



Financial Reporting Council

# Effective Stewardship Reporting

Examples from 2021  
and expectations for 2022

November 2021

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# Foreword



## Sir Jonathan Thompson

Chief Executive Officer, Financial Reporting Council

The Stewardship Code rightly sets a high standard for investor stewardship. At the same time, the FRC recognises that signatories will have different approaches to fulfilling their responsibilities. The purpose of stewardship reporting is for investors to demonstrate how they are protecting the hard-earned pensions and savings entrusted to them, by ensuring that they are managed responsibly, creating long-term value for their clients and beneficiaries.

The FRC published the first list of signatories in September. We received 189 reports and assessed 125 applicants as successful. This represents £20 trillion of assets under management across a range of asset classes and markets. We have received over 100 applications for our October deadline – significantly more than we expected. This demonstrates

the growing importance and attention paid to stewardship issues – particularly by clients and beneficiaries. We are now assessing the recent applications and will announce the successful applicants in the first quarter of 2022.

Today's publication, *Effective Stewardship Reporting* identifies good examples of reporting and areas where we wish to see improvement next year. We saw some good reporting on governance, resourcing, the integration of stewardship with investment and on stewardship activities. We would like to see improvements to reporting on how signatories are managing market-wide and systemic risks as well as their approach to stewardship in asset classes other than listed equities.

As the FRC transitions to the Audit, Reporting and Governance Authority (ARGA), both the Stewardship Code and the Corporate Governance Code remain key to maintaining trust and integrity in how UK companies are led and run, and enhancing the UK's position as a destination for long-term, sustainable investment, bringing wider benefits for the economy, the environment and society. Demonstrating effective stewardship and governance builds the trust that is necessary to continue to attract investment in the UK and improve access to capital.

A handwritten signature in black ink that reads "Jonathan Thompson". The signature is written in a cursive style and is positioned above a horizontal line.



# Executive Summary

Stewardship is the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries, leading to sustainable benefits for the economy, environment and society.<sup>1</sup> The UK Stewardship Code 2020 (the Code) sets high standards for asset owners, asset managers, and the service providers that support them, to report on their stewardship activities and their outcome. The first list of 125 signatories to the updated Code was published on 6 September 2021.<sup>2</sup>

The aim of this report is to encourage fair, balanced and understandable reporting about stewardship and to explain what we expect stewardship reports to include. We illustrate this with examples of good reporting.

We observed good efforts from many Stewardship Code applicants and encouraging disclosures on governance, resourcing and the integration of stewardship and ESG factors into investment decision-making. Reporting on the activities and outcomes relating to conflicts of interest, review and assurance, and monitoring agents was poorer.

Part 1 of the report focuses on reporting expectations which apply across the Code, including the presentation and format of reporting. Here, we reiterate and expand on points made in the Code and in our Review of Early Reporting published in 2020. We also outline how we assess reports and identify the factors we use to ensure a fair and proportionate approach.

The remaining sections of the report focus on the areas where investors and their agents can have the most impact and where most improvement is needed; market-wide and systemic risks, asset classes other than listed equity, focusing on outcomes, and effective engagement.

Part 2 looks at how investors and their agents can work more effectively with others to promote a well-functioning market and address risks of a market-wide and systemic nature. We identify where reporting between Principle 4 is aligned with Principle 10 and where it is distinct. The FRC expects signatories and applicants in 2022 to focus more intently on how they can work with others to promote a well-functioning market and address risks of a market-wide and systemic nature.

Part 3, highlights examples of effective reporting and lists some activities that may be considered when exercising rights and influence in other assets and strategies. We observed some good reporting in asset classes other than listed equity, mainly in fixed income and real estate. However, reporting was often not proportionate to the distribution of assets under management.

The Code places a strong emphasis on outcome reporting in a move away from boilerplate policy disclosures. Part 4 examines the components of effective outcome reporting and highlights the features of outcome reporting on operational procedures and on stewardship that involves external stakeholders.

The final section of the report is a Guide to Effective Engagement Reporting. Although we generally observed better reporting on engagement than some other areas of the Code, there is still room for improvement. It pulls together elements covered earlier in the report to provide a comprehensive Guide to what makes good reporting on engagement. This is an area that is important to readers of stewardship reports. Effective reporting means clearly presenting data from the reporting period, using case studies that clearly set out objectives, methods, rationale and details of an investor's role, contribution and next steps.

<sup>1</sup> FRC, 2019. [UK Stewardship Code 2020, Introduction](#), page 4

<sup>2</sup> FRC, 2021. [UK Stewardship Code Signatories](#)

The Code sets a high bar for stewardship reporting and expected practice that two-thirds of applicants achieved in the first assessment. We commend all applicants which applied to become signatories and recognise the hard work and commitment involved in stewardship and reporting. We hope this report continues to encourage ambitious stewardship practice that serves clients and beneficiaries, leading to sustainable benefits for the economy, environment and society.

To support asset owners and their advisers, we are considering how we might introduce differentiation of reporting for asset managers and service providers in the future. We are engaging with stakeholders to seek input on the timing and approach and will provide an update at the end of Q1.

Early in 2022, the FRC will publish the results of commissioned research that explores what has changed in the landscape of stewardship in the past few years, the drivers for change and the influence the Code has had on these.

# Principles for Asset Owners and Asset Managers

Purpose and governance	
Principle 1 – Purpose, strategy and culture	Signatories' purpose, investment beliefs, strategy, and culture enable stewardship that creates long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.
Principle 2 – Governance, resources and incentives	Signatories' governance, resources and incentives support stewardship.
Principle 3 – Conflicts of interest	Signatories manage conflicts of interest to put the best interests of clients and beneficiaries first.
Principle 4 – Promoting well-functioning markets	Signatories identify and respond to market-wide and systemic risks to promote a well-functioning financial system.
Principle 5 – Review and assurance	Signatories review their policies, assure their processes and assess the effectiveness of their activities.
Investment approach	
Principle 6 – Client and beneficiary needs	Signatories take account of client and beneficiary needs and communicate the activities and outcomes of their stewardship and investment to them.
Principle 7 – Stewardship, investment and ESG integration	Signatories systematically integrate stewardship and investment, including material environmental, social and governance issues, and climate change, to fulfil their responsibilities.
Principle 8 – Monitoring managers and service providers	Signatories monitor and hold to account managers and/or service providers.
Engagement	
Principle 9 – Engagement	Signatories engage with issuers to maintain or enhance the value of assets.
Principle 10 – Collaboration	Signatories, where necessary, participate in collaborative engagement to influence issuers.
Principle 11 – Escalation	Signatories, where necessary, escalate stewardship activities to influence issuers.
Exercising rights and responsibilities	
Principle 12 – Exercising rights and responsibilities	Signatories actively exercise their rights and responsibilities.

# Principles for Service Providers

Principle 1 – Purpose, strategy and culture	Signatories’ purpose, strategy and culture enable them to promote effective stewardship.
Principle 2 – Governance, resources and incentives	Signatories’ governance, workforce, resources and incentives enable them to promote effective stewardship.
Principle 3 – Conflicts of interest	Signatories identify and manage conflicts of interest and put the best interests of clients first.
Principle 4 – Promoting well-functioning markets	Signatories identify and respond to market-wide and systemic risks to promote a well-functioning financial system.
Principle 5 – Supporting clients’ stewardship	Signatories support clients’ integration of stewardship and investment, taking into account, material environmental, social and governance issues, and communicating what activities they have undertaken.
Principle 6 – Review and assurance	Signatories review their policies and assure their processes.

# **Part 1** Expectations of Reporting



# Part 1 Expectations of Reporting

✓	Read the Code and supporting documents
✓	Submit a single report
✓	Respond to all Principles and reporting expectations
✓	Include activities and outcomes from the reporting year
✓	Explain, don't state
✓	Report for all your assets
✓	Include year-on-year updates on progress

Stewardship reports should be a useful communication tool, not simply a regulatory disclosure. How information is reported is an important feature of good reporting, as well as what is reported. Reports should be informative and useful to clients and beneficiaries, as well as the regulator. It is an opportunity for organisations to tell their story and highlight their purpose, as well as explain their stewardship approach and activities undertaken in the previous year, and what those activities have delivered.

Before submitting their reports, applicants should consider the form as well as the content of their submission and use the resources on the [FRC website](#). This section contains key reminders about how to report and details important features of clear and effective reporting.

## Read the Code

Applicants should read the Code in its entirety when developing their stewardship approach and report. Many reports that were unsuccessful failed to address all Principles and reporting expectations relevant to their organisation. The 'How to Report' section of the Code explains how to apply it and what reporting is required.<sup>3</sup>

The Code is a set of 'apply and explain' Principles for asset owners and asset managers, and a separate set of Principles for service providers. These Principles are supported by reporting expectations, which indicate the information that organisations should disclose. Reports should focus on the stewardship activities and outcomes from the reporting year, and not just disclose policies and general approach. The reporting expectations form the basis of the FRC's assessment of reporting quality. Our assessment is based solely on what is contained in the report.

Applicants and signatories should also read the supporting documents on the FRC website, including our [Review of Early Reporting](#), [Application and assessment](#), the application [Terms and Conditions](#) and [FAQs](#). If applicants and signatories have specific questions about how to apply or report that are not answered in these documents, they may contact [stewardshipcode@frc.org.uk](mailto:stewardshipcode@frc.org.uk).

<sup>3</sup> FRC, 2019. [UK Stewardship Code 2020](#), 'How to Report', pages 5–6

## Submit a single report

Stewardship reports must be a single PDF or Word document, structured to give a clear understanding of how the Code has been applied. The FRC will not accept multiple documents. Reports should be engaging, succinct and in plain English: organisations should avoid excessive use of industry jargon in their reports. Reports should be understandable to a wide audience and those without a professional background in investment, stewardship or pensions. Consider the accessibility of your document to users with a disability.

The report should focus on activities and outcomes and provide enough information to the reader, without them having to refer to information elsewhere. This enables a consistent and coherent approach to transparent stewardship reporting. The report may link to more detailed policies and information to give additional relevant evidence. These should first be summarised, and the key features included within the report itself. Check links work and take the reader directly to the web page or document.

The FRC's assessment is based solely on the information and evidence provided in the report and not on a detailed knowledge of an applicant's business or on the content of external documents.

## Format

Applicants can choose their own report structure, as long as the Principles and underlying reporting expectations are reported on. In our 2021 assessment of reporting, we saw a variety of approaches. Some chose to align their existing active ownership or sustainable investment report with the Code. Others chose to report Principle by Principle, dividing the report into separate sections for each Principle and including relevant reporting in each section. We saw effective examples of both approaches.

Whichever approach applicants take, we encourage cross-referencing to other areas of the report where information is relevant to more than one Principle or reporting expectation. It is not necessary to repeat disclosures where there is alignment, but better reporting identifies where relevant information is disclosed. Throughout this report, we give examples where disclosures may be aligned.

## Respond to all Principles and reporting expectations

Reports need to 'apply and explain' all the Principles and respond to the underlying reporting expectations that are relevant to the applicant type. Organisations must determine which reporting expectations are relevant and appropriate to their business or role in the investment community (that is, whether responding as an asset owner, asset manager or service provider).

If an organisation invests directly and indirectly, or invests on behalf of others and provides services, then all reporting expectations relevant to how the organisation operates will apply.

In the few cases where reporting expectations are not applicable, it is better to acknowledge this and explain why it is not relevant, rather than leave it out. For example, the listed equity reporting expectations under Principle 12 (Exercising rights and responsibilities) will not be relevant to a fixed income-only investor. They would need to explain how they have applied the Principle and respond to the fixed income reporting expectations. This is where reporting against Principle 1 (Purpose, strategy and culture), Principle 2 (Governance, resources and incentives) and Principle 6 (Client and beneficiary needs) is important, as it provides context for the range of an organisation's operations and stewardship activities to allow readers (including the FRC) to understand the report.

## Evidence from the reporting period

Policy and process statements that describe an organisation's approach, should be illustrated with examples of how these were applied during the reporting period. Reports should include enough information to address the 'Context' reporting expectations, but policy statements alone are not sufficient.

Activities and outcomes reporting addresses the specifics of what was done and what happened as a result, providing relevant data, examples and case studies. The *Guide to Effective Engagement Reporting* at the end of this report gives more detail and highlights effective examples.

In the rare instance that an organisation justifiably might not have an example to demonstrate a specific aspect of stewardship activity or outcome from the reporting year, this should be explained. This could be communicated with reference to the business model and examples from recent years included, and in future years as they arise.

## Explain the rationale for approach – don't state

Some reporting expectations require applicants to give a rationale for their chosen approaches (for example, Principles 2 and 5). These are important disclosures, as they give organisations the opportunity to explain why a particular approach is better suited to their organisation considering aspects such as their size, type, business model, complexity, etc. It should address the *why* of a process or activity. Boilerplate statements are considered insufficient.

## Indirect investors

For applicants investing indirectly (for example, asset owners, fund of funds managers), the Code requires that they explain the expectations they have set for their external managers in exercising stewardship, as well as how they have monitored them (Principle 8, Monitoring managers and service providers). Indirect investors should clearly explain the actionable criteria they have set for their managers, and how stewardship activities have been undertaken on their behalf.

For example, indirect investors should explain what they have communicated to agents about the ESG issues they expect to be prioritised in investment, engagement or escalation undertaken by external managers on their behalf, as well as their expectations about participating in any collaborative initiatives. Reporting of activities and outcomes undertaken on behalf of the applicant should include case studies from their agents for the reporting period.

## Qualitative and quantitative reporting

Effective reporting makes appropriate use of both qualitative information such as narrative explanations of approach and case studies of activities and outcomes; and quantitative disclosures such as figures and data, for example, the breakdown of assets under management across asset classes and geographies (Principle 6), and the proportion of shares that were voted on in the past year (Principle 12). Using a balance of both qualitative and quantitative information gives insight into how your organisation practises stewardship and allows clients, beneficiaries and the FRC to understand the scope and scale of your organisation's activities.

