To: The Best Practice Principles for Governance Research Providers Group

Submitted by e-mail

Subject: Eumedion's response to the Public Consultation on Best Practice Principles for Governance Research Providers

Ref: B2013.54

The Hague, 16 December 2013

Dear Drafting Committee,

Eumedion welcomes the opportunity to submit comments on the draft Best Practice Principles For Governance Research Providers (hereafter Draft Code). The Draft Code follows on a European Securities Markets Authority (ESMA) recommendation that the proxy advisor industry should develop an EU Code of Conduct (Code) that focuses on (1) identifying, disclosing and managing conflicts of interest and (2) fostering transparency to ensure the accuracy and reliability of the advice.[1]

Eumedion is the dedicated representative of the interests of 69 institutional investors – all with a long term investment horizon – and aim to promote good corporate governance and sustainability in the companies our participants invest in. Together they have more than € 1 trillion assets under management. Through the provision of equity and non-equity, long term institutional investors are a major source of the capital that is used by listed companies to grow, create wealth and provide

[1] ESMA Feedback statement of 19 February 2013 on the consultation regarding the role of the proxy advisory industry, paragraph 38 (ESMA/2013/84).

employment, which is vital to the long term interests of the European economy.

1. Key remarks

Eumedion believes that proxy advisors provide a useful service to investors in the context of the functioning of the voting system as a whole. They provide important services to those who intend to vote on items on the agenda of the listed companies' general meetings. In particular large institutional investors who, for reasons of diversification, invest in many listed companies seated in various countries could benefit from proxy advisors' voting advices and proxy voting services. At the same time, their influence should not be overstated.[2] As ESMA has rightly stated, the ultimate decision and the voting responsibility are on the investors' side.[3] The use of a proxy voting advisor's or other third party's services could not be a substitute for the institutional investor's own responsibility to vote in an informed and responsible manner.

A number of concerns regarding proxy advisors have been identified in both the European Commission's Action Plan and ESMA analysis (e.g. potential conflicts of interests, the accuracy and reliability of advices, lack of sufficient resources). Similar points of criticism have been raised by issuers and investors. These issues demand serious attention and need to be properly addressed.[4] We concur with ESMA's view that the preferable approach is the introduction of a pan-European industry Code of conduct rather than putting in place formal regulatory measures. However, we are concerned that the issues raised have not been optimally addressed in the Draft Code.

Our main concerns can be summarised as follows:

1) The scope of the proposal has been extended beyond the remit of the ESMA 'guidance for a proxy advisory industry Code of conduct' which could potentially cover any activities provided to their institutional clients, therefore discharging them of their engagement responsibilities. Setting the scope too wide and defining terms such as 'governance research services' too broadly risk applying the Code of conduct to asset managers and not-for-profit investor fora (e.g. providers which only issue bulletins and newsletters) which carry out activities which are totally different from those of proxy advisory firms and which have completely different positions in the listed companies' governance framework. The aim of the Code of conduct should not be to maximise the number of signatories, but to profoundly mitigate the specific risks to which proxy advisors' clients are exposed to in the context of a proxy advice provided to them. Therefore, we strongly advise that the Code approach should be a targeted one, which addresses proxy advisory-like risks which are genuinely significant to the voting process.

[2] In a 2010 study regarding US listed companies it was estimated that overall, an ISS recommendation shifts 6-10% of shareholder votes (Choi, Fisch and Kahan, 'The Power of Proxy Advisors: Myth of Reality?', *Emory Law Journal*, Vol. 59, p. 869, 2010, University of Penn, Institute for Law & Economics Research Paper No. 10-24). According to the Dutch Corporate Governance Code Monitoring Committee 2010 Survey, 50% of the institutional investors investing in Dutch listed companies do not use any of the services of proxy advisors.
[3] ESMA Feedback statement, paragraph 38.
[4] European Commission's European company law and corporate governance Action Plan of 12 December 2012 (COM(2012) 740 final).

