ICGN
International Corporate Governance Network

Taiwan Stock Exchange
Corporate Governance Center

5 February 2016

Via Email: 1211@twse.com.tw

Re: **Draft Stewardship Principles for Institutional Investors**

Dear Members of the Financial Supervisory Commission, the Corporate Governance Center of the Taiwan Stock Exchange, Taiwan Depository & Clearing Corporation, the Securities Investment Trust & Consulting Association and the Taiwan Financial Services Roundtable:

The International Corporate Governance Network ("ICGN") welcomes the opportunity to comment on the proposed Stewardship Principles for Institutional Investors which have been drafted to provide guidance for how investors should fulfill their ownership responsibilities in relation to their investment in a listed company.

ICGN was founded in 1995, and is an investor-led membership organisation of more than 670 individuals based in over 45 countries from around the world. Our mission is to promote effective standards of corporate governance and investor stewardship to advance efficient markets and sustainable economies world-wide. Our members represent institutional investors with global assets under management in excess of US$26 trillion. Accordingly, ICGN's members offer a source of practical knowledge and experience in regard to governance and investment issues. For more information on the ICGN, please visit www.icgn.org.

The membership of ICGN has adopted a series of principles and best practice documents that bear on the draft Stewardship Code. In particular, the *ICGN Global Governance Principles*[1], the *ICGN Statement of Principles for Institutional Investor Responsibilities*[2] and *ICGN Model Contract Terms between Asset Owners and Managers*[3] are particularly relevant. We would also like to bring your attention to the ICGN's draft Global Stewardship Code, which is subject to ICGN Member approval at our forthcoming Annual General Meeting in June.[4]

The Global Stewardship Code will complement, and builds upon, ICGN's prior guidance statements on stewardship and investor responsibilities. It identifies seven underlying principles of stewardship, and places a strong emphasis on investors' own governance models as well as adding a new and specific focus on the integration of environmental, social, and governance (ESG) factors into investment analysis and engagement with companies. One of the explicit purposes of the Code is to provide a point of reference to other jurisdictions in developing their own codes, so we hope this will be helpful to you in this application. In particular, we would identify investor governance and consideration of ESG issues as two new features of the ICGN Global Stewardship Code that you may wish to consider for the new code in Taiwan.

[1] See: http://icgn.flpbks.com/icgn_global_governance_principles/#p=1

[2] See: http://icgn.flpbks.com/icgn_inst_investor_respons/#p=1

[3] See: http://icgn.flpbks.com/icgn_model-contract-terms_2015/#p=1

[4] See: ICGN draft Global Stewardship Code

Saffron House 6-10 - Kirby Street - London - EC1N 8TS - UK
VAT No. 927 1665 09 | Registered in England No 6467372
t: +44 (0)207 612 7011
f: +44 (0)207 612 7085
e: secretariat@icgn.org
w: www.icgn.org
@ICGNCorpGov
ICGN

In advance of the ICGN Global Stewardship Code being formally adopted by ICGN Members, we highlight the most relevant elements of the existing ICGN guidance in this letter. We also encourage you to review these documents, as well as the text of our draft global stewardship code.

In the past three years, ICGN has commented on several consultations directly related to stewardship codes for institutional investors. While each consultation is unique to the particular country and market, there are evolving similarities in regard to the relationship that institutional investors should have with investee companies. As so well stated in the consultation document, “In order to maintain the momentum for reform, the "push" by relevant policies and the "pull" from the markets are equally essential.”

The statistics from the Financial Supervisory Commission (FSC), which establish that domestic and foreign institutional investors account for 48.1% of the overall trading value, support the need for institutional investors to use their collective voice, leverage their ownership rights and discharge their stewardship responsibilities to drive companies to increase governance and bring value to the markets. The trend of adopting stewardship codes has caught the collective conscience in many markets and countries which the ICGN applauds

It is interesting that the draft calls for institutional investors to “publicly sign up” to them by making a public statement and notifying the Corporate Governance Center (CGC) of their commitment to the six Principles. It also asks signatories to disclose this position on their websites and the CGC’s website so that all stakeholders will be made aware. The Principles will be applied on a “comply or explain” basis which the ICGN supports. A comply or explain system provides for reasonable explanations to be provided where different stewardship and investment strategies are employed and we advocate that investors embrace their obligations to act fully aligned in the interests of the company, or as institutional investors, to their beneficiaries or clients, over relevant time-horizons.

