

Best Practice Principles of Proxy Advisors - a Step in the Right Direction

Listed companies call for a possibility to check voting recommendations before they are issued to investors

1 General Questions

Q1: What is the nature of your involvement in the proxy advisory industry (proxy advisor, investor, issuer, proxy solicitor etc.)? To facilitate the comprehensibility of your response to this Call for Evidence, please describe your role in and your interaction with the industry.

Deutsches Aktieninstitut has closely observed the business conduct of proxy advisors (PAs) over the last years. To improve the dialogue between issuers and the PAs we have organised the exchange of views between German issuers and the main PAs and have commented on several (self) regulatory initiatives in the field of proxy advisory – among them the Best Practice Principles for Providers of Shareholder Voting Research and Analysis (BPP).

Q2: Have you previously had concerns with the functioning of any areas of the proxy advisory industry? If yes, please specify.

Yes.

PAs de facto play an important role for the investors' attitude towards certain topics of corporate governance as well as the outcome of general meetings. Against this background Deutsches Aktieninstitut has frequently called for minimum standards ensuring that PAs use their influence on the voting decisions of institutional investors in a responsible manner and that the perspective of the individual listed company is properly analysed before voting recommendations are issued to investors.

Having said this, we observe that the general business conduct of the most important PAs has improved over the past five to ten years. This tendency is most welcome by issuers.

In sum, the openness to discuss general topics regarding the corporate governance of issuers and their general meetings has increased. In a similar way, the proxy industry (at least the most important players) has generally learnt to better recognize national or regional specifics of both binding law and corporate governance usances in their voting guidelines and has opened their voting guidelines to a public consultation (or at least some unstructured feedback) among all interested stakeholders. However, we also been reported rather negative experiences with proxy advisors such as a persistent lack of understanding of European or local corporate governance traditions as well as inaccuracies and

wrong facts in proxy statements that can have very negative consequences for issuers affected.

Therefore, we still miss a general possibility for issuers to check voting recommendations before they are passed on to investors. This might happen already today on an occasional basis but it is not a common standard of the industry.

Q3: Did you become aware of the BPP at the time of their publication, i.e. March 2014? If yes, how did you become aware of the BPP? If no, when did you become aware of the BPP and how?

Yes, because we took part in the consultation process.

Q4: What is your view on the width and clarity of the scope5 of entities covered by the BPP (i.e. do you consider that the BPP cover the European proxy advisory market appropriately)? Please explain.

In our understanding the two most important PAs in the European market (i.e. ISS and GlassLewis/IVOX) have signed the BPP, so that the most relevant players are covered.

Q5: In your view, are the BPP drafted in a way so that they address the following areas identified in ESMA's 2013 Final Report? Please provide examples to support your response.

- a. Identifying, disclosing and managing conflicts of interest;**
- b. Fostering transparency to ensure the accuracy and reliability of the advice;**
- c. Disclosing general voting policies and methodologies;**
- d. Considering local market conditions;**
- e. Providing information on engagement with issuers.**

First of all, Deutsches Aktieninstitut welcomes the BPP as they generally show that PAs are taking seriously concerns about their own governance, their de facto influence on issuers and negative effects of errors in their analyses.

Deutsche Aktieninstitut has frequently called for a set of minimum standards for the PAs that should at least include the following elements.

- A duty to publish the voting policy in due time. Furthermore, these guidelines should be open for comments also for issuers before they are

issued and the process of amendment should be transparent in terms of decisions taken.

- A duty to give issuers the opportunity to check the draft of the voting recommendation on its completeness and accuracy in a certain (short) period of time before its finalisation. Factual errors then should be corrected by the proxy advisor. In case of dissent on a particular voting recommendation the proxy advisor should ideally also pass the dissenting opinion of the issuer together with the PA's voting recommendations to the investors.
- A duty to take into consideration local market conditions when establishing voting policies by at least giving the issuers the option to comment on voting policies.
- A duty to publish possible conflicts of interest or at least to inform the client / investor about them when providing the voting recommendations.

In addition to that it should be self-evident that PAs have sufficient number of well-educated staff that is also familiar with local and regional legal specifics as well as with usances of corporate governance.

Q6: What is your overall assessment of the quality of the signatory statements? Please provide examples referring to the areas identified under Q5.

n.a.

Q7: In your view, are there proxy advisors which possibly fall within the scope of the BPP and have not signed the BPP? If yes, please:

- identify such entities;**
- explain why you consider them to be within the scope of the BPP; and**
- indicate their size and the coverage of their operations within the European market.**

n.a.

Q8: How would you describe the impact which the BPP have had on the proxy advisory industry in practice? Please provide examples to support your response.



As the BPP have been put in place only one year ago, there is still little experience with the impact. However, as expressed above (see Q2) the BPP have to be evaluated against a general change in behavior of proxy advisors over the past 5 to 10 years which – to the impression of the majority of issuers – led to improved openness to dialogue with issuers, more transparency of methodologies and a better understanding of regional and local (regulatory) specifics and their incorporation in local voting policies.

