ICGN Policy Priorities 2016/17

Background

The International Corporate Governance Network (ICGN) was founded in 1995; our members include institutional investors with global assets under management in excess of US$26 trillion, based in 46 countries around the world. ICGN’s mission is to promote effective standards of governance and investor stewardship to advance efficient markets and sustainable economies world-wide. We do this by influencing public policy, connecting corporate governance professionals at international meetings and by informing debate on matters of corporate governance and responsible investment. Accordingly, ICGN members offer a vast source of practical knowledge and experience with regard to governance and investment issues to serve the global investment community. For more information on the ICGN, please visit www.icgn.org.

As part of its role to inform debate and identify major areas of policy focus of interest and relevance to the investor community ICGN launched in 2015 an initiative to guide ICGN’s policy programme. This was named the ICGN “Policy Priorities”, and its mandate is to identify the key overarching themes that are most relevant with regard to global corporate governance and responsible investment practices – and which therefore have relevance for ICGN members. This document presents ICGN’s 2016/17 Policy Priorities, which in many ways is a continuation of work in priorities previously identified. These priorities complement ICGN’s core policy documents—the ICGN Global Governance Principles and Global Stewardship Principles, which can be found on ICGN’s website.

While the most immediate focus of the policy priorities will be to guide ICGN policy work in 2016/17, many of these issues will require medium to long term attention, and therefore are likely to remain on the ICGN agenda over a several year period. But this new restatement of ICGN’s policy priorities also provides an opportunity to review progress made in its policy work and to reflect upon new developments and current dynamics in corporate governance and responsible investment. These policy priorities seek to establish an overarching frame of reference to guide ICGN policy work and policy committees. Indeed many of the policy priorities identified have clear interlinkages with one another, and there may be scope for individual policy committees in collaborating and information sharing—both to strengthen and bring diverse perspectives to ICGN policy work.

ICGN’s policy positioning takes into consideration important initiatives by other globally important standard setting bodies that put corporate governance issues in the context of macro and systemic issues affecting investment practices and financial markets. Recent initiatives include the United Nations’ revised Sustainable Development Goals, G20/OECD’s recently updated Principles of Corporate Governance, the 2015 report on the design of a sustainable financial system by the

These Policy Priorities for 2016/17 have been reviewed and discussed in ICGN Policy Committee Chair meetings, and were also distributed to members of the GNIA (Global Network of Investor Associations) for feedback and discussion. Development of the priorities was also enhanced by feedback from ICGN’s annual membership survey. The Policy Priorities, incorporating Committee Chair and GNIA member feedback, were reviewed and approved by the ICGN board in September 2016.

In addition to sharing the Policy Priorities with ICGN members, ICGN will also reach out to other relevant standard setters and market participants, seeking to identify common ground and build cooperation where appropriate. Inevitably, a document of this nature is a living document, and will undergo periodic review and revision to ensure its relevance and effectiveness. Review and updating of the Policy Priorities is now part of the ICGN annual work programme of activities.

ICGN Policy Priorities 2016/17:

1. **Promoting long-term investment perspectives and sustainable value creation**

2. **Making successful stewardship a reality**

3. **Building effective boards amidst the changing boundaries of governance**

4. **Protecting minority shareholder rights**

5. **Seeking transparency through robust reporting, audit and metrics**

Guidance points

1. **Promoting long-term investment perspectives and sustainable value creation**

   Investors serving as fiduciary agents for their clients will look to invest in companies in both developed and emerging markets that can provide sustainable value creation. Investors need not only concern themselves with individual companies at the micro level. They must also think and act systemically with regard to the integrity and stability of financial markets as a whole— and to ensure that the financial markets
serve their intended purpose of promoting long-term economic growth and investment in the real economy by users of capital. This ultimately supports the generation of sustainable returns for providers of capital, including pensioners and other long-term savers. In particular, the advantage of ICGN’s corporate membership allows for dialogue and collaboration between investors and companies to build towards a more sustainable financial system and positive governance outcomes.

