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ICGN Policy Priorities 2017/18

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.

This document presents ICGN's 2018 Policy Priorities, which complement ICGN's core policy documents—the ICGN Global Governance Principles and Global Stewardship Principles, which can be found on ICGN's website.

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.

In addition to sharing the Policy Priorities with ICGN members, ICGN will also reach out to relevant standard setters and market participants, seeking to identify common ground and build cooperation where appropriate. ICGN Policy Priorities undergo annual review to ensure relevance and effectiveness.

ICGN Policy Priorities 2018:

- 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**
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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—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 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. 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.

Principal ICGN Policy Committee: Ethics and Systemic Risk Committee

Chairman: Peter Montagnon

ICGN’s Ethics and Systemic Risk Committee, has evolved from its former ICGN Business Ethics Committee. It maintains a focus on promoting high standards of ethical behaviour aimed at reducing risk and promoting long-term sustainable returns. It is also concerned with the way companies approach their relations with external stakeholders and their response to matters of public concern such as taxation, fraud, bribery, corruption or unethical behaviour, political donations, and lobbying. Following the 2017 AGM the Committee’s new branding reflects its extended mission of addressing systemic risks facing investors and markets.

ICGN Workplan 2018

- *Viewpoint: exclusion of companies from investment portfolios*
- *Viewpoint: fiduciary duty and systemic risk*
- *Working group around the responsibilities of investors and companies in addressing societal/systemic risks (such as income equality, political risk, lack of trust in financial markets and global warming). To prioritise systemic risk factors and lead to a Viewpoint.*

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. 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 ICGN launched its Global Stewardship Principles, which were approved by ICGN members at its June 2016 AGM. 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 active in responding to stewardship code consultations around the world.

ICGN's 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, serves 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.

Principal ICGN Policy Committee: Shareholder Responsibilities Committee
Co-chairs: Niels Lemmers (Netherlands), TerriJo Saarela (USA)

The Shareholder Responsibilities Committee seeks to influence the development of national and international corporate governance policies and proposals relating to shareholder responsibilities on behalf of ICGN members. It provides oversight of ICGN's Global Stewardship Principles and its Model Mandate to provide the foundation for ICGN's policy positions relating to shareholder responsibilities. The committee is also focused on securities lending and serves as a resource to ICGN by assisting in public consultations relating to stewardship codes.

ICGN Workplan 2018

- *Stewardship Code Developers Network*
- *Viewpoint: fiduciary duty and systemic risk*
- *Viewpoint: communications and engagement with company boards*
- *Japanese translation of Global Stewardship Principles and active engagement with Japanese regulators on stewardship*

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.

Principal ICGN Policy Committee: Board Governance Committee

Co-chairs: Catherine Jackson (Canada) and Carola van Lamoen (Netherlands)

The Board Governance committee focuses on the quality of the board of directors as the primary oversight body of the company, taking the perspective of institutional investors. It is closely aligned with ICGN’s policy priority relating to building effective boards amidst the changing boundaries of governance. Following ICGN’s 2017 AGM, the Remuneration and Corporate Risk Oversight committees were merged to form the Broad Governance committee.

The Committee’s focus includes issues relating to board structure, diversity, remuneration, independence and oversight of risk management. It can also broaden to include newer themes that directors need to be aware of, which can relate to issues such as cyber risk and tax policy. Committee outputs can help to inform company executives, boards and regulators about institutional investor expectations of good board governance. It can also be used to guide investor engagement with boards. Committee outputs can help to inform company executives, boards and regulators about institutional investor expectations of good board governance. The Committee is also a resource to ICGN by assisting in public consultations relating to corporate governance codes.

ICGN Workplan 2018

- *Viewpoint: the board's role with respect to remuneration inequality.*
- *Viewpoint: the board involvement with respect to climate change visa-vis the recently launched Task Force on Climate Related Disclosure (TCFD) guidelines*
- *Comment letter on UK Corporate Governance Code revisions*

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.

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.

Dual class shares are problematic for minority shareholders and are an area of concern that is building globally. 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 termism financial market pressures. Accordingly, there remains considerable debate as to the benefits and potential abuses of differential rights.

After publishing a Viewpoint report on differential ownership rights in 2015, ICGN conducted a membership survey on differential ownership, and produced an updated Viewpoint on this topic in early 2017. Building from this theme and the growing attention on benchmark stock indices with dual class share structures, ICGN published a further Viewpoint focusing on the criteria used by index providers.

- 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 recently convened a working group of stakeholders from the investment, corporate and custodian communities to explore in a Viewpoint report on how a vote confirmation might become a practical reality.

Principal ICGN Policy Committee: Shareholder Rights Committee

Co-chairs: Bram Hendriks (Netherlands), Eugenia Jackson (UK)

Shareholder Rights Committee focuses on the protection of minority shareholder rights – in both widely-held and controlled companies. It seeks to influence policymakers and other stakeholders relating to shareholder rights on behalf of ICGN members. This includes: voting rights, dual class share structures, shareholder participation in general meetings, shareholder director nomination, the interaction between shareholders and boards, engagement amongst shareholders and cross-border voting practices.

ICGN Workplan 2018

- *Viewpoint: Related party transactions*
- *Voting rights project: EU Expert Group on Technical Aspects of Corporate Governance Processes*
- *Viewpoint on stock exchange governance*
- *Ongoing regulatory dialogue in many markets (including UK, Malaysia, Hong Kong, Singapore, Netherlands) about differential ownership structures*

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.

Principal ICGN Policy Committee: Disclosure and Transparency Committee

Co-chairs: Gary Buesser (USA), Joyce Haboucha (USA)

As of the 2017 ICGN AGM, the Accounting and Auditing and Integrated Business Reporting committees merged to form the Disclosure and Transparency committee which seeks to influence policymakers and other stakeholders to enhance company transparency through robust reporting, audit and metrics. It will do so by responding to regulatory consultations, producing and promoting ICGN Guidelines, Viewpoints and other relevant, ad hoc projects. Specific topics can include accounting issues, audit quality, integrated reporting, and ESG disclosure

ICGN Workplan 2018

- *Viewpoint: The proliferation of non-GAAP reporting*
- *Viewpoint: quarterly reporting*
- *Viewpoint: human capital*
- *Publishing an article in an American Bar Association publication on climate disclosure.*
- *Participation in investor working group holding discussions with the Corporate Reporting Dialogue on ESG reporting for investors*

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