holdings; however, we do not follow the recommendations of our proxy voting advisors blindly. We solicit opinions from our external portfolio managers in addition to engaging directly with issuers and our proxy advisors. We also analyse each vote for compliance with our detailed proxy voting guidelines.

Comments

Background to the Principles

1. *What are your views about the Principles development process?*

We strongly suggest that the Principles should be global in scope and application, and that feedback should be sought from the global client base.

¹ The Best Practice Principles for Governance Research Providers Group (2013). Public Consultation on Best Practice Principles for Governance Research Providers <http://bppgrp.info/wp-content/uploads/2013/11/BPP-Group-Principles-Consultation.pdf>

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Several of the proxy voting advisory firms within the GRPG operate globally, servicing clients in multiple countries and offering research on issuers from multiple jurisdictions through staff teams based in multiple locations. As a client in Canada, we receive research services relating to holdings in multiple jurisdictions. It would be extremely confusing for both advisors and clients if a set of industry principles were to be applied, but only in Europe. It is also unclear what application solely in Europe would look like in practice: would the Principles apply only to advisors with operations in Europe, only for reports issued to European clients, or only for research on European issuers?

Furthermore, we note that proxy voting issues are attracting global regulatory interest, including consultations in Canada and the U.S. In our response² to the Canadian Securities Administrators (CSA) consultation in 2012 on the proxy advisory industry, we indicated that we did not consider a regulatory response to be appropriate at this time. This was not because we have no concerns about current practices in the industry. We noted that over the years we have seen instances of inaccurate research, and have been obliged to over-ride vote recommendations because we disagreed with the research conclusions or because our custom guidelines had not been followed properly; however, we see these occurrences as a client-advisor problem that in the first instance should be dealt with by the market, or by the development of voluntary industry standards among advisors. As a result, we were encouraged to see the European Securities and Markets Authority's (ESMA) 2013 response, which recommended development of a code of conduct, providing the impetus to this public consultation. We note that in response to the Canadian consultation, the CSA indicated that it would develop policy on recommended practices and disclosure for proxy advisors, to be published for comment in early 2014.³ Against this background, we strongly encourage the GRPG to work to ensure that the Principles could also provide a viable solution for the Canadian and U.S. markets.

2. Respondents are welcome to express their expectations regarding the review and monitoring of the Principles.

We expect that the review and monitoring process for the Principles document will be transparent, regular and include all relevant stakeholders. We suggest that it might be appropriate to conduct a review after the first round of disclosures to ensure that the outcome meets stakeholder expectations. Once the Principles are well-established, a review schedule could be adopted that reflects typical practice in standards-setting (for example, a review every three to five years).

It is not clear from the consultation document if there will be monitoring of the quality of individual firm's compliance with the Principles; who would be responsible for any such monitoring; how stakeholders who believe the Principles have been breached should signal concerns; and what the consequences would be if a firm failed to publish a Statement of Compliance according to the agreed schedule, or if its disclosure was clearly inadequate or inaccurate.

Comply or Explain

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

We believe the comply-or-explain approach is appropriate given the disparate nature of the proxy advisory firms' business models and operational structures, as long as deviation from the Principles is clearly justified through explanations that are

² NEI Investments (2012). Comments on CSA Consultation Paper 25-401: Potential Regulation of Proxy Advisory Firms
<https://www.neiinvestments.com/Documents/PublicPolicyAndStandards/2012/Comments%20by%20NEI%20Investments%20re%20CSA%20Consultation%20Paper%2025-401.pdf>

³ Canadian Securities Administrators (2013). CSA Notice 25-301 – Update on CSA Consultation Paper 25-401 Potential Regulation of Proxy Advisory Firms.
http://www.osc.gov.on.ca/documents/en/Securities-Category2/csa_20130919_25-301_update-25-301.pdf



accurate, comprehensive, relevant and understandable to non-experts. A comply-or-explain approach also creates space for firms to go beyond compliance and develop new good practices.

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

The GRPG could also consider the development of a voluntary assurance approach for Statement of Compliance reports.

Application of the Principles

5. *Do you believe the Principles and/or supporting Guidance conflict with obligations under legislation or other best practice principles? If yes, please elaborate and provide specific examples and/or suggestions.*

We are not aware of any conflict between the draft Principles and supporting Guidance and other obligations or principles. However, as indicated in the response to question 1, we strongly encourage the GRPG to develop a global approach that responds to emerging regulatory interest in Canada and the U.S., as well as Europe.

6. *Please share your views on the procedures for registering as a signatory, describing and disclosing how Principles and related Guidance are being applied, and for disclosing the Statement of Compliance.*

The consultation document does not set out detail on the process for registering as a signatory, beyond publishing a Statement of Compliance and providing the link. As noted in the response to Question 2, it is unclear if there will be monitoring of the quality of an individual firm's compliance with the Principles, what form this would take, and what would be the consequences of non-compliance.

