

**Main Issue with Proxy Advisors:
Improvement of Communication
with Companies still necessary**

2017 BPP CONSULTATION: QUESTIONNAIRE
Best Practice Principles for Shareholder Voting
Research & Analysis Providers “BPP”

Information on Respondent

1. Name of Organisation

Deutsches Aktieninstitut e.V.

2. Type of organisation [select one]:

- Investor
- Company
- Governance advisory / voting research service (investor advisors)
- Company advisor
- Representative body
- Other (please specify)

3. Main country / region of operation

Germany

4. Are you currently a client of a voting research provider? [Yes/ No]

No.

5. All responses will be posted on the Review website unless requested otherwise.

Please indicate below if you wish your comments to be treated as confidential.

6. If you would like to be informed of the outcome of this consultation please provide a contact email.

referenten@dai.de



General questions on the Principles

7. Were you previously aware of the Best Practice Principles? [Yes/No]

Yes.

8. If yes, how would you rate the positive impact of the Principles since they were introduced in 2014? [Scale of 0-5 where 0 is no impact, 5 is very positive]

- 0 no impact
- 1
- 2
- 3
- 4
- 5 very positive

Please give a reason for your rating

Deutsches Aktieninstitut believes there has been a certain impact by developing these principles and the duty do sign them as proxy advisors have more awareness now about their role and influence on the capital market and the responsibility that results from that fact. Therefore, they became more transparent and are more open to discuss questions of research and analysis quality.

However, there still is room for improvement regarding communication policy, management of conflicts of interest and awareness of local markets.

Deutsches Aktieninstitut's main requests, however, has always been that proxy advisors enter into a dialogue with issuers, provide issuers with draft vote recommendation in order to enable them to correct factual errors and – ideally – give issuers the opportunity to pass on comments on voting recommendations to investors in order to allow investors to check the proxy advisor's recommendation against the issuers comment. We hope that an outcome of this consultation is that these requests are laid down in the principles as good conduct. A self commitment of the signatories here would improve the situation.

9. If you are a user of voting research services, do you, or will you in future check whether a service provider had signed up to the Principles before appointing them? [Yes/No]

10. Would it be beneficial to have a set of principles that are capable of being applied in all markets? [Yes/No]

Yes.

Nevertheless, the BPP should provide that voting policies shall be tailored to each country taking into account local legislation, regulation and practices.

Deutsches Aktieninstitut also sees certain problems for companies with a dual listing; here it is important that proxy advisors apply the right national legal frame for the company they issue recommendations on.

Also there is still a certain lack of understanding for German legal forms of stock listed companies. Here, stock listed companies do not only take the legal form of a public limited company (Aktiengesellschaft; AG) or the Societas Europaea (SE) but can be also be a partnership limited by shares/silent partnership (Kommanditgesellschaft auf Aktien, KGaA). The KGaA is mixture of the public limited company and the partnership; not all recommendations of the German corporate governance code e.g. fit for it. As a consequence, it is important that proxy advisors consider the structure and legal background of such companies when preparing vote recommendations.

Scope and Structure of the Principles

11. At present the Principles address three areas: service quality (which includes duties to clients, research methodology and voting policy); managing conflicts of interest; and communications with issuers, the media and other stakeholders (see the BPPG website here). Are there other issues or activities that should also be covered by the Principles [tick each that applies]

- Intermediary vote processing and confirmation
- ESG advisory services and indices
- Governance engagement services
- Other (please specify)

Each item to be disclosed under Art. 3j of the revised Shareholder Rights Directive (2007/36/EC) should be taken into account.



12. Each Principle is accompanied by guidance which sets out practices to be followed and information to be disclosed, on a "comply and explain" basis. Is this structure clear and appropriate? [Yes/No]

Yes.

We support the "comply or explain" principle, but its application nevertheless could be improved. Statements of compliance should be published on a regular annual basis as well as detailed explanations for non-compliance.

13. If no, how might it be improved?

N.a.

The Content of the Principles (1: Service quality)

Principle 1: Service quality

14. If you are a client of one or more signatories, do you consider that this Principle deals adequately with the various service commitments that you expect? [Yes/No]

15. If no, how might it be improved?

16. Depending on the wishes of their individual clients, those signatories that make voting recommendations will follow either bespoke or house voting policies. How satisfied are you with the process used by signatories to develop their house voting policies? [Scale 0 to 5, where 0 is dissatisfied and 5 is very satisfied]

- 0 dissatisfied
- 1
- 2
- 3
- 4
- 5 very satisfied

17. How might the process be improved?

There should be more transparency regarding the way the voting policy is developed.



Voting policies should be tailored to each country, taking into account local legislation, regulation and practices. The concrete vote recommendation for a general meeting of a specific company should consider its individual situation then. There should be no box ticking, i.e. voting policies should be applied with some flexibility. One of the key factors for a high quality of the house voting policies is the number and qualification of the analysts/staff of the proxy advisor. Otherwise, box ticking is quite likely.