Relevant data, diagrams and tables should be well presented: they should be clearly titled and correctly labelled, and of appropriate size and resolution to be legible and comprehensive ([see the Brewin Dolphin example in Part 3](#)).

## Adopt a 'fair, balanced and understandable' mindset

Reports should be fair, balanced and understandable; honest and clear about the activities undertaken during the reporting year. For example, levels of participation in initiatives or levels of engagement should not be overstated. Reporting should acknowledge setbacks as well as successes, and identify lessons learned. Activities to achieve desired outcomes may not be completed within the reporting period. Where this is the case, this should be indicated, and progress reported in future years. Part 4 on outcomes and the *Guide* at the end of this report gives more detail on effective reporting on outcomes.

Reporting should reflect all asset classes and geographies invested in and clearly identify any material differences or consistency in approach across these (see Part 3).

Under Principle 5 (Review and assurance, which corresponds to Principle 6 for service providers), reports should explain how an organisation has ensured its reporting is fair, balanced and understandable. This should include, for example, details about which individuals, teams or groups are responsible for ensuring the organisation's stewardship reporting is fair, balanced and understandable, and how this is considered. A statement declaring that reporting is fair, balanced and understandable without further explanation of *how* this is ensured is insufficient.

## Focus on continuous improvement

The Code has a strong focus on continuous improvement. Reports should include reflection on how well an organisation, as well as its policies and processes, is set up to support effective stewardship. Again, the Code strongly encourages applicants to include these reflections year on year, by linking any setbacks experienced to improvements made the following year. Reports should signal, for example, any significant improvements that are underway or planned. Updates on progress should be included in future reporting.

## Review, approval and sign-off

Stewardship reports must be reviewed and approved by an applicant's governing body (board of directors or trustees), and signed by the chair, chief executive or chief investment officer. Applicants are required to confirm in the application form when submitting their report that it has been reviewed and approved. In most 2021 reports, this has also been included in a statement at the front. From 2022, all applicants should describe in their report the process for review and who has approved their report.

In a limited number of cases, for example very large organisations, the board might not be the most appropriate body to review and approve an organisation's stewardship report. In this case, the board may delegate this review and approval to the relevant board-level committee and provide an explanation for the approach. We expect this committee to include an independent non-executive member.

## Publication on website

To remain a signatory to the Code, organisations must submit an annual stewardship report. If they fail to do so, the FRC reserves the right to remove their signatory status. Signatories must make their report available on their website once their application is successful. Applicants may do so before their application has been accepted and the result published, as long as they do not refer to themselves as a signatory. Signatories may use the UK Stewardship Code logo to demonstrate signatory status.

FCA-regulated asset management firms covered by the FCA Conduct of Business Sourcebook (COBS) Rule 2.2.3 are required to disclose the nature of their commitment to the Code, or where they do not commit to the Code, their alternative investment strategy. FCA-regulated asset management firms may also include their SRD II disclosures in their stewardship report.

Pension funds may wish to include disclosures prepared for their Statement of Investment Principles and Implementation Statements for parts of their stewardship reports.

## How the FRC evaluates applications

The FRC's assessment is based on the quality of reporting against the Principles and reporting expectations. We review reports to assess if applicants have provided sufficient disclosure for us to understand their application of the Principles during the reporting period.

The Code provides a framework for a wide range of organisations, including those of different size, type, business model and investment approach. The FRC considers these factors to ensure organisations are assessed in a fair and consistent manner, and in broad comparison with their peers. In 2021, these considerations included, but were not limited to:

- The size of the organisation by assets under management (AUM) for asset managers and asset owners.
- The category of organisation – asset owner, asset manager and service provider.
- The type of organisation – by asset classes invested in, client base or business model.
- If an organisation applying was a subsidiary or business unit of a larger or global organisation.

We broadly grouped asset manager and asset owner applicants into the categories in the table. For example, we expected the most numbers of examples and case studies from large asset managers, and the fewest from small asset owners. These were used only as a guide rather than a rule, as the quality of the case studies was central.

Some of the types we considered were fund of funds, wealth managers, delegated managers, index-linked asset managers, active equity managers, multi-asset managers, local government pension schemes, corporate pension schemes, insurers, data providers and investment consultants.

Signatory Category	AUM Range
Large asset manager	<ul style="list-style-type: none"> <li>• AUM of more than £250 billion (bn); or</li> <li>• Global investor managing more than £100 million from its UK subsidiary</li> </ul>
Medium asset manager	<ul style="list-style-type: none"> <li>• AUM between £50bn and £250bn</li> </ul>
Small asset manager	<ul style="list-style-type: none"> <li>• AUM under £50bn</li> </ul>
Large asset owner	<ul style="list-style-type: none"> <li>• AUM of more than £15bn</li> </ul>
Medium asset owner	<ul style="list-style-type: none"> <li>• AUM between £5bn and £15bn</li> </ul>
Small asset owner	<ul style="list-style-type: none"> <li>• AUM under £5bn</li> </ul>

All reports are assessed against the Code and must apply all the Principles and reporting expectations. Nonetheless, these factors will inform how the application of the Code may differ depending on size, type, business model or strategy.

Reports are first read in full and analysed. Assessments are then reviewed and discussed to ensure these are fair and proportionate. To ensure fairness and consistency, a sample of reports reflecting a range of applicants is reviewed by our panel of independent advisers with expertise in stewardship and investment. The final decisions and signatory list are made by the FRC.

In October, the Government Internal Audit Agency (GIAA) reviewed the Stewardship Team's assessment process. Once the GIAA has reported to us, we will identify improvements that can be made before the first assessments in 2022.



## **Part 2** Market-wide and Systemic Risks and Collaboration

## Part 2 Market-wide and Systemic Risks and Collaboration

### Key messages

- Investors have the important duty of looking after the capital of pensioners and savers. With this responsibility comes the task of working with others to promote a well-functioning financial market, and address risks of a market-wide and systemic nature.
- Investors should identify and explain the market-wide and systemic risks they have responded to during the reporting period. These risks should be widely considered in the context of their stewardship role, not only in relation to the organisation or portfolios.
- Reports should explain their organisation's role, contribution and an assessment of their effectiveness when working with other stakeholders and participating in relevant industry initiatives.
- Some reporting under Principles 4 and 10 may be linked, where investors engage together to influence issuers about a risk of market-wide and systemic nature. Reports should make use of effective cross-referencing in these activities.
- Investors should reflect on the effectiveness of their actions across all aspects of Principle 4. Disclosure for this reporting expectation requires improvement and we expect all reports in 2022 to address this.

### Responsibility and opportunity

The Code expects asset owners, asset managers, and the service providers that support them to play an important role in responding to market-wide and systemic risks, as well as responsibly allocating, managing and overseeing the capital held in their portfolios. Investors in the UK are entrusted to look after more than £6.1 trillion in private pensions, and with that comes the responsibility and opportunity to work with others to improve how markets function and anticipate significant risks to the markets and systems in which they operate.<sup>4</sup>

Through their investment analysis and research, investors have access to information and expertise on risks. Both should be used to improve outcomes for their clients and beneficiaries, as well as develop sustainable benefits for the economy, environment and society. Market participants should work with other stakeholders or participate in relevant initiatives to address market-wide and systemic risks and promote well-functioning financial markets.

<sup>4</sup> Office for National Statistics, 2019. Total private pension wealth in Great Britain was £6.1tn in April 2016 to March 2018 (42% of total wealth), up from £3.6tn (34% of total wealth) in July 2006 to June 2008, after adjusting for inflation

## Reporting on market-wide and systemic risks

### Features of effective reporting for Principle 4 (Promoting well-functioning markets)

	List and explain the market-wide and systemic risks identified in the reporting period
	Explain the governance processes for risk
	Describe how you have worked with others to improve how markets function
	Explain involvement in relevant industry initiatives to address risks
	Explain how investments have been aligned to the risks identified
	Reflect on effectiveness

Market-wide and systemic risks are non-diversifiable and therefore have an important impact on returns.<sup>5</sup> By addressing market-wide and systemic risks and opportunities, investors can simultaneously improve the stability of portfolio investments and broader market systems.<sup>6</sup> In fact, some argue that addressing these risks may have more impact on returns than risks associated with an individual organisation or security.<sup>7</sup> Because investors seek to maximise risk-adjusted returns, it will serve their interests to support and advance initiatives that aim to reduce market-wide and systemic risks, particularly for those whose investment horizons are long-term in nature.

Beneficiaries are also increasingly urging investors to use their pensions to drive sustainable practices across the economy. In fact, 68% of UK savers want their investments to consider people and the planet alongside profit.<sup>8</sup> Some reports highlighted this increasing demand for stewardship from beneficiaries and clients in their disclosures against Principle 6.

When reporting under Principle 4, the determining factor should be whether the issue presents a risk to the market or system. The International Corporate Governance Network identified in 2019 some of the most significant systemic threats facing the stability of the financial market:

- Macroeconomic risk, including market and credit risk and changes to political, legal, regulatory and fiscal instruments;
- Environmental risk, including climate change, water scarcity and pollution;
- Social risk, including human rights, income inequality and populism;
- Governance risk, including corruption, expropriation of control and corporate culture; and
- Technological risks, including artificial intelligence and cyber security.<sup>9</sup>

<sup>5</sup> Jeffrey N Gordon, 2021. [Systematic Stewardship](#). Columbia Law and Economics Working Paper No. 640, European Corporate Governance Institute – Law Working Paper No. 566/2021

<sup>6</sup> ICGN, 2019. ICGN Viewpoint: [Investor Framework for Addressing Systemic Risks](#)

<sup>7</sup> Jon Lukomnik and James P Hawley, 2021. [Moving Beyond Modern Portfolio Theory](#)

<sup>8</sup> HM Government, 2019. [Investing in a better world: Understanding the UK public's demand for opportunities to invest in the Sustainable Development Goals](#)

<sup>9</sup> ICGN, 2019. See note 6

Reports should clearly explain the process that applicants follow at an organisational level to monitor the macroeconomic environment, as well as identify market-wide and systemic risks and prioritise responses. For example, this could include the role of a relevant groups or committees, how risks are discussed by trustee boards, or a process for escalating risks from portfolio manager level to senior management.

**Mercer Limited, page 20**



*Investment consultant*

Mercer Limited’s report lists the market-wide and systemic risks identified by their organisation, in the context of the wider economy rather than its own business. Climate change and water security are two risks identified which could also fall under Principle 7 as ESG issues of importance to the organisation when integrating investment and stewardship.

Mercer benefits from thought leadership and wider work across our global firm as well as from our parent company Marsh McLennan on other systemic risks. For example, over 2020 the World Economic Forum, in collaboration with Mercer, published the report ‘Transformational Investment: Converting Global Systemic Risks into Sustainable Returns’. This seeks to address some of the long-term, global systemic risks facing our economy, society and the planet through an investment lens.

**Hermes Fund Managers Limited, page 23**



*Asset manager*

The report provides a comprehensive explanation of the processes that they follow at the organisational level to identify, monitor and prioritise market-wide and systemic risks.

**Identifying risks:**

The Investment Office is responsible for the daily oversight of market risk across the international business of Federated Hermes, as well as the oversight of the underlying portfolio managers’ adherence to their pre-defined/client-agreed investment processes. The Investment Office’s main remit is to act as an independent investment risk consultant on behalf of our clients. While the Investment Office can challenge our portfolio managers’ decisions, positioning and risk exposures, it cannot force change. What the Investment Office can do, if the issue is sufficiently serious enough, is to escalate the matter to the Portfolio Review Committee (PRC). The PRC would then meet with the portfolio manager, consider the issue and then, along with the Investment Office and the portfolio manager, agree a resolution. If no resolution can be agreed, the matter can be escalated to the ExCo, which has the authority to force change and agree client communications. The members of our Investment Office take the time to understand individual fund managers’ styles so that they can aid and enhance their process.

(...)

We may also identify market failures or barriers to responsible investment and stewardship through our investment and engagement activities. Where this is the case, we will identify the relevant policymakers to engage with on the topic.

Investors should also explain how their investments are aligned with their identified market-wide and systemic risks. This was generally done well by signatories and there was good cross-referencing. Disclosure for this reporting expectation may be linked with Principles 7 (Stewardship, investment and ESG integration) and 9–12.

Principle 7 of the Code requires signatories to explain how they have integrated stewardship and investment, including material ESG issues, to fulfil their responsibilities. Where ESG issues identified under Principle 7 are of market-wide and systemic nature, these may also be relevant for Principle 4. Better reporting cross-references ESG issues relevant for both Principles 4 and 7 and included climate change, the COVID-19 pandemic, tailings dam disasters, antimicrobial resistance and biodiversity risk. A stewardship issue identified under Principles 9-12 might also represent a risk to the market or system. Where this is the case, individual or collaborative engagements on such issues would be relevant to Principle 4.

Frameworks may be useful for investors to consider systemic issues. Some signatories referred to the UN Sustainable Development Goals (SDGs), explaining how investment decision-making, engagement and/or the exercise of rights was aligned to the delivery of these.<sup>10</sup>

Our Review of Early Reporting highlighted the FRC's expectation that reports in 2021 address climate risk and the risks presented by the COVID-19 pandemic.<sup>11</sup> In our 2021 assessment, we saw many asset managers reporting on the pandemic and climate in the context of their business operations. For example, some reports chose to explain how their organisation responded to COVID-19 by ensuring a swift transition to remote working and providing employees with increased mental health support. While this may be interesting disclosure for clients and beneficiaries, it is not required here and the Code is focused on the interests of the clients and beneficiaries.

### Wellington Management Company LLP (Wellington), pages 7–8, page 10



#### *Asset manager*

Wellington's report explains how they have actively aligned their investments to address climate-related risks. This example is also relevant under Principle 7, as climate change is considered an ESG issue of importance; as well as a market-wide and systemic risk. Their report explains the organisation's sustainable investment strategies and how these work towards climate-related objectives: for example, through a global equity portfolio designed to help address carbon and sustainability by focusing on climate change mitigation.