Regarding the process for disclosure on application of the Principles and related Guidance, the publishing of a link to each firm's Statement of Compliance is acceptable if the Statement is made available as a download on the firm's website. This would allow archiving of statements by stakeholders so that they could then be compared over time.

We recommend that each firm's Statement of Compliance should be updated and disclosed on an annual basis, with additional timely updates in the case of a material event (such as a change of ownership, or changes related to conflict of interest). This public information would form important input for our periodic proxy voting advisor searches. The annual statement of compliance and any timely updates should also be shared proactively with existing clients.

7. *What should the regional scope of the Principles be, in terms of signatories and services provided? For example, do you think that the Principles should be global?*

As outlined in the response to Question 1, we believe that these principles should be applied globally across the operations of each of the signatories, in servicing all clients, and for research on all issuers. We think it would be challenging to do otherwise, and that a global approach would be in the interest of the proxy advisors, given the developing regulatory attention for this topic.

8. *For additional potential signatories only: Are there factors that generally would keep you from becoming a signatory to the Principles? If yes, please elaborate and provide specific examples and/or suggestions.*



Not applicable.

9. *For additional potential signatories only: What are your views on the Guidance for subscription, adoption and ongoing compliance from an organisational point of view? Do you think the ongoing management of the Principles could be improved? If yes, please elaborate and provide specific examples and/or suggestions.*

Not applicable.

Scope & Definitions

10. *Do you agree with the definition of “governance research services”? Is the scope of the definition adequate? If not, please elaborate and provide specific suggestions.*

In our opinion, the proposed definition does not provide an adequate description of the range of research-related services provided, and lacks sufficient detail to allow understanding of what is referred to under each “characteristic” bullet. For example, “policy guidance” does not appear to capture the custom implementation of client-developed proxy voting guidelines, a service we routinely purchase from our advisors. The “data and analysis” bullet does not distinguish between company-specific data and material of a more general nature.

We believe it should be a basic principle that signatories should not act on behalf of particular shareholders or issuers in attempting to influence voting. This would be unacceptable practice, even if it were disclosed as described in the final paragraph of section 2.1.1.

11. *Are the definitions of “vote agency services” and “engagement and governance overlay services” and their distinction from “governance research services” sufficiently clear and accurate? If not, please elaborate.*

We find the definition of “vote agency services” to be clear and accurate but the definition of “engagement and governance overlay services” is more problematic. If a proxy voting advisor is providing engagement overlay services, we believe that a conflict of interest is created in that the advisor, who may also be providing vote recommendations to clients, has an interest in pushing issuers it has been contracted to engage to adopt changes, and therefore an interest in influencing voting on behalf of specific shareholders. The primary responsibility for engaging issuers to upgrade their corporate governance practices lies with direct stakeholders such as regulators and investors. We do see value in proxy voting advisors communicating with issuers on research findings, to ensure that research is as accurate as possible.

We believe the Principles should include a specific requirement to declare if non-research services are being provided to either shareholders or issuers that could create conflict of interest, and to explain how this conflict is managed.

12. *Do you agree that the Principles should not impose standards of conduct on investors? If not, please explain why.*

While the conduct of investors is important because the way they utilize proxy advisory firms’ research services affects voting outcomes, the Principles are focused on improving the development and delivery of proxy research services and products, and are not relevant for investors’ operations. The ESMA final report rightly points out that institutional investors have stewardship responsibilities, but these are better addressed under investor initiatives such as the Canadian Coalition for Good Governance, the International Corporate Governance Network and the Principles for Responsible Investment.



Principle One: Service Quality

13. 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 general, we believe that Principle One and the associated Guidance is adequate in balancing our needs as clients in transparency of research processes whilst protecting proprietary practices of the proxy voting service providers.

Assessing the continuing capacity of the advisory firm to provide service is an important consideration for us in choosing providers: it would create difficulty if, for example, a firm were rendered unable to provide service at the height of the proxy season. It would be helpful if the Principles encouraged enhanced disclosure on issues such as ownership, staffing and the firm's financial position.

While the purpose of Principle One is to address the quality of services, we also believe that more could be done to improve client choice in access to services. We encourage providers to "unbundle" proxy voting platform, disclosure and research services, so that clients can more easily purchase services relating to different aspects of the proxy voting process from different providers, and assemble the package of services that best meets their needs.

14. 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.

We value research that discusses objectively the pros and cons of the vote item. Over the years, we have sometimes been puzzled as to how a proxy advisor has arrived at the final vote recommendation based on the research provided in a report. Enhanced disclosure to clients and issuers/proponents on analytical methods and the rationale for the vote recommendation would therefore be desirable in reports. However, this information does not need to be placed in the public domain.