ICGN agrees that requiring investors to either comply or explain on their application of the Stewardship Code is likely to be the most effective way to encourage investors to consider their approach to stewardship. In this regard, the FSC could also give attention to how this will be monitored, particularly for those funds that may choose to submit an explanation of non-compliance.

The proposed Stewardship Code lists six principles and guidelines:

Principle 1 **Establish and Disclose Stewardship Policies**

Guideline 1-1 An institutional investor shall establish and disclose its stewardship policy.

Guideline 1-2 In establishing its stewardship policy, an institutional investor shall contemplate its role in the industrial value chain and define its responsibilities and means of fulfilment thereof.

ICGN guidance notes the growing proliferation of stewardship codes across various markets and views stewardship as central to the modern investment management process. Asset owners should consider how to best manage the rights they have as an investor and should report on implementation of proxy voting and any other stewardship activities. Our guidance also stresses that stewardship can be exercised in collaboration with other investors and can be delegated to third party providers, provided they are monitored and held accountable. It includes fundamental institutional investor activities, such as (without limitation), oversight of stock lending practices and proxy voting. See the appendix for greater detail on this point, drawn from the ICGN Model Mandate.

See ICGN Statement of Principles for Institutional Investors, Guidance on Principles for External Responsibilities, which under 4.1 calls for the establishment and application of consistent policies;

"Institutional investors should adopt and disclose clearly stated, understandable and consistent policies to guide their approaches to key issues within their investment universe. These policies should be communicated to clients and beneficiaries in plain and understandable language."

Principle 2 Establish and Disclose Policies on Managing Conflict of Interests

Guideline 2-1 An institutional investor shall establish and disclose a clear policy on managing conflict of interests, so as to ensure its investment activities are made in the long-term interests of clients or ultimate beneficiaries.

Guideline 2-2 A policy on managing conflict of interests shall at least disclose situations in which an institutional investor may be faced with conflict of interests, as well as how such incidences will be managed.

ICGN agrees that institutional investors should adopt and disclose clear policies on managing conflicts of interests.

See ICGN Statement of Principles for Institutional Investors, Guidance on Principles for Internal Governance, which under 3.4, addresses conflicts of interest, codes of ethics, compliance;

"Institutional investors should understand, minimize and manage the conflicts of interest that they face and behave ethically, ensuring that they maintain focus on advancing beneficiary or client interests and disclosing any conflicts transparently to them."

Principle 3 Pay Continued Attention to Investee Companies

Guideline 3-1 An institutional investor shall continually pay attention to its investee companies, so as to obtain sufficient and appropriate financial or non-financial information and assess the nature, timing and extent of engagement with investee companies. However, the institutional investor shall avoid obtaining and using undisclosed information.

Guideline 3-2 An institutional investor shall have sufficient knowledge of its investee companies, including but not limited to industry profile, opportunities and risks, business strategies, financial status, financial performance, cash flow, environmental impacts, social issues and corporate governance, and assess how these factors will affect the long-term values for the investee companies, clients or beneficiaries.

ICGN agrees that institutional investors are well served when they engage with investee companies. There are restrictions and penalties for the disclosure of non-public information that investors should be aware of and pledge to uphold.

See ICGN Statement of Principles for Institutional Investors, Guidance on Principles for External Responsibilities, which under 4.2 calls for active monitoring;

"Institutional investors should monitor closely the companies in which they invest in order to assess their individual circumstances, performance and long-term potential, and to consider whether there is value in intervening to encourage change."

Principle 4 Appropriate Dialogue and Interaction with Investee Companies

Principle 4-1 To the extent in line with regulation requirements and policies on managing conflict of interests, an institutional investor shall have dialogue and interaction with investee companies for any significant issues of concern to it, thereby urging investee companies to comply with corporate governance principles and enhancing long-term values for clients or beneficiaries.

Guideline 4-2 Dialogue and interaction between institutional investors and investee companies should include but not be limited to discussions with management, making public statements, speaking or submitting motions or casting votes at shareholder's meetings.

ICGN agrees that dialogue between institutional investors and investee companies is critically important. We would note in particular that the new Taiwan stewardship principles may wish to add a provision to encourage collaboration between institutional investors. It is our experience that engagement can be particularly effective in case when institutional investor join forces in company engagement; it can also make the process more efficient, both for companies and investors.

See ICGN Statement of Principles for Institutional Investors, Guidance on Principles for External Responsibilities, which under 4.3, calls for proactive engagement;

"Institutional investors should engage intelligently and proactively as appropriate with investee companies on risk to long-term performance in order to advance beneficiary or client interests. Engagement is described as a "purposeful dialogue" with the aim of preserving or enhancing value on behalf of beneficiaries or clients. When dialogue is failing, institutional investors should communicate the steps that may be taken to escalate the activity."