Wellington also details their role in the Net Zero Asset Managers Initiative, which supports the goal of net zero greenhouse gas emissions by 2050, on page 10. This is a strong example of reporting on participation in a relevant initiative under Principle 4.

<sup>10</sup> United Nations Department of Economic and Social Affairs, 2015. [Sustainable Development Goals \(SDGs\)](#)

<sup>11</sup> FRC, 2020. [Review of Early Reporting](#), page 21

## Initiatives and working with others

Applicants should explain how they have worked with others to address market-wide and systemic risks and improve the way the market operates. This could include participation in regulatory workshops, responses to government consultations, or contribution to research.

Applicants should also explain the role that they have played in any relevant industry initiatives in which they have participated and the extent of their contribution. These should be described, and not simply listed (see Wellington example). It may be entirely appropriate for an organisation to be a signatory rather than play a more active role. For example, a small asset owner or manager might not have the resources to meaningfully respond to all the risks and issues it identifies.

Applicants should consider which risks they prioritise and why. It may be more effective for market participants to make active and significant contributions to a smaller number of initiatives, rather than be a signatory to a multitude. Reporting that is fair, balanced and understandable is transparent about the nature and extent of the role played in initiatives. Asset owners that do not participate themselves should explain the expectations they set for their agents, and how they have held them to account.

### Aviva Investors, page 44

*Asset manager*



Aviva Investors highlights how they have worked with policymakers to address biodiversity risks. They clearly explain their contribution to the Dasgupta review, by putting forward their biodiversity policy mechanisms 'to help bring natural capital externalities onto corporate balance sheets'.<sup>12</sup> This included (1) reforming the planning system through Environmental Impact Assessments; (2) democratising the financial system to enable end investors to have a say on their investments' impact on biodiversity; and (3) mapping pathways to avoid systemic destruction.

<sup>12</sup> Dasgupta, P, 2021. The Economics of Biodiversity: [The Dasgupta Review](#). (London: HM Treasury)



## Linking collaborative initiatives between Principle 4 and 10

Principle 10 of the Code states that signatories, where necessary, should participate in collaborative engagement to **influence issuers**. Where collaborative engagement to influence an issuer is undertaken to address an objective of market-wide and systemic importance, the disclosure may be relevant for both Principles 4 and 10.

### Church Commissioners for England, page 21

Asset owner



Church Commissioners for England illustrates good disclosure on collaborative engagement to influence mining companies to make disclosures on their tailings dams (Principle 10, to influence issuers) and on their contribution to a global standard on tailings dam management (Principle 4, addressing the systemic risk of a failing of a group of businesses and their role in an industry initiative).

The report explains how they aimed to influence individual mining companies and the industry to protect capital invested, while also addressing a significant social and environmental risk on a global scale.

Continues opposite

### Tailings dams – using our voice to address a systemic risk

Tailings dams represent a threat to the environment if not managed properly. There have been a number of very serious failures, most recently the Brumadinho dam disaster in Brazil in January 2019. This led to the loss of over 245 lives and 25 missing people (as of May 2019). To mark the anniversary of the disaster, in January 2020, we took part in an investor initiative led by the Church of England Pensions Board and the Swedish Council on Ethics to raise standards of tailings dam management and disclosure, including joining a collaborative investor initiative urgently calling for public disclosure by listed extractives companies of tailings facilities and risks.

During the first half of the year, we also engaged with four companies that did not respond to investors' requests, resulting in a disclosure from Exxon. We also contributed to the Global Industry Standard on Tailings Management, endorsed by the Global Tailings Review, United Nations Environment Programme (UNEP), Principles for Responsible Investment (PRI) and International Council on Mining and Metals.

Reports should clearly explain the issue, the collaborative initiative and the organisation's role and contribution (see the *Guide to Effective Engagement Reporting*). It can include a wide range of activities, methods and forums where investors work with each other and other stakeholders to achieve change. This change may be at an industry-level, targeting a group of companies on a thematic stewardship issue, or engaging with a single issuer with a specific objective.

Effective cross-referencing is strongly encouraged. Better reporting highlights disclosures that may be relevant to more than one Principle of the Code. In the reports we reviewed, we observed that applicants sometimes failed to identify opportunities for connection between the requirements for Principles 4 and 10. In other reports, where applicants did identify a link between disclosures, some repeated the disclosure. This is not necessary. In our assessment, the FRC recognises disclosures, irrespective of where they are included in the report, if they meet the reporting expectations.

### RPMI Railpen (Railpen), page 52

Asset owner



This report provides an effective case study on collaborative engagement and evidence of participation in a relevant industry initiative Climate Action 100+ to tackle climate change. The issue at stake, Railpen's role and contribution, and the outcome of the engagement are covered.

#### Case study: Tackling Market-Wide Risk: Climate Engagement and Climate Action 100+

##### Issue:

Environmental impacts such as rising sea levels, ocean acidification, extreme weather and droughts are already evident across the globe and the IPCC report recommends limiting global temperature rises to 1.5 degrees Celsius to avoid the worst impacts.

(...)

Initiative and Role: Climate Action 100+ is an investor-led, engagement initiative where investors commit to engaging with at least one of 167 focus companies that are strategically important to the net zero emissions transition and to seek commitments on the initiative's key asks:

- Implement a strong governance framework on climate change
- Take action to reduce greenhouse gas emissions across the value chain
- Provide enhanced corporate disclosure.

Railpen joined the initiative in 2017 and began engaging with CRH as the lead investors. Subsequently we led and participated in a number of engagement letters and calls with company management and investor relations.

##### Outcome and next steps:

CRH has since:

- Become a public supporter of the Taskforce on Climate Related Financial Disclosures
- Set an ambition to achieve carbon neutrality along the cement and concrete value chain by 2050
- Set further targets on CO<sub>2</sub> intensity reduction of their cement by 2030
- Committed to disclosing its approach to climate lobbying and a 'map' of its direct and indirect lobbying activities in 2021

The coalition continues to engage with the company.

Aside from our activity on CRH, Railpen remains a leading participant in engagements with Nestlé and LafargeHolcim. In 2021, Railpen has become an active participant in the CA100+ and IIGCC work on Paris-aligned Accounts. (...)

## Reflection on effectiveness

Finally, the Code requires applicants to disclose an assessment of their effectiveness in identifying and responding to market-wide and systemic risks to promote well-functioning markets. This was one of the weaker disclosures in the reports assessed in 2021, and most reports did not refer to it at all. A few reports included a general boilerplate statement of effectiveness; however, this is not sufficient to satisfy the reporting expectation.

Investors and service providers should consider and reflect on the effectiveness of their internal processes in identifying risks, as well as their impact on the overall market in responding to these. As evidence of their effectiveness, organisations may choose to refer, for example, to the successes or limitations of the initiatives they supported and whether they effectively identified any market-wide risks that materialised during the reporting period. For more detail on the features of effective reporting on outcomes, please refer to Part 4.

The FRC acknowledges that responses to risks may not always be successful and may be difficult to measure. Better reporting highlights these efforts and outcomes where possible, and considers how an organisation might change its approach in the future.

## Questions for reflection

Has the organisation:

?	reported effectively on the market-wide and systemic risks that materialised in the reporting period?
?	reduced exposure to the risk identified?
?	increased resilience to these risks?
?	reduced risk in the issuers?
?	reflected on its effectiveness in promoting well-functioning markets as a result?

**Environment Agency Pension Fund (EAPF), page 52**



*Asset owner*

The report provides a statement of EAPF’s effectiveness, highlighting how their actions have increased climate reporting and transparency. The report is honest about where there remains scope for improvement, which is encouraged by the Code.

**How do we know that we are influencing wider change across the finance sector?**

In conjunction with all the other investors and asset managers we work with, we are all bringing pressure to bear to make a change. It is hard to point to some of the above initiatives and be specific about the change it made directly. What we can say is that change is occurring and undoubtedly, the pressure on companies, investors and policymakers to take into account environmental, social and governance issues has increased significantly over the last year. Some of the initiatives do have tangible outcomes.

As a direct result of our actions, 3 more companies are now reporting on their environmental impact to CDP and 11 other companies have made commitments to decarbonise.

(...)

And finally, that Net Zero Initiative that we sponsored, well it produced a very well respected framework and by the end of 2020 we were putting it into practice to work out our own net zero target. More on that in next year’s report.

**Cardano Risk Management Limited (CRML), pages 13-14**



*Service provider and asset manager*

CRML provides a statement of effectiveness of their response to the COVID-19 pandemic. They note that, while they didn’t predict the total impact of the outbreak, they were well prepared thanks to their portfolio construction, technological infrastructure, scenario thinking, and risk management approach. They support this assessment with evidence of their above-average fund performance.

## **Part 3** Reporting on Asset Classes other than Listed Equity

## Part 3 Reporting on Asset Classes other than Listed Equity

### Key messages





- Reports should provide a clear breakdown of the organisation's assets under management (AUM) across asset classes.
- Reports should provide evidence for the organisation's approach across the different asset classes in which they invest such as fixed income, real estate, infrastructure and private equity.
- Better reports clearly demonstrate the organisation's approach across asset classes, in a way that is representative of the distribution of assets, provide evidence for activities and outcomes, and explain the approach across all relevant Principles of the Code, in particular integration, engagement, escalation and exercising rights and responsibilities.

The Code applies to all capital invested. Applicants should exercise stewardship across all the asset classes and geographies in which they invest, using the resources, rights and influence available to them and report accordingly.

Reporting on asset classes other than listed equity was mixed across the first set of applicants to the Code in 2021. A minority of reports provided detailed reporting, while others covered non-listed equity asset classes less extensively. There was some strong reporting on fixed income in both sovereign and corporate debt, while reporting on asset classes such as real estate, infrastructure and private equity remained less developed by comparison.

We recognise that many organisations are still developing their stewardship practice in asset classes other than listed equity. Applicants should be transparent about their current approach and identify where it differs across asset classes (see 'Adopt a fair, balanced and understandable mindset' in Part 1). They should identify any limitations or barriers to their current practice and explain what they are doing to address these in the future. We expect organisations continue to develop their practices and reporting in 2022 and beyond.

### Features of effective reporting across asset classes

	Disclose all AUM by asset class
	Explain how your approach differs by asset classes
	Examples should reflect the proportion of your AUM in each asset class
	Consider opportunities to exercise rights and influence beyond voting



## Asset class disclosure

Under Principle 6 of the Code, signatories should disclose their client base, - for example, institutional versus retail and geographic distribution, - and AUM across asset classes and geographies. This disclosure is important context for the reader to understand how representative stewardship activity is of AUM and determine if reporting is fair and balanced. For example, if an organisation is invested in both listed equity and fixed income, under Principle 7 and Principles 9–12, they ideally should include case studies from these asset classes, proportionate to their investments.

Most reports provided information about AUM. However, not all reports provided sufficient detail to understand how assets were distributed geographically, either providing no information on the geographic spread of investments, or insufficient breakdown of markets; for example, using very broad terms such as ‘rest of world’, ‘global’ or ‘emerging markets’ for large proportions of investments.

Better reporting used diagrams to present AUM disclosure. However, at times, tables and diagrams were incorrectly labelled or were unclear. Reports should be clear and understandable. Diagrams should be clearly titled and labelled, and should be legible. The terminology for categories should be consistent with that used elsewhere in the report. Organisations should report across their whole AUM in the first instance before any additional disclosures such as the proportion of assets in sustainable or ESG funds.

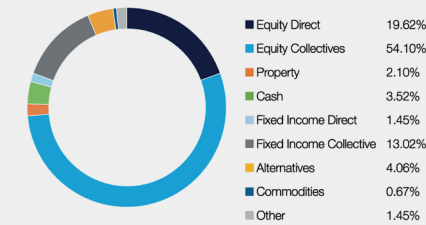
### Brewin Dolphin, page 9

Asset manager

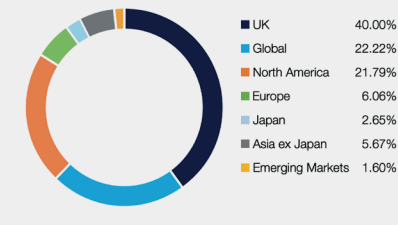


Brewin Dolphin makes use of clear and legible pie charts to disclose their AUM across asset classes and geographies under Principle 6. The charts are well labelled and enable the reader to quickly understand the scope and coverage of the organisation’s investment activities.

Asset class breakdown\*\*



Geographical breakdown\*\*



\* by value of client assets as at 31 December 2020 \*\* as at 31/12/2020

## Approach to integration

The Code expects signatories to explain how the integration of stewardship and investment has differed for funds, asset classes and geographies. Better reporting provides a clear explanation of the organisation’s approach and provides a rationale where differences exist. Signatories should report in a way that reflects their role as an asset manager or asset owner. For example, asset managers should focus on how their approach to integration has differed across asset classes, while asset owners that invest indirectly could explain how they have considered integration in tenders and mandates, across all asset classes.

There were some good examples of approaches to integration in other asset classes, but in general reporting was less developed than for listed equity. Better reporting provided a comparison of approaches across asset classes and explanations of the approaches taken in individual asset classes, with illustrative case studies.

Some reports explained common features of integration that would be applicable across many asset classes. For example, communication between different asset class teams when making investment decisions on mutual holdings such as credit and equity analysts, or drawing on wider stewardship or ESG expertise from centralised teams. Other signatories explained they take a wholly integrated approach, with analysts and portfolio managers integrating ESG and stewardship as a standardised process.

In comparison, other reports explained how integration differs across asset classes by identifying tools or approaches specific to individual asset classes. For example, some explained the development of ESG scoring methodologies or frameworks that are used in the investment decision-making process. Others explained how specific processes for asset classes differ because of the nature of investment. For instance, some real estate and infrastructure investors explained the use of external consultants during the due diligence phase of ownership.

Better reporting emphasised how stewardship and investment, including material environment, social and governance issues, are systematically integrated and reflected in the investment decision-making process, and provided examples to demonstrate how this approach is applied in practice.

