

29 March 2019

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By Electronic Transmission to: [stewardshipcode@frc.org.uk](mailto:stewardshipcode@frc.org.uk)

Dear Sir/Madam,

**CFA UK response to the FRC's Consultation on the proposed revision to the UK Stewardship Code**

The CFA Society of the UK (CFA UK) welcomes the opportunity to share its views on the FRC's consultation on the proposed revision to the UK Stewardship Code.

Having participated in last year's consultation on the future direction of the Stewardship Code<sup>1</sup> and shared views on the Stewardship Code as part of our input into the Kingman Review of the FRC<sup>2</sup>, CFA UK is extremely interested to see these final proposals and pleased with the progress that the FRC has made in further raising the bar for stewardship in the UK.

Like all professions, the investment profession aims to add value in a number of ways – but it is primarily through aiming to meet and exceed their clients' (investors') objectives over a defined time horizon. In pursuit of that goal, the investment profession should allocate capital efficiently and sustainably and also engage with users of capital to share and apply their through-the-cycle experience, knowledge and impartiality to help investees best address their customers' and society's long-term needs. This latter activity is at the heart of stewardship.

CFA UK would like at this stage to make note of the fact that the proposed new definition of stewardship in the 2019 version of the Stewardship Code is substantially broader than that on which the previous version of the Stewardship Code was based. There is clearly a balance to be struck between ambition, on the one hand, and having achievable and measurable goals on the other. CFA UK will address this point in more detail in its response to question 1 of DP19/1 - the joint FCA/FRC consultation on "Building a Regulatory Framework for Effective Stewardship". However, at this stage CFA UK would wish to signal its belief that the proposed new definition is probably too broad in that it moves to make the investment profession accountable for matters that would be hard to target and then to measure.

**HIGH LEVEL POINTS**

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<sup>1</sup> <https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-letter-to-catherine-horton-28-feb-2018--final.pdf?la=en&hash=CF53FFB72384C08CF5D6D7BC85E310C6EBF4320A>

<sup>2</sup> <https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/letter-to-beis-final-6august2018.pdf?la=en&hash=A9530BDF9F05E3C8057F43AFA89606362BCE205B>

We have responded to each of the questions as numbered below. However, we wish to make the three following general points of principle up-front:

### **1. Raising standards**

CFA UK believes that the proposed revisions set higher standards for stewardship and address the recommendations of the Kingman review.

In particular, CFA UK supports the introduction of an annual Activities & Outcomes Report. We believe the emphasis must be on outcomes rather than the substance of stewardship statements. Investors should be judged by their deeds more than their words and the proposed reporting framework will hopefully ensure there are no empty promises.

Linked to this, CFA UK would also encourage a robust tiering system that motivates signatories to enhance their stewardship activities. This should be based not only on the stewardship statement but also the Activities & Outcomes Report.

### **2. More emphasis on Principles, less on Guidance**

CFA UK believes it is of fundamental importance to hold true to the structure of the Stewardship Code as it was originally conceived – i.e. a Code, with Guidance – and not as it is in danger of becoming, a Code with Standards.

The right balance needs to be found between outlining the key stewardship responsibilities whilst leaving sufficient scope for the industry to innovate, articulate its best practices, evolve and so progress on effective stewardship.

While some guidance on current best practice would provide a useful reference to signatories, CFA UK would rather see less Guidance and more aspiration in the Stewardship Code so as to allow the profession to deliver on the Principles as best suits their investment style and according to their fiduciary duty to clients.

CFA UK would also suggest a greater emphasis on the importance of the Principles to signatories' fiduciary duties to clients.

### **3. Resources**

CFA UK would suggest greater encouragement for signatories to ensure they have the appropriate resources needed to undertake effective stewardship.

Critical to this is the employment of skilled professionals. CFA would like to see “professional qualifications” and evidence of continuous professional development (“CPD”) added to the list of evidence to demonstrate that a signatory’s work-force was well-qualified to exercise proper stewardship.

We would also encourage signatories to indicate the scale of their budget to support stewardship activities to demonstrate that they are devoting sufficient resources to effective stewardship.

## **MAIN RESPONSE**

### **Questions**

*Q1. Do the proposed Sections cover the core areas of stewardship responsibility? Please indicate what, if any, core stewardship responsibilities should be added or strengthened in the proposed Principles and Provisions.*

- CFA UK believes that the five Sections are broadly well ordered and thought through.
- However, CFA UK have concerns about the the downgrading of both conflicts of interest and collective engagement in the new draft. Both were Principles in the former code. While conflicts remains as a Principle, collective engagement becomes only a Provision. This could be interpreted as a downgrading of these issues, which would be unfortunate and may not be intended.
- CFA UK support the alignment of investment and stewardship activities with the time horizons of beneficiaries; however, where possible, we would encourage a long-term focus.
- In Section 2 Investment Approach we would encourage a greater emphasis on ESG integration in the Provisions.