2) Whilst we generally the support the use of the 'comply or explain' framework, we are concerned that the Draft Code consists of just three high level "principles" and some "guidance" on each of them. This is a different and less robust structure to that of the many corporate governance codes in the EU which contain "principles" which listed companies must comply and "detailed provisions" which they have to apply, or explain. We caution that the Code approach does not become one of lowest common denominator: if the scope is too broadly defined and/or principles are so easy to achieve as to be meaningless, then the Draft Code becomes a piece of self-regulation that does not improve standards within the proxy advisory industry, nor remove the desire of some to introduce binding rules. Therefore, we advise to make significant changes to the Draft Code's structure to ensure that the Code makes a strong debut. This means that the Code should:
(i) contain principles, elaborated in the form of specific best practice provisions,
(ii) operate on a comply-or-explain basis,
(iii) require proxy advisers to state publicly whether or not they apply the best practice provisions.

3) Partly as a result of the wide scope, the Draft Code seems not to be fully comprehensive and lacks precision in areas such as 'avoiding conflicts of interests' and 'ensuring the accuracy and reliability of the advices'. It is fundamental that clients can have confidence that the proxy advisors have adequate systems and controls in place to ensure that advices are rigorous, free from conflicts of interest and timely. We would strongly suggest that serious consideration is to be given to include in the Code at least the "Principles regarding the Proxy Advisory Industry derived form ESMA's analysis" as formulated in the 19 February 2013 ESMA Feedback Statement. Furthermore, we would like to see best practice provisions on:
1. how the proxy advisor seeks to reflect the views of its clients and how it seeks to ensure accuracy;
2. the proxy advisor's approach to dialogue with issuers, including whether it shows issuers copies of its voting analyses before publication, and its approach to corrections;
3. the resources dedicated to voting advices, including reliance on junior support staff and a mechanism to assess the adequacy of resources;
4. whether the proxy advisor has a contact point for companies and clients wishing to raise concerns.

2. Specific remarks

We will answer specific questions in the consultation paper which are most relevant to us below.

Q 2. Respondents are welcome to express their expectations regarding the review and monitoring of the principles. As the on-going governance of the principles has yet to be determined, the committee particularly welcomes suggestions by stakeholders as to how a representative feedback mechanism can be implemented.

Apart from narrowing the scope, which is vital, we believe that the effectiveness of the Code could benefit from establishing an independent body that monitors the Code on a regular basis and publicly reports on the monitoring outcomes, similar to the UK Financial Reporting Council and the Dutch

Corporate Governance Code Monitoring Committee, which monitor the workings of the Corporate Governance Codes of their respective countries. We also believe that the Code should be reviewed periodically in a formal manner with consultation on particular aspects that may have emerged over time.

Q 3. Please share your views on the practicality of a comply-or-explain approach to the principles.

In principle, we believe that comply-or-explain approach properly reflects that institutional clients are primarily responsible to hold proxy voting agencies to account and also offers flexibility to proxy advisors to use higher standards in their own policies rather than a one-size-fits-all approach or the obligation of the law. However, for this approach is to work properly, we believe that the standards against which the firms should comply or explain should be sufficiently high. We are currently not convinced they are. Also, the comply-or-explain mechanism breaks down without investor clients to whom the explanations are directed taking account of those explanations and engaging with proxy advisors to understand them better and, if applicable, suggesting their own views.

Q 4. Could the effectiveness of the principles be further enhanced? Please elaborate and provide specific examples and/or suggestions.

Other than narrowing the scope and establishing an independent body that monitors the Code's application on a regular basis, we believe that certain amendments should be made to the principles to make them effective:

- As a minimum there should be no dilution of the principles as set out in the earlier mentioned ESMA statement;
- proxy advisors should inform their clients about any changes in their initial advices as a result of the issuer's input;
- Essential terms in the principles should be clarified and if necessary defined or better explained. These terms include 'conflicts of interest', 'material conflicts' and 'investor-client influence'.

Q 7. What should the regional scope of the Principles be, in terms of signatories and services provided? For example, do you think that the Principles should be global?

The best practices are developed in response to ESMA's recommendation to develop a Code of conduct for the proxy advisory industry. Therefore the best practices should in first instance apply to all proxy advisory service providers with a European client base. Extending the scope to all global providers of proxy advisory services at this stage will delay the implementation process. However, the proxy voting industry is potentially a global market and therefore the Code can eventually set a worldwide scope.