Fidelity International, page 44



Asset manager

The report explains how they integrate stewardship and investment in real estate assets, using a diagram to identify relevant issues at different stages of the investment process.

Sustainability principles are applied to each stage of our real estate investment: acquisition, development and refurbishment, and ongoing asset management. The graphic below shows the steps we may take at each stage of the process.

Sustainability throughout the life cycle of property ownership

Acquisition		Development & Refurbishment		Ongoing Asset Management	
Detailed due diligence	Identify and engage key local stakeholders	Establish a BREEAM rating	Post occupancy evaluation	Agree and monitor sustainability strategy per asset	Engage tenants to promote sustainability
Consider sustainability risks for all assets	Fidelity exclusions list	Incorporate sustainability in design and refurbishment	Establish a best practice EPC target	Assess technical installations to improve sustainability performance	Measure monitor and manage risks
Sustainability improved plan formed	Engage with external sustainability consultancy	Integrate sustainable transport features	Consider and implement wellness improvements	Encourage biodiversity control and improve plans	Obtain asset level green building certification (e.g. BREEAM)

Practical examples:

Acquisition	Development	Ongoing Management
Industrial, Netherlands	Industrial, Germany	Office, UK
Assessment	Prime warehouse development completed in 2017	£1m Maintenance and improvement project
Energy Levels (A/B)	DGNB Gold building certification	Electric vehicle charging points
BREEAM pre-assessment 'Good'	High efficacy gas fired radiators and insulation	PIR and daylight sensors
Next steps and targets	Biodiversity protection and rain irrigation	Showers, lockers and drying room
Tenant engagement	Café opened up to community use	'Platinum Standard' cycling accredited building
Technical		
'Very good' rating		

**LaSalle Investment Management (LaSalle), pages 24-27**

*Asset manager*



The report explains how they integrate stewardship and ESG factors in direct real estate investments, using a diagram to identify relevant issues at different stages of the investment process. LaSalle also explains on pages 25–27 how the integration of ESG factors differs across different asset classes including real estate debt and indirect investments.



**Jupiter Fund Management plc (Jupiter), pages 30-31**

*Asset manager*



The report summarises how the integration of stewardship and investment differs across asset classes and provides a reporting period-specific example in systematic equities. The report also provides reporting period specific examples across different asset classes, see example in the link above.

INTEGRATION ACROSS ASSET CLASSES BEYOND LISTED EQUITY	
ASSET CLASS	ESG PROCESS AND STEWARDSHIP TRANSMISSION MECHANISMS
UK Equities	<ul style="list-style-type: none"> <li>– Long-standing engagement programme with both management and independent non-executive directors.</li> <li>– We uphold UK corporate governance and ESG best practice via voting, engagement and collaborative activity.</li> </ul>
Global Equities	<ul style="list-style-type: none"> <li>– We engage with management and non-executive directors (where this is available to us).</li> <li>– Our emphasis is on protecting minority investor interests and board independence in markets where a controlling shareholder is a prevalent governance feature.</li> <li>– We push for better disclosure and governance of ESG matters in all markets.</li> </ul>
Corporate Fixed Income	<ul style="list-style-type: none"> <li>– ESG systematically integrated into credit analysis.</li> <li>– We routinely engage with management both prior to and once invested.</li> <li>– We utilise voting rights in limited circumstances where available.</li> <li>– We push for market-wide improvement in ESG standards, particularly issuer openness to bondholder engagement and disclosure.</li> </ul>
Sovereign Fixed Income	<ul style="list-style-type: none"> <li>– We consider governance and social factors such as a country's political stability and cohesion and the credibility of its political and monetary institutions.</li> <li>– Environmental factors assessed include vulnerability to physical climate risks and reliance on fossil fuel production and revenues.</li> <li>– We conduct research trips to engage with government departments, policy makers, NGOs and multilateral institutions to understand these risks.</li> </ul>
Fund of Funds	<ul style="list-style-type: none"> <li>– We monitor underlying fund managers, including manager interviews typically twice a year.</li> <li>– We review portfolio holdings, voting records and details of effective engagement with investee companies.</li> <li>– We require underlying managers to articulate the evolution of sustainability and governance within their own investment process, and evidence their engagement strategy, with a focus on demonstrating outcomes.</li> <li>– Findings are collected within our proprietary ESG matrix. Each manager receives a score based on our assessment of their stewardship approach.</li> </ul>
Systematic Equities	<ul style="list-style-type: none"> <li>– We use ESG data as a potential source of alpha through the incorporation of an ESG factor within the investment model.</li> <li>– Our systematic approach allows us to use highly granular ESG data and its evolution over time.</li> <li>– Our approach benefits from Jupiter's company-wide commitment to ESG.</li> </ul>
Private Markets	<ul style="list-style-type: none"> <li>– The Chrysalis Investments ESG policy outlines principles and commitments during the four stages of investment: i) deal origination, ii) investment decision, iii) ownership, and iv) exit. Given investment in late-stage tech enabled companies, ESG monitoring is centred on governance, human capital, cyber and data security and business ethics.</li> </ul>
Gold & Silver	<ul style="list-style-type: none"> <li>– The Responsible Investment Charter sets portfolio standards around the UN Global Compact, good governance, environmental impact and shareholder relations.</li> </ul>

## Engagement

The Code asks signatories to explain how engagement has differed for funds, assets or geographies. This is important because there are different opportunities to engage in different asset classes. For example, fixed income investors may have different levels of access to management, being more likely to engage the CFO or treasurer in comparison with equity holders who are more likely to have access to the chair or senior independent director of a company. Investors may also be able to combine engagement across asset classes to maximise influence and access with investee companies. For example, investors with equity and debt in an issuer can engage with an issuer across these, where objectives across asset classes align.

In real estate and infrastructure, signatories explained the different opportunities for engagement depending on the way they invest. The form of engagement may differ depending on whether the investor has direct control of the investment or board representation, which in turn influences the opportunities to engage, the escalation strategies adopted and the overall exercising of rights and responsibilities. We saw some good examples of investors describing their engagement with tenants and the communities to maintain or enhance the value of assets. Energy efficiency was a commonly featured engagement topic for real estate assets. Overall, reporting on engagement in real estate and infrastructure requires significant improvement.

There were also some good explanations of how organisations approach engagement in fixed income. Many reports identified the key differences or limitations when engaging with corporate issuers and sovereign issuers. Better reporting supplemented these explanations with case studies that clearly articulated the outcome of engagement with fixed income issuers.

### Royal London Asset Management (RLAM), page 32



#### *Asset manager*

RLAM's report explains how their rights in fixed income assets differ in comparison to equity holders, why they view engagement with fixed income issuers as beneficial for all stakeholders and how they engage using both their debt and equity holdings where possible. Their report also explains how they prioritise engagement by focusing on the sectors and issuers with the most significant material ESG impact/risk.

### UBS Asset Management (UK) Ltd (UBS), pages 65, 67, 68



#### *Asset manager*

UBS's report explains their approach to engagement in real estate and infrastructure, and uses case studies to evidence their approach. The case study on page 67 of their report focuses on UBS's direct real estate portfolio and explains their engagement with a property manager with the aim of assessing the social value of their property, and expanding this process to other properties. On page 68 of their report, UBS uses a case study to demonstrate engagement with a third-party real estate fund manager following concerns over the fund manager's performance in the GRESB survey results. This example also explains how UBS used their rights and influence to improve the fund manager's GRESB scores.

## Collaborative engagement

Under Principle 10, organisations should consider how they can collaborate to influence issuers. Better reports identified relevant initiatives that investors in other asset classes participate in. Some organisations explained that they do not currently engage collaboratively in asset classes other than listed equity but good reporting acknowledges where there are limitations and explains how they intend to improve.

The BlueBay case study below is also an example of how collaborative engagement can be used in fixed income as an escalation tool.

## Escalation

Principle 11 (Escalation) expects signatories to explain how escalation has differed for funds, assets or geographies. This is important because different asset classes will have different rights and influence. For example, in most circumstances bondholders cannot use voting as an escalation strategy with a company in the same way equity holders can. In real estate and infrastructure assets, investor rights and escalation strategies will differ because of the type of investment. Investors may own and operate real estate and infrastructure assets where the emphasis of escalation is with users of the assets, for example, tenants in real estate buildings. Other investors may use external managers that manage investments in these assets on their behalf or invest through a specialist fund manager to gain exposure to assets such as real estate and infrastructure. In both cases, escalation would be aimed at the expectations they have set for asset managers that escalate stewardship activities on their behalf.

Reporting on escalation was weaker in comparison with other Principles, with fewer effective examples of escalation in other asset classes. Reports should explain how they selected and prioritised issues and developed well-informed objectives for escalation. This included the factors they considered most important in deciding to escalate and in choosing their escalation approach. Reports should also better explain the expectations they have set for those that escalate stewardship activities on their behalf. This reporting expectation is particularly relevant to asset owners or asset managers that invest through a service provider such as an external real estate fund manager. Finally, signatories should fully describe the outcomes of escalation undertaken directly or by others on their behalf.



**BlueBay Asset Management LLP (BlueBay), page 40***Asset manager*

The report explains the challenges of escalating issues with fixed income issuers, the methods or strategies they use to escalate concerns and a case study that demonstrates their overall approach to escalation. This case study is also an example of collaboration through Climate Action 100+ and explains BlueBay's role, contribution and overall outcome.

**Sector:** Oil and gas**Region:** Emerging markets**Aim:** Influence for improved practices across climate, health and safety and broader ESG practices and disclosure.**Engagement overview:**

In March 2020, BlueBay joined Climate Action 100+ (CA100+), agreeing to co-lead on engagement with a Mexican state-owned oil and gas company through this initiative. This followed our own bi-lateral engagement with the company in 2020, where we had a call with management to discuss how the company was addressing some of key ESG risks. We focused on its approach to corporate responsibility more broadly, sustaining improved health and safety performance, improving transparency and disclosure of ESG metrics and climate change. In July 2020, the co-leads of the initiative on the company engagement wrote to the board of the company to provide it with formal notice of their inclusion in the CA100+. The letter also advised that, alongside the co-lead investors, several supporting investors were keen to ensure a more progressive approach to climate change from the company. The company responded to this letter, stating it was reviewing the best way to respond and engage with investors.

**Status and outcome:**

Ongoing - we will continue to check in with the company to get an update on next steps. From an investment perspective, we feel that ESG issues create a much higher hurdle to owning the company. That said, we believe valuations are currently compelling relative to the sovereign, so we are holding the company as a core position in several funds. However, this gives us an increased ability to engage with management (as we are a financial stakeholder), a position we are using wherever possible to help influence the company on ESG improvements.

**Exercising rights and responsibilities**

The Code sets expectations that organisations explain how they exercise their rights and responsibilities, and how their approach has differed for funds, assets or geographies. The Code has specific reporting expectations for listed equity and fixed income assets. Investors in all asset classes should apply the Principle and explain how they have exercised their rights and responsibilities across other asset classes they are invested in.

There were some good explanations of how signatories had exercised their rights and responsibilities in fixed income assets. Reporting on how rights were exercised, and responsibilities used in asset classes outside of listed equity such as real estate, infrastructure, private equity and derivatives, needs improvement. Better reporting clearly stated the different rights and opportunities for influence that investors have and used case studies to illustrate.

RBC Global Asset Management (RBC GAM), page 38

Asset manager



RBC GAM's report explains their approach to exercising rights and responsibilities across fixed income assets while also explaining the actions they have taken during the reporting period and how frequently they have exercised their rights.

Seeking amendments to terms and conditions in indentures or contracts: During the new issue stage, our investment teams may have opportunities to seek inclusion of certain terms and conditions. For example, in 2020, there were instances where we sought the inclusion of a "tax par call" feature that would be triggered by a tax event at a particular issuer. There was also another private placement where we asked for a change in the "Additional Indebtedness Test" to be a maintenance covenant rather than one that is only contemplated prior the entity issuing additional debt.

During the holding period stage, circumstances may arise where we respond to proposals from issuers to amend terms. For example, in 2020, we responded to specific issuers' requests to allow temporary relief on certain covenants that could trigger an event of default as a result of COVID-related disruptions to business activities.

(...)

Impairment rights:

Most of our work in impairment rights takes place during the due diligence stage. Our approach is to analyse scenarios around event of default, cures, and associated step in rights. For example, in 2020, one of our investment teams reviewed event of default and step in rights for a particular hospital P3 project, where the project company faced ongoing challenges in hitting milestones. This was a situation that could have led to default if failures were not addressed.

Reviewing prospectus and transaction documents:

This takes place before our investment teams invest in any deal. Teams review prospectus documents in great detail to understand covenants, terms, structure and risk. The approach taken varies depending on the complexity of the structure and bond offering. For example, analysis of one particularly complex issue in 2020 led our investment team to question whether the deeply subordinated notes would be eligible for clients' fixed income portfolios. The team passed on the inaugural issuance and sought opinions from the legal department directly, and discussions around eligibility and suitability are ongoing.



## Robeco Institutional Asset Management BV (Robeco), pages 19–20



### Asset manager

Robeco describes their approach to exercising rights and responsibilities in corporate debt. They acknowledge the challenges of doing so, but they clearly articulate what they do to ensure that ESG issues are considered with all asset classes. This example also explains how Robeco has worked with other stakeholders to promote continued improvement of the functioning of financial markets (Principle 4) through their seat on the board of the European Leveraged Finance Association (ELFA) and what collaborative engagements they have participated in (Principle 10).

Robeco's active ownership programme spans across several asset classes, and in some circumstances, engagement approaches may differ for equity and fixed income portfolios. As stated in our engagement policy, engagements for credit portfolios are likely to be focused on downside ESG risks whereas engagements for equity portfolios are more likely to focus on both ESG risks and opportunities and shareholder rights.

An example of this differing approach in the past year has been our engagement with automakers on product quality. With strong interest in the topic from Robeco's fixed income team, and a history of product safety related recalls in the industry, one of the objectives in our ESG Challenges in the auto industry theme was customised towards the priorities of our credits analysts.