*Q2. Do the Principles set sufficiently high expectations of effective stewardship for all signatories to the Code?*

- CFA UK believes that the Principles do set higher standard for stewardship.
- However, this needs to be balanced with leaving sufficient scope for the industry to continue making its own progress on effective stewardship. CFA UK would not like to see signatories adopt lowest common denominator compliance approaches in response to an overly detailed checklist.

*Q3. Do you support 'apply and explain' for the Principles and 'comply or explain' for the Provisions?*

- CFA UK believes that this approach would make the Code applicable across the the investment industry while providing some flexibility for the differences in structure, size and other characteristics of different firms.
- However, its level of appropriateness is dependent on the split between the Principles and Provisions being the right one.

*Q4. How could the Guidance best support the Principles and Provisions? What else should be included?*

- CFA UK believes that, as with the Principles, a balance needs to be found between highlighting the important considerations while sufficient scope for the industry to continue its own evolution and progress on effective stewardship.

- While some guidance on current best practice could be useful for firms with less developed processes, CFA UK would rather see less guidance and more aspiration by the profession to deliver on the principles as best suits their investment style and according to their fiduciary duty to clients.
- CFA UK would like to see "professional qualifications" and evidence of "continuous professional development ("CPD") added to the list of evidence to demonstrate that a signatory's work-force was well-qualified to exercise proper stewardship.

*Q5. Do you support the proposed approach to introduce an annual Activities and Outcomes Report? If so, what should signatories be expected to include in the report to enable the FRC to identify stewardship effectiveness?*

- CFA UK believes that the production of such reports is already considered best practice. CFA UK are supportive of this becoming more prevalent.
- CFA UK believes the content of such reports should be left to the discretion of signatories in order to ensure they are produced in a manner both in keeping with both the Code and their investment approach. However, a description of best practice could be included in the Guidance.
- Additionally, signatories could provide a statement around how they plan to enhance their stewardship practices in the upcoming year. Signatories could then report on progress against these plans on an annual basis.

*Q6. Do you agree with the proposed schedule for implementation of the 2019 Code and requirements to provide a Policy and Practice Statement, and an annual Activities and Outcomes Report?*

- CFA UK believes the timeframe is appropriate.
- In the absence of guidance on tiering, CFA UK would also encourage the FRC to consider offering recognition to early signatories of a new Code.

*Q7. Do the proposed revisions to the Code and reporting requirements address the Kingman Review recommendations? Does the FRC require further powers to make the Code effective and, if so, what should those be?*

- CFA UK believes that the proposed revisions set higher standards for stewardship and address the recommendations of the Kingman review.
- We agree that the emphasis must be on outcomes rather than the substance of individual Stewardship Statements. Hence, our full endorsement of the proposal for an Activity & Outcomes Report.

*Q8. Do you agree that signatories should be required to disclose their organisational purpose, values, strategy and culture?*

- Yes. CFA UK believes this would provide important context for signatories' approach to investment and stewardship.

*Q9. The draft 2019 Code incorporates stewardship beyond listed equity. Should the Provisions and Guidance be further expanded to better reflect other asset classes? If so, please indicate how?*

- CFA UK fully supports the extension of stewardship beyond listed equity.
- However, CFA UK believes the nature and extent of this incorporation should be conducted and assessed based on its relevance to each signatories' investment approach and the asset classes it is invested in.

*Q10. Does the proposed Provision 1 provide sufficient transparency to clients and beneficiaries as to how stewardship practices may differ across funds? Should signatories be expected to list the extent to which the stewardship approach applies against all funds?*

- CFA UK believes that signatories should be responsible for outlining to what extent their Statement and Report applies and how this relates to their investment approach both generally and with regard to specific funds, especially where practice at the individual fund level diverges from the firm's general approach.

*Q11. Is it appropriate to ask asset owners and asset managers to disclose their investment beliefs? Will this provide meaningful insight to beneficiaries, clients or prospective clients?*

- CFA UK believes that this would provide useful context for the Statement and Report.
- It should be noted that many asset managers will run many different investment strategies and within one firm there may exist multiple investment beliefs rather than one central firm-wide investment belief.
- There is a danger that such disclosures could prove to be quite high-level, aspirational and use boiler-plate language. In this context again, CFA UK welcomes the introduction of the Activities & Outcomes Report in the Code .
- Although not commented on in the Code, the disclosure of an asset owners or asset manager's investment beliefs could give greater transparency to investee companies and enhance the quality of engagement between asset managers and the investee companies.

*Q12. Does Section 3 set a sufficiently high expectation on signatories to monitor the agents that operate on their behalf?*

- CFA UK believes it does.
- Wherever elements of stewardship responsibilities are delegated by a signatory, there should be an expectation that they monitor those carrying out these services.