This all requires a long-term perspective on the purpose of the company, finance and corporate governance. It means deep consideration with regard to balancing the needs and interests of investors and other key stakeholders.

A fundamental stakeholder relationship is that between the two providers of risk capital and bearers of residual risk: shareholders and creditors. ICGN has begun to explore the role of the creditor in corporate governance with other standard setting bodies and in its conference programming.

Consideration of company purpose and its broader social role also gives rise to how environmental, social and governance (ESG) factors are built into company strategy and operations – and integrated in investment analysis and engagement. A key example is that investors should build awareness of how climate change affects systemic stability, and on how company boards are addressing climate risks at investee companies.

This is an overarching priority that touches most, if not all, ICGN policy committees, and is likely to be an on-going focus of ICGN conferences and policy output.

**ICGN Workplan 2016/17**

- **Long-term risk Viewpoint**

- **Fiduciary duty and long-term investment Viewpoint**

- **Role of the creditor in corporate governance Viewpoint**

- **Involvement in global initiatives relating to financial markets and systemic risk (The Investment Integration Project, PRI)**

- **Plenary session at ICGN conference in London, in partnership with the International Integrated Reporting Council, December 2016**

**2. Making successful stewardship a reality**

ICGN has long emphasised that with shareholder rights come shareholder responsibilities. Promoting effective investor stewardship is a core objective of ICGN,
and this policy priority carries over from 2015/16. Both in controlled and widely held companies, a diligent investor base supports good governance practices that can contribute to sustainable value creation and sustainable financial markets.

ICGN’s policy guidance in the area of stewardship and responsible investment practices dates back to 2003, including the 2011 **Principles for Institutional Investor Responsibilities** and ICGN’s **Model Mandate**, published in 2012. The latter provides model contract language for investment management agreements between asset owners and asset managers to integrate core stewardship practices into the asset management process.

As a key policy initiative in 2015/16 ICGN launched its Global Stewardship Principles, which were approved by ICGN members at its June 2016 AGM, following an extensive consultation period. These Principles provide a global framework for stewardship to guide investors, companies, regulators and standard setters in jurisdictions around the world. The Principles support the development of stewardship codes in new markets, and ICGN, through its Shareholder Responsibilities Committee, has been very active in responding to stewardship code consultations around the world.

The Global Stewardship Principles provide guidance on internal governance for investors and external stewardship activities relating to monitoring, engaging and voting. A distinguishing feature of the Principles relative to most other stewardship codes is the emphasis on investor governance, which we believe is the foundation for successful stewardship. This is the first principle identified in the Global Stewardship Principles, and remains an on-going focus. Building from the Global Stewardship Principles, ICGN will also explore the issue of fiduciary duty of institutional investors—and where the obstacles might lie.

In June 2016, ICGN formally established the Global Network of Stewardship Code Developers at its annual conference in San Francisco. The group, comprised of regulators and other stewardship code developers from around the world, will serve as a forum for dialogue on effective stewardship code implementation. ICGN also hosts a website page raising the visibility of national stewardship codes to a global audience.

ICGN’s advocacy effort for stewardship includes providing comment letters and submissions for feedback on stewardship codes in development around the world, and ICGN is particularly interested in supporting the culture of stewardship in emerging markets.

**ICGN Workplan 2016/17**

- Webinar on Global Stewardship Principles
- Stewardship Code Developers Network
3. Building effective boards amidst the changing boundaries of governance

In addition to facing traditional challenges relating to boards in their oversight of companies, the “boundaries” of corporate governance are often fluid and bring new risks and opportunities that require board attention and oversight. Many of these new challenges relate to business interface with society, including its interactions with customers, employees and other key stakeholders.