Principle 5 Establish and Disclose a Clear Policy on Voting and Voting Results

Guideline 5-1 An institutional investor shall cast votes on shares it holds or manages. In the case where an institutional investor is unable to exercise its voting rights due to restrictions by regulations or policies on managing conflict of interests, it shall publicly provide an explanation.

Guideline 5-2 An institutional investor shall establish and publicly disclose a clear voting policy.

Guideline 5-3 An institutional investor shall carefully read the handbook for shareholder's meetings prior to voting and, based on its attention to and dialogues and interactions with the investee companies; assess impact of motions on long-term values of clients, beneficiaries and investee companies. The institutional investor shall judge on its own about how it should exercise its voting rights even in the case where a voting recommendation report has been obtained from a proxy advisory agency, so as to avoid mechanically voting for or against proposals or abstain.

Guideline 5-4 An institutional investor shall appropriately record, analyze and disclose voting activities which it has made in accordance with relevant policies, including number of times of attendance to shareholder's meetings, number of votes cast, status of support, opposition or abstention for each type of motions.

ICGN agrees that proxy voting is one of the most important ways that investors can communicate their support or lack of support in board nominees, policies and performance.

See ICGN Statement of Principles for Institutional Investors, Guidance on Principles for External Responsibilities, which under 4.4, calls for delivery of informed voting decisions;

"Institutional investors should make informed and independent voting decisions at investee companies, applying due care, intelligence and judgement. They should develop and publish a voting policy so that beneficiaries and investee companies can understand what criteria are used to reach decisions."

Saffron House 6-10 - Kirby Street - London - EC1N 8TS - UK
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w: www.icgn.org
@ICGNCorpGov
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Principle 6 Periodically Disclose Status of Fulfillment of Stewardship Responsibilities to Clients or Beneficiaries

Guideline 6-1 An institutional investor shall properly record its stewardship activities.

Guideline 6-2 An institutional investor is advised to periodically disclose to its clients or beneficiaries the status of its fulfillment of stewardship responsibilities according to request of or agreement with clients or beneficiaries. Such disclosure may be made in the form of public disclosure, report or any other means.

Guideline 6-3 In the case where an institutional investor does not directly carry out an investment activity, such as when management of funds is mandated on a discretionary basis to an asset manager, it shall disclose measures it has taken to ensure compliance with the stewardship policy when making disclosure to its clients or beneficiaries on the status of fulfillment of stewardship responsibilities.

ICGN agrees with the need for investors to properly record their stewardship responsibilities. See ICGN Statement of Principles for Institutional Investors, Guidance on Principles for Internal Governance, which under 3.6, calls for transparency and accountability;

"Institutional investors should be transparent and open with their beneficiaries or clients so as to be fully accountable for the effective delivery of their duties."

ICGN would emphasise the importance of establishing fiduciary and stewardship responsibilities explicitly in investment management agreements—the contracts between asset owners and asset managers that define the scope and deliverables of an investment mandate. The ICGN Model Mandate[5] provides a practical example of contract language that can incorporate aspects of investor monitoring, voting and engaging that are linked to stewardship and fiduciary responsibilities, and we encourage widespread use of the Model Mandate by fund trustees.[6]

Finally, you may be aware that the ICGN website provides a space for the publication of stewardship codes from around the world and we would welcome the inclusion of your Code. We hope these comments will be helpful. If you wish to discuss our comments further, please contact ICGN Policy Director, George Dallas, whose contact details are listed below.

Yours truly,

Erik Breen

Chair, ICGN Board of Governors

[5] See: http://icgn.flpbks.com/icgn_model-contract-terms_2015/#p=1

[6] For example, the Code for Responsible Investment in Southern Africa (CRISA) announced in 2015 its use of the ICGN Model Mandate to guide implementation of CRISA in South African. This involved the adaptation of Mandate's model contractual provisions for application in a South African legal context.

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e: secretariat@icgn.org
w: www.icgn.org
@ICGNCorpGov
ICGN

ICGN contacts:

Kerrie Waring, ICGN Executive Director: kerrie.waring@icgn.org

George Dallas, ICGN Policy Director: george.dallas@icgn.org

Niels Lemmers, Co-Chair, ICGN Shareholder Responsibilities Committee: nlemmers@veb.net

Carol Nolan Drake, Co-Chair, ICGN Shareholder Responsibilities Committee: cdrake@opers.org