*Q13. Do you support the Code's use of 'collaborative engagement' rather than the term 'collective engagement'? If not, please explain your reasons.*

- The term 'cooperative' is being introduced by the FCA to reflect the language in SRD II.
- CFA UK believes that using 'co-operative' would provide greater consistency with regulation. Additionally, the definition of 'cooperative' alludes more towards the pursuit of an outcome than collaboration alone.

*Q14. Should there be a mechanism for investors to escalate concerns about an investee company in confidence? What might the benefits be?*

- CFA UK believes that investors already have multiple approaches for escalating issues and signatories should be responsible for determining which of these to utilise. Such a mechanism would arguably reduce the emphasis on signatories' own stewardship activities, which is counter to the objectives of the Code.

*Q15. Should Section 5 be more specific about how signatories may demonstrate effective stewardship in asset classes other than listed equity?*

- No, CFA UK would hope that signatories would make this clear in their Annual Activities & Outcomes report. CFA UK would also encourage the guidance not to be overly proscriptive in this area in order for innovation to prosper and individual initiatives to develop.

*Q16. Do the Service Provider Principles and Provisions set sufficiently high expectations of practice and reporting? How else could the Code encourage accurate and high-quality service provision where issues currently exist?*

- CFA UK believes that, as part of their own monitoring responsibilities, it is the clients of Service Providers who have the primary duty to hold them to account. This is referenced in Provisions 16 and 24. CFA UK do not believe there is a need for separate Principles and Provisions for Service Providers embedded within the Code.

We are grateful for the opportunity to respond to these valuable consultations and would welcome the opportunity to take any questions you may have.

Yours sincerely,



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### **Appendix 1: About CFA UK & the CFA Institute**

**CFA UK:** serves nearly 12,000 leading members of the UK investment profession.

- The mission of CFA UK is to build a better investment profession and to do this through the promotion of the highest standards of ethics, education and professional excellence in order to serve society's best interests.
- Founded in 1955, CFA UK is one of the largest member societies of CFA Institute (see below) and provides continuing education, advocacy, information and career support on behalf of its members.
- Most CFA UK members have earned the Chartered Financial Analyst® (CFA®) designation, or are candidates registered in CFA Institute's CFA Program. Both members and candidates attest to adhere to CFA Institute's Code of Ethics and Standards of Professional Conduct.

**CFA Institute:** is the global association for investment professionals.

- The mission of CFA Institute is to lead the investment profession globally by promoting the highest standards of ethics, education, and professional excellence for the ultimate benefit of society.
- It awards the Chartered Financial Analyst® (CFA), and Certificate in Investment Performance Measurement® (CIPM) designations worldwide; publishes research; conducts professional development programs; and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry.
- As of 1<sup>st</sup> February, CFA Institute has more than 165,000 members in 162 countries, of which more than 160,000 hold the Chartered Financial Analyst® (CFA) designation.



## **Appendix 2: Previous CFA UK consultation responses to FRC on UK corporate governance and stewardship:**

- Response to FRC's consultation on proposed revisions to the UK Corporate Governance Code and the future direction of the Stewardship Code (Feb 2018):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-letter-to-catherine-horton-28-feb-2018--final.pdf?la=en&hash=CF53FFB72384C08CF5D6D7BC85E310C6EBF4320A>
- Response to Green Paper on UK Governance Reform (Nov 2016):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/cfa-uk-response-to-corporate-governance-reform-green-paper-nov-2016.pdf?la=en>
- Response to FRC's consultation on proposed revisions to the UK Corporate Governance Code (May 2014):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/letters/2014/6-june/ukcorporategovernancecode.pdf?la=en>
- Response to FRC's consultation on revisions to the UK Corporate Governance Code (July 2012):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/letters/2012/7-july/codeforcorporategovernance.pdf?la=en>
- Response to FRC's consultation on revisions to the Stewardship Code (June 2012):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/letters/2012/7-july/stewardshipcode.pdf?la=en>
- Response to the Kay Report Interim Review (April 2012):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/letters/2012/4-april/kayreviewinterimreport.pdf?la=en>
- Response to the FRC's consultation on proposals to reform the FRC (January 2012):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/letters/2012/1-january/reformtothefinancialreportingcouncil.pdf?la=en>
- Response to the Kay Review of UK equity markets (December 2011):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/letters/2012/11-november/kayreviewrecommendations.pdf?la=en>
- Response to FRC's consultation on revisions to the UK Corporate Governance Code (March 2010):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/letters/2010/3-march/reviseducorporategovernancecode.pdf?la=en>
- Response to FSA's consultation paper (10/03) on effective corporate governance (May 2010):  
<https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/letters/2010/4-april/effectivecorporategovernance.pdf?la=en>