Related to this, the so-called “soft” issues of ethics and culture have been shown to have hard impacts on companies – particularly as they emerge as risks and opportunities. Examples include the emissions scandal at Volkswagen, the loss of confidence in the banking sector in the global financial crisis and the pernicious effects of bribery and corruption in both developed and emerging markets. Trust in business is low, and social concerns including income disparity are attracting significant public attention.

Ethical and cultural failures can have profound impacts on company finances, reputation, strategic positioning and reputation. New forms of risk are becoming visible as they relate to values, behaviour and stakeholder relations. Increasing attention is being focused on board diversity to address cultural issues and the broad understanding of risks within companies and their boards. While cybersecurity is not a new risk, concerns are heightening in particular with regard to cyber risk and other risks relating to the abuse of technology.

Key ICGN initiatives focusing on matters of board governance in 2015/16 included the update of our Guidance Statements on board diversity and on executive and non-executive remuneration. To explore newer issues confronting boards, ICGN also published Viewpoint reports on corporate tax policy and cyber risk—framing these issues in a corporate governance context—and focusing on what investors should be asking in terms of board responsibilities and oversight. ICGN also published a Viewpoint at the occasion of the COP-21 climate summit in Paris to discuss the issue of climate risk and the role that companies and boards should play to address these risks. These Viewpoints complement existing ICGN Guidance on Anti-corruption and Corporate Risk Management Oversight.

Given the growing interest globally in the topic of corporate culture and its links to governance, ICGN also partnered with the Institute of Business Ethics and the Institute of Chartered Secretaries and Administrators to convene a workshop focusing on identifying the “red flags” of corporate culture. This led to a jointly
sponsored report being published in early 2016, and will be an on-going focus of ICGN’s work in areas relating to business ethics, risk management and remuneration.

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- Viewpoint on corporate lobbying and political donations
- Webinar on tax policy
- Webinar on cyber risk
- Webinar on board diversity
- Webinar on executive remuneration

4. Protecting minority shareholder rights

As institutional investors in most cases are minority investors in companies, the protection of minority shareholder rights is fundamental to ICGN policy work—particularly with regard to promoting long-term investment perspectives. Concerns can be particularly acute in companies with controlling shareholders—a common theme of ownership around the world. While controlling shareholders in many cases can be strong long-term partners with minority shareholders, there is also the risk that the interests of the controlling shareholder might conflict with those of minority shareholders. These challenges can be particularly difficult in developing or emerging markets, where enforcement of minority shareholder rights can be challenging.

In the case of widely held companies, the risks are different. If no single investor has a large enough voting control to directly influence a company’s managers or board directors, investors run the risk of being marginalised by the interests and incentives of management. Shareholder rights are critical to ensure that management is not entrenched and working without accountability against the long-term interests of investors and the company more generally.

This calls for supporting minority shareholder rights and protections. Key areas of focus by ICGN in this context include:

- Differential ownership rights through loyalty shares or dual class shares. ICGN challenges differential structures of this nature for their potential for abuse by controlling shareholders. While differential ownership rights are viewed by some companies and regulators as a viable way to encourage long-term ownership and thinking by investors, ICGN views this as a flawed tactic. Avoiding mismatches between voting control and economic ownership is an important principle of protecting minority shareholder rights. After publishing a Viewpoint report on
differential ownership rights in 2015, ICGN conducted a membership survey on differential ownership, with a view to updating the Viewpoint on the subject in the year to come.

Dual class shares are problematic for minority shareholders and are an area of concern that is building globally—a major issue in Europe, where ICGN has been actively engaged with regulatory initiatives. ICGN engagement has focused not only on the EU Shareholder Rights Directive, but also on legal initiatives in France and Italy, where ICGN challenges the merits of differential ownership structures. This is also a significant and growing concern for investors in markets including Canada, Brazil and Hong Kong. At the same time the US technology sector in particular is taking a different tack, and purposefully employing differential rights to “protect” companies from potentially short termist financial market pressures. Accordingly, there remains considerable debate as to the benefits and potential abuses of differential rights.