Q 10 Do you agree with the definition of "governance research services"? Is the scope of the definition adequate? If not, please elaborate and provide specific suggestions.

Q 11. Are the definitions of "vote agency services" and "engagement and governance overlay services" and their distinction from "governance research services" sufficiently clear and accurate? If not, please elaborate.

We would disagree. As mentioned above, the scope of the Code should be narrowed to proxy vote advisory services only. The slightly artificial concept of 'governance research services', is neither clearly defined nor could be really differentiated from (other) 'vote agency services' and 'engagement and governance overlay services'. For instance, it is not consistent that 'providing regular and intellectual contributions to company-specific engagement services' would fall under the scope of the Code (paragraph 2.1.1), while at the same time 'engagement services' are excluded (paragraph 2.1.2).

Instead of using the current three definitions, we would suggest introducing a clear and single definition of proxy advisors in order to clarify the scope of the Code: 'firms, other than asset managers or representing bodies, who provide commercial based services that consist of analysing agenda items of general meetings and providing voting recommendations, either based on the proxy advisor's own voting guidelines or on the client's customised voting guidelines.'

Q 12. Do you agree that the Principles should not impose standards of conduct on investors? If not, please explain why.

Yes we totally agree. A key feature of self regulation is that you only regulate yourself (and not your potential investor clients). Investors have already to deal with own regulations (e.g. MiFID, UCITS, MAD, Transparency Directive), codes as well as best practices (e.g. UK Stewardship Code, EFAMA Code for External Governance, Eumedion Best Practices on Engaged Share-Ownership).

However, as we understand it, investors may actually fall under the scope of the Code in case they act as engaged owners, individually or collectively, on the basis of their own governance analyses of investee companies. For an investor it is hard to engage successfully with a company without having conducted any governance research on the company. We believe that engagement practices and related research activities that institutional investors and their managers conduct on their own, individually or via collective vehicles, should be excluded from the scope. The Code should focus on third party voting recommendations and the processes and issues related to that.

Q13. Do you think that Principle One will help the market to better understand the different kinds of services and approaches that participants operate? If not, please explain.

For institutional investors it is very important to know whether issuers have tried to influence the content of voting recommendation rather than just checking the accuracy the voting analysis. We would urge the Drafting Committee to transform the current 'guidance' on transparency regarding the dialogue with issuers into a 'best practice', i.e. that the Code should contain a best practice regarding transparency on i) whether a dialogue between the proxy advisor and the issuer has taken place, ii) the contents of this dialogue and iii) whether the contents of the dialogue had a material impact on the content of the draft voting recommendation.

Q 19. Do you agree with the proposed conflict management and mitigation procedures? If not, please explain why and what additional measures you would propose.

Conflicts of interest are in particular relevant in situations when other considerations than the best interests of the client may affect the voting recommendations. Examples of potential conflicts of interest situations are when a proxy advisor:

- has an asset manager as client who is part of a larger financial group with a stock market listing;
- provides services to both institutional investors and issuers.

Although we generally believe that the mitigation measures proposed are appropriate, there is a need for at least more specific disclosures about actual conflicts of interest. Accordingly, we make reference to our answer on Q 20 below.

Q 20. Do you agree with the proposed approach on disclosure of material conflicts? If not, please explain.

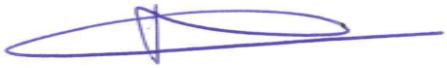
With regard to voting recommendations, we believe that conflicts that arise from offering both services to investors and issuers are most important in terms of negatively affecting the advisor's independency and reliability. We believe that these should be identified as material conflicts and always be disclosed to clients. In addition, for reasons of integrity and avoiding any doubt about conflicting interests within the same group, we would also generally support restrictions for proxy advisors to provide consulting services to investee companies.

Q 23. Are there any other aspects of issuer-related dialogue that should be taken into account? If yes, please elaborate and provide specific examples and/or suggestions.

In addition to what is set out in the Draft Code, we believe that proxy advisors should always inform their clients about any changes in their initial advices as a result of the issuer's input. We refer to our answer to Q 13.

If you would like to discuss our views in further detail, please do not hesitate to contact us. Our contact person is Wouter Kuijpers (wouter.kuijpers@eumedion.nl, +31 70 2040 302).

Yours sincerely,



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