Even though proxy voting, as elaborated on later in the report, is a more widely recognised form of stewardship, Robeco is also active in exercising our rights and responsibilities that result from holding fixed income assets.

(...)

As a global asset manager, we are familiar with the systemic difficulties in seeking amendments to terms and conditions in indentures or contracts. The lack of an organised and efficient channel to structurally engage issuers on these topics has led to the creation of the ELFA. Robeco holds a seat on ELFA's board, and is actively involved in setting the agenda for improved market transparency in the high yield and leveraged finance market. The aim is to organise buy-side parties to ensure we can make use of our rights.

Besides working with our peers to work towards a better functioning bond market, our day-to-day processes incorporate the need for close scrutiny of prospectuses and covenants. All fixed income analysts are trained in reading and interpreting covenant language, with senior analysts directly responsible for analysing terms and conditions of transactions. Building expertise in this field is vital, and Robeco organises regular trainings for analysts conducted by external experts from ratings agencies and law firms.

Robeco carefully evaluates the terms of any potential transaction. In addition to our in house legal expertise, we retain an external legal advisory firm for in-depth analysis where needed. Our one-on-one relationship with specialised lawyers gives us full access to their thorough analysis on weaknesses and strengths of proposed terms. Their recommendations provide a useful input for our assessment.

## Stewardship activities in other asset classes and strategies

There are high-level commonalities to the overall stewardship approach taken for listed equity and other asset classes such as identifying the conditions that enable positive outcomes from stewardship activities, the types of performance and value those undertaking stewardship are delivering for their client or beneficiaries, the use of targets to assess stewardship performance, the interaction investors have with investee companies to encourage better stewardship outcomes and overall measurement of success from stewardship activities.

There are also important differences in asset classes outside of listed equity that signatories should consider when practicing stewardship. Issues such as access to management, size of holding, ownership rights, liquidity, time horizon and the direct or indirect nature of the investment will determine the approach to stewardship in different asset classes.

The table suggests stewardship activities that signatories invested in fixed income, real estate, infrastructure, private equity, hedge funds and derivatives could report on to demonstrate the exercise of influence and rights to maintain and enhance the value of assets. These examples are indicative and may be particularly relevant for reporting under Principles 7 and 9-12 of the Code.

### Corporate Debt

- Integrate material ESG factors into credit research and assessments.
- Work with bond index providers on sustainable methodologies to promote well-functioning financial markets.
- Engage with issuers to improve ESG risk management and develop sustainable business practices.
- Engage with investee companies at investor roadshows particularly at debt origination and reissuance.
- Engage with CFOs or treasurers to raise stewardship and ESG issues.
- Engage investee companies with the full weight of holdings, for example, using equity and credit investments.
- Escalate engagement using methods such as collaborating with other investors, contacting the board, choosing to avoid new debt issuance, underweighting or divesting.
- Explain how proxy voting rights have been exercised where appropriate, for example, through convertible bonds.

### Sovereign Debt

- Consider whether investment in different sovereign debt markets is compatible with client and organisational values.
- Integrate governance and political factors in addition to broader environmental and social issues into sovereign credit analysis.
- Work with bond index providers on sustainable methodologies to promote well-functioning markets.
- Engage with government economic and finance ministries on ESG-related issues, for example, commitment and progress on the UN Sustainable Development Goals (SDGs).
- Engage beyond the issuer with other stakeholders such as trade unions and supranational institutions such as the World Bank and the International Monetary Fund (IMF) to raise stewardship and ESG issues.

### Direct Real Estate

Identify significant issues which could impact the investment thesis such as environmental impact, health and safety issues during construction and community relations.

Investigate issues identified in due diligence thoroughly, for example, through the use of non-financial third-party reports.

Use investment committees to discuss issues identified during due diligence to ensure transparency.

#### Ownership phase

Set targets for stewardship and ESG issues faced in the ongoing ownership of the asset, for example, energy usage and greenhouse gas emissions.

Set out and implement clear action plans to address the issues identified.

Use appropriate certifications and frameworks for real estate to validate performance and demonstrate issues have been addressed.

Engage with external property managers to ensure ESG issues are managed in line with expectations.

Engage and exercise rights with building tenants and other stakeholders such as contractors to manage the issues identified.

### Indirect Real Estate

Identify intermediaries with strong responsible investment and stewardship credentials through due diligence.

Include stewardship and ESG requirements in legal agreements with fund managers.

Monitor and hold to account intermediaries such as fund managers on their stewardship activity.

### Direct Infrastructure

Take account of stewardship and ESG issues in the due diligence phase of the investment.

Make use of rights and influence available such as board representation to respond to the issues identified.

Explain how the stewardship approach differs for debt and equity infrastructure investments.

Consider relevant stewardship and ESG issues across the lifespan of the asset including responsibly constructing, operating, maintaining and exiting the investment, including end-of-working-life issues such as asset disposal.

### Indirect Infrastructure

Identify intermediaries with strong responsible investment and stewardship credentials through due diligence.

Influence counterparties prior to investment to ensure ESG and stewardship issues are taken into account.

Monitor and hold to account intermediaries such as fund managers to ensure stewardship is integrated.

Explain how the stewardship approach differs for debt and equity infrastructure investments.

Consider relevant stewardship and ESG issues across the lifespan of the asset including responsibly constructing, operating, maintaining and exiting the investment, including end-of-working-life issues such as asset disposal.

## Private Equity

Incorporate stewardship and ESG considerations in fund terms.

Ensure stewardship and ESG issues are considered in due diligence and investment decision-making.

Measure the ESG performance of the portfolio company.

Exercise rights from representation on portfolio company boards.

Encourage investee companies, where appropriate, to report on the [Wates Corporate Governance Principles for Large Private Companies](#) or alternative corporate governance codes.

Make operational improvements at the portfolio company to address material ESG risks and opportunities.

Consider key stewardship and ESG issues in the exit process.

Limited Partners (LPs) set clear expectations for General Partners' (GPs') stewardship in tenders and mandates.

LPs monitor the stewardship and ESG activity of GPs and hold them to account, for example through LP Advisory Committees.

LPs consider GPs' stewardship and ESG performance when deciding on committing to new fundraising.

## Hedge Funds

Explain how the fund's strategy is consistent with effective stewardship, for example, why the investment time horizon is appropriate and how it contributes to sustainable behavioral change in issuers and markets.

Consider relevant stewardship and ESG issues in investment analysis and quantitative models, where these are used.

Consider how hedging can be used to align client and beneficiary portfolio with long-term risks which have been identified such as market-wide and systemic risks.

Explain how the use of derivatives and short-selling (e.g. to take positions or to hedge an exposure) is consistent with a long-term approach to stewardship.

## Derivatives

Derivatives have a variety of uses across the asset classes identified above. For example, derivatives can be used in active management such as individual security holdings at stock and sector levels. Alternatively, they can also be used in wider portfolio management, for example for leverage or risk management.

### Active management

Explain how derivatives are used, for example, for risk control, hedging or financial returns, and how the derivatives strategy is consistent with your approach to stewardship and time horizon.

Seek opportunities to engage and influence where possible the voting policy of the prime broker or counterparty (for example, an ISDA counterparty).

Use rights where you have them and where you do not have them look for other opportunities for engagement and influence.

### Portfolio management

Consider how derivative positions are consistent with long-term risks identified.



The HM Treasury-led *Asset Management Taskforce report – Investing with Purpose*<sup>13</sup> emphasises how collaborative engagement can be used in corporate debt as an escalation tool. The report also explains the role of the Investment Association’s Special Committee, which facilitates collaborative engagement between bond issuers and bondholders.

The UN Principles for Responsible Investment website has a range of publicly available ‘investment tools’, including guides and case studies covering a wide range of asset classes.<sup>14</sup>

13 Asset Management Taskforce, 2020. [Investing with Purpose: placing stewardship at the heart of sustainable growth](#)

14 UN PRI. [Investment Tools](#)



## **Part 4** Focus on Outcome Reporting

## Part 4 Focus on Outcome Reporting

### Key messages

- Clearly stating outcomes for each Principle of the Code is a key component of good reporting.
- Organisations should report on how effective they have been in achieving desired outcomes.
- Reporting outcomes should be supported by relevant evidence including internal metrics, reviews, client feedback, and case studies.

Reporting on outcomes is a required element of each Principle of the Code. Outcomes are the results of activities undertaken in the reporting period. An integral part of reporting on outcomes is a reflection on how effective organisations have been in achieving their desired results. This assessment of effectiveness must be sufficiently evidenced. The assessments should be fair and balanced and acknowledge shortcomings in the reporting period. Reports with clear reference to these issues and plans for improvement are often more effective than those that simply allude to weakness. We would then expect to see reporting on progress in future reports.

Many organisations did not consistently report outcomes of their activities across all the Principles, and as a result did not achieve the standard expected by the Code.

### Fidelity International, page 36

*Asset manager*



Fidelity International identifies an opportunity for improvement in their current communications to non-institutional clients, and directly connects this to plans for research and improvement.

We believe that our methods for understanding client needs were effective during the year but could be improved, particularly for non-institutional clients. We are aware of the asymmetry of available information on stewardship activities whereby institutional clients, and some wholesale clients, receive significantly more than those who come through intermediaries.

This reflects the different levels of access we have to these customers, which also precludes us from the type of face-to-face dialogue on stewardship and ESG we have with institutional investors. We intend to conduct more research into intermediated client views to gain a better understanding of their stewardship priorities and use this information to tailor the content we provide to our non-institutional clients.

## Policies and organisational processes

Several Principles require reporting on internal policies and the activities that apply to operations. For each of these Principles, applicants are expected to assess the effectiveness of their operational activities in relation to stewardship and support this with evidence from the reporting period.

Reports can refer to internal metrics, internal reviews, client reviews and feedback as evidence of their effectiveness. Citing a range of evidence results in a more comprehensive disclosure than relying on a single measure. Organisations may wish to refer to external grades or accolades to demonstrate their effectiveness in this area. We encourage applicants to carefully consider the credibility and independence of the awards cited before placing too much emphasis on these. Becoming a signatory to a robustly assessed national or global standard carries more weight than an industry award. Organisations should explain how these awards have been the result of their activities and how they plan to improve their policies and processes.

### Lindsell Train Limited (Lindsell Train), pages 6–7

*Asset manager*



Lindsell Train lists several outcomes from the reporting period that demonstrate how they have continued to progress on their long-term ESG strategy. Reporting within this section is cohesive; all the pieces of evidence work well together to support their statement of effectiveness along with their organisational purpose and goals (Principle 1).

#### Examples of some of the specific outcomes include:

- ESG (within the broader context of Stewardship) is a standing agenda item at all meetings of the LTL Board and the Management Committee.

- We have initiated and continued to upgrade our ESG client reporting, which now forms an important part of our client communications.
- Lindsell Train became a signatory of UN PRI in November 2019.
- Lindsell Train appointed Glass Lewis to aid the administration of proxy voting and provide additional support in this area. Given its enhanced reporting capabilities, we are now able to publish an annual record of our voting activities. We also believe that its research and engagement platform will further improve the inputs to our decision-making. However, an important part of our investment process and proactive company engagement strategy is that the portfolio managers retain responsibility for voting decisions, based on their detailed knowledge of the companies in which we invest.
- We have begun preparing a strategic framework to guide our future ESG work.

(...)

To date, our stewardship activities have proved effective and we have been able to deliver good investment returns for our clients, a commitment to investing responsibly and also, we hope, the level of service that our clients deserve and have come to expect. However, like our expectations of the companies in which we invest, our clients' expectations of us are constantly evolving and rightly so. There is more work to be done.

## Principles 2 (Governance and resourcing) and 5 (Review and assurance)

When reporting the outcomes of Principle 2, organisations should assess how they have governed and resourced stewardship. For example, their existing team structures, training, diversity policies and other aspects listed under Principle 2. Organisations should then report on their review and assurance measures with Principle 5 disclosures. Here, they should note any changes they have made to improve their function because of a review.

Reporting for Principles 2 and 5 is connected. It is often the case that the same organisational reviews will determine what is working well and what needs to change. If following a Principle by Principle approach to reporting, organisations may cross-reference their disclosures, as long as the specific reporting expectations for each Principle are met in the report. If the organisation has chosen its own format, then these disclosures could be grouped together.

Applicants that have recently reorganised their governance structure or undertaken organisational changes following a review may find it easier to fulfil these requirements because they have more recent information to disclose. It is certainly appropriate to discuss recent organisational changes to meet these reporting requirements, but it is possible to report on these outcomes well without having undergone a recent overhaul.

### Mercer Global Investments Europe Limited (Mercer), page 10



#### Asset manager

Mercer's report presents a summary table under Principle 2 demonstrating how they have assessed the effectiveness of their governance structures in the year. They also note several key changes they have made to better align their functionality with overall stewardship goals. Reporting in this section is very well connected to the themes throughout the entire report.

Table 2. Highlights, Outcomes and Focus for Next 12 months

<b>Governance Structure</b>	<p>Our governance structure has supported the business well by successfully leveraging scale, accessing and disseminating specialist stewardship knowledge to our investment teams and helping clients meet and exceed regulatory stewardship requirements. Year-on-year the level of responsible investment and stewardship knowledge across the business continues to grow.</p> <p>Over 2021, as the number of clients producing their first set of implementation statements grows substantially, we will need to ensure the structure remains fit for purpose to disseminate evolving best practice effectively and support growing client demand. Business-wide integration efforts and ESG training schedules in place will support our work but this will be an area to keep under review.</p>
<b>Manager Research and Monitoring Processes</b>	<p>Over 2020 we agreed a number of substantial improvements to assessing stewardship within our research process, including fully integrating stewardship into the rating process for passive strategies and capturing voting and engagement data within our manager database. We also introduced substantial improvements to our stewardship monitoring reports. The benefits from these improvements will only start to be seen over 2021.</p> <p>We expect more clients to make use of these research and monitoring services in order to support their implementation statements but we will need to ensure that there is sufficient resource to roll out these updates.</p>
<b>Third Party Data Providers</b>	<p>The appointment of ISS for impact mapping has increased our capabilities over the last 12 months. Our third party data providers enable clients to access more granular data, assisting with identifying trends and supporting more effective manager engagement.</p> <p>We will continue to work on impact measurement approaches over 2021 and how this might be more effectively supported by engagement activity.</p>

In these circumstances, investors should report on how they have assessed their internal operations and why they have concluded that they did not require significant changes during the reporting period. If organisations conduct reviews on a less than annual basis, they should state this and report where they are in this review cycle. Investors may also report on past or planned changes outside of the reporting period if relevant. This would include changes where effects are still being felt in the reporting period, or imminent changes after the reporting period.

