The Stewardship Code and its implementation

Sir Win Bischoff, chairman of the Financial Reporting Council (FRC), was the guest speaker at the eleventh Centre for Audit Committee and Investor Dialogue dinner. The discussion focused on the Stewardship Code. First published in 2012, the Stewardship Code is soon subject to review by the FRC.

Viewpoints and issues arising from the discussion

Scope for more fund manager engagement with companies
The Stewardship Code has been a success with more than 300 institutions signed up to it and the expectation of asset owners for fund managers to subscribe. There is, however, still scope for a number of signatories to engage more fully with companies in which they hold shares. An investor considered that if asset owners were ‘tough enough’ their fund managers would engage more and that they should place greater emphasis on engagement when assessing managers’ performance.

Proxy owners have a role to play but better quality engagement needed
Proxy advisers are considered to have a role to play in good governance as they act for a significant number of shareholders. Concern was expressed that they tend to adopt a ‘tick box’ approach to governance matters and engagement by companies with proxy advisers on a timely and constructive basis when the latter have concerns can be difficult. An investor noted that proxy advisers tend to take the different views of their various clients and come up with an ‘aggregated fudge’ in determining their position on an issue.

The importance of proxy advisers was highlighted by an investor with more than 10,000 holdings. They directly decide their voting policy for around 1,000 of their holdings, with the vast majority of the remainder determined on their behalf by one of the main proxy advisers. In addition to proxy advisers, it was thought index trackers also needed to engage actively with investee companies.

Measuring the real impact of the Stewardship Code
A challenging investor view was that whilst the Stewardship Code seems to have led to more meetings between companies and investors or fund managers, it was less clear that there has been a sustained increase in company performance or, more generally, in companies being held more to account as a result. Without clear objectives, engagement is not going to have a transformational impact.
Is there a clear link between good governance and performance?
There was discussion on whether good governance leads to good performance with an instance being cited of strong results notwithstanding governance weaknesses. Alternative views were that on the balance of probability good governance is to be preferred and that poor governance can definitely destroy performance.

Too much investor attention focused on remuneration
The general view was that investor/company dialogue is far too focused on remuneration issues though an investor indicated significant concern remains in this area and therefore engagement continues to be important.

Investor engagement with boards on succession planning essential
There was widespread agreement that succession planning is an area where dialogue between investors and the chair is essential. Moreover, when investors are unhappy with the performance of a business it is increasingly the chair’s role, rather than the CEO, which first comes under the spotlight. In addition, with more powers often being devolved to committees, investors also need to take an interest in the audit committee chair’s effectiveness and, if the committees exist, in that of the chair of the risk and safety committees.

Understanding the business model valuable for investors
There is now more information in the annual report on the business model of companies and the consensus was that understanding the value creation process is very useful. An investor, however, felt that the public disclosure, at least, can sometimes be expressed in fairly general terms for fear of giving information to competitors.

More engagement needed with audit committees
An audit committee chair mentioned that investors very rarely raise matters with them. More than one investor said that unlike with remuneration committee chairs, where there was a ‘well trodden path’, it could be difficult to get access to audit committee chairs though when meetings were held they were insightful. If there is to be greater access, a business view is that it will be important for NEDs not to ‘usurp’ the role of the CEO and CFO as the primary point for discussion with investors on performance and financial issues.
The Centre provides regular opportunities for discussion between Audit Committee chairs of FTSE 350 companies and leading institutional investors on topics of mutual interest. Should you require any further information on the Centre, or wish to participate in future meetings, please do not hesitate to contact:

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The next meeting of the Centre for Audit Committee and Investor Dialogue will be held on 4 November 2015.