- Chronic problems relating to the efficient execution of proxy voting also remain unresolved, both in domestic markets and in cross-border applications. This inhibits the most basic of shareholder rights: the ability of shareholders to vote at shareholder meetings and the ability to confirm whether their votes have formally been counted. These voting challenges also compromise the ability of shareholders to exercise appropriate stewardship in line with their fiduciary duties. There is scope for greater efficiencies across the vote execution chain and for more awareness building and dialogue with intermediaries—custodian banks in particular. ICGN has convened a working group of stakeholders from the investment, corporate and custodian communities to explore how a vote confirmation might become a practical reality.

Also in the proxy voting space ICGN is also becoming active in challenging a piece of legislation that was developed in the US Congress – The Duffy Act-- that would have a significantly negative impact on proxy advisors—and on investors that use proxy advisors as service providers to facilitate the voting process. ICGN has joined forces with the Council of Institutional Investors in the US and other investors to oppose this legislation.

- A fundamental shareholder right is the right to influence board membership and composition directly. This relates both to voting at shareholder meetings, but also for mechanisms to allow shareholders to put forward director candidates on the ballot; such rights are not universal to all companies and should be an area of focus. The issue of proxy access in North America remains problematic in many cases, and sets North America apart from other jurisdictions that encourage more active shareholder involvement in the nominations process.

- The UK’s vote to exit the European Union (“Brexit”) also raises questions with regard to the future of corporate governance in Europe after the UK’s departure and how that might affect shareholder rights in European companies-- or in UK listed companies as well. While Brexit is a regional issue it is also global in scope,
since investors in jurisdictions around the world invest in both European and British companies.

**ICGN Workplan 2016/17**

- Duffy Act—letter to US House of Representatives with regard to proxy voting agencies
- Updated Viewpoint on differential rights following the ICGN members’ survey
- Ongoing dialogue with the European Commission regarding the revisions to the European Shareholder Rights Directive
- Vote confirmation project
- Viewpoint on implications of Brexit on European corporate governance
- Plenary discussions on differential voting rights at the ICGN conference in Kuala Lumpur in 2017

**5. Seeking transparency through robust reporting, audit and metrics**

For investors to monitor, vote and to engage with companies effectively, accurate unbiased and relevant information must guide investor decisions. Detailed disclosure does not always ensure transparency, nor does it ensure the integrity of the accounting and auditing process. A significant debate continues in the sphere of accounting and auditing standards, relating the Conceptual Framework to IFRS standards, enhanced audit quality and disclosures. ICGN’s submission to the 2015 IFRS Conceptual Framework addressed a wide range of issues, including a nuanced approach to the issue of prudence and conservatism in enhancing investor stewardship. ICGN’s focus on audit quality standards and the integrity of the accounting and auditing professionals is reflected in our conference programmes which regularly feature these issues.

It is important to link financial statements and accounting matters to broader factors that affect sustainable corporate value creation. So beyond financial statements our focus on reporting extends to integrated reporting – particularly to capture all material information (such as relating to factors of culture, ethics, risk and strategy) in a holistic report to guide investors. This is not just as a more comprehensive and better integrated way of reporting by companies, but it also requires them to look at what strategically and operationally drive the fundamentals of the business, particularly with regard to critical stakeholders and social impacts.
Disclosure of appropriate ESG factors should be reflected in both “integrated thinking” by the company and in reporting to shareholders. Developing the right metrics is critical to understanding a company’s long-term risks and opportunities—as well as to designing an incentive pay system that motivates appropriate behaviour by executives. This puts the focus on the relevance and challenges of performance reporting generally and more specifically on the use of non-GAAP measures in performance reporting.

ICGN Workplan 2016/17

- PCAOB consultation
- Webinar on Integrated Reporting Guidance
- Joint conference with the International Integrated Reporting Council, December 2017
- Viewpoint on non-GAAP measures

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