Environment Agency Pension Fund (EAPF), page 17



Asset owner

EAPF’s report describes how they review their governance structures to determine that they are appropriate, along with the outcomes of these reviews from the reporting period. Although they have not undertaken any significant changes to their governance structure in 2020, they demonstrate why this was appropriate by discussing changes performed just before the reporting period.

As a fund, we do a number of things to allow us to assess the effectiveness of our governance. Below we set out some examples of these that are relevant to our responsible investment approach and management of investment risks.

(...)

We are also subject to an internal audit. As a result of our 2019 internal audit on compliance and risk the Pension fund achieved 92% compliance with the internal auditors concluding “effective controls are in place for identifying, assessing and mitigating key risks.”

In 2020, a further internal audit review of pensions was carried out to evidence the progress made on the 2019 management actions, which evaluated the fund’s compliance with the Pensions Regulator Code14 and risk management arrangements. As a result of the work performed, five management actions were agreed relating to learning and development, conflicts of interest, policies, assurance on controls operated by third parties, and risk management. Based upon testing performed, a substantial assurance rating was given, confirming that four actions had been fully addressed and one action substantially addressed with alternative mitigations.

(...)

We ask our Governance Adviser to undertake a review of our governance every two or three years. This is done either through a confidential questionnaire of all pensions committee members, senior officers and advisers or an independent review by the adviser against its own good governance framework. The last review took place in 2019 and the next one will be this year. In 2019, the adviser concluded that “the effectiveness of the EAPF governance arrangements is of an extremely high standard.”

(...)

Finally, we sometimes benchmark ourselves against other funds, by occasionally applying for awards. In December 2020, we won ‘The Best Pension Fund in the United Kingdom’ Award at the IPE Awards 2020. IPE is Europe’s premier pensions website. The judges commented: “This fund should be applauded, with strong performance figures backed by a proactive, efficient and innovative response to the pandemic, while keeping focus on environment, social and governance issues and the views of its members.”

### Principle 3 (Conflicts of interest)

The reporting expectation under the activity section of Principle 3 requires organisations to explain how they have identified and managed any instances of actual or potential conflicts of interest. This requirement asks applicants to demonstrate how they have applied their conflicts policy in the reporting period. This would include providing details on how committees and staff have evaluated conflicts during the reporting year and what mechanisms and processes have been followed to mitigate potential and actual conflicts.

This is closely connected to the reporting expectation under the outcomes section, where the FRC would expect organisations to report on specific examples of potential or actual conflicts that have arisen during the previous 12 months. Organisations may present examples of actual conflicts that materialised in the reporting period and resulted in consequences, or they may present potential conflicts, and how they have been mitigated.

#### Sarasin & Partners LLP, pages 12-13

*Asset manager*



Sarasin & Partners provides numerous examples of conflicts and how they may manifest in the management of assets. For each conflict, they state how they would manage the conflict to ensure that it is mitigated. They state that they have identified 14 potential conflicts in the reporting period, which were then added to their conflicts register and monitored.

These examples of conflicts should clearly state that they occurred during the reporting period. Organisations should disclose how they identified the conflict and how they managed it. The case study should state the status of the conflict and whether it is still a risk to the organisation's operations.

#### Lombard Odier Investment Management (Europe) Ltd (LOIM), page 33



*Asset manager*

LOIM reports that they had several areas of focus in carrying out their conflicts of interest policy in the reporting period. They outline their targeted approach to conflict identification and explain that this resulted in fewer conflicts materialising. Of those that were identified, they provide two examples from the reporting period and explain how they were mitigated.

During 2020, we have paid close attention to conflicts of interest, given the rollout of our stewardship function, with increased voting and engagement. We have particularly monitored the conflict identification phase in order to prevent any real or perceived conflict from materialising. This has allowed us to stop conflicts from happening and undertake further escalation. Some of the conflicts we have identified and managed this year:

- the desired voting instructions of a client being different to those recommended by our proxy guidelines. As we have a preference not to instruct split voting (although operationally possible), we engaged with the party to better understand their views on the vote. It became clear that their views were informed, researched and justified. We then engaged with the company itself in order to get a complete picture. We instructed votes that took into account the conflict (acting in the interests of all clients).
- during some engagements seeking to better understand business practices, we have had CEOs or CFOs attending the calls as well. Overall, we think this is positive, as it sends the message that those responsible for implementing strategy are also taking responsibility for ESG and sustainability matters. Our conversations included remuneration matters, at which point, we have been stern in stopping the conversation, explaining that it would not be appropriate to discuss the matters with the beneficiaries being present.

Rarely, it may be appropriate to report that there were no conflicts, actual or potential. In these instances, organisations should state this explicitly, and instead provide a complete picture of the output of their conflicts policy in the reporting period. This may include information on how they examined conflicts in the reporting period and how they determined that there was nothing material to report. They could provide examples of conflicts that might affect the organisation in the future, explaining how they would address them. Reports may also include examples of conflicts from recent years outside of the reporting period. The Code has a strong focus on activities and outcomes from the reporting period, but it would be better to include a recent example than none.



The FCA's Conduct of Business Sourcebook requires firms to annually disclose their engagement policy and how it has been implemented in the year. As a part of this policy, firms are required to describe how they manage actual and potential conflicts of interest in relation to the firm's engagement. Further to this, firms that invest on behalf of an SRD institutional investor must disclose annually whether any conflicts have arisen as a result of engagement activities, and if so, how they were dealt with. [FCA COBS 2.2B.6 and 2.2B.9](#)

## Interactions with external stakeholders

### Relationships with clients and beneficiaries

In reporting on the outcomes of communications with clients and beneficiaries under Principle 6 (and under Principle 5 for service providers), organisations are asked to meet several reporting expectations. They should explain how they have evaluated the effectiveness of their communication methods. This assessment should be fair and balanced. Reporting should also include examples of how investors have considered client or beneficiary feedback and incorporated it into their policies and operations.



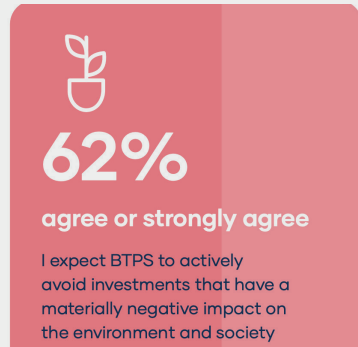
**BT Pension Scheme, page 34**



*Asset owner*

BT Pension Scheme describes how they annually assess member views with benchmarks and a review. They provide statistics from the reporting period's surveys and connect them to their measures of success.

In 2020 to better assess the effectiveness of our stewardship reporting, we asked members a range of questions in relation to responsible investment and stewardship. The findings from the 2020 survey with 8500 members surveyed online were as follows:



**Lane Clark & Peacock (LCP), pages 13, 27 and 33**



*Service provider*

LCP provides detail on how they have sought feedback from clients during the reporting period, and they provide summary statistics of the information gathered. Several locations in their report refer to changes and improvements made during the reporting period in order to better align their services with client demand.

We held 121 client care meetings in 2020. As well as their qualitative feedback, clients rated us as follows:

- 8.6 out of 10 average satisfaction score (where asked); and
- 9.2 out of 10 average recommendation score (where asked).

Aside from this structured arrangement, we are very keen to receive informal feedback from our clients on an ongoing basis, for example, at the end of a meeting, or over a quick coffee. This really helps us to tailor our service to exactly what our clients want – every client is unique and has their preferred way of working, and our personal and attentive service means we are well placed to deliver that and ensure that what matters to the client is reflected in the delivery of LCP CARES to them described in box 1.

As part of our client satisfaction programme, we undertake a triennial client survey. Nearly 400 clients participated in our 2019 client satisfaction survey and we were delighted with the results which echoed those of previous surveys.

*Table continues below*

From page 27

Our integrated risk management tool, LCP Sonar, combines our “big picture” insight and analysis of assets and liabilities with an understanding of the strength of covenant offered by the sponsor to the scheme. In response to client questions about how systemic risks such as climate change fit with the tool, we added an outer “external risks” ring (see image below). This recognises that many external influences are potential sources of risk for DB pension schemes. They may cause a combination of the covenant, funding and investment stresses examined in the inner rings of the tool. Our clients can explore material and suggested actions relating to some of these external influences by clicking on the external risks ring.

Asset owners are also asked to explain any instances where their managers have not followed their stewardship policies. If this has not occurred in the reporting period, organisations should state explicitly that they are satisfied with the services provided by their managers and explain how their managers’ activities are well aligned with their policies. In these instances, it may also be useful for organisations to explain how they would handle such an issue if it were to arise. Alternatively, reports could provide an example of this occurring recently, but outside of the reporting period. The Code requires organisations to provide content from the reporting year, but in this case, a recent example would provide more detail than no example.

BT Pension Scheme, page 45



Asset owner

BT Pension Scheme provides information on how they would handle concerns with a manager should they arise. They imply that this has not happened during the reporting period by providing an example of divestment from 2018.

As part of asset manager oversight, BTPSM also reviews the ESG ratings of its portfolio through ESG data providers, including MSCI, Trucost, Bloomberg and UBS Delta. These reviews include an ongoing evaluation of the ESG characteristics of the portfolio, the manager’s ESG integration approach, ESG and stewardship activities, and quality of reporting. Should the monitoring process reveal deficiencies or concerns that cannot be remediated, the mandate will be terminated. An example of this in practice occurred in 2018, when we took the decision to divest from an equity value strategy, driven in part by the high-carbon intensity the portfolio exhibited relative to the rest of our public equity portfolios.

## Integration of stewardship and investment

Principle 7 expects signatories to report how they integrate stewardship and material ESG issues into their investment decisions. When reporting on the outcomes of this integration, investors should provide clear examples of how stewardship considerations have been incorporated into an investment decision from the reporting period. Reporting should state a clear cause and effect relationship between ESG research and tools, investment beliefs and engagement with issuers, and the decision that was ultimately made to invest, monitor, or divest, where applicable.

Asset owners are also expected to report on how their chosen asset managers have integrated stewardship and investment over the reporting period on their behalf, ideally providing examples from the reporting period.

### Brewin Dolphin, pages 26–27

*Asset manager*



Brewin Dolphin reports their research and engagement from the reporting period related to holdings in the fashion company, Boohoo. They explain how their investment beliefs, research, and interactions with fund managers culminated in their decision to remain invested in the company.

Our second approach included speaking to the managers of funds with large holdings in the fast fashion company Boohoo. We are aware that the stories in the media about Boohoo are not isolated and that this issue is much more systemic, impacting most if not all fashion companies with production activities in the UK.

Our engagement focused on two funds in which we have sizeable holdings, and who in turn have sizeable holdings in Boohoo. The events surrounding Boohoo have continued to cause discomfort for investors in these funds.

They revealed many specific and industry-wide challenges that Boohoo must face, while calling into question the ESG integration in the investment processes of the funds. While these funds do not have 'sustainable' or ESG specific mandates, it is reasonable to expect these issues to be considered as part of the research process.

We interrogated the fund managers' approach to researching and engaging with companies in which they invest. Through email and telephone contact due to the pandemic, we were able to understand their thoughts relating to issues such as supply chain resilience, company culture and remuneration structures; issues at the heart of the recent news stories.

Throughout the course of this engagement, which is still ongoing, we were clear in our position which was to encourage the fund manager, and indirectly Boohoo, to strive towards complete transparency of the issues and the solutions. An example of this is the report issued to Boohoo by Allison Levitt QC. We and the fund manager felt that it must be published by the company in a complete and timely manner, and this was made clear to Boohoo. We were pleased that they published the report in full very shortly after receiving it, alongside their acknowledgement of the issues and onboarding of all recommendations which were put forward in the report.

We have decided to stay invested in these funds and continue to recommend them to our investment managers. We retain our conviction in the managers' stock picking abilities and have continued to be reassured by their feedback on the situation and their reasons for maintaining their conviction in Boohoo.

Some believe that disinvesting from companies with contentious issues is the only way to adhere to ESG principles. Sometimes it is the only option. In some cases, it is perhaps the easiest option, but not necessarily the best. In situations like this we believe that engaging and trying to influence positive change is the best first step to take, even if the eventual outcome is divestment.

## Relationships with asset managers and other service providers

Investors are asked to report on their relationships with service providers during the reporting period. Under Principle 7, they should state how they have given clear and actionable criteria to their providers. This could include describing the service-level agreements they have set, the key issues that were considered, including material ESG factors, and how these were included in tender documents.

### Coutts & Co, page 19

#### Asset manager



Coutts & Co outlines the details of their selection process for service providers, including how ESG matters are considered from the start.

#### Service providers:

All our service providers are subject to our selection process, which includes, where relevant, a number of questions on their approach to ESG and sets out minimum criteria that we expect to be fulfilled for them to be considered.

Our service providers are kept informed of our commitment to responsible investing. For service providers that enable us to effectively carry out our stewardship activity, we will disclose our ESG-related policies and commitments, such as our exclusions policy, our carbon-reduction targets and our ESG integration process.

Our stewardship provider, EOS, makes voting recommendations based on our responsible ownership principles and has a clear and proprietary milestone system, detailed in Principle 9, to track success of engagements over the short, medium and long term. In addition to this, we maintain ongoing dialogue with data providers to ensure we have access to all required data to make informed investment decisions.

