

EPFSF Breakfast Discussion

4 May 2010, Radisson Blu EU Hotel, Brussels

“Crisis Management and Corporate Governance”

**Speech from Liz Murrall
Director Corporate Governance and Reporting, IMA**

Good morning and thank you for inviting me. I am here on behalf of EFAMA, the association for the European asset management industry and which with 26 member associations and 42 corporate members represents approximately EUR 12 trillion of assets under management and major investors in companies. I am here to look at the role of shareholders or stewardship in crisis management and contribute EFAMA's perspective.

Now in the run up to the crisis, it was apparent that at times there were failings in asset managers' stewardship, i.e., their scrutiny and challenge to banks' strategy and excesses. These did not cause the crisis nor would changes to governance have prevented it but nevertheless there were lessons to be learnt. EFAMA identified something was needed to restore confidence in the European capital markets. It thus created a fund and corporate governance Working Group with nearly 40 participants from its largest members throughout Europe to analyse how governance standards within the industry could be improved.

EFAMA had already taken steps in this area in 2006 when it published a Discussion Paper on “A Code of Conduct for the European Investment Management Industry” which encouraged asset managers to use shareholder rights “in a considered way, in the best interest of investors and to enhance the portfolio value”. And to have a policy which is disclosed to investors.

EFAMA is developing this and a draft paper has been accepted by the Working Group and will be submitted to EFAMA's board for approval soon. This aims to enhance and strengthen the role of the asset management industry and promote responsible stewardship. It is based on the new Stewardship Code that the UK's Financial Reporting Council is consulting on.

It has a set of Principles and recommendations and it is intended that it is applied on a comply or explain basis - very much as the UK's Corporate Governance Code. The principles seek to:

- ensure transparency and accountability to clients or the end beneficiaries; and
- enhance the quality of the dialogue so that asset managers derive value from their investments by dealing with concerns.

So looking at transparency and accountability first.

There is a principle that asset managers have a policy on how they exercise responsibilities. This should be public so that the end beneficiaries and companies are clear as to the manager's approach. Guidance specifies the matters to be covered.

The mandates of institutional shareholder clients such as pension funds, insurance companies, and investment trusts and other collective investment vehicles when they appoint asset managers should specify the policy on stewardship, if any, that is to be followed.

There is also a principle that both clients and the asset managers report on their stewardship and voting activities. Thus those that are principals or represent the interests of the end-beneficiaries should report at least annually to those to whom they are accountable on their policy and its execution.

Asset managers should report more regularly to their Clients/Investors how they have discharged their responsibilities and give both qualitative as well as quantitative information. The format should be agreed between the asset manager and its clients.

Certain calls for transparency of voting records but this undervalues much of stewardship activities so to address - there is guidance in the paper that asset managers disclose publicly their voting records and if they do not explain why.

So what about the second objective and enhancing the dialogue. First, asset managers need to monitor their investee companies to determine when it is necessary to enter into an active dialogue with boards. They need to have clear guidelines on when and how they will escalate their activities such as when they have concerns about the company's strategy and performance, its governance or its approach to social and environmental matters.

Thus, for example, they may hold additional meetings with management or with the independent directors or the chairman.

They should also act collectively with other managers where appropriate.

For example, in the run up to the current crisis in instances when managers had concerns and attempted to engage, they were ignored or even received misleading information. A number of our members asked for the Chief Executive of the Royal Bank of Scotland to stand down as early as the initial rights issue in June 2008 and yet it was not until the Government refinancing was arranged in October that he did so.

To facilitate collective dialogue we have set up an industry working group to see if we can get investors to work together more effectively in the future.

Investors should also exercise their voting rights in a considered way and vote all shares held. If they register an abstention or vote against the resolution, they should let the company know in advance of their intention and the reasons why.

So how are we ensuring that the Code will be effective? I can at this juncture only talk about the experience we have in the UK. Following Sir David Walker's Review of corporate governance in financial institutions it will be a regulatory requirement that asset managers state publicly whether they apply the Code or their alternative business model. Thus it will be transparent to all who exercises their stewardship responsibilities and who does not.

But how will we determine that those that comply adhere to its provisions? The UK Corporate Governance Code is enforced through the actions of shareholders who have statutory rights and judge explanations on their merits and either accept or challenge them. However, the relationship between asset managers and their clients is different and the Stewardship Code will not be subject to the same enforcement mechanism. Thus if the manager's policy did not meet clients' expectations then clients will tend to appoint a manager whose policy does rather than seek to change an existing policy.

The association that I work for recognised this some time ago and has monitored the industry's adherence to the ISC Statement of Principles on which the Code is based from 2002 through regular surveys. These have demonstrated that engagement has evolved and become more transparent since the first survey in 2003. The latest to 30 June 2008 shows that 32 fund managers representing 68% of the UK market actively engage, vote their UK shares, and have a public policy on engagement - they thus adhere to the Code. We are working with the UK's FRC to take this forward.

In conclusion, good governance will help ensure a sustainable and stable financial system but directors and investors should not be ascribed a public interest role. Directors' responsibility is to the company and that of asset managers is to their beneficiaries/clients. Asset managers do not run companies; do not set strategy nor are they insiders, in that they only have access to information that is available to the market as a whole. But the majority agree that where they have a significant long term shareholding stewardship is a good thing and they need to be able to exercise that responsibility effectively. They also accept that there may be lessons to be learnt from the crisis and have been and are taking steps to address these.