Regarding the essential features of the voting policies that apply for each market, proxy advisors should publish at the latest in November an update of their voting policies on their website. It is also important that the updates be published in a consolidated format, otherwise there are ambiguities whether some provisions are still valid or not. The policies should be clear and understandable both for issuers and investors and a definition of the different notions used should be disclosed. Issuers encounter more and more difficulties to understand some technical aspects of the voting policy.

The methodology used to update the voting policies should be disclosed together with a synthesis of the responses received when a consultation process has been launched.

18. In addition to national law and listing rules, which, if any of these considerations should signatories take into account when deciding whether to adjust their house policies for different markets? [Tick all that apply]

Standards in national corporate governance codes and equivalent

Views and practices of local companies

Views of local and international investors

Other (please specify)

19. How informative are signatories' descriptions of their research methodologies (see BPPG website here), including how they ensure that the research is reliable? [Scale 0 to 5, where 0 is uninformative and 5 is very informative]

0 uninformative

1

2

3

4

5 very informative



20. While recognising the need for signatories to protect their intellectual property, how might the statements be made more informative?

The Content of the Principles (2: Conflicts)

Principle 2: Conflicts

21. The Principle does not attempt to eliminate potential conflicts, but to ensure that the signatories disclose the procedures by which they are managed. Is this an adequate approach? [Yes/No]
22. If no, how might it be strengthened?

We see a potential conflict of interest in the fact that some proxy advisor offer different services such as consulting services, voting platform etc. to different clients. Therefore, proxy advisors should have the duty to disclose any relationship

- a. with the issuer who is subject to voting recommendations,
- b. with shareholders who have tabled resolutions,
- c. with any persons who control directly or indirectly the issuer or the shareholders mentioned previously.

It is an important step to disclose how conflicts of interest are managed. However, this is not sufficient to tackle the issue. Conflicts of interests should be properly addressed and resolved.

For instance, some proxy advisors have an own method of calculation to assess the remuneration of the management. To receive knowledge of the assessment issuers have to pay quite high fees. Another service of the proxy advisor (or subsidiaries) is quality rating of the issuers. Companies might have free access to their own evaluation result from the proxy advisor. However, they are also invited to subscribe to advice provided by service in order to improve their rating or to assess if their resolutions respect the proxy advisor's voting policy.

23. The Principles include the following non-exhaustive list of potential sources of conflict:

- A signatory's ownership or shareholder base/structure, such as when a signatory is owned by an investor that owns shares in

companies under coverage or when the investor is owned by an issuer under coverage;

- A signatory's employee activities, such as board memberships, stock ownership, etc;
- Investor-client influence on the signatories, such as when an investor who is a client of the service provider is a shareholder proponent or is a dissident shareholder in a proxy contest;
- Issuer-client influence on the signatories, such as when signatories provide consulting services to companies under coverage for research; and
- Influence of other investor clients.

Are there any others that should be included in this list?

24. If yes, please identify them.

The above-mentioned list seems to be sufficient.

25. If you are a client of a signatory, how satisfied are you with the information you receive on how potential conflicts are being managed? [Scale 0 to 5, where 0 is dissatisfied and 5 is very satisfied]

- 0 dissatisfied
- 1
- 2
- 3
- 4
- 5 very satisfied

26. How might procedures be improved?

The Content of the Principles (3: Communications policy)

Principle3: Communications policy

27. How satisfied are companies with their communication with signatories? [Scale 0 to 5, where 0 is completely dissatisfied, 5 is very satisfied]

- 0 completely dissatisfied
- 1
- 2
- 3

- 4
- 5 very satisfied

28. How might communication be improved?

Communication between proxy advisors and issuers has certainly improved in the last few years. Nevertheless, BPP provisions concerning dialogue with issuers should be strengthened.

We believe that the BPPs should not leave it to proxy advisors choice whether or not they engage in dialogue with issuers. Instead, the BPPs should require that proxy advisors having an engagement policy with issuers and disclose its main features in their compliance statement. Moreover, engagement with companies should be encouraged during the entire year. When proxy advisors do not engage with issuers, they should disclose their reasons.

Moreover precisely, the BPP should stipulate the engagement policy should state that companies should have are allowed sufficient time to analyse the draft recommendation report (a minimum of 2 days, preferably 3 days) provided that the company has disclosed its AGM agenda with the draft resolutions in due time. The proxy advisors should then correct all factual errors in due time and in any case, before the report is sent to their clients. This is the only solution to prevent proxies from sending inaccurate reports to their clients and to avoid factual errors and misunderstandings on the draft resolutions which are unfortunately very frequent and may lead to serious consequences.

Proxy advisors should also insert companies' quotes in their recommendation report provided that these quotes are concise enough and can enlighten shareholders on the draft resolutions submitted to the vote.