#### Example – Service provider selection:

When selecting our custodian, we included questions on living wage and human rights in our selection process, and this has a direct influence on our assessment.

Once the provision of services has started, we expect organisations to report how they have monitored service providers (Principle 8). We ask organisations to state how services provided have met the criteria that were set, or if an issue were to arise, how they would hold the provider to account. If a service provider has not met the organisation's needs in the reporting period, the report should explain what actions they have taken as a result. Better reporting presents this as a case study, explaining whether they were able to solve the issue or if other measures needed to be taken, including termination of contract. We appreciate that disclosure on such issues might be confidential, so we understand if organisations prefer to provide examples in an anonymised form. However, the examples should be clear in explaining what actions have been taken and their outcome.

If an investor has not had to address an issue with a service provider in the reporting period, they should state that the services have met their needs. However, we would encourage organisations to provide more detail on outcomes here. It may be relevant to report on the processes in place to provide feedback to a provider if the need arose.

### Hermes Fund Managers Limited (Federated Hermes), page 46



#### Asset manager

Federated Hermes provides two examples of specific issues they identified during the reporting period, with an explanation of how they resolved them. The examples are contextualised by how they generally view data services and why they feel it is important to have a wide range of sources to inform decisions.

As noted earlier we use a number of external ESG data providers, as each data provider has developed their own methodology which can result in differing views. Taking this range of views into account, along with our qualitative fundamental analysis and insights from engagement by EOS or the investment teams, helps us to form a more comprehensive view of the company.

There have been instances during 2020 when companies were impacted by major ESG risks that had not been identified in advance by our data providers. For example, the allegations of poor conditions and below-minimum-wage pay at some of Boohoo's Leicester suppliers had not been identified by our data providers as a significant risk. Even after the news broke, there was a time lag before it was reflected in the relevant ESG scores. While we did speak to our data providers about this instance, the issue was largely difficult to avoid due to the retrospective methodologies used by many data providers.

This reinforced our view that such third-party data sources can only be one input alongside our fundamental analysis and engagement insights.

We may also engage with data providers when we identify incorrect information. For example, while investigating the carbon emissions of an aluminium producer for investment this year, we found that the data providers failed to capture emissions from its subsidiary. Through engagement with the data provider, we were able to rectify the figures and capture the correct emissions data.

### HSBC Global Asset Management, page 32



#### Asset manager

HSBC Asset Management provides well-rounded reporting on their relationships with service providers during the reporting period. They disclose that they had no issues with service providers in the year, and instead provide details of the positive relationships they've worked to maintain.

As MSCI is one of our ESG data providers, it receives the brunt of our feedback and comment on the data available. We raise specific errors we uncover as well as where there are unwarranted gaps in data. This feedback is conveyed as part of our regular dialogue with MSCI and in meetings to raise concerns.

(...)

We provide ISS with instant feedback when we identify apparent errors in their research or their interpretation of our policy. In some cases, we ask for the custom recommendations to be reissued so as to ensure there is an accurate record of recommendation, intended vote (pre-engagement) and instruction. We also push ISS when research is not yet available for meetings with imminent instruction deadlines. Each of our local offices using ISS has a local customer support and provides feedback on service levels. We have an annual meeting to review the service globally and identify where improvements are required. For example, last year we identified an inconsistency in how meeting volumes were recorded for our Canadian office, which resulted in work involving the custodian and ISS to ensure that processes were aligned.

Asset owners should aim to provide similar disclosure on the outcomes of monitoring asset managers in the reporting period. Under Principle 7, organisations should report how the tenders and mandates they have set have included requirements to integrate stewardship and investment, including material ESG issues. Here they should clearly lay out how they set expectations and they should report how they monitor asset managers to ensure they fulfil these expectations (Principle 8). Again, if reporting on a Principle by Principle basis, then cross-referencing is helpful. If the organisation chooses its own format, then these could be grouped together.

### Scottish Widows Group Limited (Scottish Widows), pages 10-11



*Asset owner*

Scottish Widows' report describes how they set different mandates for their external asset managers, based on the varying degrees of control over their funds. The mandates enable them to place certain restrictions on the use of funds and incorporate stewardship considerations as is appropriate.

### Universities Superannuation Scheme (USS), page 28



*Asset owner*

USS explicitly states the outcomes of monitoring their asset managers in the reporting year, with several case studies illustrating how they resolved problems with a few managers.

We welcomed a refreshed emphasis on ESG during the year at one of our US GPs, which included updated ESG policies, a consultant hire and strong statements on ESG in its 2020 fund raising due diligence questionnaire, following our earlier feedback that its ESG programme was dated and overly narrow.

We signalled our disappointment with another US GP regarding the lack of reference to ESG within its pitch book and fundraising presentations from investment partners. This lack of reference was surprising given the materiality of ESG themes to the strategy, the explicit ESG commitments in the fund DDQ and the firm level commitments on responsible investment and stewardship. We indicated that we will continue to monitor progress as the fund deploys capital.

We escalated our concerns with a European GP regarding their practices for the agreement of conflict waivers. Sign-offs had drifted to one-to-one conversations with individual LPs (particularly post-COVID) rather than being collectively discussed at the fund's Advisory Boards. Following formal engagement with the GP's managing partners, good governance practices have resumed.

In 2020, we also saw a multi-year engagement rewarded when another GP finally agreed to adopt in-camera sessions for LPAC's to facilitate full participation from overseas LPs in fund governance.



## Engagement with issuers and voting

Reports should include several examples of engagement, reflect on the effectiveness of their actions and note if any follow-up is required. Reports should include examples with a variety of outcomes to accurately represent the organisation's total activities for the reporting period. For more information on how to report on the outcomes of engagement, see the *Guide to Effective Engagement Reporting*.

The Code also asks organisations to provide examples of voting in the reporting period. In disclosing the outcomes of these votes, organisations should state their rationale, which is the explanation of the reasons behind a particular vote (or group of votes). This can be related to stewardship priorities and/or voting policies and other factors.

When determining which examples to include, asset managers might want to consider most significant votes as required by COBS 2.2B.7. The same applies to asset owners which are required to consider most significant votes when drafting their Implementation Statement. Examples should:

- provide information on whether the resolution passed or failed (including percentages)
- explain what the response was to the resolution from the issuer and other shareholders
- include a reflection on the impact that the vote had on the company
- explain if the organisation reached its goals
- describe further steps to be taken in the future if not satisfied with the result.

As explained in Part 3, although Principle 12 specifically includes reporting expectations for the outcomes of voting in listed equity, we expect investors in other asset classes to explain the outcomes, where possible, when exercising their rights and responsibilities.



The [UK Corporate Governance Code 2018](#) requires companies to report when 20% or more votes have been cast against the board recommendation. In these instances, the company should explain what actions it intends to take to consult shareholders and understand the rationale behind the dissent. An update on the case is expected within six months of the shareholder meeting.<sup>15</sup>

### UBS Asset Management (UK) Ltd (UBS), pages 40, 48 and 54



*Asset manager*

UBS provides detailed context for each of the votes that they disclose. They clearly state the outcome of each resolution and provide reflection on the impact of the vote and next steps with the issuer.

<sup>15</sup> FRC, 2018. [UK Corporate Governance Code 2018](#), page 8



### Indirect investment activities

For several Principles, asset owners (and others investing through agents) are asked to report on activities that may be undertaken by asset managers on their behalf. In these instances, asset owners should communicate their reporting needs to investment managers so that relevant information can be relayed for inclusion in the report.

Asset owners can report on the outcomes of these activities by providing direct information from asset managers' reports through screenshots and extracts, or by summarising the case studies presented in their managers' reports, focusing on outcomes and further actions. If able, asset owners should also include their own reflection on the outcome as well any reflection from the managers along with.

Asset owners that engage both directly and indirectly with issuers should report this and include examples of both types of engagements from the reporting period. As above, these examples should give the current status of the engagement and reflection from everyone involved.

### Greater Manchester Pension Fund, page 29



#### Asset owner

Greater Manchester Pension Fund clearly articulates the result of several resolutions voted on their behalf. They provide some of their own reflection on the methods of engagement and the outcomes of the resolutions.

GMPF considers shareholder resolutions a useful tool to proactively raise issues of concern either where boards of investee businesses are resistant to dialogue or change, or to amplify the shareholder voice where engagement with boards has been positive. GMPF co-filed resolutions at Chevron, Citigroup, Comcast, Delta Air Lines, Eli Lilly and Walt Disney Company, during the 2020 AGM cycle. In all cases, the proposal sought alignment of the companies' lobbying practices with their publicly stated positions on climate change. While none of the resolutions was successful this year, each generated significant shareholder support, sending a strong message to the boards. GMPF has not been deterred by the outcomes of 2020's shareholder resolutions and has co-filed a similar resolution for the 2021 AGM at Citigroup and is actively exploring further opportunities.

Although the resolution co-filed at Delta Air Lines wasn't successful, the lead filer along with GMPF and its responsible investment adviser have been in active dialogue with management as a consequence of the filing of the shareholder resolution. The company shared its reasoning behind its decision to announce its net zero ambition for the current decade and ways it is working to ensure it will achieve this goal.

**RPMI Railpen (RailPen), pages 35–36***Asset owner*

Railpen explains their preference to engage directly with issuers for their most significant holdings. They describe their overall approach and provide two case studies from the reporting period with clearly articulated outcomes and reflection on the results.

**Outcome and next steps:**

- Discussions confirmed that the multi-million dollar bonus reported for a long-standing Named Executive Officer primarily related to the accounting effects of an amendment to their previously awarded restricted stock units. Therefore, we felt comfortable supporting the compensation report in line with 97.5% of votes cast.
- It became evident that Company A's efforts to protect its workforce were evolving and there had been multiple learning points. For example, company representatives noted that questions were sent to subsections of the workforce on a daily basis via the employee connection programme, with real time responses reported to management. Despite this, we continued to feel that there was disparity between the views expressed by management and those 'on the ground'.
- We also felt that disclosure on the impact of Company A's efforts to protect its workforce, alongside the effectiveness of board-level oversight, would provide better insight to shareholders and reinforce accountability for worker safety. We therefore voted in favour of those 2020 shareholder resolutions aimed at improving disclosure on these issues.
- We have used our 2021 Voting Policy update –with its new lines on the importance of treating the workforce fairly both during Covid-19 and beyond – to prompt further dialogue with senior company executives in early 2021. Intelligence from this meeting will inform our vote in the 2021 AGM.

# **Part 5** Guide to Effective Engagement Reporting

## Part 5 Guide to Effective Engagement Reporting

### Demonstrate engagement

This section provides a guide to the key features of effective engagement reporting. Engagement, escalation, collaboration and exercising rights are key aspects of effective stewardship (Principles 9–12). The Stewardship Code asks applicants to evidence their stewardship using appropriate ‘data, diagrams, tables, examples and case studies’.<sup>16</sup> Among applicants to the Code in spring 2021, reports generally provided more detail about activities and outcomes in these areas of stewardship than others. However, even among those that were successful, there was considerable variation in the quality and depth of information provided. Effective reporting on engagement is important because it allows readers to understand how investors interact with those in which they invest.

Organisations investing indirectly, such as asset owners investing through asset managers, or fund of funds managers, have different reporting expectations to cover this activity. Where an applicant delegates some aspects of engagement, escalation, collaboration or voting to others, they should explain the expectations they have set for others who will carry this out on their behalf, and how they monitor these agents (Principle 8). As well as including examples of their own monitoring work, they should provide case studies of the engagements carried out on their behalf.

### Distinguish between monitoring and engagement

We observed differences in the activities that asset managers consider to be engagement. Some relied heavily on examples of meetings with companies as part of general information-gathering and monitoring, rather than involving targeted engagement on specific issues.

When reporting on engagement, applicants should distinguish between interaction that has clear objectives and seeks changes and activities that seek to gather information. While there is a role for both, applicants should not overly rely on examples of general information-gathering or monitoring to demonstrate effective engagement. Instead, engagement examples should focus on specific issues or objectives raised with the issuer to seek change.

### Engagement data relating to the reporting period

The Code’s emphasis on activities and outcomes means it is important for organisations to effectively discuss how their engagement approach has been applied during the reporting year. Effective activity reporting should balance breadth and depth in explaining the approach by making use of a combination of data, examples, case studies, charts and diagrams.

Most applicants reported on engagement activity by providing a summary and key metrics on their overall activity, supported by data and diagrams. This is particularly useful for medium or large organisations. Better reporting goes beyond simply reporting on key engagement metrics by explaining the extent to which they have been used.

<sup>16</sup> FRC, 2019. [UK Stewardship Code 2020, ‘How to Report’](#), page 6

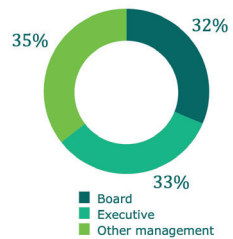
**J O Hambro Capital Management Limited (JOHCM), page 18**



Asset manager

JOHCM’s report provide an overview of their engagement activity during the year. This example places the engagement activity in context and illustrates the extent to which they used different types of engagement methods. They also provide additional information such as who attended the engagement, who they met, and the company type.

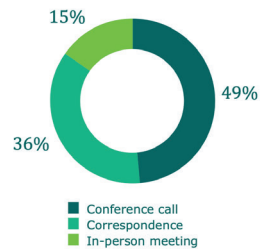
Company attendee level



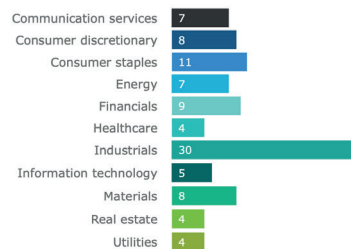
Who we met



Type of engagement



Company type



The charts show the proportion of engagement undertaken by our investment teams, and how we have continued to influence decision-making with senior management teams.