However, there is still room for improvement regarding the dialogue in general and even more concrete voting recommendations (see also Q5). As laid down in a number of position papers, Deutsches Aktieninstitut would most welcome if the BPP incorporated the general duty for PAs to give the issuers the opportunity to check the draft of the voting recommendations on its completeness and accuracy in a certain (short) period of time before its finalisation. Factual errors then should be corrected by the PA after this issuer fact checking. In case of dissent on a particular voting recommendation the PA should ideally also pass the dissenting opinion of the issuer together with the PA's voting recommendations to the investors. Though still not incorporated in the BPP, the BPP may indirectly have accelerated the change of business conduct already under way. E.g., GlassLewis appears to have just started a process that allows issuers to fact check the data used for proxy analyses in the US market. This is at least a step in the direction of Deutsches Aktieninstitut's recommendation.

Besides this, the BPP should demand to involve issuers in the development of general voting policies (which is at least not common practice) as long as these policies are not client research policies in order to get a full picture of the written and unwritten local governance traditions. This would help to better adjust voting policies to local market conditions and provide for a fair treatment of governance issues across markets. In addition to that we suggest that a clear guidance is included in the BPP until when the general voting policies should be reviewed and made public before the general meetings' season. Also, it should be a recognized minimum standard in the industry that there is a sufficient number of well-trained staff being familiar with local legal and non-legal corporate governance traditions.

Q9: Have you observed any changes in signatories' practices in the areas mentioned under Q5 since the publication of the BPP in March 2014 and specifically during the 2015 proxy season? Please provide examples to support your view and specify whether these changes addressed the concerns you mentioned in response to Q2, if any.

See Q8.

No, as the BPP have been in place for one year only and are embedded in a general improvement of transparency of the industry.



2 Questions to Issuers

Q34: As regards your experience with proxy advisors before and after the publication of the BPP, please describe:

a. whether proxy advisors have provided research, advice and/or recommendations on your company;

Deutsches Aktieninstitut's responses are based on the feedback we have received from our member companies. As these companies belong mainly to the DAX it has been common practice that voting recommendation are issued for these companies.

b. whether you have used services from proxy advisors (please specify which services, e.g. research, consultancy).

n.a.

Q35: In your experience, to what extent have the BPP enhanced clarity as regards the expectations issuers can have towards communication with proxy advisors? Please provide examples to support your response.

The feedback we have received indicates that the expectations towards the communication with proxy advisors from an issuer's point of view have already been clear before to the publication of the BPP (which is one reason why we are of the opinion that the development of the BPP have to be regarded against a general change of behavior of PAs, see Q8). However, overall we have received mixed feedback on the experiences of issuers regarding openness and accuracy of communication.

Nevertheless, we assume, that the BPP provide for better common understanding of the industry, the processes and the recommendations issued. At least for the most important proxy advisors the signatory statements offer an overview on their work which has in this form not been available in a single document.

Q36: Has your approach to seeking or maintaining dialogue with proxy advisors within or outside the proxy season changed in any way as a result of the publication of the BPP (e.g. in terms of frequency, nature, circumstances)? If yes, please provide examples and quantitative evidence.

The feedback we have received indicates that the approach to seeking and maintaining dialogue with proxy advisors has not changed after the BPP have been published. Most of the issuers have already been satisfied with the dialogue prior to the BPP. However, we still are of the opinion that the dialogue could further improved (see Q2 und Q8).

Q37: In your experience, to what extent have the BPP improved proxy advisors' procedures for managing and disclosing conflicts of interest, and specifically the following two types?

- a. The proxy advisor provides services to both the investor and the issuer;**
- b. The proxy advisor is owned by an institutional investor or by a listed company to whom, or about whom, the proxy advisor is providing research, advice and/or recommendations. Please provide examples to support your response.**

As we have laid down in a number of previous responses to the issue, conflicts of interests do not appear to be a major problem in the industry. From an issuer's point of view, it is rather transparency, reliability and – above all – openness to a fair and open dialogue with issuers that should be ensured.

Q38: In your experience, to what extent have the BPP enhanced clarity as regards proxy advisors' methodologies and the nature of their information sources, thereby allowing you to better assess the accuracy and reliability of the proxy advisors' research, advice and/or recommendations as regards your company?

The signatory statements on the BPP-website allow for a better understanding of the processes within PAs for all stakeholders and thus have improved access to information though there is still room for improvement (as negative experiences suggest).

However, the general impression of German bigger issuers is, that the proxy advisor research also before the publication of the BPP, stated, why certain recommendations have been given. The recommendations have furthermore been clearly aligned to the publicly available proxy guidelines.

Q39: In your experience, have the BPP enhanced:

- a. proxy advisors' level of awareness of local market, legal and regulatory conditions which your company is subject to?**
- b. proxy advisors' disclosure of the extent to which they take the above conditions into account?**

As expressed above, also before the BPP were published, proxy guidelines were generally better adapted to local market regulations, so that a country-wise differentiation helped investors to understand why a certain recommendation had been given differently from country to country. E.g. the board structure, board independence and share repurchase plans. Therefore it is hard to identify direct improvements through the BPP – at least for the most important market players.

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