One given explanation of not be able to enter into dialogues during the season of general meetings is that the proxy advisor do not have time then. Deutsches Aktieninstitut thinks that this should not be a valid reason; we believe that giving a correct voting recommendation should be worth it to have the time to crosscheck. In the past such checks of facts led to changes in the voting recommendation, as we heard of.

There should also be the possibility to comment in efficiently replace in-depth dialogue, especially regarding complex topics that require an extensive understanding of companies. This process should preferably not be reduced to only written comments.

29. If you are a company, have you used the procedures set up by one or more signatories to make a complaint or provide feedback on their research on, or engagement with, your company?

30. If yes, how satisfied were you with how your complaint was handled? [Scale 0-5 where 0 is not at all satisfied, 5 is very satisfied]

- 0 not at all satisfied
- 1
- 2
- 3
- 4
- 5 very satisfied

Please give a reason for your rating

31. Many companies consider they should have the opportunity to comment on the analysis and recommendations in research reports before they are finalised. If you are an investor, which of these statements most closely reflects your view? [Tick one only]

- I find it helpful to know the company's views on the research report before deciding how to vote, ahead of the custodian cut-off
- I have no objection in principle to this practice, as long as it does not reduce the amount of time I have to make voting decisions or impact on costs
- Companies already have opportunities to explain their case in their annual reports, the papers for the general meeting and direct engagement with their shareholders; they do not need another one
- It is not appropriate for companies to have a right to review or comment on draft research reports of which they are the subject
- Other (please specify)

Reporting on the Principles

32. At present, signatories are required to produce a public statement on how they have applied the Principles, which they update as necessary; some have chosen to update the statement every year.



Signatories also produce a summary in a standard format for purposes of comparison (see BPPG website here).

Do the statements adequately cover all the matters that signatories are supposed to report on under the Principles? [Yes/No]

No, it depends of the subjects. Some are adequately covered such as the engagement policy with issuers, others insufficiently

33. If no, please identify which matters are not adequately reported on.

34. How informative and useful are the statements? [Scale 0-5 where 0 is uninformative, 5 is very informative]

- 0 uninformative
- 1
- 2
- 3
- 4
- 5 very informative

35. How might the statements be made more useful?

The revised Shareholder Rights Directive requires regular publication of statements of compliance. We would suggest that proxy advisors take inspiration from the Commission Recommendation (2014/208/EU) on the quality of corporate governance reporting ('comply or explain') regarding usefulness of explanations.¹

Monitoring the Application of the Principles

36. As part of this review, the BPP Group intends to introduce an independent element into the monitoring arrangements. Which of the following features should be part of the arrangements for monitoring the implementation and impact of the Principles? [tick all that apply]

- Oversight body including members independent of the sector
- Surveys of market participants
- Third party certification of how the Principles have been implemented by signatories
- Other (please specify)

For comment and suggestions see below, answer to question 37.

¹ <http://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX:32014H0208>

37. If you have specific suggestions for how the Principles should be monitored, please provide details

First of all, it could be usefully to have a survey/study to collect data about the way the BPPs are applied and explanations given in case of deviation from the principles.

We believe that proxy advisor are mostly aware of their responsibility by having voting policies and giving voting recommendations on an enormous number of the general meetings of companies. The fact that the consultation of the BPP review committee asks for the possible necessity of a monitoring proves this.

So, according to the BPP, the BPP Group will perform an ongoing monitoring of the implementation of the Principles and will review the Principles and the Guidance no later than two years following the launch. At present, there is no feedback on the activity carried out.

As a minimum, it would be useful to know if the members of the group meet, how many times, if the independent chairman plays a special role, etc. It would also be useful if the Group engages to publish a (annual) report on its activity where it expresses its view on the application of the Principles and the room for improvements, etc. It should also be possible to submit issues that relate to their relations with the signatories (e.g. dialogue, erroneous data, content of voting policies, conflicts of interest).

As there is already a procedure for feedback and complaints installed by the BPP Group it would be helpful to have some transparency on the experiences of the BPP Group with the handling of complaints. It would also be helpful when a more independent committee with also various stakeholders like investors and issuers would handle these topics. This committee could do some monitoring on an annual basis and could disclose the outcome. This would contribute to the effectiveness of the Principles.

38. Have you ever used the complaints procedure to complain about a breach of the Principles (see BPPG website here) [Yes/No]

39. If yes, how satisfied were you with how your complaint was handled? [Scale 0-5 where 0 is not at all satisfied, 5 is very satisfied]

- 0 not at all satisfied
- 1
- 2
- 3



- 4
- 5 very satisfied

Please give a reason for your rating

Signing-Up Process

- 40. The process of signing up to the Principles is being looked at as part of this review. Other than a commitment to apply and report on the Principles and to be subject to the monitoring arrangements, are there other criteria that service providers should have to meet in order to be accepted as signatories? [Yes/No]
- 41. If yes, please specify

Other comments

- 42. If there are any additional comments you would like to make as part of this consultation, please do so here:



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