**Use examples and case studies**

- ✓ Explain the issues that led to the engagement
- ✓ State objectives for engagement
- ✓ Use representative examples (e.g. by geography and sector)
- ✓ Be specific about activities in the reporting year
- ✓ Give the rationale for the chosen engagement approach
- ✓ Explain your organisation’s role and contribution in collaborative engagements
- ✓ Explain the reasons for escalation
- ✓ Explain the outcomes of the engagement and identify next steps

As well as providing an overview of activity during the reporting period, reports should demonstrate how organisations have applied this in practice by providing case studies or examples of their engagement activity.

Organisations can use case studies that effectively demonstrate the application of multiple Principles. For example, the case study could explain how an initial engagement with a company (Principle 9) led to collaboration (Principle 10), escalation, or exercising rights (Principles 11 and 12). Where case studies are used to demonstrate the application of multiple Principles, organisations should provide a range of case studies, reflective of their size and the asset classes they are invested in.

## Explain the issue that led to the engagement

Effective case studies should explain the issues that have led to the engagement. Many organisations identified in general terms the key issues they consider important topics for engagement. However, not all reports referred to the issues addressed in their engagement case studies.

Some organisations embedded the issues into a narrative case study, while others adopted a more structured approach, with sub-headings specifically for the issues identified. As well as providing case studies of engagements with single companies, some organisations chose to provide thematic case studies that followed the issues they have selected and prioritised for engagement. Effective case studies on thematic engagements explained in detail how organisations engaged individually with companies on specific themes considered to be material. Better reporting combined both approaches.

## State your objectives for engagement

Effective case studies ensured that the objectives for engagement were clearly stated. Objectives explain what investors intend for the issuer to achieve; these can often include targets on a specific ESG issue. Some reports embedded the objectives into the narrative, while other reports stated them in a structured format. Clearly stated objectives help readers understand the reasons for engagement. Better case studies also include an explanation of how objectives have changed, if they have, particularly for ongoing engagements spanning multiple reporting periods.

### Amundi Asset Management, page 28

*Asset manager*



Amundi Asset Management clearly explains the issue and provides an explanation of why they engaged with 253 companies. They then set out their objectives for the engagement campaign, including details of the actions they will take.

In 2020, we wrote to 253 companies across a range of sectors, inviting them to commit to or upgrade their Science-Based Targets (SBTs) to fight climate change. SBTs are targets that are in line with what the latest climate science considers necessary to reach the goals of the Paris Agreement, specifying by how much and how quickly a company needs to reduce its greenhouse gas emissions to limit global warming to well below 2°C. We regard SBTs as a robust, credible standard for companies and investors alike, and we also welcome the transparency that they bring to disclosures and progress.

*Table continues below*

Our objective with these engagements is to encourage companies to set validated scientific objectives to reduce their GHG emissions in line with the 2015 Paris Agreement. As for all of our engagements, we set clear and tangible objectives for the campaign:

- Request 203 companies that have not yet committed to SBTs to do so;
- Invite 31 companies that have made the commitment to have their targets validated;
- Encourage 19 companies that have validated 2°C targets to commit to tougher 1.5°C targets.

## Use representative examples by geography and sector

In line with the Code, organisations should demonstrate how engagement has differed for funds, assets or geographies. In doing so, organisations should report on a range of case studies that are representative of the geographies and sectors of their AUM. For example, from the reports assessed, UBS Asset Management, which has \$1.1tn in AUM, provided a range of engagement case studies, which cover their invested regions (Europe, Middle East and Africa, the Americas and Asia-Pacific) and invested sectors (industrials, communication services, media and entertainment, energy, integrated oil and gas). For a smaller asset manager, it would be acceptable to include fewer examples; however, these should still be representative of the organisation's assets and activity during the year.

Better reports will also discuss how their engagement approach has differed across geographies. This can be discussed within the case studies or explained within the narrative on how engagement has differed for funds, assets or geographies.

### Fidelity International, page 53

*Asset manager*



Fidelity International explains that their engagement topics will vary depending on their region. Diversity is a topic of focus across Europe and Australia, whereas in Asia their engagements focus on board structure and culture due to less developed governance arrangements.

## Be specific about your activities in the reporting year

An essential feature of the Code is its focus on reporting on stewardship activities and outcomes in the reporting year. In doing so, organisations should be specific about explaining when different activities were undertaken. Additionally, organisations that report on multi-year case studies should also be specific about activities undertaken in the reporting year. For example, with ongoing engagements spanning multiple years, organisations should report clearly on any progress achieved over the previous 12 months. When explaining activities conducted within the reporting year, organisations should discuss examples of how the companies responded.



## Explain the rationale for the chosen engagement approach

Organisations should explain the reasons for their chosen engagement approach. Asset managers are encouraged to draw a link between their chosen engagement approach and their purpose, investment beliefs, strategy (Principle 1) and their client base, AUM and geographic spread (Principle 6). This explanation can be set out in a separate paragraph from the outset or within the case study discussion.

### Oldfield Partners, pages 19-20

*Asset manager*



Oldfield Partners provides two specific examples of collaboration that they have used in the reporting period: One with Korea Electric Power, coordinated by ClimateAction 100+; and another with Rio Tinto, coordinated by the Investor Forum. Both case studies explain Oldfield's reasoning for joining the collaborative initiatives, and how they monitored progress throughout the year. They state the current outcomes for each initiative and provide some reflection on the progress that has been made thus far.

## Role and contribution in collaborative engagements

The Code encourages organisations to report on their collaborative engagement activities and outcomes during the reporting period, not just a policy. Simply listing collaborative initiatives without providing examples does not give information on the activities undertaken in the reporting period. Better reports used several case studies to explain their collaborative engagements, and we would expect more examples from larger organisations.

Effective case studies for collaborative engagement should clearly explain why the organisation sought to engage collaboratively with others. When an organisation discusses its collaboration with other investors to engage an issuer, it should explain how its activity contributed to achieving change at the issuer level. Additionally, when an organisation works as part of a coalition of wider stakeholders to engage on a thematic issue, an effective case study should clearly state the role and contribution of other organisations.

## Jupiter Fund Management plc (Jupiter), page 45

Asset manager



Jupiter discusses its collaborative engagement alongside ShareAction in addressing Barclays' lending arrangements with fossil fuel companies that fail to align with the Paris Agreement. This example explains why they sought to engage, and it is clear about their role, emphasising areas of work that they led and acknowledging where ShareAction took a leading role. The case study also explains how their engagement informed their voting activity and their voting rationale, as well as the outcome.

(...)

### What were some of the key issues?

Barclays is the largest financier of fossil fuels in Europe and one of the biggest globally. Of its competitors, Standard Chartered and RBS had already strengthened their energy financing policies. Barclays was reluctant to do so as they have a large oil and gas banking business in North America and typically view their competitors as being US banks, which have not been subject to similar scrutiny. In January 2020, ShareAction, a non-profit organisation, and a small group of co-filers put forward a proposal, the first climate change resolution at a European bank, which called for Barclays to take concrete action to phase out providing lending to fossil fuel companies that fail to align with the Paris Agreement.

*Continues opposite*

### What did we do during the year?

ShareAction sought our support for the resolution, so we engaged with them to inform our approach. Considering the scale of the bank's financed emissions and its reticence to commit to meaningfully reduce them, we felt collective action was warranted. The text of the resolution also made clear that the bank could continue to finance energy and utility companies which were themselves in the process of aligning their businesses with the Paris goals, in line with our own approach. Consequently, in March we became the first >1% shareholder of Barclays to publicly announce our support for the resolution.

We subsequently engaged with the CEO and chair of Barclays on several occasions to confirm our support for the resolution and to discuss the group's climate strategy. This included both individual engagement and collaborative dialogue facilitated by the Investor Forum and IIGCC. Barclays subsequently, and prior to its AGM, produced its own resolution by which it committed to set a net zero target to reduce emissions from its financing activities and operations. We voted in favour of the bank's revised climate strategy at the AGM but also supported the ShareAction resolution. The reason for this was because we supported the shareholder resolution's call for the bank to explicitly 'phase out' lending to energy and utility companies that are not aligning their strategies with Paris, which the Barclays' board opposed. Ultimately, the ShareAction resolution did not pass. But it is clear that the rapid speed of change at Barclays was sparked by the resolution.

*Table continues below*

### What were the implications for our investment?

Much work remains to be done, but we view Barclays' climate commitment as a major step forward that will reduce its climate risk and place the company in a leading position among its peers. Barclays has committed to a Paris-aligned climate change strategy for which the board will be accountable. In our view, this is a good example of successful engagement and collaboration with other stakeholders. The bank has since disclosed details of the new strategy and we continue to engage with management in order to monitor its implementation.

### Explain the reasons for escalation

Organisations should explain when they have chosen to escalate their engagement, including the issue and the reasons for their chosen approach. Case studies are a good way of illustrating how an escalation approach works in practice. Escalation can take various forms. These include writing to the investee company, collaborative engagement, voting against directors' items at shareholder meetings, filing shareholder resolutions, engaging with regulators and policymakers, and divestment. Effective case studies for escalation should clearly explain the approach taken and the reasons for this. Additionally, asset managers should explain how they have selected and prioritised issues and developed well-informed objectives for escalation. This explanation can be set out in a separate paragraph from the outset or within the case study discussion.

### Lindsell Train Limited (Lindsell Train), page 35



*Asset manager*

Lindsell Train explains why they escalated to the company's management following their unsatisfactory solution to a human rights issue at one of their Japanese portfolio companies (Kirin Holdings).

Lindsell Train became aware of the fact that one of our Japanese portfolio companies (Kirin Holdings) is potentially implicated in human rights atrocities associated with Myanmar's progress towards democratisation, which has been marred by continued military control of the economy and, worse, human rights abuses committed by the military particularly against the Rohingya people.

During the second half of 2020 we have engaged extensively with the management of Kirin and their advisory board. We have recently escalated our engagement activity and will continue to do so until a satisfactory solution is presented.

(...)

Our initial conversations with company management confirmed that Kirin has engaged with Amnesty International and has also appointed Deloitte to verify these assertions, with Deloitte expecting to report back in the New Year. While we appreciate that Kirin should wait for the Deloitte report, we also believe that once it is published it is essential that it acts swiftly. As such, we have continued to engage with Kirin in order to encourage it to adopt a faster course of action.

*Table continues below*

We have spoken to senior management and have now heightened our engagement to help ensure that the company's actions fit their intent. We have written to the chair of Kirin's International Advisory Board (IAB), which is responsible for providing the board with strategic advice pertaining to the Group's global growth strategies, risk management and corporate governance. We sought clarification as to the advice given by the IAB and have also urged the IAB and management to consider the various eventualities of the Deloitte report in order that they can ready themselves and be in a position to move fast following the publication of Deloitte's findings.

We have been encouraged that Kirin seems to take its responsibilities in Myanmar seriously and appear committed to taking necessary action to ensure that its business activities adhere to the highest standards of corporate and social responsibility. For example, Kirin management wrote to us in November 2020 to inform us that that all dividend payments from Myanmar Brewery Limited and Mandalay Brewery Limited to Kirin and MEHPCL have been suspended in view of a significant lack of visibility regarding the future business environment for their Myanmar joint-ventures. It also reiterated its hope that the Deloitte review would be concluded by the end of the year.

## Clearly explain the outcomes of the engagement and identify next steps

Organisations should clearly state whether an engagement has concluded or is ongoing. Reporting should also acknowledge setbacks experienced and lessons learned, as well as successes. Therefore, the outcomes reported should vary, including positive and negative. Asset owners and those investing indirectly should also report on the outcomes undertaken by asset managers on their behalf.

Engagements with companies can take multiple years and may require escalation and continued monitoring over the longer term. Recognising this, better case studies provide information about the next steps and any planned follow-on from their engagements. This could include, for example, whether the intended outcome was achieved or is ongoing, how engagement progress or targets set will be monitored, and, if the engagement is still ongoing, whether any future action or escalation is planned. Better reporting goes beyond general statements that 'we will continue to monitor the company' and instead specifically identifies what is being monitored and what actions are planned.

**Wellington Management Company LLP (Wellington), page 24**



*Asset manager*

Wellington outlines the outcome of their engagement with the board of a company (American Electric Power) following concerns about their lack of a net zero by 2050 goal. This is an example of a positive outcome, where the company changed its practices following engagement. They also discuss how they followed up with the board.

**Outcome: Company changed practices**

We encouraged showing different carbon-reduction alternatives alongside the cost of alternatives as an approach when AEP tackles this topic with its many stakeholders. In a follow-up call with the board, we pressed it on whether they've considered including any ESG measures, particularly related to climate, in their compensation plan. It has now stated that the long-term compensation plan will include progress toward their carbon-reduction goal. We believe this indicates responsiveness to shareholder input and a recognition that aligning executive pay with climate goals is a critical step in moving toward carbon neutrality.

**Status and reflection: Ongoing**

We will continue to engage with AEP on this topic and encourage a more rapid shift toward net zero.

**Majedie Asset Management Ltd (Majedie), page 43**



*Asset manager*

Majedie reports on the outcome and conviction following the engagement with the company, Orange, on their lack of transparency on their accountancy approach. This is a good example as they go beyond stating the status of engagement and offers a reflection alongside their personal convictions on the progress made.

**Outcome:**

Subsequent to our meeting, Orange again relied on unusual categorisations of revenues and profits to flatter its Q2 results. We feel the Group relies too heavily on adjustments and often fails to be completely upfront about issues. The Group appeared not to take on board our feedback. It compounded the feeling that Orange's management are quite disconnected from shareholders, and unlikely to prioritise improving financial performance for the benefit of shareholders. As a result, we reduced our overall holding in Orange. Conviction – Decreased (largely due to an unsuccessful outcome from engagement).



A helpful explanation of some of the different forms of engagement can be found in the Investor Forum paper *Collective Engagement: An essential stewardship capability*.<sup>17</sup>

<sup>17</sup> Investor Forum, 2019. [Collective Engagement: An essential stewardship capability](#), pages 8–9





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