15. 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.

Yes.

16. Please express your views on the scope and content of the proposed research-related disclosure under this principle with respect to: research policy; voting guidelines; research methodologies.

The proposed scope and content is adequate, appropriately balancing transparency with the need to protect intellectual property.

17. 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.

Not applicable.



Principle Two: Conflicts of Interest Management

18. 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.

As discussed in the response to Question 11, the list of possible conflicts should be expanded to include Investor-Client influence on signatories, where signatories are providing engagement overlay services.

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

Yes.

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

The approach to conflict disclosure described on page 20 and page 21 appears to differ. The first reference (last paragraph, p20) implies signatories should disclose only if the conflict cannot be managed effectively. The second (first paragraph, p21) implies that all potential and actual conflicts should be disclosed. In our opinion, the latter approach should always be followed, allowing clients to determine for themselves if the management of the conflict is appropriate. We believe that where a potential conflict of interest impacts a specific research product, such as a research report, this conflict should be disclosed clearly within that product.

21. 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?

Not applicable.

Principle Three: Communications Policy

22. Please express your views on the scope and content of the proposed policy disclosure under this principle with respect to: issuers; media and the public.

The proposed scope and content is adequate, appropriately accounting for the differing communication practices of the proxy voting advisors. We are pleased to see guidance on communicating with shareholder proponents and encourage transparency with regard to any discussions advisors have with proponents. Details of relationships and communications between advisors and other stakeholders with an interest in a specific research report should be included in the report in question. For example, we regularly file shareholder proposals, and advisors sometimes speak with us about those proposals in the course of preparing their research. In some cases, we also have a client relationship with the advisor. It would be appropriate for these contacts and relationships to be disclosed in the research report.

23. 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.

To enhance research quality, we believe there is value in letting issuers or proposal proponents see research in draft, so they can comment on the accuracy of content and analysis. However, it would not be appropriate to increase the potential for issuers or proposal proponents to influence the vote recommendation. When we have filed proposals ourselves, we have



sometimes challenged the quality and accuracy of a proxy research report, for example because it has misrepresented our position as set out in the proposal or because of mistakes in the background research. However, we make it clear in these discussions that we only seek to discuss quality and accuracy questions, and we accept that the decision on the recommendation should be taken independently by the advisor.

24. 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 find that proxy voting advisors may benefit from adopting consistent communications policies to ensure that they comment appropriately on their areas of expertise and knowledge and avoid editorializing. In one situation in which we had withdrawn a shareholder proposal, a proxy advisor commented publicly on our decision, without knowing the background on the agreement that had been reached with the issuer through extensive engagement. We also have concerns if proxy advisors comment publicly on proxy battles, indicating what their vote recommendation will be. We would prefer to see advisors maintaining a more neutral position in contacts with the media.

25. 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?

Not applicable.

General Features of the Principles

26. 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.

No additional comments.

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

The Principles appear to exceed the scope of the ESMA policy principles. We view this positively, and as indicated in the response to Question 1, we believe the GRPG should strive to develop principles that respond to current regulatory initiatives in North America, as well as Europe.

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

No additional comments.

Conclusion and recommendations

We commend the GRPG's commitment to seek public input. Overall, we believe the draft Principles could contribute to improving the quality of the proxy advisory products and services that we rely upon in stewardship of our investments. Our key recommendations include:



- The Principles should be global in scope, covering all operations of the signatory, services to all clients, and research on all issuers. Efforts should be made to address the outcomes of North American consultations, as well as the ESMA process.
- A comply-or-explain approach appears reasonable, given the disparate nature of services provided, and to encourage providers to go beyond compliance.
- We believe it should be a basic principle that signatories should not act on behalf of particular shareholders or issuers in attempting to influence voting.
- All potential and actual conflicts of interest should be disclosed. This disclosure should be included within any research product that could be affected by the conflict.
- Each signatory's Statement of Compliance should be updated and disclosed on an annual basis, with additional timely updates in the case of a material event (such as a change of ownership, or conflict of interest).
- More detail should be provided on any plans for monitoring the quality of individual firm compliance with the Principles, what form this would take, and what would be the consequences of non-compliance.

We have no objection to publication of our comments on your website. Should you have any questions with regard to this submission, please do not hesitate to contact Michelle de Cordova, Director, Corporate Engagement & Public Policy (mdecordova@NEIinvestments.com, 604-742-8319).

Sincerely,
NEI Investments

A handwritten signature in black ink, appearing to read "Robert Walker", followed by a long horizontal line.

Robert Walker
Vice President, ESG Services & NEI Ethical Funds

CC:
Ms. Michelle de Cordova, Director, Corporate Engagement & Public Policy, NEI Investments
Mr. Randy Evans, Senior ESG Analyst, NEI Investments